Palestine's looming socio-economic danger:
From Washington politics to the Washington Consensus

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1. Introduction

Just as unconstructive as Washington-centric Middle Eastern politics, two April 2011 reports on Palestine economics by the Washington-based multilateral banks – the International Monetary Fund (IMF) and World Bank – reflect an overarching failure to grapple with Israel's malevolent power, and rely upon an incorrect assumption that political freedom and free markets are tightly aligned. The IMF and Bank studies downplay the region's fundamental problem, namely Israeli Occupation of both Palestinian territories (as well as economic oppression of Israeli Palestinians). In the two Bretton Woods Institution reports, only Israeli 'restrictions', 'barriers' and the Gaza 'blockade' are remarked upon, not the underdeveloping nature of the settler-colonial economy, ongoing land invasions for illegal settlements, systemic violence, nor the Israeli regime's propensity to sabotage any visible Palestinian progress. (Only at one point, in passing, does the IMF raise the matter of the inability of Palestinians to invest in "Area C", the largest share of West Bank land.) In turn this leaves the IMF and Bank to apply old-fashioned 'Washington Consensus' ('neoliberal') dogma to the West Bank and Gaza, attacking the living standards of poor Palestinians while promoting the same destructive free-market policies that also caused severe strife across the Middle East in recent months.

On 28 May in France, yet another World Bank and IMF attack on the economic integrity of the Middle East is anticipated, at G8 meetings at which US President Barack Obama anticipates uniting his May 19 Middle East policy speech with more concrete economic offers. It is vital to understand the ways the Bretton Woods Institutions have already locked Palestine into neoliberal development strategies, such as adoption of export-led growth, means-testing for social policy, electricity privatization and prepayment metering, pension 'reform' and civil service shrinkage. And it is vital to trace the ways these kinds of policies heightened tensions in three of the most important Arab Spring countries over the past year, something this report can merely hint at based on other IMF documentation that will be discussed in a longer statement in coming days.

The following pages first identify the main lines of argument within the two recent documents about Palestine. We start with the Bretton Woods Institutions' analytical scope and then consider the merits of the export-led economic growth strategy, neoliberal social policy advice, and pressure to shrink the civil service.

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[1] This report is part of a week of consultation in Gaza and the West Bank (16-22 May 2011) while based at TIDA-Gaza. The author also thanks the Rosa Luxemburg Foundation in Ramallah for covering expenses. Patrick Bond is director of the University of KwaZulu-Natal Centre for Civil Society (on sabbatical at University of California-Berkeley Department of Geography).

2. World Bank and IMF limited analytical scope

The World Bank's most recent report to the major Western donors, 'Building the Palestinian State: Sustaining Growth, Institutions, and Service Delivery',[2] begins with a familiar argument: "If the Palestinian Authority (PA) maintains its performance in institution-building and delivery of public services, it is well-positioned for the establishment of a state at any point in the near future."

A cut-and-paste version of this line was simultaneously presented in the IMF's 'Macroeconomic and Fiscal Framework for the West Bank and Gaza'[3] – "**IMF staff considers that the PA is now able to conduct the sound economic policies expected of a future well-functioning Palestinian state, given its solid track record in reforms and institution-building in the public finance and financial areas**" (original emphasis) – but with the added (and very unusual) flattery of praising a Washington financial bureaucrat who serves as the PA Prime Minister:

> **IMF staff considers that the PA is now able to conduct the sound economic policies expected of a future well-functioning Palestinian state, given its solid track record in reforms and institution-building in the public finance and financial areas... Following steady institutional reforms since 2007, the Palestine Monetary Authority (PMA) is now in a position to carry out the functions of a central bank...** The West Bank's strong performance since 2008 has been enabled by PM Fayyad government's sound economic management and reforms supported by donor aid, as well as some easing of Israeli internal barriers. Nevertheless, the West Bank's growth, which is estimated at 8 percent in 2010, is also bound to wane, especially with the PA's continued fiscal retrenchment and declining aid, without a strong stimulus from a further easing of Israeli restrictions. (original emphasis)

There is, here, no acknowledgement whatsoever of the recent reconciliation of Fatah and Hamas, the proposed 'technocratic government' anticipated to commence in June, or the proposed September announcement of statehood for Palestine currently consisting of the West Bank and Gaza (WB&G). Instead, the narrative seems to be the dangling of statehood endorsement from multilateral institutions (even though the United States and Israeli governments are expected to sabotage such an effort), based on continuing with several tendencies in existing PA practices, which the Bank repeatedly encourages in its report.

Gaza's recent governance, Palestinian refugees demanding right of return to Israel, and the struggle of Palestinian Israelis, all go unmentioned even though the numbers of people involved are a majority of the Palestinian people.

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[2] World Bank (2011), 'Building the Palestinian State: Sustaining Growth, Institutions, and Service Delivery', Economic Monitoring Report to the Ad Hoc Liaison Committee, Brussels and Washington, 13 April.

[3] International Monetary Fund (2011), 'Macroeconomic and Fiscal Framework for the West Bank and Gaza', Report to the Ad Hoc Liaison Committee, Brussels and Washington, 13 April.

So on the one hand, the Bank's grand ambition of helping 'build' a Palestinian state will lack some crucial foundations. On the other hand, the Bank immediately acknowledges one of the most obvious problems with the high (9 percent) Gross Domestic Product (GDP) rate recorded in 2010, which more generally casts doubt on Palestine's organic economic activity:

> **Growth does not, however, appear *sustainable*. It reflects recovery from the very low base reached during the second intifada and is still mainly confined to the non-tradable sector and primarily donor-driven… The economic growth observed in WB&G is arguably donor-driven, and sustainable growth remains hampered by Israeli restrictions on access to land, water, a range of raw materials, and export markets, to name a few.** (original emphasis)

As discussed in the Conclusion, Section 3, the Bank misses an opportunity to explore the unsustainable economic setting in environmental terms. The idea of sustainability appears limited to whether Palestine is as profoundly aid-dependent as it is now, but to its credit the Bank concedes that the high GDP growth is a function of donor support. In other words, removal of donor inflows that are at least 20 percent of GDP (perhaps far higher) would have a devastating impact on GDP, and hence it is impossible to judge whether there is any genuine organic growth occurring through the PA's adoption of Washington-friendly economic policies.

3. An export-oriented economy?

There are several ways to generate organic GDP growth, and they boil down to whether the emphasis in economic activity is internally oriented (to meet local needs through local production) or externally oriented (to meet world market opportunities).

The Bank has traditionally opposed the former, and for Palestine there is no exception, notwithstanding the Palistinian people's oft-remarked creativity in adapting to extreme economic strangulation at the hands of Israel. So it is no surprise that the Bank aims to increase Palestine's international trade as 'the basis' for its future economy:

> **In order to lay the basis for future sustainable economic growth, the PA stands to benefit from a focus on its trade regime and infrastructure as well as the readiness of its human capital.** Developing the legal, institutional, and physical infrastructure required to manage a sophisticated trade regime will take time and considerable resources, so it is important that the PA begin immediately…
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> As a small open economy, the future Palestinian state is likely to depend upon increasing trade and especially the export of high value added goods and services that exploit its comparative advantage arising from a workforce with low wages relative to its high level of education…
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> The Palestinian market's small size means that, without access to the world market, Palestinian producers will not be able to achieve minimum efficient scale. In addition, becoming competitive on the export market will force Palestinian

> producers to improve their productivity, thereby increasing employment, raising wages, and lowering poverty. Since 1967, trade in WB&G has been overwhelmingly oriented towards Israel. As of 2008, Israel accounted for nearly 89 percent of WB&G's exports and 81 percent of imports. The majority of exports were for low value added goods that required a minimal level of processing. In order to achieve sustainable growth, the WB&G economy must increase overall trade, expand trade beyond the Israeli market, and increase the value added in exports. To do this, an appropriate trade policy regime must be in place, including the necessary institutional, regulatory, and physical infrastructure that will facilitate trade.
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> **Globally speaking, the last 60 years have witnessed a significant drop in transportation costs, matched by a similar increase in international trade…** the PA needs to publicly establish goals and principles now so that investors in the private sector can begin to prepare and make investments that will prosper and not be untenable under the trade regime of a future state…
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> The policy must be set to facilitate trade, not to raise government revenues, redistribute resources, or favor one sector over another. Tariffs must be low and there should be no quantitative restrictions or other non- tariff barriers to trade. Given the vital importance of trade, the government of a future Palestinian state might consider eventually moving to a policy of free trade as Estonia, Hong Kong, and Singapore have done. Above all, trade policy must be transparent and not captured by special interest groups. Keeping it simple and anchored in international agreements, such as those of the World Trade Organization (WTO), will help the government resist pressure and should be a key part of the strategy. (original emphasis)

The Bank's supreme confidence in promoting export-led growth strategies is evident in the last paragraph's insistence on low tariffs and its prohibition of infant-industry protection and policy 'capture' by self-interested Palestinians (whether crony-capitalists or trade unionists or simply democrats). But the overweening focus on exports is disturbing not only because this was the core belief that left so many Resource Curse economies so maldeveloped in recent decades, but because there appear to be no studies by the Bank or allied institutions that bear out the cheap-labour comparative advantage argument. The Israeli economy's easy 1990s substitution of imported labour (both migrant and immigrant) for hundreds of thousands of Palestinians (allegedly with no adverse impact on the wage bill) is one indication of the need to reconsider this claim more carefully.

Moreover, there appear to be no World Bank Domestic Resource Cost studies about the economic merits of light industrial sectors in which Gaza retains a small semblance of manufacturing capacity: furniture and garments. The three agro-export examples typically invoked for Gaza – strawberries, carnations and cherry tomatoes – are hampered in the short/medium-term by Israel's stop-start-stop border controls (not to mention the Boycott Divestment Sanctions movement which aims to close Israeli ports) and in the longer-term by Europe's growing use of carbon taxation and ecological footprinting against long-distance agricultural and horticultural imports.

Instead, the World Bank acknowledges that organic economic activity currently faces a narrow range of options:

> The fastest growing sectors in WB&G included agriculture, and hotels and restaurants, which grew by 22.8 and 46.3 percent, respectively. Construction grew by an impressive 35 percent, and public administration and defense continued to expand, growing by 6.4 percent in 2010. By contrast, initial estimates indicate that manufacturing output fell by nearly 6 percent and it remains more than 10 percent below its 1999 level… Though firms in Gaza report that most needed inputs are now available, the increase in imports from Israel combined with the lack of exports appears to have led to a fall in manufacturing by nearly 4 percent.

This is economic growth paralleling the parasitical style of the US economy prior to the bubble crash of 2008, not the productive economy so desperately needed. Gaza's deindustrialization, for example, is usually estimated at 75 percent thanks Israel's Operation Cast Lead and the subsequent siege. And not only does Israel present itself as a terribly unfriendly trade partner, it was also a small and stagnant contributor to Palestinian trade, the Bank admits:

> Israel remains WB&G's largest trading partner, yet in the first three quarters of 2010, exports of goods and services to Israel were only about US$480 million in nominal terms. This is only 6 percent higher than in the same period in 2009 and nearly 22 percent lower than in 2008.

As for the potential for increased trade with emerging democracies in the region, or for taking advantage of the apparent destruction of the Cairo-TelAviv-Washington alliance? Not a word (see Section 2 for some reasons the Bretton Woods Institutions would be nervous). Trade is an unrealistic driver of growth if the Allenby crossing to Jordan, the potential routes north via Lebanon or Syria, direct access to Mediterranean Sea ports, the regional airport and indeed all Palestinian contact with the outside world aside from (still-policed) tunnels to Egypt, are all controlled by Israel.

In this regard, it is all too easy to declare not only that "The IMF is a toy of the United States to pursue its economic policy offshore" (as did Massachusetts Institute of Technology professor Rudiger Dornbusch in 1998),[4] but also its foreign policy. A direct link between what the Bretton Woods Institutions impose in Palestine (export-led growth) and what is good for Israel (Palestine's trade dependency) can be drawn from Dominique Strauss-Kahn, the disgraced IMF Managing Director who resigned on May 19. On April 28, Strauss-Kahn acknowledged to *Liberation* that he once publicly stated, "*se lever chaque matin en se demandant comment [il pourrait] être utile à Israël"* ("each morning I rise thinking what can I do to be of use to Israel").[5]

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[4] Cited in Doug Henwood (1999), 'Marxing up the Millennium', paper presented to the 'Marx at the Millennium' conference, University of Florida, 19 March.
[5] Guirale, A. (2011), "Oui, j'aime les femmes et alors", *Liberation,* 28 April, http://www.liberation.fr/politiques/01012337606-*oui-j-aime-les-femmes-et-alors*

4. Neoliberalising social policy

Wherever they go, both IMF and Bank intervene in state social policy in a manner that degrades the potential for generous, universal, dignity-enhancing, gender-equitable, rights-based welfare and basic services. This is also evident in the way the IMF understands the challenges a Palestinian state will face from an impoverished, restive citizenry:

> By 2009, a staggering 71 percent of the Gaza population benefited from at least one form of social assistance. The reliance on social assistance means that even those households that are currently above the poverty line remain highly vulnerable, i.e. at high risk of falling into poverty…
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> **Because of the need to fund development projects for which designated aid was not received, the PA was forced to increase bank borrowing and accumulate arrears at an unsustainable rate.** Net domestic bank financing increased by about US$84 million, with gross borrowing of US$200 million, so that at the end of 2010, total domestic debt stood at about US$840 million, which may be close to the PA's borrowing limits. In 2010, the PA paid close to US$23 million in arrears in net lending, but it accumulated another US$144 million in new arrears. While most of this was to the pension system, about US$50 million was in non-wage and development spending. (original emphasis)

The IMF solutions to these multiple problems are simple: impose a 'means tests' (to check incomes), privatize electricity with prepayment meters, dramatically reduce state subsidies and raise the retirement age:

> **To ensure steady progress toward fiscal sustainability and reduced reliance on recurrent budgetary aid in line with the medium-term fiscal targets, it is essential to step up the implementation of the key structural reforms as set out in the draft PNP:**
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> **Further streamline and better target social assistance.** In 2010, several cash assistance programs in the West Bank have been merged into one central program with a single payment modality, based on a proxy means test that more accurately identifies vulnerable households. The Ministry of Social Affairs will be regularly updating the database of targeted households to ensure that only those below the poverty line receive assistance. A key measure to be implemented by mid-2011 is the "lifeline electricity tariff", for households in the latter database, at which a "lifeline" amount of household electricity consumption is billed only at cost. This measure is especially important given the increase in prices as electricity distribution is commercialized.
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> **Phase out electricity subsidies (imposed on the MoF due to non-payment by municipalities of their electricity bills) by completing the transfer of electricity distribution from municipalities to commercial companies.** An important step taken in early 2010 was the transfer of electricity distribution from the municipality of Nablus to the Northern Electricity Distribution Company (NEDCO), and the installation of about 170,000 pre-paid meters to improve bills

> payment. An action plan was prepared in 2010 to complete the transfer of distribution from the remaining local governments in the northern West Bank region to NEDCO, with the regions of Qalqilya and Tulkarm to be covered by mid-2011. The transfer of distribution in the remainder of the West Bank to other private electricity companies is expected to be completed by end-2011. Progress in electricity sector reform has helped reduce electricity subsidies from 6 to 3 percent of GDP in 2009–10.
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> **Reform the public pension system**. An important step taken in July 2010 was the adoption of a comprehensive public pension reform action plan for 2010–12, in collaboration with the World Bank. The plan aims at restoring the viability of the pension system in several phases during 2010–12. The first phase, to be completed during 2011, consists of indexing pensions to the CPI, raising the retirement age from 60 to 62, and ensuring that pensions are paid only to those who have reached the minimum age and served the minimum number of years required by law. The remaining steps for 2012 include the elimination of lump sum payments at retirement…
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> [I]t is essential for the PA to step up the implementation of structural reforms, including electricity sector, pension, and civil service reforms. For 2011, it is particularly important for the PA to abide by the expenditure ceilings set in the 2011 budget to achieve the targeted reduction in the recurrent deficit from 16 to 13 percent of GDP, especially given the highly uncertain global environment and prospects for donor aid.

Even though some administrative tasks will dramatically increase as a result of this kind of social policy shrinkage (such as stigma-inducing means-testing), the IMF and Bank believe it is logical to also cut back the civil service, no matter that it is Palestine's main employer.

5. Civil service shrinkage?

The World Bank recognized the perilous situation in the dysfunctional labour market, with unemployment above 30 percent in Gaza alone:

> The current PA payroll is just over 150,000… In the fourth quarter of 2010, unemployment for WB&G was 23.4 percent, compared to 24.8 percent in the fourth quarter of 2009… the share of the government in total employment rose from 17 to 26 percent between 1999 and 2009, while that of private sector jobs fell from 47 to 38 percent… Israel and its settlements remains an important employer of Palestinian labor, employing nearly 79,000 Palestinians from the West Bank in the fourth quarter of 2010, up from about 72,000 in the fourth quarter of 2009.

Even in this context, the IMF endorsed shrinkage of the largest source of employment, given

> a sharp reduction in donor aid for recurrent spending, from $1.8 billion in 2008 to $1.2 billion in 2010, with a view to a further reduction to less than $1 billion in 2011… **The PA has pursued a tight fiscal stance in 2010, and continued to**

> **undertake structural reforms in line with the vision toward statehood… The draft Palestinian National Plan (PNP) for 2011–13 envisages a steady reduction in the recurrent budget deficit to about 4 percent of GDP by 2013…** The 2010 wage bill was about 4 percent higher than budgeted (or by about $63 million) partly reflecting adjustment of allowances to some categories of Employees… The number of public sector employees rose by 3,317 in 2010 (of which 452 in health, 1,762 in education, 362 in security, and 741 in other sectors).

That wage bill would now have to be cut, the IMF advised, because (usefully for Washington),

> **So far, in 2011, donor aid has fallen short of financing requirements.** During the first quarter of 2011, only about $0.2 billion has been disbursed, and another $0.5 billion was indicated by donors for the remainder of the year. Given the projected financing need of $967 million, this yields a financing gap of about $0.3 billion for 2011… Given the uncertainty regarding availability of financing for 2011, it is particularly important to avoid further increases in public sector wage rates beyond those given in January 2011. Any compensation for increases in food and energy prices should be targeted to the needy households using the social safety net, and offset by cuts in lower priority expenditure items.

How should this compression of wages be done, and how far should they be lowered (in relation to GDP)? The IMF answers:

> **Initiate civil service reform aimed at a steady decline in the wage bill and greater public sector efficiency**. So far, the authorities have relied on controls on wage rates and new employment to contain the growth of the wage bill. While this approach has yielded substantial budgetary savings, it will need to be complemented by additional measures to ensure long-run sustainability and increased efficiency in the delivery of public sector services, especially in view of the continued real erosion of average government wage rates. One important measure that should be implemented in 2011 is a careful review of personnel needs in key sectors, including health and education, to fine-tune the current “blanket ceiling” of 3,000 new employees that is automatically placed in annual budgets.
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> The average public real wage rate is estimated to have declined by a cumulative 6 percent during 2008–10, and is projected to rise by 1 percent in 2011…
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> While the share of the wage bill in GDP has declined in recent years due to limits on increases in wage rates and new employment, at 22 percent it is still significantly higher than the 10–15 percent that is typical of countries at a similar stage of development. Bold measures are needed toward a comprehensive civil service reform to reduce the wage bill while improving public sector efficiency. It will becomeincreasingly difficult to reduce the wage bill by relying on a “blanket” restraint on wage rates and new employment, especially as the average public sector wage rate has already declined significantly in real terms since end-2007. (original emphasis)

6. A tentative conclusion

The result of these multiple attacks by the IMF on Palestine is going to be substantially increased misery. The irony is that with Hamas in a strong position in Gaza (albeit probably moving ministers out of formal power soon so as to implement reconciliation with Fatah), its own impressive self-reliant strategies could infuse a spirit of resistance, just as tens of thousands of non-violent protesters marched against Israel's borders on May 15. These potentials are terribly important for generating alternatives that Palestinians can pursue, so as to evade the IMF and World Bank neoliberal traps. But that is a strategic matter that only Palestinians can properly deliberate.