

NOTE ON THE IMPACTS OF THE CONFLICT IN THE MIDDLE EAST ON THE PALESTINIAN ECONOMY

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SYNOPSIS

Since the beginning of the conflict in October 2023, hostilities in the Gaza Strip have resulted in massive loss of life.¹ The effects of the conflict on the Palestinian economy have been consequential as the loss of life, as well as the speed and extent of damages to fixed assets and reduction in production flows across the Palestinian territories are unparalleled.

The conflict is expected to leave lasting impacts on the affected populations in Israel, Gaza, and the West Bank, extending far beyond any economic assessment. According to United Nations sources, 40 percent of all fatalities involved in the current conflict in the Middle East are children under the age of 18. The conflict has exacerbated the pre-existing humanitarian crisis in Gaza and dramatically augmented the economic and development challenges both in the Strip and in the West Bank. About 1.7 million Palestinians living in Gaza (approximately 75 percent of the total population in Gaza) have been internally displaced, in some cases multiple times, and the Strip's entire population of 2.3 million is suffering from a shortage of food, water, electricity, fuel and medicine.

The observed level of fixed assets damage and destruction is catastrophic. The conflict has resulted in the destruction of tens of thousands of housing units, with over 1.2 million individuals cur-

rently without homes. The conflict has also had an impact on the health sector with only one third of Gaza's 36 hospitals even partially functional, while the rest have shut down due to damage and/or lack of electricity supply.²

Since the start of the conflict, the Palestinian economy experienced one of largest shocks recorded in recent economic history. In Gaza, GDP plummeted by more than 80 percent in Q4-2023—from approximately US\$670m in Q3 to roughly US\$90m in Q4. Almost all economic activity in Gaza has ground to a halt, with little indication of substantial improvement at the time of publication. According to initial estimates from the Palestinian Central Bureau of Statistics (PCBS), the GDP in Gaza saw a decline of over 80 percent in the fourth quarter (Q4) of 2023.³ and a drop of 24 percent for the whole year (2023). The private sector is estimated to have

¹ This note was written based on information available as of February 10, 2024.

² Source: OCHA's Flash Updates. Visited online at <https://www.unocha.org/publications/report/occupied-palestinian-territory/hostilities-gaza-strip-and-israel-flash-update-113>.

³ Source: PCBS, «The Performance of the Palestinian Economy during 2023 and the economic forecasts for 2024», January 2024 https://www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_ForecastingPCBSE.pdf.

facéd production losses totaling around US\$1.5 billion in the first two months of the conflict or roughly US\$25 million per day.⁴ The economic decline in the Palestinian territories already exceeds the impact of the conflicts in 2008, 2012, 2014, or 2021, and over the past two decades, it is behind only the second intifada in terms of impact.

The combination of preexisting high levels of poverty, widespread internal displacement, the destruction of homes, fixed assets, and productive capacity, coupled with a massive economic downturn, realistically means that nearly every resident of Gaza will live in poverty, at least in the short term.

Over the past four months, non-monetary welfare conditions, which are indicative of multidimensional poverty, have rapidly deteriorated. This is reflected in the disruptions to children’s access to education and in the colossal challenges preventing Gazans from obtaining essential health and other basic services. Every person currently in Gaza faces acute food insecurity, with at least one in four experiencing catastrophic hunger,⁵ with a growing risk of famine. Approximately three in four people are displaced.

Effectively managing a spiraling fiscal crisis remains a top priority for the Palestinian Authority (PA), especially given the knock-on effects of the conflict in the West Bank. A pre-existing structural fiscal crisis has been worsened by a reduction in clearance revenue transfers,⁶ starting in October 2023. This, together with the decrease in domestic revenues (reflecting lower economic activity) forced the PA to further reduce public salary payments in

the last quarter of 2023⁷, and made the 2023 financing gap grow approximately fivefold vis-a-vis the pre-conflict baseline, reaching 3.0 percent of GDP. In a context of no access to traditional economic policy instruments, the only alternative sources of financing remain additional accrual of arrears and foreign aid.

The outlook hinges largely on the conflict’s intensity and the level of restrictions. Should the intensity of the conflict remain high beyond the first months of 2024, or should the limits on the movement and access in the West Bank not be removed, the economic downturn could become even more pronounced. Additionally, a protracted absence or sharply reduced clearance revenues may prompt the PA to resort to extreme—and potentially disorderly—fiscal consolidation measures, resulting in further reductions of public salaries. This in turn, would exacerbate the decline in consumption and ultimately depress growth further with long-term adverse effects.

⁴ Ibid.

⁵ This refers to Level 5 of the Integrated Food Security Phase Classification scale (IPC)

⁶ “Clearance revenues” are revenues collected by the Government of Israel and transferred to the Palestinian Authority as agreed in the Paris Protocol. Most clearance revenues are VAT and import duties, and they should be remitted on a monthly basis. Clearance revenues represent roughly two thirds of the PA’s total fiscal income.

⁷ October 2023 salaries were paid at a rate of 50 percent. November salaries were paid at a rate of 65 percent and December salaries were paid at a rate of 60 percent.

ASSESSMENT

Since October 7, the Palestinian economy experienced one of the largest economic shocks ever recorded in recent economic history. In Gaza, specifically, GDP plummeted by over 80 percent in Q4-2023. All economic activity in Gaza virtually ground to a halt, with little indication of substantial improvement any time soon. According to initial estimates from the Palestinian Central Bureau of Statistics (PCBS), the GDP in Gaza saw a decline of over 80 percent in the fourth quarter (Q4) of 2023,⁸ and a drop of 24 percent for the whole year (2023). While the West Bank has not experienced massive destruction of fixed assets, its economy has been severely impacted by ripple effects from the conflict. Importantly, the combination of increased movement and access restrictions imposed by the Government of Israel (GoI) within the West Bank impeding workers from reaching their places of work and the cancellation of work permits for over 170,000 Palestinian workers,⁹ weighed heavily on demand in the West Bank. Further, a decline in trade and private sector activity, reduced incomes due to job losses, and temporary cuts in public salaries have all led to an estimated 22 percent contraction in the West Bank's GDP during Q4-2023, as reported by the PCBS, and a 2.5 percent contraction for the entire year 2023.

The hostilities have led to a catastrophic downturn, prompting a substantial downward

revision to the World Bank economic projections for the Palestinian economy. The World Bank's pre-conflict projection for the calendar year 2023 anticipated a 3.2 percent real GDP growth rate in the Palestinian territories. Our estimates have now been revised to a 6.4 percent contraction, attributing this change to the conflict and the overall deterioration in the West Bank. This revision implies an approximate loss of US\$2.5 billion in nominal GDP for the year 2023 alone. The economic decline in the Palestinian territories already exceeds the impact of the conflicts in 2008, 2012, 2014, or 2021, and over the past two decades, it is behind only the second intifada (2000–05) in terms of impact.

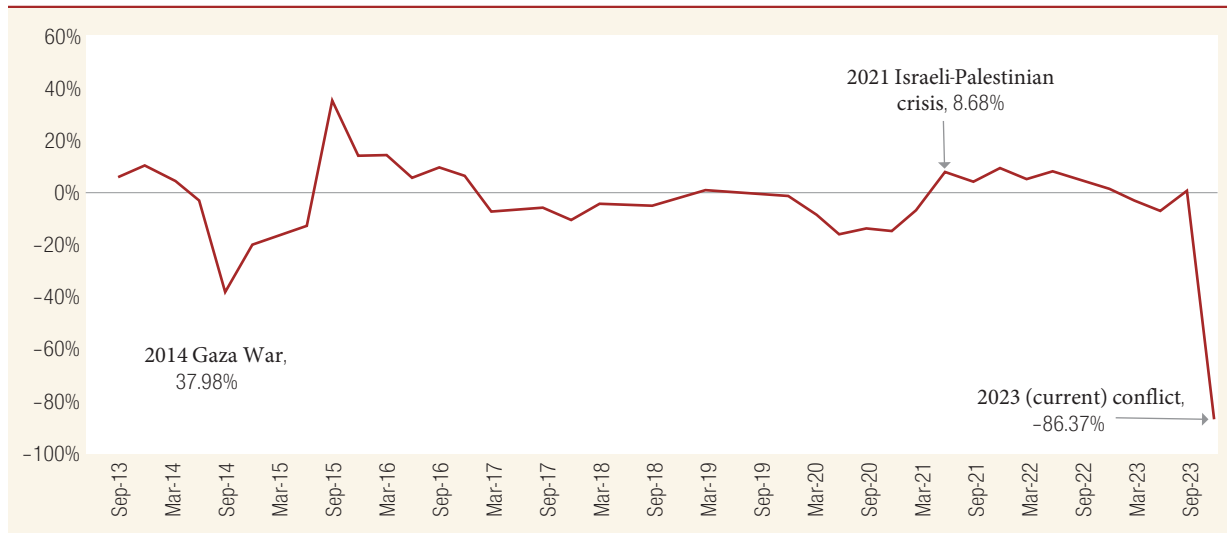
IPSOS data describe a dire situation in Gaza: the observed level of fixed asset damage and destruction is catastrophic. An estimated 1.2 million people are facing homelessness,¹⁰ and approximately 62 percent of residential buildings have incurred some form of damage. The UN

⁸ Source: PCBS «The Performance of the Palestinian Economy during 2023 and the economic forecasts for 2024», January 2024. https://www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_ForecastingPCBSE.pdf

⁹ Palestinian workers in Israel earn approximately three times more than the average West Bank wages.

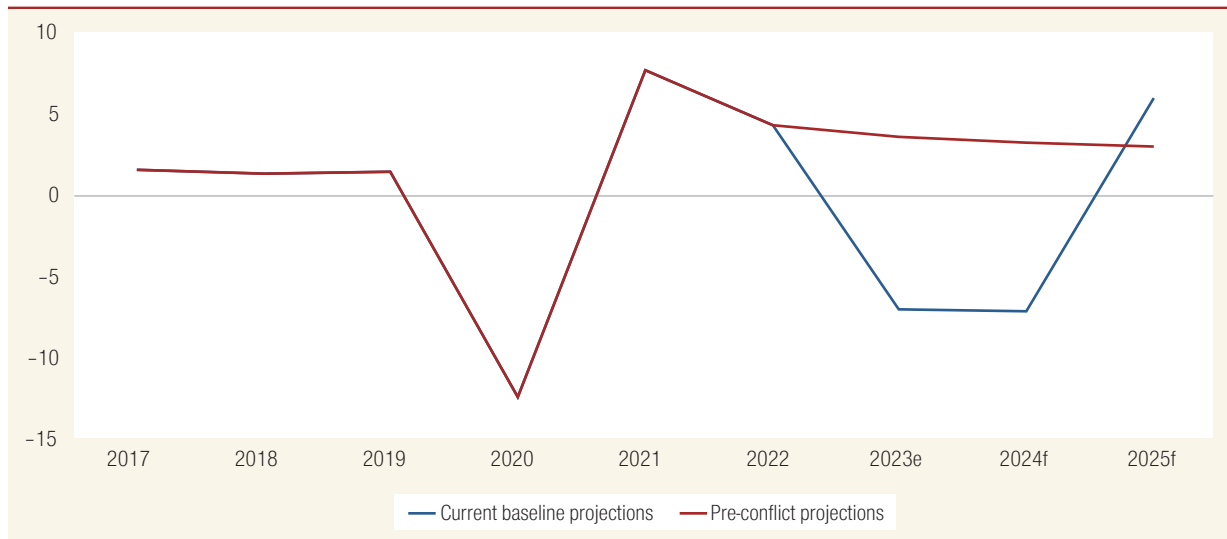
¹⁰ World Bank estimate based on IPSOS data, based on SAR and high-resolution satellite imagery.

FIGURE 1 • Gaza Real GDP Growth
(quarterly real GDP, year-on-year percent change)



Source: Palestinian Central Bureau of Statistics (PCBS).

FIGURE 2 • GDP Growth (%), Palestinian Territories



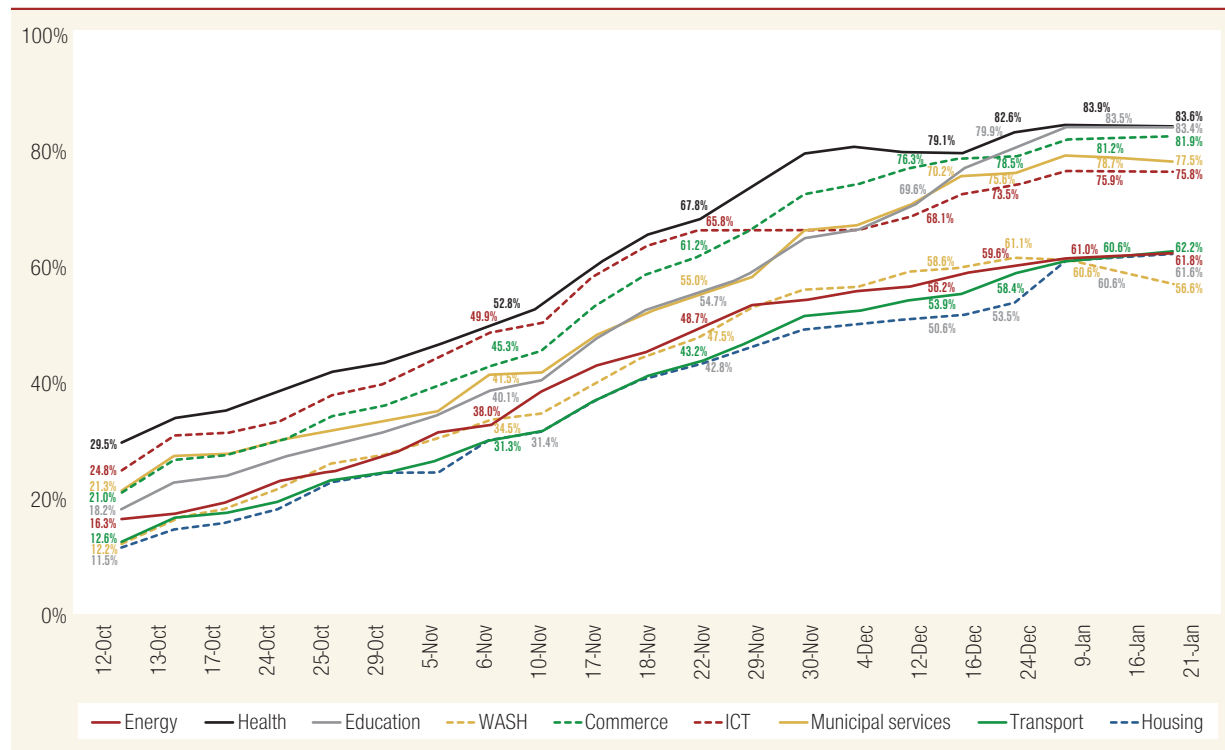
Source: WB Staff estimates, based on PCBS and Palestinian Ministry of Finance data.

Shelter Cluster has reported 1.7 million internally displaced persons (IDPs) in Gaza, making up nearly 75 percent of the population.¹¹ Infrastructure is heavily impacted, with over 62 percent of all roads damaged or destroyed. Primary roads bear the brunt, with 92 percent affected, almost 60 percent of which are destroyed. Secondary roads also face severe damage, with just over 60 percent rendered unusable. The predominant challenge across various sectors

is the lack of accessibility, as conflict-related activities hinder transportation services. The health sector

¹¹ Data reported as of January 10, 2024. People without homes refers to people whose homes have been severely damaged or destroyed and are separate from internally displaced persons (IDP) assessments. IDPs indicate people who have left their homes, which may still be habitable, as a result of conflict.

**FIGURE 3 • Impact (Damaged and Destroyed) Percentage by Sector
12 October--21 January 2024**



Source: IPSOS, based on satellite data.

is severely impacted, with nearly 84 percent of health facilities suffering damage or destruction. Concerns have been raised by the World Health Organization (WHO) and the International Committee of the Red Cross (ICRC) about the functionality of hospitals in Khan Younis¹² in Southern Gaza, as conflict activity and recent evacuation orders limit public access to several facilities. The education sector was also heavily affected, with schools non-functional, either serving as shelters for displaced individuals or damaged beyond repair. Before the conflict, Gaza had over 625,000 students attending school, and the United Nations (UN) Office for the Coordination of Humanitarian Affairs (OCHA) estimates that schools that cater to more than 70 percent of the student population are damaged or destroyed. Nearly 84 percent of education facilities have sustained damage or destruction. On the energy front, almost 62 percent of the Strip's electricity feeder lines are damaged or destroyed. During the early stages of the conflict, Israel turned off the supply of electricity to Gaza. The sole remaining power station ceased operating as the main supplier

ran out of fuel on 11 October 2023. Fuel shortages persist with dire consequences since both health and WASH (Water, Sanitation, and Hygiene) facilities rely on commercial generators for power. Access to clean water remains a critical issue for the Gaza population. Functional WASH assets, such as municipal wells and desalination plants, operate significantly below capacity, with almost 57 percent of assessed WASH facilities being damaged or destroyed¹³ and the remaining ones lacking access to grid electricity or fuel for commercial generators.¹⁴

¹² Source: WHO, and ICRC. Visited online respectively at <https://www.who.int/ar/news/item/12-07-1445-who-and-partners-bring-fuel-to-al-shifa-as-remaining-hospitals-in-gaza-face-growing-threats> and https://www.icrc.org/en/document/gaza-risk-complete-medical-shut-down-with-out-urgent-action-preserve-services?utm_source=twitter&utm_medium=social.

¹³ Source: OCHA Flash Updates. Visited online at <https://www.ochaopt.org/content/hostilities-gaza-strip-and-israel-flash-update-103>.

¹⁴ Source: Figures in this paragraph reflect IPSOS data.

TABLE 1 • Value of Economic Sector Losses of Production since October 2023 in West Bank and Gaza (US\$ thousands)^a

Sector	Value of two month production due to war			Value of average two month production in 2023			Differential (i.e. value of two months losses due to war)		
	West Bank	Gaza Strip	West Bank and Gaza	West Bank	Gaza Strip	West Bank and Gaza	West Bank	Gaza Strip	West Bank and Gaza
Industry	562,574	11,852	574,426	969,954	110,715	1,080,669	407,381	98,862	506,243
Construction	9,283	0	9,283	37,134	5,568	42,702	27,850	5,568	33,418
Internal trade	503,708	16,534	520,242	868,462	203,892	1,072,354	364,754	187,359	552,113
Transport and storage	10,917	320	11,237	24,261	5,873	30,134	13,344	5,553	18,897
Telecommunications and information	95,798	1,763	97,561	119,748	5,765	125,513	23,950	4,002	27,952
Services	489,019	34,433	523,452	743,460	140,315	883,775	254,441	105,882	360,323
Total	1,671,299	64,902	1,736,201	2,763,019	472,128	3,235,147	1,091,720	407,226	1,498,946

Source: PCBS, December 2023.

^a Source: PCBS website, visited online at: <https://www.pcbs.gov.ps/site/512/default.aspx?lang=en&ItemID=4665>.

The private sector in the West Bank and Gaza is estimated to have suffered losses of around US\$1.5 billion in production during the first two months of the conflict, equivalent to US\$ 25 million in losses per day.¹⁵ In Gaza, as of January 26, 2024, an estimated 82 percent of private sector establishments have either been partially damaged or fully destroyed, with the most significant damages suffered in North and Central Gaza. An estimated 83 percent of retail facilities, including supermarkets, grocers, and bakeries have also been damaged.¹⁶ While businesses in the West Bank have not been physically damaged, an estimated 86.5 percent of industries indicate a decline in production capacity.

The conflict has affected private sector activity in the West Bank due to increased Israeli military incursions, road closures, settlers aggressive activities,¹⁷ and restriction of movement and access within West Bank governorates.¹⁸ An estimated 42.1 percent of private sector establishments in the West Bank have reported a decrease in the total number of employees reporting for work during the months of November and December 2023.¹⁹ Establishments in the Services sector, in particular, reported the highest decline in number of employees, equivalent to 63.6 percent in the last two months of 2023, followed by Industry at 48.8 percent, and Com-

merce at 33.3 percent. An estimated 95.5 percent of West Bank establishments reported a decline in their monthly sales.

Most private sector enterprises in the West Bank report increasing obstacles to economic operations, such as a decrease in consumer spending, soaring prices, and constraints on the movement and access of goods and people. Roughly 96.4 percent of establishments identified a decline in consumer purchases as a primary obstacle

¹⁵ Source: PCBS's Press Release on the "Losses of Private Sector in Palestine due to the Israeli occupation Aggression on Gaza Strip", January 2024. Visited online at: <https://www.pcbs.gov.ps/site/512/default.aspx?lang=en&ItemID=4665>.

¹⁶ Source: IPSOS data reflecting damage assessment as of January 21st, 2024.

¹⁷ Source: The Economist. Visited online at: <https://www.economist.com/the-economist-explains/2024/02/08/a-history-of-settler-violence-in-the-west-bank>.

¹⁸ Source: Data from the Palestinian Ministry of National Economy (MoNE), based on the latest "Survey of West Bank Establishments", 2023. The study included 1,803 affected firms during the months of November and December 2023.

¹⁹ Source: Palestinian Ministry of National Economy's Note on the "Performance of Economic Establishments in the West Bank during the War in Gaza", January 2024.

to their economic activity. Furthermore, an estimated 80.4 percent of establishments cited the increasing cost of goods and 75.6 percent pointed to difficulties in distribution and transportation of goods between governorates as major impediments.²⁰ This disruption has led to an estimated 29 percent of establishments experiencing either complete or partial closures.

Damage to Gaza’s electricity infrastructure is currently estimated at nearly US\$ 280 million, underscoring the urgent need for repair and—where repair is not an option—replacement. The damages to the electricity sector in Gaza primarily involve: (i) the electricity distribution network;²¹ (ii) ground-based utility scale and off-grid distributed rooftop Solar photovoltaic (PV) electricity supply systems;²² (iii) specific equipment like demineralized water tanks and switchgear in the Gaza Power Plant (GPP); (iv) some of the ten high voltage electricity connection points through which electricity is imported from the Israel Electric Corporation (IEC); and (v) Gaza Electricity Distribution company (GEDCO’s) Warehouses, offices, vehicles and cranes. Initial reports from the Palestinian Electricity and Natural Resources Authority (PENRA) and GEDCO suggest that due to the severity of impacts from targeted strikes, much of the electricity supply equipment may not be repairable—with the exception of some cables—thus necessitating replacement. The estimated cost of electricity infrastructure damaged or destroyed in Gaza is nearing US\$ 280 million, based on data triangulated from IPSOS bi-weekly damage assessments.

The conflict has exacerbated the already fragile labor market in the Palestinian territories: based on ILO estimates, employment losses led to US\$ 20.5 million in forgone daily labor income.²³ Even before the onset of the conflict, unemployment rates in Gaza were alarming, reaching 45.1 percent in September 2023, with youth unemployment at 59.5 percent. According to preliminary UN estimates, an estimated 80 percent of the Gazan labor force have lost their jobs, equivalent to 192,000 jobs, with the exception of workers in the fields of health and humanitarian assistance.²⁴ The unemployment rate in the West Bank and Gaza is estimated to have increased from 24 percent in Q4-2022 to 29.7 percent in Q4-2023 as a result of the conflict.²⁵ Around

170,000 workers from the West Bank, who were previously employed in Israel and the settlements (comprising 20 percent of the employed population in the West Bank and accounting for one third of overall demand) before October 7, have either lost their jobs or are now unable to access them due to new Israeli restrictions imposed on Palestinians’ entry into the Israeli labor market. In addition, due to the newly imposed Israeli restrictions on movement within the West Bank, approximately 67,000 workers employed in governorates outside their place of residence are no longer able to reach their workplaces.

The conflict has heavily affected the governance and performance of public procurement, bringing it to an almost complete standstill in Gaza, while ripple effects are being felt in the West Bank, too. The only mechanism currently available for bringing in publicly procured items into Gaza is complex and restricted to humanitarian aid and basic needs mostly through UN agencies. In the West Bank, increased restrictions on movement have contributed to delayed deliveries, slow work completion, irregular attendance of workers, as well as bidding cancellations and the extension of submission deadlines. More broadly, the current security climate has adversely affected the import supply chain to the West Bank via Israeli ports. This has led to a shortfall of available supply stocks, particularly in vital sectors like food, medicine, and I.T. equipment, contributing to inflationary pressures.

In the fourth quarter of 2023, consumer price inflation (CPI) in Gaza surged by

²⁰ Ibid.

²¹ This also includes all the associated electricity sector assets associated, such as transformers, cables, switchgears, poles, accessories, smart meters, Supervisory Control and Data Acquisition – SCADA systems.

²² These are deployed across Gaza in public buildings including schools, hospitals and health facilities, water supply and wastewater treatment facilities, residential buildings.

²³ Source: ILO brief “Impact of escalation of hostilities in Gaza on the labor market and livelihoods in the Occupied Palestinian Territory – Bulletin No. 2”.

²⁴ Ibid.

²⁵ WB Staff estimates based on official country data and the World Bank’s MFMod database.

TABLE 2 • Selected Economic Indicators

	Actual		Pre-conflict estimates		Current baseline estimates		Differential		
	2020	2021	2022	2023e	2024f	2023e	2024f	2023	2024
Real GDP	-11.3	7.0	3.9	3.2	3.0	-6.4	-6.5	-9.6	-9.5
Nominal GDP	-9.3	16.6	5.5	5.1	4.8	-8.6	-5.4	-13.7	-10.2
GDP per capita (nominal)	-11.6	13.8	3.0	2.6	2.4	-10.2	-7.3	-12.8	-9.7
Private consumption	-13.1	7.5	20.5	4.8	3.8	-6.4	-7.3	-11.2	-11.1
Government consumption	0.3	10.3	-10.5	-10.5	3.0	-11.3	0.3	-0.8	-2.7
Gross fixed investment	-20.9	13.7	11.8	6.0	3.5	-3.4	-4.0	-9.4	-7.5
Exports, goods and services	-11.2	17.3	6.2	5.0	5.0	2.9	3.0	-2.1	-2.0
Imports, goods and services	-14.2	14.8	25.7	5.0	5.0	-2.6	-2.0	-7.6	-7.0
Agriculture	-9.1	-0.7	-5.7	-1.0	-1.0	-11.3	-5.2	-10.3	-4.2
Industry	-19.4	4.5	3.4	3.2	3.0	-7.5	-6.0	-10.7	-9.0
Services	-10	7.5	1.5	3.7	3.4	-5.6	-6.8	-9.3	-10.2
Unemployment rate (%)	25.9	26.4	24.4	24.4	24.5	29.7	29.2	5.3	4.7
CPI (year-average)	-0.7	1.2	3.7	4.4	3.0	5.9	4.6	1.5	1.6
General government balance	-7.5	-5.8	-1.4	-0.5	-0.8	-3.0	-2.9	-2.5	-2.1
Current account balance	-12.3	-9.8	-15	-13.7	-13.2	-14.7	-19.2	-1.0	-6.0
Memorandum Items:									
Nominal GDP (US\$ million)	15,532	18,109	19,112	20,085	21,056	17,466	16,517	-2,619	-4,539

Source: PCBS, PMA, and MoF for actual data, and World Bank staff for projections.
Note: e = estimate, forecast.

33 percent compared to the previous quarter, primarily due to disruptions in the supply chain resulting from the conflict. Widespread shortages of essential goods have significantly constrained the purchasing ability of hundreds of thousands of households, irrespective of their financial means. Food prices in Gaza saw a quarter-on-quarter (q/q) increase of 39 percent in Q4-2023, driven by challenges in accessing food, increased transportation costs, and decreased volumes of aid. The complete halt of fuel and gas supplies through the crossings contributed to a 143 percent rise in transportation prices in Gaza during Q4-2023, q/q. In contrast, the Consumer Price Index (CPI) in the West Bank experienced a marginal increase of 0.9 percent, q/q, during the same period.

Agricultural infrastructure was heavily impacted by the conflict, exacerbating unemploy-

ment, poverty, and food insecurity cycles. Prior to the conflict, primary agriculture contributed approximately 6 percent of the GDP in the West Bank and Gaza, with the entire agri-food value chain representing roughly 15 percent. Historically, agriculture has been a significant source of employment²⁶ and has played a crucial role in ensuring food security, both through local production of food and by enhancing the socio-economic conditions of Gaza's population. According to IPSOS data, between 80 to 96 percent of agricultural assets have been damaged or destroyed, as of present. This includes different

²⁶ Source: Center for Economic and Policy Research (CEPR), CEPR, "Agriculture in Palestine: a post-Oslo analysis", 2017. Approximately 13.4 percent of the formal labor force and over 90 percent of total informal employment is absorbed by the agricultural sector.

types of agricultural production assets, such as irrigation infrastructure, livestock farms, orchards, agricultural holdings, machinery, storage facilities, as well as research stations. Damages are mainly concentrated in the north of Gaza and in the Khan Younis governorate. As a result, the sector's functionality and service delivery have been severely compromised, leaving those reliant on the agri-food value chains for their livelihoods without a dependable source of both nutrition and income.

Poverty was prevalent in Gaza long before the conflict, with social assistance playing a crucial role in mitigating its impacts. The 2017 household survey²⁷ indicated that 79 percent of residents in Gaza were recipients of governmental or non-governmental aid. For those living below the poverty line, almost half of total income came from assistance. More recent estimates (2022) suggest that more than half of Gazan households continue to report aid as their primary source of income,²⁸ including for food assistance. On the eve of the conflict, 8 out of 10 individuals received some form of aid.

At present, it is reasonable to consider almost every resident in Gaza as poor, at least in the short term. A vast number of Gazans were pushed into poverty, due to the multi-layered shock affecting productive capacity; on account of the destruction of agricultural land, fishing ports and local fleets, the destruction or inoperability of food shops and markets, the scarcity of water, flour, fuel and electricity, as well as starving livestock that is unable to provide sustenance or serve as a food source.²⁹ These factors were compounded by the extensive internal displacement, and the destruction of homes and assets, coupled with a steep recession. These developments altogether have intensified the poverty levels for those who were already vulnerable. **Nearly every individual in Gaza currently faces acute food insecurity and is in urgent need of assistance, with more than half a million people facing catastrophic levels of food insecurity.**³⁰

Non-monetary welfare (multidimensional poverty)³¹ conditions in Gaza have deteriorated rapidly over the last four months, while the need for assistance has correspondingly increased, along with displacement. The hostilities have also

led to a substantial increase in multidimensional poverty, stemming from disruptions to children's access to education and challenges in obtaining essential health and other basic services. At the time of writing, around 3 in every 4 people in Gaza are displaced.³² Two-thirds of the territory has been subject to evacuation orders, and more than 650,000 people will not be able to return home in the near future because of extensive infrastructure damage. Only roughly one third of Gaza's hospitals are partially functioning, while more than three quarters of the school buildings have been significantly damaged.

The conflict's impact on poverty levels extends beyond Gaza. The effectiveness of social protection programs is hampered by the PA's severely limited fiscal capacity. The overall economic slowdown estimated for the last quarter of 2023 will also impact poverty levels in the West Bank. With a projected national GDP reduction of 6.4 percentage points, all the progress in welfare achieved in the Palestinian territories since the end of the pandemic is

²⁷ See Atamanov, A., & Palaniswamy, N. (2018). *West Bank and Gaza Poverty and Shared Prosperity Diagnostic 2011–2017*. Available online at: <http://documents.worldbank.org/curated/en/985801536125679274/West-Bank-and-Gaza-Poverty-and-Shared-Prosperity-Diagnostic-2011-2017>.

²⁸ Source: United Nations Office for the Coordination of Humanitarian Affairs. (2022). *2022 Multi-Sector Needs Assessment: Key Cross-Sectoral Findings* [Presentation]. <https://www.ochaopt.org/data/2022/msna>.

²⁹ Source: United Nations Office of the High Commissioner for Human Rights; <https://www.ohchr.org/en/press-releases/2024/01/over-one-hundred-days-war-israel-destroying-gazas-food-system-and>.

³⁰ Source: IPC Global Initiative. (January 2024). *The Gaza Strip – IPC Special Brief*. https://www.ipcinfo.org/fileadmin/user_upload/ipcinfo/docs/IPC_Gaza_Acute_Food_Insecurity_Dec2023Feb2024.pdf.

³¹ Multidimensional poverty covers income, access to education and basic infrastructure inter alia. For more info, please see <https://www.worldbank.org/en/topic/poverty/brief/multidimensional-poverty-measure>.

³² Source: United Nations Office for the Coordination of Humanitarian Affairs. (February 2, 2024). *Hostilities in the Gaza Strip and Israel | Flash Update #109*. <https://www.ochaopt.org/content/hostilities-gaza-strip-and-israel-flash-update-109>.

expected to be nullified. Poverty levels at the close of 2023 are anticipated to surpass those in 2020, during the peak of COVID-related restrictions, when it stood at 26.5 percent.

On the fiscal front, an already severe crisis was exacerbated by a reduction in the revenues that Israel collects on behalf of, and remits to, the PA monthly, known as “clearance revenues.” Since October 2023, the Government of Israel has increased deductions from clearance revenues, bringing the monthly figure to around NIS 500–600 million, up from the previous NIS 200 million.³³ According to Israeli authorities, this increase reflects the amount that the PA spends in Gaza and offsets the debt owed by the Jerusalem District Electricity Company (JDECO) to the Israeli Electricity Company (IEC). As a result, clearance revenue transfers shrank by over 50 percent in the conflict’s aftermath. In response, the PA decided to decline several of these transfers since last October.

Consequently, total revenues in 2023 (excluding grants) contracted by 10 percent compared to pre-conflict estimates, also reflecting a general fall in domestic revenues amid depressed economic activity. As clearance revenues represent roughly two thirds of the PA’s total income, the situation has precipitated a massive fiscal crisis, exacerbating preexisting weaknesses and potentially posing a threat to the foundations of the social contract. The PA was compelled to substantially reduce and postpone public salary payments in the third quarter of 2023. For the months of October³⁴ and November, 50 and 64 percent of the total monthly salary bill was paid—respectively—by December 30th, 2023. For the month of December, 60 percent of the monthly salaries were paid on February 7th, 2024. January’s wage bill remains unpaid.³⁵ The conflict-induced macro fiscal impact, compounded by the absence of primary income sources, has exacerbated an already challenging fiscal situation, and resulted in higher risks that could severely jeopardize the capacity of the institutions to provide the most basic services in the West Bank. The situation could also irreversibly undermine progress in key areas of the Palestinian development plan. **Against this backdrop, the 2023 financing gap proved to be roughly five times larger than**

the pre-conflict baseline, totaling US\$516 million (3.0 percent of GDP) instead of the original pre-conflict baseline of US\$106 million.³⁶

While facing substantial and increasing risks, the banking system remains intact. The banking sector has continued to act cautiously, with modest levels of lending. Q4 data indicated an incremental uptick in customer deposits in the Gaza Strip, signaling, among other considerations, continued trust in the resilience of the banking system. Despite a low non-performing loan (NPL) ratio of 4.2 percent by the end of 2023, projections indicate an increase in NPLs and classified loans, while the Gaza loan moratorium expiration was just extended to April 2024. This moratorium, implemented by the Palestinian Monetary Authority (PMA) in response to the crisis, represents one of several emergency measures aimed at avoiding the accumulation of excessive risks in order to safeguard financial stability. The PMA recently concluded a round of stress testing by the PMA and the banking sector for a range of scenarios stemming from the recent escalations. According to PMA reporting, the stress testing results confirmed the sector’s resilience with regards to capital adequacy and liquidity.

³³ According to the PA MoF, Israeli deductions in October amounted to NIS600 million resulting in a net transfer of NIS200 million that was rejected by the PA. Deductions reached NIS525 million in November resulting in a net transfer of NIS430 million which the PA accepted. Deductions reached NIS500 million in December resulting in a net transfer of NIS200 million, which has so far been rejected by the PA. An arrangement where the deductions related to PA payments reserved for Gaza would be transferred from Israel and held in escrow by Norway is being discussed but a final agreement had yet to be reached at the time of writing.

³⁴ The October partial salary payment was initially made through direct loans from the commercial banks to the PA employees in November. Those loans were then repaid to the banks by the Palestinian Ministry of Finance on December 30th, 2023.

³⁵ This note is updated to February 10, 2024.

³⁶ This is under the assumption that the PA would eventually pay 80 percent of the Q4 2023 committed salaries. The fiscal deficit (before grants) is estimated to be as high as US\$794 million in 2023 (close to 4.5 percent equivalent of GDP). Aid received is estimated at US\$278 million.

TABLE 3 • Key Fiscal Indicators (2020-2025)

	Actual			Pre-conflict projections			Current baseline projections*		
	2020	2021	2022	2023e	2024f	2025f	2023e	2024f	2025f
Key fiscal indicators, percent of GDP, unless indicated otherwise									
Overall balance	-7.5	-5.8	-1.4	-0.5	-0.8	-0.6	-3.0	-2.9	-2.7
Primary balance	-7.1	-5.1	-0.7	0.1	-0.1	0.1	-2.2	-2.2	-2.0
Total revenues and grants	25.7	25.0	27.3	24.6	25.9	26	25.5	27.9	27.7
Tax revenues	20.5	21.6	23.3	21.1	22.3	22.4	21.7	23.8	23.7
Taxes on goods and services	3.5	4.3	4.5	4.1	4.2	4.3	4.6	4.6	4.7
Direct revenues	1.2	1.2	1.5	1.5	1.5	1.6	1.5	1.6	1.6
Taxes on international trade ^a	15.1	15.3	16.5	14.8	15.9	15.9	14.9	16.8	16.7
Other taxes	0.6	0.8	0.9	0.7	0.7	0.7	0.7	0.7	0.7
Non-tax revenues	2.4	2.2	2.4	2.3	2.4	2.5	2.5	2.5	2.5
Grants	3.1	1.7	1.8	1.5	1.4	1.3	1.6	1.9	1.7
Tax refunds (-)	0.3	0.6	0.2	0.2	0.2	0.2	0.3	0.2	0.2
Total expenditures	33.2	30.7	28.7	25.1	26.7	26.6	28.5	30.8	30.4
Current expenditures	28.0	26.0	23.2	20	21.5	21.4	22.2	25.2	24.3
Wages and compensation ^a	14.2	14.6	13.4	10.9	10.8	10.7	12.2	13.5	13.0
Goods and services	4.2	4.4	4.2	4.2	4.2	4.2	4.6	4.6	4.5
Interest payments	0.4	0.7	0.7	0.7	0.7	0.6	0.7	0.8	0.7
Current transfers	9.2	6.3	4.8	4.1	5.8	5.8	4.7	6.3	6.1
Capital expenditures	2.0	1.5	1.6	1.8	1.8	1.8	2.5	2.1	2.6
Other expenditures	3.2	3.3	3.9	3.3	3.3	3.3	3.7	3.5	3.5
Financing requirement	7.5	5.8	1.4	0.5	0.8	0.6	3.0	2.9	2.7
Government financing	3.6	0.5	-0.6	0.0	0.0	0.0	0.0	2.7	0.0
External financing (net)	0.7	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Domestic financing (net)	2.9	0.5	-0.5	0.0	0.0	0.0	0.0	2.7	0.0
Financing gap	3.9	5.3	2.0	0.5	0.8	0.6	3.0	0.2	2.7
Memorandum items:									
Stock of arrears	31.6	34.8	34.7	33.6	32.8	31.9	40.9	43.5	43.4

Source: MoF for actual data, and World Bank staff for projections.

Note: f = Forecast. *Cash basis.

^a The wage figures included in this item represent 80 percent of the committed amount. In line with the practice that the PA has adopted since late 2021. It is important to underscore that the fiscal ramifications arising from the underlying austerity measures - e.g. resorting to only partial payment of public salaries - are far-reaching in both magnitude and impact.

With the deepening fiscal crisis, the PA's growing reliance on bank financing raises concerns. Following several years in which PA borrowing broadly declined, the banking system's exposure to the public sector increased considerably in Q4-2023, reaching US\$2.4 billion in December 2023 following

the approval of a US\$400 million syndicated loan to the PA, financed by local banks.

The combined credit and deposit exposure of the banking system to Gaza is comparatively limited when contrasted with that of the West Bank. A range of factors, including concerns related

to Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT) as well as operational risks, have prompted the majority of the 13 banks functioning in the West Bank to limit their exposure to Gaza. Of the several banks active in Gaza, only one bank is designated as systemically important by the PMA.

Initial data on financial sector damages confirm that the impact on banking and non-banking sectors in the current conflict is more severe than in past conflicts. The damages and losses in the banking sector encompass physical assets, losses in cash stored in vaults and ATMs, and expected credit losses in loan portfolios in Gaza and certain segments of the West Bank. The PMA has confirmed the complete destruction of several financial sector assets in Gaza, including the PMA's own office. Currently, only a small fraction of ATMs in Gaza are operational, and very limited financial services are being accessed through point-of-sale (POS) systems and banking agents, resulting in difficulties and delays in accessing personal funds. In recent months, the percentage of returned checks continued to rise, reaching 25 percent, exceeding the pre-conflict average of 8–10 percent per month. This likely reflects a rise in instances of non-payment of wages to both public and private sector employees.³⁷

Given the absence of viable alternative financing options, the PA has continued to accrue arrears to the private sector and the public pension fund. The projected stock of arrears reached 40.9 percent of GDP by the end of 2023, surpassing the pre-conflict baseline of 33.6 percent of GDP. To finance the salary payments, the PA has also increased its borrowing from domestic banks by US\$400 million, raising its exposure near the all-time high that was reached during COVID times.

Besides increasing arrears, foreign aid stands as the only other viable source of financing available to address the ongoing fiscal and humanitarian crises, as well as to maintain a minimum of basic service delivery. The disbursement of humanitarian aid funds, primarily administered through UN agencies, is anticipated to provide a vital lifeline for those directly impacted by the widespread destruction. However, the extensive damage of Gaza poses significant challenges to recovery efforts, underscoring the

urgent need for preparation and continued international support to address the immediate impact and vast needs for recovery once a ceasefire is reached.

Gaza's long-term economic trajectory is anticipated to face vast challenges not only from the destruction of fixed assets, but also from the effects of the conflict on the people of Gaza, including on their mental health. Prior to this conflict, a recent study³⁸ by the World Bank found that 58 percent of the Palestinian adult population exhibit symptoms consistent with depression.³⁹ The share of population exhibiting depression symptoms was 50 percent in the West Bank and soared to 71 percent in Gaza. The trauma associated with displacement and destruction during the ongoing conflict is likely to lead to a further deterioration of mental health. Moreover, labor participation is also predicted to suffer, as physical displacement, security concerns, and disrupted infrastructure will limit employment opportunities at least over the medium term. Segments of the population that are already vulnerable, including women and marginalized groups, will bear a disproportionate burden, as these groups face increased challenges in accessing education, health-care, and economic opportunities already under normal circumstances.⁴⁰

After the cessation of hostilities, the short to medium-term recovery and reconstruction efforts in the electricity sector will depend on restoring functionality to the electricity distribution network. This involves: a) repairing damaged water tanks and step-up transformers in the Gaza Power Plant (GPP), and ensuring sufficient fuel supply (diesel and heavy fuel oil) to operate its turbo-generators; b) rehabilitating or replacing affected main feeders at high-voltage connection points with the Israel Electric Corporation (IEC) to restore electricity imports; c) rehabilitating and reconstructing the dis-

³⁷ Source: WB staff based on information from PMA

³⁸ Source: Palestinians' Psychological Conditions Survey 2022, World Bank. Available online at <https://microdata.worldbank.org/index.php/catalog/5807>.

³⁹ Based on the "WHO-5 wellbeing index".

⁴⁰ Source: The World Bank Annual Report 2023, available online at <https://www.worldbank.org/en/about/annual-report/addressing-multitude-global-challenges>.

tribution network, including cables and meters for low voltage customers. Immediate relief measures, falling under humanitarian support, include providing backup generators, diesel fuel for essential facilities like hospitals and schools, and mobile solar kits to ensure basic energy services resume promptly.

Overall, the outlook hinges largely on the conflict's intensity and the level of restrictions.

The economic contraction could be a lot more pronounced if the current level of conflict extends beyond early 2024, if Israel further tightens restrictions on the movement and access of Palestinians in the West Bank, and if clearance revenues continue to be largely absent. This in turn, may prompt the PA to resort to extreme—and potentially disorderly—fiscal consolidation measures, including further reductions in employee salaries, thus intensifying the decline in public consumption and household incomes. The timing, extent and pace of reconstruction remain highly uncertain, both hinging on a cessation of the hostilities and the materialization of significantly larger external aid flows.

Averting a dramatic recession, a large uptick in poverty, and a continued unparalleled

shock to the economy will require immediate action on the following:

- **First**, the cessation of hostilities would pave the way for significant changes on the ground. Primarily, it would save lives, opening the opportunity for economic and social reconstruction;
- **Second**, reducing or reversing recent decisions to increase deductions from Clearance Revenues and thus restoring the flow of fiscal income to PA as soon as possible;
- **Third**, facilitating trade and private sector activity in the West Bank and Gaza, to allow income generation;
- **Fourth**, urgently increasing financial support by the international community, during and after this crisis. With a fiscal gap of US\$516m in 2023, increasing humanitarian needs and—when the conflict ends—reconstruction needs, aid will need to continue to play a pivotal role in supporting the PA, especially in the short-to-medium term;
- **Finally**, undertaking renewed efforts towards policy reforms by the PA, including on fiscal sustainability.



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