

Public Disclosure Authorized

Economic Monitoring Report

to the

Ad Hoc Liaison Committee

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WORLD BANK GROUP

THE WORLD BANK
IBRD • IDA

IFC International
Finance Corporation

MIGA Multilateral Investment
Guarantee Agency

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Acronyms

AHLC	Ad Hoc Liaison Committee
AML/CFT	Anti-Money Laundering and Combating Financing of Terrorism
CBRs	Correspondent Banking Relationships
DHIS2	District Health Information Software 2
DSL	Digital Subscriber Line
FATF	Financial Action Task Force
FCDO	Foreign, Commonwealth, and Development Office
GDP	Gross Domestic Product
GoI	Government of Israel
GNI	Gross National Income
IFRS	International Financial Reporting Standard
HR	International Health Regulations
IFMIS	Integrated Financial Management Information System
LGUs	Local Government Units
MENA	Middle East and North Africa
LTD	Loan to deposit
MENAFATF	Middle East and North Africa Financial Action Task Force
MoF	Ministry of Finance
MoH	Ministry of Health
NCD	Non-communicable disease
NCTP	National Cash Transfer Program
NEDCO	Northern Electricity Distribution Company
NPL	Non-performing loans
OMR	Outside medical referrals
OCHA	UN Office for the Coordination of Humanitarian Affairs
PA	Palestinian Authority
PCBS	Palestinian Central Bureau of Statistics
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PHEOC	Public Health Emergency Operation Center
PLA	Palestinian Land Authority
PMA	Palestine Monetary Authority
PNIPH	Palestinian National Institute for Public Health
PPA	Power Purchase Agreement
PPE	Personal protective equipment
SMEs	Small and Medium Enterprises
TEDCO	Tubas Electricity Distribution Company
UN	United Nations
VAT	Value Added Tax
WHO	World Health Organization

Executive Summary

- 1. The Palestinian economy is in a precarious situation.** The COVID-19 pandemic struck a weakened economy that was barely keeping up with the population growth in three years prior to the onset of the pandemic, with persistent fiscal deficits, high unemployment, growing poverty levels, especially in Gaza, and continuously declining levels of international support.
- 2. The Palestinian Authority (PA) has a limited set of fiscal and monetary policy instruments to effectively respond to the worst global health and economic crisis in a century.** These constraints narrow the range of economic policy decisions available for the PA. In a global economy transformed by the pandemic, where it is no longer ‘business as usual’, building a resilient recovery will depend increasingly on domestic policy efforts, but also pragmatic and stable cross-border arrangements, for example, on the issues of tax revenues and health. Support from the international community will remain important, but has been declining for several years, and will likely confront significant additional limitations due to the impact of the pandemic on governments’ budgets across the globe. In this new and rapidly changing international context, tackling much needed previously identified reforms will strengthen trust and create a more sustainable, inclusive, and resilient future for the Palestinian people, while contributing to the creation of additional fiscal space and financial stability.
- 3. In 2020, the combined effect of the COVID-19 outbreak, a severe economic slowdown, and a political standoff with the Government of Israel (GoI) over clearance revenues, resulted in one of the sharpest contractions in economic activity in the Palestinian territories on record.** The PA’s initial response, from early March until about end-May, to combat the spread of the COVID-19 outbreak was successful, despite the limited fiscal and monetary policy instruments available. But the second wave of infections, starting in July, proved to be more severe; and a third wave of the outbreak was registered in November peaking by the end of 2020. Although lockdowns remained limited during the second half of 2020, Gross Domestic Product (GDP) for the entire year is expected to have contracted by 11.5 percent. A modest recovery is expected in 2021 with growth returning to around 3.5 percent, reflecting in part the base year effect from a sharp contraction in 2020 and the uncertainty about the rollout of COVID-19 vaccinations. The crisis impacted employment levels in the Palestinian territories especially in sectors that have been affected by social distancing measures, such as tourism, restaurants, construction, and for workers that cross to Israel. In Gaza, 43 percent of those in the labor force were unemployed in the fourth quarter of 2020, while the West Bank recorded an unemployment rate of 15 percent during the same time. Overall, the unemployment rate for the Palestinian territories reached 23.4 percent at the end of the fourth quarter of 2020. Projections based on GDP per capita growth suggest that the poverty rate has been constantly increasing since 2016, reaching 28.9 percent in 2020, a significant increase of 7 percentage points in the last four years. This represents approximately 1.4 million people living in poverty in 2020.
- 4. The COVID-19 outbreak added pressure to the Palestinian economy’s structural fiscal dilemma.** Public revenues suffered in 2020 as lockdowns negatively impacted economic activity and, hence, revenue collection. In addition, the decision to stop accepting clearance revenues (the majority of PA revenue) from the GoI from May to November 2020, compounded the impact of COVID-19, reducing available resources to respond to and mitigate the impact of the crisis on households and firms. The PA’s overall spending increased in 2020 mainly due to higher transfers to households and businesses affected by the crises.
- 5. Most importantly, the crisis confirmed that if corrective policy decisions are not promptly adopted and more stable cross-border arrangements are agreed, the fiscal position would remain fragile.** In a context where the potential for additional domestic and external borrowing by the PA is becoming increasingly limited due to financial sustainability and stability concerns, and donors’ support may face increasing constraints, clearance revenues remain a key viable option. Aid to the budget received in 2020 reached US\$488 million – 20 percent less than what was received

in 2019 and the lowest in decades. Even though lockdowns were limited during the second half of the year and clearance revenue transfers were resumed in November, the PA's financing gap reached about US\$1.1 billion in 2020, forcing the PA to deplete its financial buffers and to start 2021 with a tough fiscal position. Looking forward, new and stable revenue arrangements should be agreed with the GoI given the important role these revenues play in stabilizing the PA's fiscal position and, hence, the economy.

- 6. The direct and indirect exposure of the banking system continues to pose a significant risk to financial sector stability, and potentially crowds out private sector borrowing.** The pre-existing level of stress, due to the 2019 liquidity crisis caused by the clearance revenue standoff, limited the ability of local governments to manage COVID-19 impacts, and the financial sector's ability to play a significant shock-absorbing role. Also, the rising exposure to domestic public debt, and its implications for the stability of the banking system, could potentially limit private sector access to much needed liquidity. In this regard, the efforts to reduce borrowing and avoid a concentration of risks need to remain an important policy goal. This also confirms the importance of an urgent resolution to ensure stable and automatic clearance revenues transfer, which would reduce the PA's need to access the domestic banking sector to partially finance its budget and, consequently, contribute to reducing financial risks.
- 7. The health sector plays a critical role in successfully mitigating the COVID-19 crisis and overcoming its disruptive economic and social consequences.** The Palestinian health sector has been suffering from significant challenges even prior to the outbreak. Some of these challenges relate to external restrictions that limit movement and access to resources and markets and have resulted in a fragmentation of the territory. Others are related to internal problems, such as a limited fiscal space, and poor economic growth, which have created additional bottlenecks. Timely implementation of comprehensive pending reforms would create this significantly needed fiscal space. In addition, the PA has been facing constraints with regards to controlling the movement of people, goods, and services across its borders, and deployment of qualified human resources to prevent, detect, and respond to pandemics.
- 8. Notwithstanding the challenges, the PA took proactive steps to respond to the pandemic, in collaboration with the GoI and development partners, who played a key role in the initial stages.** The cumulative confirmed case count of COVID-19 infections in the Palestinian territories reached 163,573 in the West Bank (119,904 cases) and Gaza (44,279 cases) until January 7, 2021. To contain the spread, the PA reached out to 362,000 people through community engagement campaigns, delivered personal protective equipment (PPE), and administered more than 170,000 COVID-19 tests. Thirteen hospitals in the West Bank and three in Gaza were dedicated to COVID-19 management. Quarantine facilities were also established in both the West Bank and Gaza, and more than 500 health workers were trained in COVID-19 case management. An Inter-Agency COVID-19 Task Force, led by the Resident/Humanitarian Coordinator, as well as the Inter-Cluster Coordination Group, was established to ensure coordination at all levels. Finally, in the early stages of the pandemic, medical and procurement-related coordination between the GoI and the PA ensured the movement of goods and services.
- 9. Despite this early success in containment, cases surged in the second and third waves of the pandemic and the temporary suspension of coordination between the GoI and the PA has further complicated the situation.** Since end-June, the Palestinian territories have seen daily cases rise significantly and currently the surge continues in the West Bank and in the most densely populated areas of Gaza. In January 2021, the daily average number of new confirmed cases was 995. COVID-19 has disrupted health system financing and service delivery for other essential health services, such as maternal, newborn, and child health, and non-communicable diseases. Delivery of essential health inputs in Gaza has been delayed considerably and there are still shortages of PPE and key laboratory and other critical medical equipment. Finally, the increase in the number of cases is partly attributable to the movement of Palestinian workers between Israel and the Palestinian territories with the pandemic surge in Israel spreading to the Palestinian territories.

- 10. The report identifies policy recommendations which can contribute to overcoming the health and humanitarian crisis created by the pandemic.** First and foremost, improved coordination between the West Bank and Gaza, as well as between the PA and the GoI, would serve as a public good not only for public health and clinical management of COVID-19 but more importantly for the vaccination efforts given the public good nature of vaccinations. Second, scaled-up testing, tracing, and quarantining, as well as surged case management capacity should be strengthened. Third, it is necessary to establish a Public Health Emergency Operations Center (PHEOC) to liaise with all partners, centralize epidemiological and routine health service data, and communicate and coordinate with all stakeholders. Fourth, it is essential to facilitate the procurement and movement of health commodities, including COVID-19 vaccines as they become available, between Israeli ports, the West Bank, and Gaza. Fifth, to ensure that previous progress made with outside medical referrals is not jeopardized, processes must be institutionalized for referral permits, with continued coordination between Palestinian and Israeli medical providers.
- 11. The international community can help mitigate the current challenges that the health sector in the West Bank and Gaza faces.** The PA requires support from the international community to increase investment in the health system. For example, according to the PA's financing plans, at least US\$113 million is needed to respond to the surge of COVID-19. Estimates on COVID-19 vaccine purchase and deployment cost suggest that a total of about US\$55 million would be needed to cover 60 percent of the population living in the West Bank and Gaza. Also, in order to ensure there is an effective vaccination campaign, the Palestinian and Israeli authorities should coordinate financing, purchase and distribution of safe and effective COVID-19 vaccines. From a technical perspective, it is critical that both PA and Israel share information on the comprehensive readiness assessment for launching and progressive expansion of the COVID-19 vaccination plans, as this impacts the success of vaccination efforts for both Palestinian and Israeli populations.
- 12. As discussed in the previous AHLC report,** the PA has made significant fiscal progress with reductions of the total deficit over the years, while aid to the budget fell. Looking forward, despite efforts to adjust the budget to address the effects of the pandemic, continued budget support from the international community remains critical for the PA and for a resilient economic recovery in the West Bank and Gaza.
- 13. The main body of the report is organized in two chapters and one supporting annex.** Chapter I focuses on recent economic developments in the real, fiscal, and banking sectors, while providing a near-term outlook that highlights critical challenges facing the Palestinian economy. Chapter II highlights the current status of the COVID-19 pandemic in the West Bank and Gaza. This chapter describes the evolution of the pandemic, as well as its impact on other essential health services, ending with recommendations to control COVID-19 and strengthen the Palestinian health system. Annex I assesses the status of the World Bank recommendations to the AHLC meeting over the years.

Chapter I: Recent Economic Developments

1. Economic Activity

- 14. The COVID-19 pandemic has severely affected an economy already weakened by three years of low economic growth, high unemployment, persistent fiscal deficits, declining international support, resulting in one of the sharpest declines in economic activity in the Palestinian territories in 2020 on record.** Despite taking early necessary measures to contain the spread of the pandemic, a second wave returned in the beginning of July, forcing partial reintroduction of measures to restrict movement. The third wave of the outbreak was registered in November and peaked by the end of 2020. For 2020, it is projected that the COVID-19 crisis has had a substantial negative impact on the economy and the Palestinian people. With uncertain prospects for obtaining the vaccines for the population, the COVID-19 shock will likely continue to adversely affect activity in 2021 as well.
- 15. Both Palestinian territories and Israel have seen concurrent increases in COVID-19 infections through September 2020, with the Palestinian territories witnessing another wave in November while Israel is experiencing a significant increase since December of 2020.** The state of emergency that was declared on March 5 and the resultant closures were effectively ended by May 25, following the end of the Eid Al Fitr holiday and the start of the 12th-grade exams on May 30. However, by the end of June, the second wave of the pandemic surged (Figure 1). In response, by the beginning of July, new measures restricting movement and activity were reintroduced. Nonetheless, the number of cases continued to rise until end-September and peaked in mid-October. After having stabilized through October, new cases reached their peak in early December, and since then have been declining. As of January 12, 2021, the Palestinian territories have had over 145,000 confirmed cases. A similar pattern of infection rates has been observed in Israel (Figure 2) up until late September when the GoI announced a second nation-wide lockdown, as Israel recorded some of the highest rates of infection per million people of population in the world at the time. Since the lockdown, new cases have decreased considerably through November, but have since peaked again up until mid-January 2021; current biweekly cases per million people in Israel are still the highest they have ever been. As of January 12, 2021, Israel has had over 500,000 confirmed cases and over 3,700 deaths.

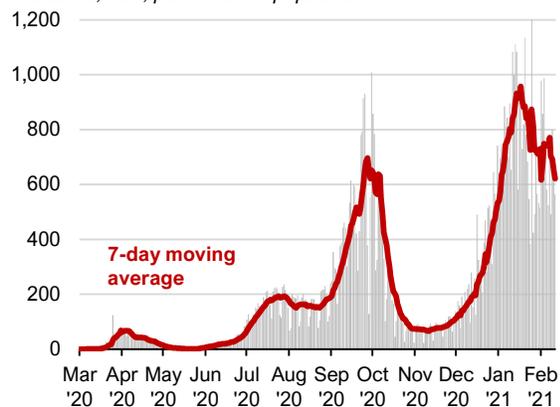
Figure 1: New COVID-19 infections in the Palestinian territories

Infections, new, per million of population



Figure 2: New COVID-19 infections in Israel

Infections, new, per million of population



Source: Johns Hopkins University CSEE and World Bank staff calculations.

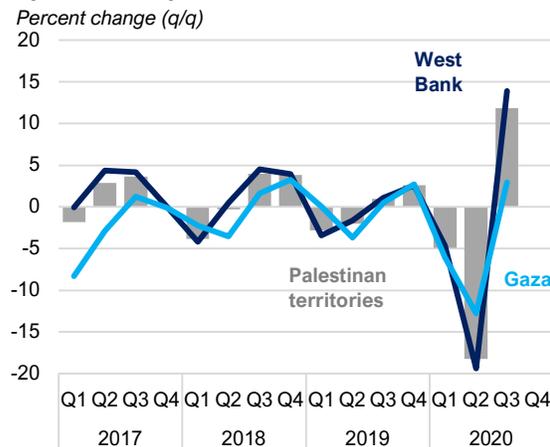
- 16. Economic activity in the Palestinian territories posted a sharp contraction in the first quarter of 2020.** Even though the lockdowns at the start of the pandemic were introduced at the beginning of March, thereby affecting only one month in the first quarter, the decline in activity was rapid and

broad (Figure 3). Gross Domestic Product (GDP) for the West Bank and Gaza in the first quarter of 2020 registered a contraction of 4.9 percent compared to the previous quarter (q/q) or 3.4 percent compared to the same quarter of the previous year (y/y). All components of GDP declined with consumption, both private and public, as well as capital investments falling the most.

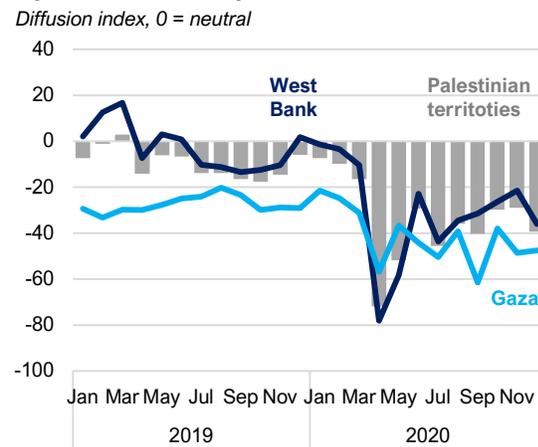
17. The one of the largest economic contraction was recorded during the second quarter, while activity rebounded partially in the third quarter (latest available data). In the absence of a discretionary fiscal response to mitigate the crisis impact on the households and the private sector, economic activity experienced the one of the largest contraction on record in the second quarter declining by 18 percent compared to the first quarter or 19.5 percent compared to the same quarter of 2019 (Figure 3). Private consumption contracted by nearly 20 percent (y/y), while capital investments collapsed by 37 percent (y/y) during the second quarter. The trade deficit shrank as exports contracted less than imports (18 percent vs. 27 percent (y/y)). There was a rebound in the third quarter as the economy grew by 12 percent (q/q), but nonetheless, it was still nearly 12 percent lower than the same quarter of 2019 with private consumption and capital investment continuing to record significantly lower levels.

18. Monthly indicators of economic activity painted a similar picture of sharp contraction and partial rebound in the second and third quarters, respectively, with activity softening again towards the end-2020. The Palestinian Monetary Authority published its monthly Business Cycle Index (PMABCI, Figure 4). This index is obtained by surveying a representative sample of businesses on the current conditions in their respective markets.¹ In April, when the index recorded its lowest value, more than two thirds of surveyed firms were completely shut down. The index improved in the subsequent months until July, when the second wave of infections hit, and new restrictions were announced. Similar movements have been observed in industrial production (Figure 5) and the proportion of returned checks (i.e., the number of checks issued that could not be cleared due to insufficient funds, Figure 6).

Figure 3: GDP growth in the Palestinian territories **Figure 4: Business cycle index**



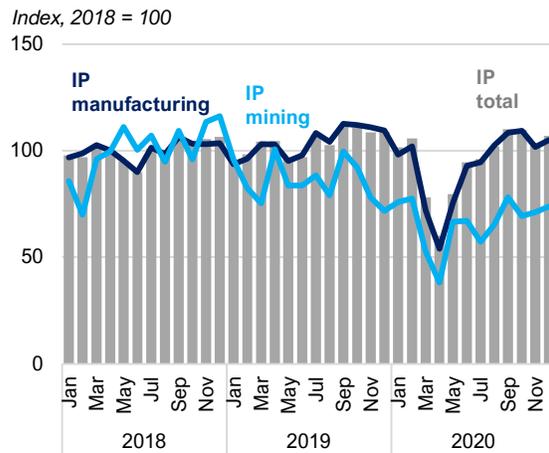
Source: PCBS.



Source: PMA.

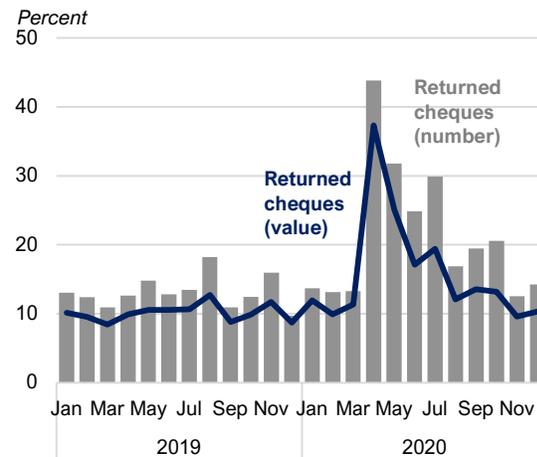
¹ PMABCI is represented as a diffusion index, which means that it gives a central tendency within the group of businesses surveyed. A value of zero indicates unchanged conditions, a positive value indicates improving conditions (up to 100) and a negative value indicates deteriorating conditions (up to -100).

Figure 5: Industrial production index



Source: PCBS.

Figure 6: Returned checks as a share of total checks issued



Source: PMA.

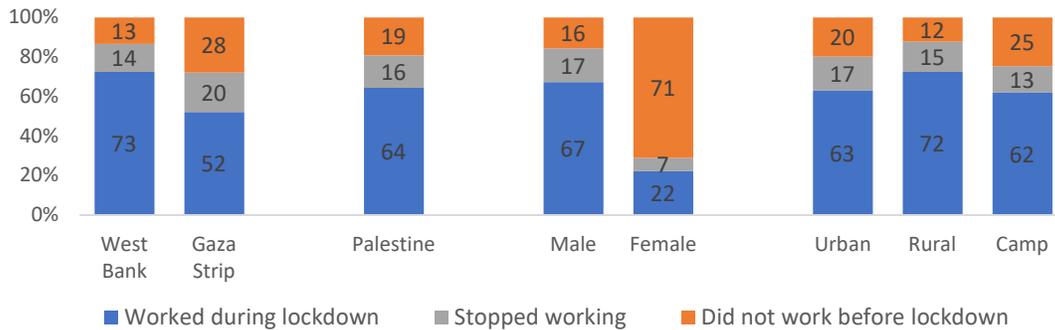
- 19. Inflation in the Palestinian territories turned negative during 2020 reflecting overall weak demand.** Growth in consumer prices had been modest prior to the outbreak of COVID-19, where prices generally moved in the 1-2 percent range. However, since April, growth in prices has turned negative and by December, prices were 1.5 percent lower than in the same month of 2019, reflecting weak demand by consumers. The Israeli Shekel, which is the main currency in circulation in the Palestinian territories, has continued its appreciation and this had a deflationary effect on the prices of imported goods. In addition, the prices of food products (most of which are produced domestically or in Israel) remained stable.
- 20. The unemployment rate in the Palestinian territories has increased further as a result of COVID-19, but has improved towards the end of 2020.** The unemployment rate rose in the first half of 2019 as a result of the slowdown in the economy resulting from disruptions in clearance revenues, reaching 27 percent. It then eased to 24 percent in the fourth quarter as the clearance revenue issues were resolved, and economic activity rebounded. However, it deteriorated again in 2020 with the onset of the COVID-19 outbreak. During the peak closures of activity in the second quarter, some 121 thousand people lost their jobs. Of this, some 96 thousand people have lost a job in the Palestinian territories, especially in sectors that have been affected by social distancing measures, such as tourism, restaurants, and construction, while some 25 thousand Palestinian workers that cross to Israel lost their job in the second quarter of 2020. Both third and fourth quarters saw an improvement with some 110 thousand people regaining their jobs since end of second quarter. This put the unemployment rate at 23.4 percent at the end of the fourth quarter of 2020. This headline story, however, masks a regional divergence. In Gaza, 43 percent of those in the labor force were unemployed in the fourth quarter of 2020, while the West Bank recorded an unemployment rate of 15 percent during the same time. Box 1 further illustrates the heterogenous geographic impact of the pandemic in the Palestinian territories in terms of employment, as well as in terms of gender.
- 21. Poverty has been adversely affected by slow growth over the past few years and the Covid-19 pandemic during 2020.** Based on the latest available data, 22 percent of Palestinians lived below the US\$5.5 2011 PPP a day poverty line in 2016/17. In the West Bank, poverty rates are lower but sensitive to shocks in household expenditures, while in Gaza any change in social assistance flows can significantly affect the population's wellbeing. Projections based on GDP per capita growth suggest that the poverty rate has been constantly increasing since 2016, reaching 28.9 percent in 2020, a significant increase of 7 percentage points in the last four years. This represents approximately 1.4 million people living in poverty in 2020.

Box 1: Monitoring the Socio-economic Impacts of the COVID-19 Pandemic

Considering the progression of the COVID-19 pandemic and how the containment measures could affect household welfare through their impact on labor and non-labor incomes, and access to services, the World Bank, UNDP/PAPP, as well as other UN agencies (UN-Women, UNFPA, UNICEF, WHO and WFP), and the Palestinian Central Bureau of Statistics (PCBS) implemented a Rapid Assessment Phone Survey during June and August of 2020 to measure the impact of COVID-19 on the Palestinian households' socio-economic conditions.

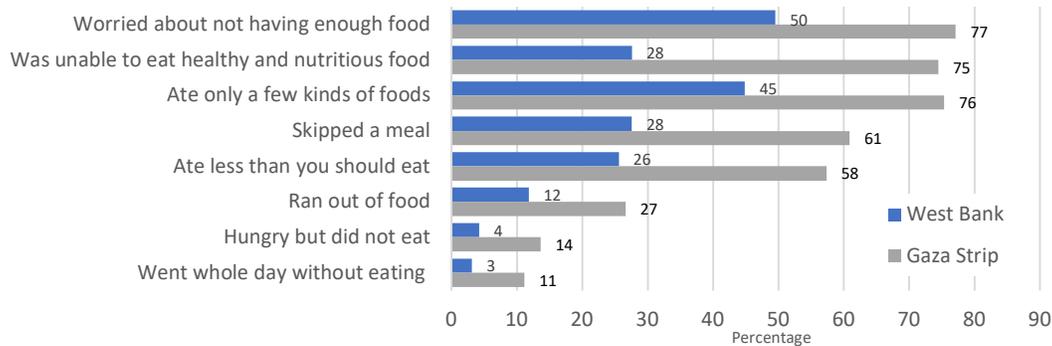
The survey finds that the COVID-19 pandemic had a negative impact on the socio-economic outcomes of households. Not only did 16% of main income workers in the Palestinian territories stop working during the period of emergency (from March to May of 2020), but only 23% continued receiving their usual wages, and most of them reported working less than usual. The lockdown also impacted the ability to work differently by economic sector, with services and industry being the most affected. While 48% of main income earners who stopped working were active in the services sector, 42% were from the industry sector.

Box 1 Figure 7: Heterogeneous Impact of the Pandemic



However, the national level estimates conceal significant gender and regional heterogeneities. While 73% of main income earners worked during the lockdown in the West Bank, only 52% did so in Gaza Strip. In addition, 14% and 20% of main income earners stopped working in the West Bank and Gaza Strip, respectively. The negative impact of COVID-19 on wages was stronger in the West Bank, as 61% and 31% of main income earners received no wages, respectively. The phone survey also shows that 61% of households reported worrying about not having enough food to eat, and this numbers rises to 77% in the Gaza Strip. In this context, more than a quarter of households (26%) consider that cash transfers are the most relevant program to help minimize the effect of the COVID-19, followed by job creation (19%).

Box 1 Figure 8: Heterogeneous Impact of the Pandemic



Going forward, it is important to continue securing the continuous delivery of social protection programs, which have been critical in helping households contend with the fallouts of the crisis. Similarly, the implementation of policies that support the restart of the economy will help with the recovery of labor incomes and address the second preferred government measure among Palestinian households to address the effects of the COVID-19, especially in areas hit harder by the pandemic such as the Gaza Strip.

Source: PCBS, <http://www.pcbs.gov.ps/post.aspx?lang=en&ItemID=3825>

22. **The outlook for the Palestinian economy looks grim especially given the lack of clarity on prospects for obtaining the vaccine against COVID-19.** The Palestinian economy has been in a very difficult situation in 2020 facing triple crises reinforcing each other: i) a resurgent COVID-19 outbreak, ii) a severe economic slowdown, and iii) a political standoff with the Government of Israel that disrupted clearance revenues for over six months (May-November 2020). Of particular importance is the impact of clearance revenues disruption on GDP. The drag on growth from the fiscal shocks in 2019 and 2020 is estimated to be in the range from 0.3 to 0.8 percentage points. In 2019, economic growth could have ranged between 1.6-2.1 percent in absence of the fiscal shock, compared to actual growth of 1.4 percent (Box 2).

Box 2: Fiscal Shocks of 2019 and 2020 and Impacts on the Economy in the Palestinian territories.

The short-term impact of discretionary fiscal policy on output is measured using fiscal multipliers. Fiscal multipliers are defined as the ratio of a change in output (ΔY) to a discretionary change in government spending or tax revenue (ΔG or ΔT). Put simply, the fiscal multiplier measures the effect of a \$1 change in government spending or tax revenue on the level of GDP.

The fiscal multipliers are not widely used by economists in operational work given that it is very difficult to estimate them properly. It is difficult to isolate the direct effect of fiscal measures on GDP, because of the two-way relationships between these variables. In addition, data availability limits the scope for estimating multipliers. Econometric and model-based methods need 15 years of quarterly data to produce unbiased estimates.

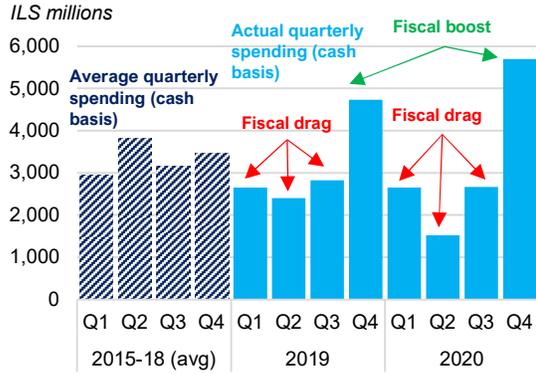
There is an emerging consensus in economic literature that spending multipliers vary both across countries and across time. Recent research has shown that the size of government spending multipliers ($\Delta Y/\Delta G$) depend on the key characteristics of the economy in question. For example, the higher trade openness of a country leads to a lower multiplier as part of the extra demand can be met from abroad. Also, the nature of the exchange rate regime matters as countries with flexible exchange rate regimes tend to have lower multipliers. In addition to the structural characteristics of economies, temporary factors tend to increase or decrease multipliers from their “regular” levels as well. For example, the stage of the business cycle in which an economy finds itself affects the size of the multipliers as they tend to be larger in a recession.

Given lack of data, we employ a simple approach as outlined in Batini, et al. (2014). These authors propose to group countries into three groups that are likely to have similar multiplier values based on their characteristics. They employ a three step approach where they: i) assign scores based on the country’s structural characteristics; ii) sum the scores to determine the likely level of the first-year multiplier (low, medium, or high) in “normal” times; iii) scale up or down the range assigned through the scoring method depending on whether the country is undergoing any of the “temporary” characteristics. Following this approach, we obtain estimate for the government spending multiplier to be in the range between 0.2-0.6.

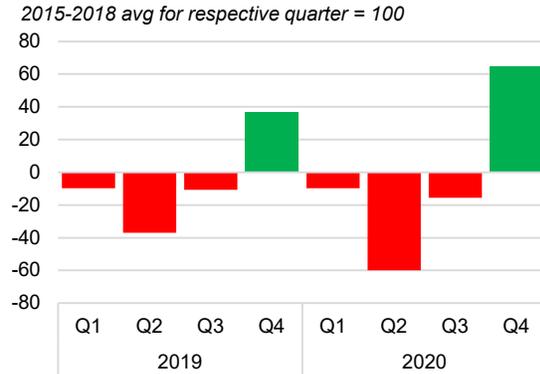
Both 2019 and 2020 saw large disruptions in spending as a result of the suspension of clearance revenue receipts resulting in massive fiscal shocks. For about six months, the PA was without some 60 percent of its regular revenues without the ability to rely on other sources to compensate for the lack of this revenue. Consequently, spending in six out of last eight quarters was lower than 2015-18 average (Box2 Figure 1). In the second quarter of 2019 spending was almost 40 percent lower than trend and again in 2020, spending was 60 percent lower. Fairly large spending multiplier implies that a large and sudden shock has a sizable effect on the economic activity in addition to other shocks. Consequently, drag on growth from the fiscal shocks in 2019 and 2020 is estimated to be in the range from 0.3 to 0.8 percentage points. In 2019, economic growth could have ranged between 1.6-2.1 percent in absence of the fiscal shock, compared to actual growth of 1.4 percent.

Beyond impact on economic growth, these disruptions potentially have other adverse effects. Periodic clearance revenue disruptions lead households and firms to engage in “precautionary savings.” This lowers the multiplier and dampens the catch-up effect when back-payments are cleared. In addition, financial sector exposure to households and firms increases which can lead to more risk averse lending in the future. Going forward, important to find a solution to “ringfence” clearance revenues given their large role in sustaining government spending, especially given absence of deficit financing options and lack of monetary policy tools.

Box 2 Figure 9: 2019 and 2020 public spending compared to 2015-18 average



Box 2 Figure 10: Changes in spending for 2019 and 2020 compared to 2015-18 average



Source: MoF for data and World Bank staff estimates and calculations.

Batini, N., L. Eyraud, and A. Weber, 2014, "A Simple Method to Compute Fiscal Multipliers," IMF Working Paper 14/93 (Washington: International Monetary Fund).

23. Consequently, for 2020, the GDP for the entire year is expected to contract by about 11.5 percent. Uncertainty about the rollout of COVID-19 vaccinations implies that the ongoing "lockdown-open-surge-lockdown" dynamic will disrupt the economic activity until enough population is vaccinated to achieve herd immunity. Accordingly, a modest bounce back is expected in 2021 with growth returning to around 3.5 percent, reflecting in part the base year effect from a sharp contraction in 2020.

Table 1: Palestinian territories: Selected Macroeconomic Indicators

	2017	2018	2019	Est. 2020	Forecast		
					2021	2022	2023
Real economy, annual percent change, unless indicated otherwise							
Nominal GDP	4.7	0.9	5.3	-12.1	2.3	3.1	3.0
Real GDP	1.4	1.2	1.4	-11.5	3.5	3.2	3.0
GDP per capita (nominal)	1.9	-1.7	2.6	-14.3	-0.3	0.3	0.3
Contributions to Real GDP Growth							
Private Consumption (growth)	-1.1	1.1	3.8	-11.0	2.4	2.5	2.5
Gross Fixed Investment (growth)	6.9	2.5	0.9	-31.8	22.8	9.2	5.7
Exports (growth)	13.9	2.5	2.0	-9.6	3.8	3.0	3.0
Imports (growth)	1.3	4.5	1.4	-12.0	5.0	4.0	3.0
Unemployment Rate (ILO Definition)	25.7	26.2	24.0	25.9	24.9	24.0	23.5
GDP Deflator	3.2	-0.3	3.8	-0.7	-1.2	-0.1	0.0
CPI (year-average)	0.0	1.2	0.8	-0.7	0.7	0.9	0.9
Fiscal Account, percent of GDP unless otherwise indicated							
Expenditures	29.7	27.8	27.5	33.8	30.8	30.1	29.5
Revenues (including grants)	26.6	25.2	23.0	26.1	25.9	25.9	25.8
General Government Balance	-3.2	-2.5	-4.5	-7.6	-4.9	-4.2	-3.7
General Government Debt, ex. arrears	15.8	14.5	16.3	24.2	24.8	25.1	25.4
Balance of Payments, percent of GDP unless indicated otherwise							
Current Account Balance	-13.2	-13.2	-10.4	-6.5	-8.1	-8.3	-8.9
Imports, Goods and Services	52.7	55.4	53.5	51.3	54.9	56.5	57.4
Exports, Goods and Services	15.7	16.0	15.5	15.8	16.3	16.6	16.8
Net Foreign Direct Investment	1.2	1.7	1.1	0.9	0.8	0.8	0.8
Gross Reserves	2.8	3.3	3.8	4.7	4.6	4.4	4.5
External Government Debt	6.5	6.3	7.1	8.8	8.6	8.3	8.1
Terms of Trade (growth)	-5.4	-1.6	9.9	3.3	-2.5	-0.3	-0.4
Memorandum items:							
GDP nominal (US\$ million)	16,128	16,277	17,137	15,061	15,408	15,883	16,365

Source: PCBS, MoF and PMA for history and WB Staff for Estimates and Forecasts.

2. Public Finance

Fiscal performance 2020

- 24. The Palestinian Authority (PA) suffered from an extremely challenging fiscal situation in 2020 due to the COVID-19 pandemic and the suspension of coordination with the Government of Israel (GoI).** To control the spread of the pandemic, the PA imposed several lockdowns throughout 2020 which had a negative impact on economic activity and, ultimately, revenue generation. In parallel, the pandemic also resulted in additional medical spending and higher social transfers to address the growing needs of the new poor. The suspension of coordination with the GoI, which started on May 19, 2020 and lasted for six months, compounded the impact of the COVID-19 crisis on the PA's fiscal situation as it resulted in a cessation of clearance revenue transfers, which constitute more than two thirds of public revenue.
- 25. Domestic revenue dropped by 5 percent, on a commitment basis, in 2020 due to a decline in tax collections while nontax revenue was close to its previous year's level.** All major domestic tax items witnessed a drop including income tax and VAT by 14 and 3 percent, respectively, as a result of the overall economic slowdown. Interestingly, domestic collections from tobacco excise increased by a third in 2020 as the closure of the border with Jordan has eliminated tobacco smuggling, resulting in higher public revenues. The increase in this item, however, was not enough to offset the deterioration in other domestic taxes. Despite a 7 percent decline in collections from fees and charges given the economic slowdown, nontax revenues were maintained at their 2019 level due to two large transfers of investment profits from the Palestine Investment Fund (PIF)² in the amounts of NIS41 million in February and NIS53 million in October.
- 26. The cessation of clearance revenue transfers for half of 2020 severely impacted the fiscal situation but their resumption later in the year helped ease the fiscal stress.** On November 17, 2020 the PA announced its decision to resume all levels of coordination with the GoI, including on clearance revenues. Around NIS3.7 billion (US\$1.08 billion) of revenues have accumulated with the GoI, between May and November, and they were transferred in one shot which helped the PA repay obligations accrued over the previous months (See table 2). With the transferred amount, total clearance revenues in 2020 were about 7 percent lower than in 2019, on a commitment basis. The decline was mainly driven by a 14 percent drop in VAT in line with a comparable decline in imports. Also, petroleum excise decreased by 10 percent given the decline in manufacturing and other economic activity.

Table 2: Breakdown of PA spending of the clearance revenue lumpsum transferred by GoI in November 2020

Total clearance revenue transfer by GoI in November 2020 (NIS mill)	3,700
Wage arrears	2,400
Private sector arrears	600
Payment to domestic banks	450
Other	250

Source: PA MoF

- 27. The PA's recurrent expenditure increased by 5.5 percent in 2020 mainly driven by higher transfers.** Transfers rose by 13 percent as the PA increased its assistance to those mostly affected by the crises. In particular, social payments to the poor, assistance to vulnerable families and unemployment benefits witnessed a significant increase (See Table 3). Even though the PA was

² PIF is the sovereign wealth fund.

only paying fifty percent of salaries between May and November, wage arrears accrued over this period were repaid towards the end of the year and, on a commitment basis, the wage bill increased by 3.5 percent in 2020. This increase reflects annual increases, cost of living allowances and additional hiring of medical staff. Net lending³ increased by less than 3 percent in 2020 due to an increase in water-related costs as local government units struggled to collect enough revenues to cover utility bills amid the economic crisis and also due to higher lending by the PA to a number of public entities in 2020. Finally, spending on goods and services was slightly reduced in 2020 as a large share of public employees worked from home for several months as part of the national emergency announced to deal with the COVID-19 breakout.

Table 3: Social assistance by the PA, 2019 and 2020

Social Assistance (NIS million)	2019	2020
Assistance to poor households	1,031	1,063
Assistance to vulnerable families	646	765
Unemployment benefits	145	207
Total	1,822	2,035

Source: PA MoF

28. To maintain core recurrent spending, the PA had to increase borrowing from domestic banks and accrue large arrears in 2020. On a commitment basis, the PA’s total deficit amounted to US\$1.6 billion in 2020, while aid received was US\$488 million – 20 percent lower than in 2019 and the lowest in decades. As a result, the financing gap after aid reached US\$1.1 billion in 2020. To finance the gap, the PA increased its net domestic bank financing. Even though the PA managed to repay some of its domestic bank debt in December, its total stock of domestic debt reached US\$2.3 billion as of end-2020, up from US\$1.6 billion as of end-2019. In addition, the PA had to accrue arrears mostly to private suppliers and the pension fund. According to data provided by the MoF, gross arrears accumulated in 2020 peaked at US\$1.1 billion, but the PA managed to pay some of this debt later in the year reducing net arrear accumulation to US\$611 million in 2020.

Table 4: The Palestinian Authority’s deficit financing, 2020

(million)	NIS	USD
Total balance	-5,614	-1,637
financing	5,614	1,637
External Budgetary Support	1220	356
Development Financing	452	132
Net Domestic Bank Financing	1,895	553
Net arrear accumulation	2,096	611
Other	-49	-14
Residual	0	0

Source: PA MoF

Beyond the crises, a longer-term fiscal agenda for recovery

29. The fiscal position needs to be more sustainable to ensure a solid recovery strategy based on strong and stable macroeconomic foundations. The unreliable funding of some services, and the high level of payment arrears to private sector suppliers is inhibiting the development of the

³ Net lending represents deductions made by the GoI from clearance revenues to offset utility bills owed by Local Government Units and distribution companies to Israeli suppliers.

economy and adding to firms' liquidity constraints. To support a more sustainable fiscal position, the fairness, effectiveness, and efficiency of public spending, including the wage bill, need to be improved and prioritized towards supporting the most vulnerable. On the expenditure side, focus should be on tackling recommended reforms including to the generous public pension system, and untargeted transfers that result in significant support to those connected to the PA at the expense of other, often more needy, parts of society. Better managing health referrals is a priority. There is also a case for reorganizing civil service arrangements to establish a more responsive and efficient government sector.⁴ Using digital technology to reform the provision of government services and enhancing transparency and predictability should be central to this effort.

30. A commitment by donors to continue supporting the PA after the COVID-19 crisis ends remains important. Full economic recovery to pre-crisis levels is likely to be gradual and will take some time. This will continue to have an impact on the PA's ability to collect taxes. This also applies to Local Government Units (LGUs), which will continue to need support to cover their recurrent expenditures after the COVID-19 crisis is over, as the economic fallout will impact their ability to generate enough revenue for some time, making it difficult to sustain basic service delivery.

31. Cooperation by the GoI to implement institutional measures to reduce fiscal leakages on clearance revenues in a sustainable way would significantly help the PA's finances and contribute to a sustainable recovery. Clearance revenues are a key source of public revenues and they play a key role in the sustainability of public spending and, hence, in the stability of economic conditions in the Palestinian territories. Given the role that clearance revenues play in stabilizing the Palestinian economy, ensuring their uninterrupted flow should be a priority for the benefit of both parties. Recommended actions to achieve this goal include:⁵

- a) Putting in place a mechanism to electronically link the VAT systems of both authorities to exchange real-time information on all purchases being made.
- b) Transferring customs responsibilities to the PA and establishing Palestinian bonded warehouses.
- c) Transferring VAT on bilateral trade with Gaza to the PA.
- d) Establishing greater transparency regarding deductions from clearance revenues by the GoI.
- e) Renegotiating the 3 percent handling fee charged by the GoI to handle Palestinian imports as it is considered too high.
- f) Exempting the PA's fuel imports from taxes.
- g) Exit fees collected at the Allenby Bridge should be allocated between the parties according to the shares specified in the Paris protocol.

⁴ For more details, see the World Bank's Public Expenditure Review of The Palestinian Authority: Towards Enhanced Public Finance Management and Improved Fiscal Sustainability. September 2016. <http://documents1.worldbank.org/curated/en/320891473688227759/pdf/ACS18454-REVISED-FINAL-PER-SEPTEMBER-2016-FOR-PUBLIC-DISCLOSURE-PDF.pdf>

⁵ For additional information regarding these recommendations, see the World Bank's "Economic Developments in the Palestinian territories" published in November, 2020 and which can be accessed here: <http://documents1.worldbank.org/curated/en/574441606230442130/pdf/Economic-Developments-in-the-Palestinian-Territories.pdf>

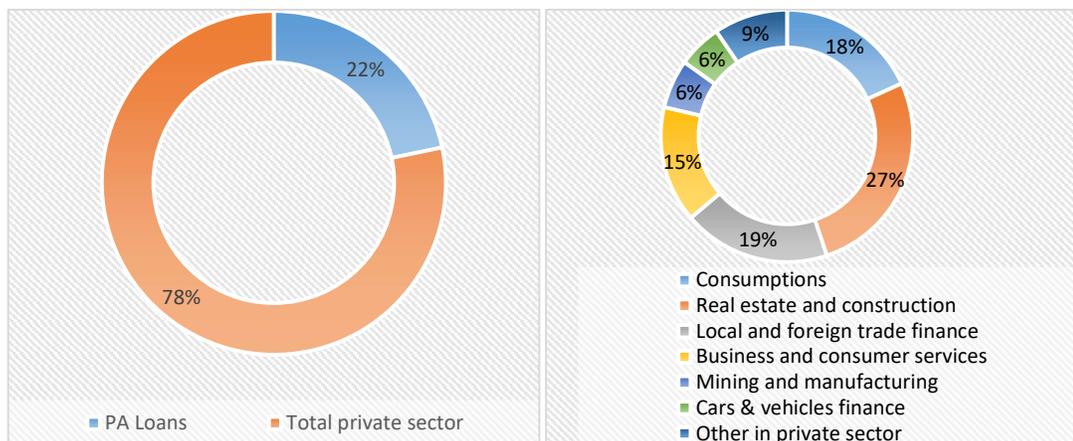
3. Money and Banking

- 32. The COVID-19 crisis has further compounded the financial sector risks, driving stability concerns to new highs.** The Palestinian financial sector entered the COVID-19 crisis with already limited liquidity or capital buffers and significant vulnerabilities due to the 2019 clearance revenue standoff. This pre-existing level of stress means that it has limited ability to absorb large shocks or play a significant counter-cyclical role, creating a challenge for the authorities when managing the financial implications of this crisis – especially given the lack of control of the monetary base. It also reinforces the importance of more effective coordination between the PA, the PMA, and the financial industry to conduct fact-based analysis of the impact of the crisis and of measures already adopted to assist banks and firms through the financial sector. On that basis, the authorities and the industry would then be in a better position to mobilize as effectively as possible limited resources for impact and targeting.
- 33. Policies to mitigate the financial impact of COVID-19 need to be targeted, well-designed, maintain sound prudential regulations, and ensure trust and confidence in the banking system.** The four- and six-month moratoriums on credit repayment announced in March 2020 by the PMA, and the temporary suspension of the classification of bad checks, had the advantage of providing fast relief. They are also extraordinary measures that do not discriminate between impacted and non-impacted borrowers and can increase credit risk going forward. The downside risk is also an unintended decline in new lending to truly distressed or recovering solvent enterprises. This is especially relevant in the Palestinian context, given the increase in Loan-to-Deposit Ratio over recent years (peaking at 70 percent in November 2020), further raising liquidity concerns and potentially hampering the ability of banks to continue serving the financial needs of the public and private sectors.
- 34. To partially mitigate the economic implications of the pandemic and inject additional liquidity, the PMA launched an SME-focused COVID-19 response program, *Istidama (Sustainability)*.** The program aims to inject low-cost financing into the market using existing bank channels, targeting “borrowers who have been directly affected by the current economic situation only”.⁶ The success of the program hinges on (among other things) take-up by financial intermediaries and the perceived risk-reward calculation of participating banks (taking into account the cap on interest rate, and level of credit-risk within the targeted sectors).
- 35. Credit guarantees should be considered complementary to prudential and stability measures.** In addition to direct lending, credit guarantees are a crucial and customizable instrument that should be further used to direct financial sector support in response to the current crisis. Partial credit guarantees are not new to the Palestinian market, and some adjustments to existing schemes have been implemented as a COVID-19 response window by the PA and donors. Expanding the role of existing partial credit guarantees serves both the immediate need to inject additional liquidity to MSMEs, and the longer-term recovery needs of distressed borrowers. The use of credit guarantees should be reflected in the PMA’s and PCMA’s prudential and risk requirements (e.g., with regards to provisioning). Special consideration should be given to use across different financial intermediaries (e.g., microfinance institutions and non-bank financial institutions such as leasing).
- 36. Protracted shocks so far had a clear and increasing effect on the performance of the Palestinian financial sector in 2020.** According to preliminary reporting by the PMA through December 2020, the profitability of the banking sector declined significantly in 2020 when compared to 2019 (35 percent decline). Return on equity dropped to 5 percent in 2020 compared to 8.3 (2019) and 9.4 (2018); return on assets dropped to 0.5 percent compared to 0.95 (2019) and 1.15 (2018). Bank deposits and direct credits grew at a similar pace of 12 and 11 percent respectively, resulting in a slight decline in the credit-to-deposit ratio to 67 percent. A review of credit exposure

⁶ <https://www.pma.ps/en/Media/Press-Releases/palestine-monetary-authority-issues-instructions-to-mitigate-the-effects-of-covid-19-crisis>

to the private sector indicates persistent sectoral concentration, with two thirds of all private lending going to construction, trade finance, or consumer loans.

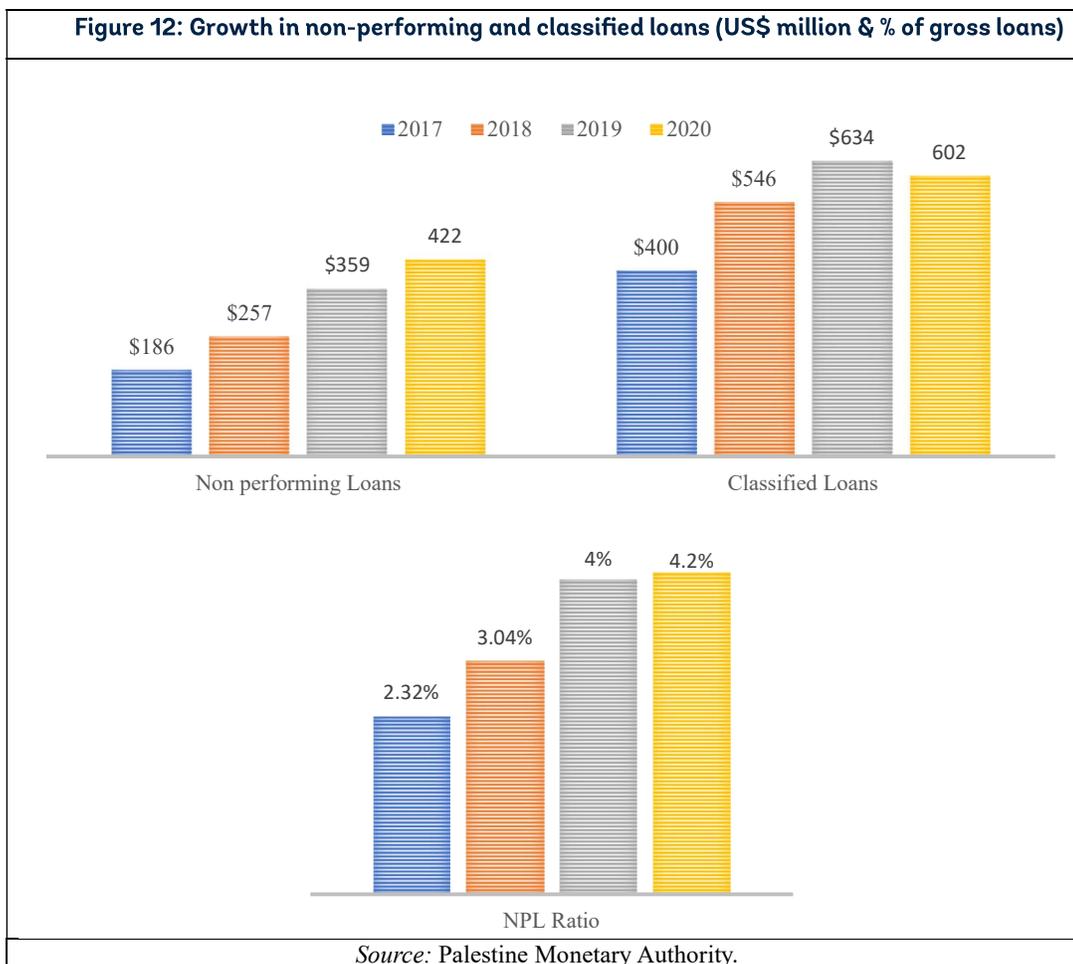
Figure 11: Distribution of credit by sector (left) and by economic activity in the private sector (right)



Source: Palestine Monetary Authority⁷.

- 37. The impact of COVID-19 on the economy and the PA’s decision to only pay partial salaries has deteriorated the quality of loan portfolios, and further deterioration is likely.** Non-performing loans (NPLs) have maintained an upwards trajectory from 2018. The NPL ratio (which represents the percentage of nonperforming loans out of all direct loans and is a lagging indicator) stands at approximately 4.2 percent as of December 2020. While this NPL ratio appears manageable given the context, discussions with several local banks indicated that NPLs are concentrated in critical portfolios (e.g., SMEs), and that aggregate NPL indicators are likely underestimated as a result of the COVID-19 moratorium and the subsequent rescheduling of PA employee loans (based on PMA guidance issued in recent years). The expected further deterioration in the quality of SME and consumer loan portfolios could translate soon in delayed higher NPLs, particularly in banks with substantial exposure to SMEs and PA employees.
- 38. The PA borrowing practices from the local banking sector to finance fiscal imbalances, and the disruption in clearance revenues for more than 6 months in 2020, may generate new risks.** Following a few years of relative stability in PA borrowing (about US\$ 1.3-1.4 billion), the banking system’s exposure to the public sector (through domestic public debt) registered an increase in 2020, reaching US\$2.2 billion by the years end. With declining revenues due to COVID-19 implications and clearance revenue transfer issues, the PA has significantly increased borrowing from domestic banks, exceeding PMA exposure limit by 10 percent. Bank loans to PA employees (backed by future salaries) also represents an indirect channel of exposure to the public sector, standing at US\$1.7 billion by December 2020. When combined, PA and public employees account for US\$3.9 billion, or 40 percent of total banking sector credits.

⁷ According to December 2020 data.



- 39. Palestinian policymakers must carefully balance fiscal, monetary, and financial considerations.** The independence of the PMA, as supervisor and prudential regulator of the banking system, should be respected and upheld especially during times of crisis. The rising direct and indirect exposure of the banking system to the PA continues to pose a significant risk to financial sector stability, and potentially crowds out private sector borrowing. In light of the growing fiscal challenges faced by the PA over the past decade, the banking sector’s credit exposure to the public sector has been a cause of unease, exceeding PMA set limits on multiple occasions. With banks already constrained by growing credit risks and potential liquidity problems, additional borrowing by the PA may also crowd-out private sector borrowers impacted by COVID-19 implications.
- 40. The PMA and Financial Follow-up⁸ Unit have been taking steps toward upgrading the Palestinian anti-money laundering and combating financing of terrorism (AML/CFT) system to be more in line with international practices.** The authorities have been making steady progress toward upgrading integrity standards across the financial sector. In 2018, the local authorities conducted their first self-assessment with the aim of enhancing the ability of relevant AML/CFT stakeholders to identify, assess, understand, and mitigate the money laundering and terrorism financing risks. The assessment was officially endorsed by the Palestinian Cabinet in October 2018, followed by the adoption of the national AML/CFT strategy by the Cabinet in November 2018. In 2019, the PMA’s Inspection and Supervision Department issued instructions (15/2019) and circular (74/2019), setting requirements for banks to maintain adequate policies and procedures to prevent the abuse of financial services, and instructing banks to implement strengthened risk based internal

⁸ This corresponds to the Palestinian Financial Intelligence Unit.

controls in accordance with the national AML/CFT strategy. Other improvements on AML/CFT internal controls that are currently under implementation include reforms to governance and reporting procedures. This represents a step towards the commitment to, and implementation of, the Financial Action Task Force (FATF) AML/CFT standard conditions of membership to the MENAFATF. MENAFATF recently approved a request by the Palestinian Authorities to postpone the onsite visit (a requirement for the Mutual Evaluation) initially planned for 2020 due to the outbreak of COVID-19 and the continuation of the state of emergency.

- 41. Due to the global heightened money laundering and terrorist financing concerns, banks operating in the West Bank and Gaza are experiencing difficulties in maintaining their correspondent banking relations with foreign banks, including Israeli banks.** Payment activity between Israel and the West Bank and Gaza has an estimated yearly value of more than NIS44 billion. In 2016 Israeli banks canceled some of their correspondent banking relations with Palestinian banks as part of a general de-risking strategy. Following this decision, Israeli banks have continued to provide correspondent banking service to Palestinian banks under temporary letters of indemnification and immunity approved by the Israeli Cabinet, while a broader and longer-term solution is to be worked out for payments between Israel and the West Bank and Gaza. Various initiatives are underway to provide long-term solutions for solving the current issues in correspondent banking and in further facilitating the use of electronic payments with a focus on bank transfers, check payments, and cash payments,⁹.

⁹ Banks in the West Bank and Gaza are having to manage large amounts of excessive cash due to limits on the amount of cash which can be shipped to Israel. Part of the strategy is to reduce the amount of cash stored and the costs associated with this.

Chapter II: Building Health System Resilience in the Time of COVID-19

1. Introduction

42. Against the backdrop of the COVID-19 pandemic, which knows no boundaries, the PA grappled with a three-pronged health, economic, and political crisis. Since Spring 2020, the escalating health crisis due to COVID-19, the economic impact of closing businesses and increasing unemployment, and the political crisis have devastated the economy.¹⁰ Coordination between the PA and Israel was suspended in May 2020, and the PA announced resumption of the coordination in mid-November 2020.¹¹ However, there are still coordination constraints that risk exacerbating the humanitarian and health crises, including on customs clearance and movement restrictions between the West Bank and Gaza. Coordination also poses a threat for vaccination: as of January 2021, Israel has the highest COVID-19 vaccine coverage rates, but no one in the West Bank or Gaza has been vaccinated, even as the infection trends in Israel and the Palestinian territories are correlated with each other. Effective humanitarian, economic, and political coordination between the two authorities is critical to effectively control COVID-19 both through case detection and vaccination. This chapter highlights the health system context and pandemic preparedness in the Palestinian territories; the current status of COVID-19 in the West Bank and Gaza, as well as its impact on other essential health services; and provides recommendations to minimize the impact of the pandemic.

2. Pandemic preparedness and health system context

43. COVID-19 has exacerbated pre-existing weaknesses in the Palestinian health system, which has long been facing challenges due to protracted conflict, reduced fiscal space, and fragmented governance structures. There are unique governance and service delivery challenges. Due to the lack of adequate provision of health services, patients in Gaza frequently must travel to seek essential non-communicable disease (NCD) care. Due to limited government revenue and poor economic growth, almost half of all health spending in West Bank and Gaza is financed by households directly at the point of care, which is regressive, particularly for the poor and the vulnerable. The Palestinian Authority finances only a third of overall health expenditures, mostly on salaries and other recurrent expenditures, leaving it unable to scale up health system investments to achieve universal health coverage.

44. Prior to COVID-19, the West Bank and Gaza had already been facing significant issues with pandemic preparedness, exacerbated by the control of Israel over border crossings as well as fiscal constraints. The PA has faced constraints in its ability to control the movement of people, goods, and services across its borders, and deploy qualified human resources to prevent, detect, and respond to pandemics.¹² These constraints are attributable to security control over border crossings and the PA's access to markets, as well as an overreliance on donors and the associated fluctuations in financing, resulting in economic and fiscal vulnerabilities. Since 2015, pandemic preparedness capacity has been strengthened with trainings on surveillance, laboratory analysis, infection prevention, and control. However, challenges with regards to lack of control over the movement of people, goods, and services, limited jurisdiction over 61 percent of the West Bank comprising Area C, and the geographical divide between the West Bank and Gaza, continue to be bottlenecks to

¹⁰ Nickolay Mladenov (UN Special Coordinator for the Middle East Peace Process) “Briefing to the Security Council on the Situation in the Middle East” 21 July 2020

¹¹ “Palestinian authority to resume coordination with Israel” <https://www.aljazeera.com/news/2020/11/17/pa-to-restore-israel-ties-as-annexation-threat-fades> 17 November 2020

¹² Harutyunyan, V., 2012. International Health Regulations in the Occupied Palestinian Territory, *The Lancet*, vol 380

prevent and control pandemics.¹³ In addition, refugee camps, overcrowded conditions in Gaza, and building restrictions in Area C of the West Bank, pose significant obstacles to infection prevention and control.¹⁴ Finally, the fragmentation and weak baseline capacity of the health system create significant bottlenecks across constrained financing, service delivery, and physical and human resources.

3. COVID-19 from March to June 2020: control through coordination

- 45. West Bank and Gaza and Israel have both been impacted early by the COVID-19 pandemic, but despite early successes in containment, there was a surge from July through September; a new November surge has stabilized in the Palestinian territories while a significant surge continues in Israel.** The first cases were identified on March 5, 2020, and the cumulative confirmed case count was below 1,000 until June 20, 2020.¹⁵ August and September saw a significant surge in cases, and the pandemic has continued to spread since then. As of January 6, cumulative confirmed cases have increased dramatically to more than 160,000 in West Bank and Gaza.¹⁶ The rate of increase of confirmed cases in Israel has also increased significantly since June. As of January 12, 2021, Israel has had over 500,000 confirmed cases and over 3,700 deaths and continues to record some of the highest new cases per million people. Mortality remains relatively low compared to other lower-middle income countries, with a case fatality rate of 1 percent with 1,684 deaths in the West Bank and Gaza as of January 7, 2021. Initially, the pandemic was limited to the West Bank, but recently cases have been growing faster in Gaza than in the West Bank, highlighting concerns regarding the weak health system capacity. Of the 18,055 active cases as of January 6, 8,947 are in the West Bank, and 9,108 in Gaza; of the total confirmed cases since the beginning of the pandemic, 118,578 have been in the West Bank and 43,744 in Gaza. There are significant movement restrictions, including targeted lockdowns in Israel and movement restrictions especially during the weekends in the West Bank and Gaza. Despite these restrictions, Palestinian workers in construction, agriculture and health continue moving between Israel and the Palestinian territories, even though there are now requirements for randomized COVID-19 testing for those moving across borders.¹⁷
- 46. The PA, in collaboration with Israel and the support of international organizations and development partners, has taken proactive steps to prevent, detect, and respond to the pandemic.**¹⁸ Through the end of June, 362,000 people were reached through community engagement campaigns; personal protective equipment, including more than 1 million surgical masks and 2.6 million disposable gloves, were delivered to health workers; and more than 170,000 COVID-19 tests were administered. Thirteen hospitals in the West Bank and three in Gaza have been dedicated to COVID-19 management, including with equipment for respiratory triage. Quarantine facilities were established in both the West Bank and Gaza, and more than 500 health workers were trained in COVID-19 case management. Laboratory capacity was expanded, and community engagement campaigns were implemented. An enhanced electronic surveillance system was introduced, built on the District Health Information Software 2 (DHIS2) information system. The system includes data on case reporting for suspected and confirmed cases, documenting cases of quarantine over a 14-day status, hospital isolation cases, and laboratory requests and results, with information being tracked to the patient level managed by the Palestinian National Institute for Public Health (PNIPH). An Inter-Agency COVID-19 Task Force, led by the Resident/Humanitarian

¹³ “WHO and Ministry of Health strengthen capacities for International Health Regulations for Palestine” 3 February 2017 <http://www.emro.who.int/pse/palestine-news/ihr-workshops.html>

¹⁴ AlKhalidi, M., Kaloti, R., Shella, D., Basuoni, A.A., Meghari, H., n.d. Health system’s response to the COVID-19 pandemic in conflict settings: Policy reflections from Palestine. GLOBAL PUBLIC HEALTH 14.

¹⁵ All figures in this section are from Our World in Data, <https://ourworldindata.org/coronavirus/country/palestine?country=~PSE>, accessed on October 9, 2020

¹⁶ WHO Coronavirus Situation Report 58, issued 6 January 2021

¹⁷ United Nations Office for the Coordination of Humanitarian Affairs, COVID-19 Emergency Situation Report 19 (22 September – 5 October 2020) <https://www.ochaopt.org/content/covid-19-emergency-situation-report-19>

¹⁸ Data and information in this paragraph is based on Health Cluster Bulletin for Occupied Palestinian Territory: 1 May – 30 June 2020 & COVID-19 situation report 37, issued July 23, 2020

Coordinator as well as the Inter-Cluster Coordination Group, leads the coordination from the UN side. Finally, coordination with Israel was also ensured in the early stages of the pandemic, with medical and procurement-related coordination between the two authorities, ensuring the movement of goods and services. As a result, current COVID-19 management capacity in West Bank and Gaza has improved, with a 58 percent bed occupancy rate and a 52 percent ICU bed occupancy rate as of early January 2021.¹⁹ However, significant input gaps remain, as highlighted in the next section.

4. COVID-19 since June 2020: surge, suspension and resumption of coordination

47. Despite initial progress made against the first wave of the pandemic, challenges have rapidly mounted with the expansion of the pandemic to Gaza and the explosive surge of December 2020. There are significant challenges across every priority aspect of the pandemic response, including testing and tracing, vaccine introduction and delivery capacity, financing, points of entry, procurement, and lack of physical and human resources.

48. *Testing, effective surveillance, contact tracing, isolation, and quarantine remain a significant bottleneck,* even though significant increases in testing capacity have taken place since the beginning of the pandemic. Currently, 174,129 tests are conducted per million people in the West Bank and Gaza, which is one of the lowest rates in the Middle East and North Africa region.²⁰ The PA has a test positivity rate of over 21 percent, which is significantly higher than the WHO guidance of 5 percent or lower and indicates uncontrolled spread of the pandemic.²¹ Test positivity rates in Gaza are higher, at 29 percent, highlighting further limited testing capacity and faster spread.²² Limited testing not only has an immediate impact on case isolation and management, but it also delays the ability to open up the economy while controlling the increase of cases. Incoming travelers to Gaza enter a 21-day quarantine in six designated facilities, and those entering the West Bank must quarantine at home for 14 days. The discrepancy in quarantine policies poses difficulties in governance, and the quarantine requirements provide challenges in both contexts: in Gaza, not all quarantine facilities have the necessary support systems, and in the West Bank, those living in low-income families or crowded refugee camps are not able to effectively quarantine at home. While adherence to COVID-19-related lockdowns has been high and quarantine facilities have been set up, there have been capacity issues with quarantine facilities, and enforcement challenges in rural areas and refugee camps, as well as mobility issues for Palestinian workers between Israel and the West Bank. In addition, due to the suspension of coordination, COVID-19 test sites were dismantled in certain areas.²³ Finally, the lack of an integrated epidemiological surveillance system poses a threat: there are currently efforts to establish a Public Health Emergency Operation Center, which would assist in managing emergencies through integrating public health services and other functions, not only through improving surveillance capacity but also through stockpiling commodities, engaging communities, and training staff. As such, there is a double problem of lack of inputs and coordination with regards to testing and surveillance, posing a significant obstacle to an effective response.

49. *COVID-19 vaccine introduction and delivery capacity.* West Bank and Gaza are eligible for the COVAX AMC facility, which provides subsidies and facilitates access to a safe and effective COVID-19 vaccine for 92 low- and lower-middle income countries. COVAX is expected to provide free vaccines to 20 percent of the Palestinian population, and the Ministry of Health (MoH) plans to procure additional vaccines to reach 60 percent population coverage. Doing so will require a

¹⁹ COVID-19 Emergency Situation Report 25, 17-30 December 2020 <https://www.ochaopt.org/content/covid-19-emergency-situation-report-25>

²⁰ Our World in Data, <https://ourworldindata.org/coronavirus/country/palestine?country=~PSE>, accessed January 12, 2021

²¹ *ibid*

²² WHO Coronavirus Situation Report 58, issued 6 January 2021

²³ United Nations Office for the Coordination of Humanitarian Affairs, COVID-19 Emergency Situation Report 19 (22 September – 5 October 2020) <https://www.ochaopt.org/content/covid-19-emergency-situation-report-19>

significant level of financial mobilization of around US\$55 million, which is difficult given the existing funding gaps.²⁴ As of February 4, PA has not signed any bilateral agreements for direct procurement of vaccines and received fewer than a total of 20,000 doses of vaccines²⁵, which puts its procurement and coverage plans at risk, given the fact that many high-income countries have already placed advance market orders. While planning for the launch of COVID-19 vaccines is in progress, these plans have not been finalized. Vaccinating even 20 percent of its population will imply a 2.5-fold increase in annual vaccinations delivered by the Palestinian Ministry of Health, highlighting significant capacity constraints across procurement, cold chain, and physical and human resources, as well as the urgency of operational and financial planning. In the meantime, as of January 2021, while Israel has been leading the world in terms of per capita vaccinations, no one has been vaccinated in the Palestinian territories yet and the Israeli MOH has not formulated an allocation strategy, beyond providing 5,000 vaccines to Palestinian doctors. Humanitarian organizations in both Israel and West Bank and Gaza have called for Israel to reserve a higher amount of vaccines for the Palestinian territories. Given the challenges for the Palestinian Authority to procure vaccines, the statement calls for operational and financial support from Israel to PA.²⁶

50. *Financial constraints pertaining to COVID-19 response.* There are currently two response plans: one from the UN Health Cluster, and one from the Palestinian Local Aid Coordination Secretariat; both plans are underfunded. As of December 2020, 51 percent of the US\$29.5 million required for the UN Health Cluster's COVID-19 response plan is covered.²⁷ Identified gaps are particularly highest for the delivery of essential services, pertaining to activities for technical support with regards to supply and distribution planning; provision of essential health services, particularly for maternal, newborn, and child health services, and micronutrient supplies; provision of health services to marginalized groups and refugees; procurement of infection prevention control and personal protective equipment, including key infrastructure and ambulance inputs; strengthening the continuity of immunization programs; and supporting ongoing health system strengthening interventions through supporting health facilities and institutionalizing quality of care at health facilities. In addition, the PA's US\$113 million COVID-19 response plan covering personnel and equipment needs through October 2020 has faced significant funding challenges from the government's side, particularly with regards to the procurement of key medical equipment.²⁸
51. *Cross-border movements.* Points of entry to the Palestinian territories are controlled by the Israeli authorities. These controls not only have an impact on the flow of individuals, and thereby making quarantine and isolation difficult, but also on the speed with which key inputs needed to respond to the pandemic are allowed by Israeli authorities to leave their airports and ports for urgent transport into the Palestinian territories. As of January 2021, movement restrictions are prohibiting international NGO staff from entering Israel due to movement restrictions and lockdowns there, which has negative implications for continued delivery of essential services in West Bank and Gaza.²⁹
52. *Procurement and clearance of key inputs due to suspended coordination and financing gaps:* Although there were no issues with regards to procurement and customs at the beginning of the pandemic, clearance of humanitarian shipments, including essential health inputs, were delayed

²⁴ Estimates based on Gavi/COVAX documentation as of December 2020

²⁵ Palestine has received 2,000 doses of Moderna (from Israel) and 10,000 doses of Sputnik V vaccine as of February 4, 2021.

²⁶ Joint Statement 10: Israeli, Palestinian and international health and human rights organizations: Israel must provide necessary vaccines to Palestinian health care systems <https://reliefweb.int/report/occupied-palestinian-territory/joint-statement-10-israeli-palestinian-and-international>

²⁷ United Nations Office for the Coordination of Humanitarian Affairs, COVID-19 Emergency Situation Report 19 (22 September – 5 October 2020) <https://www.ochaopt.org/content/covid-19-emergency-situation-report-19>

²⁸ Plan by Local Aid Coordination Secretariat and the Ministry of Health

²⁹ United Nations Office for the Coordination of Humanitarian Affairs, COVID-19 Emergency Situation Report 25 (17-30 December 2020) <https://www.ochaopt.org/content/covid-19-emergency-situation-report-25>

considerably following the suspension of coordination between the PA and Israel, despite efforts by the Humanitarian Coordinator and key partners, between May – November 2020.³⁰ Even though coordination issues have been resolved, there is still a shortage of over 1 million gloves, 1.6 million surgical masks, 30 ventilators, 84 ICU beds, and 319,136 PCR tests.³¹ While a Logistics Cluster has been activated by the UN consisting of development partners, clearance processes remain slow and dependent on Israeli authorities.

53. *Limitations in health workforce and physical resource capacity:* There are important limitations in human resources to respond to COVID-19 and ensure continuity of essential services. 81 health workers have already been infected with COVID-19 and there is a significant shortage of health workers across the board, which also impacts case detection and management. Specifically, there are shortages of specialized medical staff (i.e., intensive care specialists, anesthesiologists, specialized nurses) and related ancillary services. In addition to human resources, there are also physical resource capacity shortages, and certain areas such as Nablus face challenges in hospital capacity to respond to the surge in cases as well as to continue delivering essential services.

5. Impact of COVID-19 on the health system and other essential health services

54. **As COVID-19 evolves from an emergency into a prolonged pandemic, it remains more essential than ever to monitor its impact on other health system functions.** As is the case with other impacted countries, COVID-19 has significantly disrupted health system financing and service delivery for other essential health services, such as maternal, newborn, and child health, and non-communicable diseases. Coupled with the suspension of coordination with Israel, essential health services face significant continuity challenges in the West Bank and Gaza.

55. **The fiscal situation is expected to remain extremely difficult through 2021 (as explained in chapter 1), and the economy is expected to shrink.** This will have a definite impact on the health sector. Latest available figures point to only about a third of the US\$280 per person spent on health being financed by the PA, demonstrating an already limited fiscal space for health. Against this, the needs of the Palestinian health system have been increasing dramatically, given the second and the ongoing third wave of COVID-19 and the prolonged impact on the health system.

56. **COVID-19 has weighed heavily on the health budget.** While the Ministry of Health budget for 2020 was planned to be at NIS2.39 billion (US\$700.8 million), the budget has decreased by more than a quarter to NIS1.88 billion (US\$527.8 million) due to the adverse fiscal impact of COVID-19, as well as the suspension of coordination with Israel.³² In addition, significant amounts of the existing health budget are being allocated to COVID-19-specific expenditures of commodity procurement and infrastructure investments, constraining the delivery of other essential services. Due to this reduction, as well as the prolonged fiscal uncertainty, the operating budget of the MoH that covers medicines, consumables, and salaries has been negatively impacted. All public sector staff, including MoH staff, received 50 percent of their salary for May and June, and the cuts continued until the end of 2020. The European Union and other donors provided a certain share of salaries, staffing and funding gaps remain.

57. **While efforts have been made by development partners and NGOs to maintain maternal and child health services, there remain significant gaps due to the weak baseline capacity of the health system, and reallocation of limited resources to respond to the pandemic.** Baseline physical and human resources were limited in the West Bank and Gaza prior to COVID-19, and due to the redistribution of scarce health system resources toward the COVID-19 response, other

³⁰ This is due to the disruption in the transfer of tax and customs documentations needed for the import of supplies from the Palestinian Authority to the Israeli authorities.

³¹ United Nations Office for the Coordination of Humanitarian Affairs, COVID-19 Emergency Situation Report 25 (17-30 December 2020) <https://www.ochaopt.org/content/covid-19-emergency-situation-report-25>

³² Figures provided by the Palestinian Ministry of Health, July 28, 2020

essential services have been impacted negatively. Many health facilities have been closed: in Gaza, 20 primary health care centers have closed and the staff reassigned to manage quarantine and respiratory triage centers, exacerbating the already limited access to care, and the centers that are open are only providing essential services such as dispensing chronic medicines.

- 58. Services are also interrupted in primary health facilities that are open.** Since the beginning of the pandemic, primary health care clinics around the West Bank and Gaza have only been open one day a week, although recently efforts have been taken to increase it to two days a week. About 50 percent of primary healthcare staff have been reassigned to support the COVID-19 response. In Hebron, several physicians working in hospitals and primary health care centers had to be reallocated temporarily to help manage and contain the ongoing surge of COVID-19 in the region, which meant that the MoH had to temporarily contract physicians to cover the posts left by the reallocated medical staff. Outreach for maternal, newborn, and child health services has also been paused with the intention of curbing the spread of COVID-19. Essential medicine shortages continue to be a challenge, particularly in Gaza, where 47 percent of essential medicines have less than a 1-month supply and 42 percent are fully stocked out as of September 2020.³³
- 59. Across the board, the availability of qualified human resources for health and lack of physical resources continue to be of concern.** Despite recent efforts, gaps in key cadres such as ICU attendants, anesthetists, internists, radiologists, specialized nurses, and lab technicians continue to be a problem. Immunization services particularly remain at risk, resulting in almost 700,000 children under threat of vaccine-preventable diseases: even after recent resource mobilization, there remains a gap of US\$2 million associated with the procurement of vaccines (about a third of the total annual routine vaccine needs). In addition, funding gaps remain for renewal of refrigerators and the expansion of cold room capacities, demonstrating a significant bottleneck not only for routine immunization but also the upcoming introduction of COVID-19 vaccines when they become available.³⁴ Contributions by partners have resulted in the provision of pediatric chemotherapy, dialysis, respiratory illness treatment, and anemia treatment, as well as provision of essential primary healthcare services and home visits. Health cluster members noted interruptions in activities to prevent gender-based violence and deliver child protection services, as well as to deliver mental health and psychosocial support to impacted populations.³⁵
- 60. Due to limited specialized treatments at the MoH facilities in the West Bank and Gaza, patients are regularly referred for diagnostic and therapeutic interventions to health facilities in East Jerusalem, Israel, Jordan, and Egypt; this has been significantly disrupted due to COVID-19 and the suspension of coordination.** Outside medical referrals (OMR) are an integral part of the Palestinian health system due to the lack of specialized services in secondary and tertiary facilities operated by the MoH, particularly in Gaza. Between 2017-2019, an average of about 53,000 patients a year were referred to health facilities outside the administration of the MoH, mainly in East Jerusalem, Israel, Jordan, and Egypt, for treatment of specialized conditions such as cancers, kidney diseases, heart diseases, and neurological conditions.³⁶ The first direct impact of the suspension of coordination on OMR was the inability of Palestinian residents, particularly those in Gaza, to obtain the necessary exit permits to seek treatment. Due to the suspension of processing of exit permits, as well as reductions in care-seeking due to COVID-19 and associated quarantine policies,³⁷ monthly referral applications from Gaza declined from about 2,500 to 150; a WHO report on movement and access of patients from June 2020 highlights that only about five people a day in a very serious condition were permitted to leave, with Augusta Victoria Hospital in East Jerusalem

³³ WHO COVID-19 situation report 47, October 8, 2020

³⁴ Information obtained from UNICEF, 7/29/2020

³⁵ United Nations Office for the Coordination of Humanitarian Affairs, COVID-19 Emergency Situation Report 14 (15-28 July 2020) <https://www.ochaopt.org/content/COVID-19-emergency-situation-report-14>

³⁶ Data from Palestinian Ministry of Health, Services Purchasing Unit

³⁷ All patients from Gaza must be under quarantine for three weeks once they re-enter Gaza, and as such, patients need to stay in the West Bank to complete treatment, which poses further accessibility challenges.

alone having seen a 50 percent decline in referrals.³⁸ A significant number of patients are currently awaiting treatment, particularly for cancer.³⁹ While referrals from West Bank have recovered to their pre-COVID levels, referrals from Gaza remain low, indicating the higher impact of movement restrictions and coordination issues on those residing in Gaza. 27 percent of referral applications were delayed in November 2020, highlighting that even for those who can obtain a referral, obtaining timely care remains an important bottleneck.⁴⁰

61. COVID-19 has also had an impact on OMR through the change in the composition of referred cases. Given the designation of various Palestinian hospitals as exclusive COVID-19 facilities, various cases that would normally not be referred, such as certain maternal health services, have also had to be referred to facilities outside the MoH. In addition, certain cases had to be referred to costlier private facilities within the same governorate, due to the closure of other facilities as well as increased movement restrictions. COVID-19 and the suspension of coordination between Israel and the PA also resulted in a significant reduction of referrals to Israel, which only continue for lifesaving conditions, such as for bone marrow transplants, which are only available in Israel for Palestinian patients due to the closure of the border with Jordan. In the absence of official and institutional referral application and coordination mechanisms due to the suspension of bilateral agreements, these referrals have been taking place through the mediation of international humanitarian organizations or Palestinian individuals with Israeli identification cards. While recent steps have been taken to improve billing practices with Israeli hospitals for OMR, these measures were suspended due to the suspension of coordination, resulting in even more constrained fiscal resources. For example, the Hadassah Ein Karem hospital in Israel has returned NIS7.5 million (US\$2.19 million) less than the amount agreed with the Palestinian MoH.

6. Recommendations

62. Improved coordination between the West Bank and Gaza, as well as between the PA and Israel, would serve as a regional public good in combatting COVID-19 and ensuring continuity of essential health services. Control of COVID-19 in the West Bank and Gaza will benefit Israel, and vice versa, given the significant amount of cross-border movements. Even though coordination has resumed as of November 2020, the pre-existing challenges in terms of border controls and fiscal autonomy remain and continue to have a significant negative impact on the health sector. In addition, significant steps must be taken to allow for the procurement of lifesaving medical supplies.

63. Coordination is essential for the administration of the COVID-19 vaccine, which Israel has already deployed. Vaccination is a global public good, and it is in the benefit of both parties to ensure high vaccine coverage rates across the Palestinian territories and in Israel. As of January 2021, there is no coordination between Israel and PA regarding the deployment of the COVID-19 vaccine, even as Israel has made significant progress with vaccinating its priority populations. In order to ensure there is an effective vaccination campaign, Palestinian and Israeli authorities should coordinate in the financing, purchase and distribution of safe and effective COVID-19 vaccines. From a humanitarian perspective, Israel can consider donating the extra doses it has ordered that it

³⁸ “For Some Palestinians, Cutting of Cooperation with Israel Means No Medical Treatment” Haaretz, June 9, 2020 <https://www.haaretz.com/middle-east-news/palestinians/.premium-cooperation-cutoff-leaves-hundreds-of-palestinians-with-no-medical-treatment-1.8906090> & “COVID-19 and the Absence of Israeli-Palestinian Coordination Spell Grim Fate for Gaza Cancer Patients” Haaretz, July 24, 2020 <https://www.haaretz.com/israel-news/.premium.MAGAZINE-COVID-19-and-no-israeli-palestinian-coordination-spell-grim-fate-for-sick-gazans-1.9017948>

³⁹ According to the WHO from June, from January to May 2020, 67 percent of exit applicants have been successful, but this figure is expected to decline significantly as coordination has been suspended since the of end May. In May, only 160 patient permit applications were submitted from Gaza, with 41 percent for cancer patients and 49 percent for hospitals in East Jerusalem. 1,525 patients applied from the West Bank, with a 59 percent approval rate.

⁴⁰ Monthly Report on Referral Access: November 2020 http://www.emro.who.int/images/stories/palestine/documents/WHO_Nov_2020_Monthly_Report.pdf?ua=1

would not be using; it could also consider procuring vaccines for priority health workers and most vulnerable populations in West Bank and Gaza. From a technical perspective, it is critical that both PA and Israel share information on the comprehensive readiness assessment for launching and progressive expansion of the COVID-19 vaccination plans, as this impacts the success of vaccination efforts for both Palestinian and Israeli populations. Coordination for financing and procurement will be essential in ensuring equitable vaccine coverage and sustained immunity towards COVID-19 in both Palestinian territories and Israel.

- 64. From a humanitarian and public health perspective, it is essential to facilitate the procurement and movement of health commodities between Israeli ports, the West Bank, and Gaza.** Disruption of health inputs is costing lives in both the West Bank and Gaza. While the United Nations Logistics Cluster has been making progress in clearing shipments, this must be institutionalized, and coordination must resume, as control of COVID-19 in the West Bank and Gaza will also benefit Israel. Coordination in movement of commodities is particularly crucial as the PA finalizes its COVID-19 vaccine deployment plans.
- 65. Establishment of a Public Health Emergency Operations Center, as well as capacitating local authorities, is crucial in facilitating internal and external coordination.** Establishing a PHEOC, which has full capacity to communicate and coordinate with all partners, collect, collate, and analyze epidemiological and routine health service data, deploy resources including surge capacity and other needed inputs, and prepare communications and coordinate with all needed stakeholders, can centralize data management for informed decision-making: there is currently a proposal from the WHO to fully operationalize a PHEOC. This is a key step in ensuring an effective response and would assist not only in ensuring effective COVID-19 control but also continuity of essential services, both internally between the West Bank and Gaza, as well as externally, ensuring data sharing between the GoI and the PA. The PHEOC can serve as an effective body of coordination between the two entities. To ensure the PHEOC functions effectively in responding to local needs, it is also very important to ensure that PHEOC empowers and works closely with decentralized, local entities in deciding on key measures pertaining to infection prevention and control, while ensuring harmonization between plans.
- 66. Scaled-up testing, tracing, and quarantining, as well as surged case management capacity will be essential to curb the current wave of COVID-19.** The West Bank and Gaza succeeded early in the pandemic due to its focus on testing, tracking, tracing and isolation measures to break the chain of transmission and to control the outbreak. Physical and human resources constitute the main bottleneck to testing and quarantining. Financing flows for COVID-19 management should prioritize these areas to ensure rapid control of the current wave. In addition, it is crucial to ensure that testing is managed and executed in a decentralized way, with more laboratories capacitated to readily process results. Finally, given the surge in infections and the limited health system capacity, it is crucial to ensure increased human resources and infrastructure.
- 67. To ensure that previous progress made with outside medical referrals is not jeopardized, processes must be institutionalized both in terms of the processing of referral permits, as well as continued coordination between Palestinian and Israeli medical providers.** Even as most referrals are to facilities within the jurisdiction of the PA, obtaining exit permits has proven to be very difficult, and patients continue to rely on Israeli facilities for lifesaving processes. As such, coordination is required among all stakeholders, both for direct referrals as well as for coordinating exit permits to providers in East Jerusalem, Jordan, and Egypt.
- 68. Donors can help mitigate the current challenges that the health sector in the West Bank and Gaza face with increased investment in the health system to control COVID-19 and continue delivering essential services.** The PA has lost a significant amount of revenue, which has constrained its ability to spend on critically needed health inputs, as evident in the significant financing gaps for COVID-19 case management, essential service continuity, and COVID-19 vaccine introduction. To ensure effective support and coordination, the Health Cluster and other

partners would need to provide support, particularly to ensure the poor and vulnerable, including those in Gaza, are targeted. Additional and well-targeted financing is critical for ensuring essential services that have already been disrupted can continue, including OMR. In addition, this financing should be used to introduce flexible service delivery modalities, such as mobile medical units or community health workers, to ensure that maternal, newborn, and child health services, immunizations, and other chronic and infectious diseases are addressed rapidly. To enable this, the PA and development partners within the Health Cluster should work on a costed implementation plan for the COVID-19 response and essential service continuity; further, this plan should be regularly updated with available resources and gaps. Improving the capacity of the Palestinian health system remains a priority for all stakeholders in the sector.

Annex I: Stocktaking of World Bank recommendations to the AHLC meetings over the years

69. The Palestinian economic outlook is worrying, and bold actions are needed from all parties to get the Palestinian economy out of its deteriorating trajectory. Several necessary actions have been identified in previous reports by the World Bank to the AHLC meeting, but implementation has been limited. In the World Bank's September 2016 report to the AHLC, a stocktaking of all previous World Bank recommendations to the meeting was conducted. This exercise was intended to provide a baseline for evaluating progress in achieving the Palestinian territories' development priorities. In addition, it was expected to galvanize the reform efforts of all parties to address the immediate need while setting in place reforms that will deliver over time. In this report, the stocktaking is updated to show progress since June 2020 using the same three pillars: (1) fiscal sustainability, (2) economic development, and (3) Gaza reconstruction and recovery.

A. Fiscal Sustainability

70. The current COVID-19 outbreak makes it difficult for the PA to embark on challenging expenditure reforms, but once the crisis eases the PA needs to start addressing several long-standing areas of ineffective expenditure for long-term fiscal sustainability. In particular, they need to adopt a comprehensive plan for civil service reform that looks at inefficiencies and overstaffing – especially in the West Bank. Parametric reforms are also needed to support the public pension system's sustainability. Progress has been made on steps to control electricity net lending – although the problem is increasing with other utility payments, mainly water and sewerage. The net lending situation for the water sector continues to face challenges: i) net lending for water and sanitation is at NIS35 million per month; ii) Israel charges the Palestinian Ministry of Finance NIS110 million per year to treat the transboundary wastewater. There is no agreement on accounting principles for these costs; and iii) service providers continue to accumulate debt, which has increased due to COVID-19. A national committee was formed to agree with service providers on settling the accumulated debts, but progress is slow. All stakeholders need to agree on a new mechanism to ringfence water revenues and increase payments of bulk water purchases from the Israel water utility Mekorot. Outside medical referrals (OMR) also represent an ongoing fiscal burden for the PA, but steps have been taken to control this category of spending including introducing a digitalized system to monitor OMRs and linking this e-referral system to the MoF's Integrated Financial Management Information System (IFMIS) which will enhance transparency regarding OMRs and allow for better financial planning.

71. Domestic revenue collections dropped in 2020 due to the COVID-19 crisis, but away from this shock comprehensive efforts are still needed to bring revenues close to their potential. Despite strong performance in 2018 due to administrative measures introduced to widen the tax base, the PA's revenues declined in 2019 as a result of the impact that the clearance revenue standoff had on economic activity, and hence tax collection. The pandemic has also weighed heavily on revenue generation as economic activity slowed down in 2020. However, tax avoidance is still widespread, particularly among high earning professionals, and the PA needs to focus efforts on this group of taxpayers. Encouragingly, the MoF has recently prepared a three-year revenue strategy (2021-2023) that focuses on tax administration and improving compliance. Progress has also been made on updating public fees and charges with a notable decision to increase the license fee for petrol stations. Further, the PA and the Government of Jordan have agreed to further cooperation on customs through electronically linking their customs systems, which is expected to significantly reduce smuggling. These efforts have recently slowed due to COVID-19 but are expected to pick up again as the crisis eases.

- 72. Payments made by the GoI in 2020 to the PA to offset fiscal leakages, and prior to the suspension of clearance revenue transfers, have been encouraging, but a more systematic approach to fully eliminate these losses is yet to be adopted.** Efforts should focus on implementing existing agreements that provide for full information sharing on trade that takes place between both parties, including Israeli sales to Gaza. The parties could also reach an agreement regarding the sharing of Allenby bridge exit fees. Talks have been under way for some time between the GoI and the PA to initiate the introduction of bonded warehouses for Palestinian imports and the transfer of some customs authority to the PA over the coming years. Even though there were encouraging talks about exempting fuel taxes from the clearance process, this did not materialize as these taxes are still collected by the GoI and then transferred to the PA after deducting a 3 percent handling fee.
- 73. The PA is continuing to make progress on improving the public financial management (PFM) system.** The PA has a comprehensive PFM strategy, which has been updated to incorporate the findings of the latest Public Expenditure and Financial Accountability (PEFA) assessment. A World Bank-funded project is providing support with a focus on budget execution, financial accountability, and procurement. A highlight is the catch up on implementation of the procurement law with the Higher Council for Public Procurement Policy now resourced, the single procurement portal operational, new standard bidding documents approved by the Council of Ministers, a capacity-building program of the procurement workforce launched, and the operationalization of the complaint mechanism under way. Progress has also been made on addressing the major delays in the production and audit of financial statements. The 2014 and 2015 audits were published in November 2019, and the 2016 and 2017 financial statement audits were finalized in December 2020 by the State Audit and Administrative Control Bureau. In line with the PFM strategy, support continues on the commitment control system (CCS). While some ministries have already implemented a CCS under a pilot program, the project supported expansion for all ministries to implement a CCS. The project is also supporting the modernization of financial control, intergovernmental fiscal transfers, and improvement of payroll management. New procedures were introduced to ensure that all health referrals are reflected in the financial management information system in a timely manner. A FCDO-funded PFM project continues to focus on budget management, revenue administration, and improving the policy development/planning processes led from the Prime Minister's Office.
- 74. Budget support from donors has significantly declined in recent years and funds remain insufficient to close the large financing gap.** As a share of GDP, aid to the budget fell from 27 percent in 2008 to below 4 percent in 2019 and has further dropped to 3 percent in 2020.

B. Economic Development

- 75. The constraints on movement, access, and trade continue to be the main impediment to economic growth in the Palestinian territories.** Area C remains key to Palestinian economic development but access to this area for Palestinian economic activity remains severely limited. Further progress has been made on the piloting of door-to-door transport through the West Bank crossings, with the initial Hebron pilot being extended to Nablus and Qalqilia regions, however the current scope of this activity remains limited and the situation has become more complicated with the suspension of coordination between the GoI and the PA. There had been some easing on the movement of people in and out of Gaza, but this is no longer the case. The long list of dual-use items key for the development of the economy and whose access is restricted has been updated but not significantly eased. With time, and as more incentives are put in place to promote compliance, access to dual-use items should be based on a risk-based criterion rather than a blanket approach. For instance, all Palestinian businesses that have established a strong track record of their ability to safely and securely handle hazardous materials and dual-use goods should be granted access to these goods without the need for cumbersome licensing procedures. Encouragingly, the GoI granted one-off permits for certain items in early 2020, particularly in Gaza.

- 76. At a domestic level, the PA has initiated steps to reduce the cost of doing business and improve the business climate, but these have yet to be fully implemented.** The Ministry of National Economy is working on finalizing a new draft of the Companies Law. Similarly, a draft competition law has been prepared and the draft is in the consultation process before final approval by the Cabinet. With support from the World Bank, the PA has also updated the Law of Crafts and Industries of 1953 to facilitate municipal business licensing through simplifying the approval process and reducing the cost. The amendments took effect from January 1, 2019 and the focus is now on removing administrative obstacles to faster processing of municipal business licenses. To establish strategic and policy oversight of institutions in land administration, in November 2018 the Cabinet of the previous administration adopted a draft Amendment to the Palestinian Land Authority (PLA) Laws. The amendment calls for the establishment of a Board of Directors that would oversee the operations of the PLA and would facilitate increased transparency in the land sector in line with the ongoing reform process. The legal amendment remains pending for ratification by the executive branch. It was scheduled for review in Q4 2020 by the current Cabinet before resubmission to the President. However due to the pandemic, the process has been delayed. Land registration is proceeding in the West Bank under the mandate and direction of the Land Water Settlement Commission (LWSC) in cooperation with local government units (LGUs). However, the registration activities continue to be hampered by the pandemic, experiencing delays as a result of the corresponding closures and travel restrictions within the West Bank. In addition to national closures there have been numerous localized closures at the land agencies from COVID-19 outbreaks among the staff.
- 77. Progress in the energy sector has slowed down due to COVID-19.** The interim Power Purchase Arrangement (PPA) between the GoI and the PA continues to be implemented. Based on this agreement, the Palestinian Electricity Transmission Company (PETL) is supplying electricity from the Israeli Electricity Company (IEC) through Jenin substation to Northern and Tubas Distribution Companies (NEDCO and TEDCO). The same infrastructure is also allowing PETL to provide solar energy, supplied by two independent power producers (IPPs) in the Northern West Bank. PETL has a good payment record under the interim and solar PPAs. Building on the Jenin interim PPA, similar agreements have been signed enabling the remaining three high-voltage substations to be energized. This was crucial to alleviate supply constraints being seen across the West Bank. The December 2019 settlement of JDECO debt had opened the door for improved management of the existing debt and elevated the urgent need for the PA and JDECO actions to reduce further accumulation of debt. The Palestinian Energy and Natural Resources Authority (PENRA) is implementing reform measures that are starting to improve collection and payment-related performance. However, the pandemic and economic slowdown has resulted in reduced financial flows across the energy supply chain, which is affecting all energy sector institutions. In particular, revenue collections in areas served by municipalities and village councils has seen a sharp reduction. A Revenue Protection Program, along with updated management information systems, is being rolled out to the distribution companies in the West Bank. Improvements in the sector continue to be hampered by a lack of progress in other areas - particularly those related to electricity infrastructure in Area C. Diversification of electricity supply from neighboring countries and distribution grid reinforcements are needed to enable stable supply but are hindered primarily by land access issues. Construction restrictions in Area C are major obstacles to strengthening the energy supply and sustainability through renewable IPPs and interconnections. The need for a comprehensive energy action plan for Gaza to enable increased supply, improved operations, and institutional reforms remains urgent. The ongoing institutional review and audit of energy sector finances in Gaza is a welcome development and is a priority in addressing the energy crisis in Gaza and its fiscal impact.

C. Gaza Reconstruction and Recovery

- 78. Most physical damage after the last Gaza war has been fixed, except for housing, but recovery needs remain significant and the shortfall of donor funds is a critical obstacle.** Good progress has been made in most sectors, with physical damage repaired. However, not all the fully damaged houses have been replaced and recovery needs that go beyond physical destruction remain

significant. Inadequate donor funding is a critical constraint to completion of housing reconstruction. There has been progress in accelerating materials entry through the Gaza Reconstruction Mechanism, particularly cement, but some materials remain in short supply and delays in approval and delivery prevail, particularly for more complex infrastructure projects.

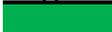
- 79. Efforts to support Gaza municipalities to expand local services provision through labor-intensive operation and maintenance are being scaled up.** The reduced transfers to Gaza are impacting the deteriorating municipal service provision as municipalities are unable to pay staff salaries. Maintaining the municipal infrastructure is key to expanding economic activity and improving productivity – fundamental requirements for job creation. Additionally, creating employment to mitigate the livelihood impacts of the liquidity squeeze in Gaza will help avoid escalation of instability in the strip.

Table 5: Summary of World Bank Recommendations to AHLC meetings

Actions	Responsible Party	Progress as of Sept 2016	Progress as of October 27 th , 2020
<u>FISCAL SUSTAINABILITY</u>			
Expenditures			
Control the oversized wage bill	PA	Red	Yellow
Control medical referrals to Israel	PA	Green	Green
Control medical referrals to local facilities	PA	Red	Yellow
Implement administrative reforms for the pension system	PA	Green	Green
Implement parametric reforms to restore the pension system's sustainability	PA	Red	Red
Reduce the size of net lending	PA	Yellow	Red
Revenues			
Enhance the PA's tax effectiveness in Gaza	PA	Red	Red
Increase the number of registered large taxpayers	PA	Yellow	Yellow
Strengthen legislation to penalize non-compliant taxpayers	PA	Red	Red
Revise government fees and charges upwards	PA	Red	Red
Transfer to the PA fiscal losses accumulated over the years	GoI	Yellow	Yellow
Implement institutional measures to reduce fiscal losses on clearance revenues	PA and GoI	Red	Red
Public Financial Management			
Improve budget preparation procedures	PA	Yellow	Yellow
Align budget execution with available resources	PA	Yellow	Yellow
Clear the backlog of outstanding financial statements	PA	White	White
- 2012-2015		Green	Green
- 2016-2018		Yellow	Yellow
Develop systems for monitoring and reporting expenditure arrears	PA	Green	Yellow
Budget support			
Provide sizable, predictable, and timely support to the PA's budget	Donors	Yellow	Red
<u>ECONOMIC DEVELOPMENT</u>			
Area C			
Expand spatial plans for Palestinian villages in Area C	GoI	Red	Red
Increase number of building permits approved in Area C	GoI	Red	Red
Grant approval to Palestinian business projects in Area C	GoI	Red	Red
The Gaza economy			
Allow exports out of Gaza to reach pre-2007 level	GoI	Red	Red
Significantly reduce items on restricted dual-use list for Gaza	GoI	Red	Red
Create a unified legal system in the West Bank and Gaza	PA	Red	Red
The business climate			
Adopt the Secured Transactions Law & establish a movable asset registry	PA	Green	Green
Adopt the new Companies Law & the Competition Law	PA	Red	Yellow
Accelerate land registration in Areas A and B	PA	Red	Yellow
Improve access to finance for SMEs	PA	Yellow	Yellow

Actions	Responsible Party	Progress as of Sept 2016	Progress as of October 27th, 2020
Reform the education system to bridge gap between graduates' skills and labor market needs	PA	Yellow	Yellow
Securing energy for development Sign an interim PPA to energize the Jenin substation PETL operating on commercial basis Diversify electricity supply	GoI and PA PA GoI and PA	Red	Green Yellow
Access to dual-use items Make the process to import dual-use goods more transparent Allow access to potent fertilizers in the West Bank Facilitate access to machinery in the West Bank Adopt a risk-based approach in the West Bank and Gaza to control dual-use items Meet international standards for controlling and regulating dual-use goods	GoI GoI GoI GoI and PA	Red	Yellow Red
<u>GAZA RECONSTRUCTION AND RECOVERY</u> Complete a DNA to guide reconstruction and recovery Establish and monitor timeline indicators for review and approval of dual-use items Include delivery monitoring in GRM system Establish Gaza import mechanism able to handle long-term recovery needs <u>Gaza Development</u> ⁴¹	PA GoI GoI and PA GoI and PA	Green Red	Green Red
Streamline trade procedures at commercial crossing and expand capacity Expand Gaza's fishing zone Implement donor-financed labor-intensive projects	GoI GoI PA, GoI, donors	Red	Red

Legend

-  On track
-  Some progress achieved
-  No progress

⁴¹ These are additional recommendations that were made in the World Bank's March 2018 report to the AHLC.