



PALESTINE MONETARY AUTHORITY

Annual Report **2018**



Research and Monetary Policy Department

September, 2019



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Ramallah – Palestine

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Designed by:

Public Relations and Communications Department - PMA

Vision

To be a full-fledged, modern central bank for the Palestinian state, capable of maintaining monetary stability by keeping inflation under control, and maintaining financial stability. PMA also works to achieve sustainable economic growth and promote further integration into regional and global economies.

Mission

To Maintain financial stability by ensuring a safe, sound and secure banking system, an efficient national payments system, boarder financial inclusion; and ensuring monetary stability by keeping inflation under control.



 PMA's Board of Directors



Mr. Azzam Shawwa

Governor &
Chairman



Dr. Ryad Abu Shehadah

Deputy Governor



Mr. Ibrahim Barham

Member



Mr. Iyad Joudeh

Member



Dr. Bashir Rayyes

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Dr. Taleb Sarie

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Member

Forword

I am honored to present to you, on behalf of the PMA, the publication of the new Annual Report. The Report addresses the tasks and responsibilities PMA assumes and its effective role in macroeconomy to ensure financial and monetary stability and support of sustainable economic growth.

The report was issued during a period that experienced a number of economic and political developments at international, regional, and local levels resulting in noticeable slow local growth pace along with huge increase in current deficit of public finance and current account deficit in the balance of payment.

This publication includes four main parts addressing the most important developments in macroeconomy, fiscal sector, external sector including balance of payments and international investment, and the Palestinian financial sector. The Report also includes the most important achievements of the PMA and its role in regulating and controlling the institutions under its direct supervision such as banks, specialized lending institutions and money changers.

I hope that we at the PMA have, through this representation, succeeded in addressing the key changes and developments of 2018 through a framework of analysis based on accurate information, which is supported by statistical time series that includes the most important local and international economic indicators.

Finally, I would like to express my sincere gratitude to the PMA's Board of Directors and its employees for their diligent efforts to achieve the objectives of the PMA and realize its aspiration to be a full-fledged and modern central bank for the State of Palestine. I would also like to express my appreciation to the Arab, regional and international organizations that continue to support and develop the PMA and the banking and financial system, which boost the resilience of Palestinian citizens and sustainable development in Palestine.



Governor

Azzam Shawwa

Azzam A Shawwa

Board of Directors

Governor

Deputy Governor

INDEPENDENT OFFICES

Ethics Officer

Ombudsperson

Chief Internal Auditor

Chief Legal Counsel

Enterprise Risk Management

MONEY STABILITY GROUP

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Real Economy Division

MP and Financial Markets Division

Public Finance Division

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BoP and External Sector Division

Statistics Division

Library

Monetary Operation Department

Reserve Management Division

Risk Management Division

Open Market Operation Division

FINANCIAL STABILITY GROUP

Supervision and Inspection Department

Licensing Division

Foreign Banks Supervision Division

Local Banks Supervision Division

Macroeconomic Analysis Division

Money Changers Supervision Division

Microfinance Institutions Supervision Division

AML/CFT Division

Consumer's Relations and Market Conduct Department

Credit Bureau Systems Division

Analysis and Technical Support Division

Awareness and Complaints Division

Payment Systems Department

Systems Development Policies & Support Division

Banking Operations and Treasury Back Office Division

Payment Systems Division

ADMINISTRATION GROUP

Security and Public Safety Office

Accounting and Financial Reporting Division

Budgeting and Expenses Division

Finance Department

Human Resources Department

Operations and Staff Relations Division

Training and Development Division

Information Systems and Technology Department

Operations and Control Division

Applications and Development Division

Technical Support Division

Infrastructure and Operating Division

Governor Office

Project Management Unit

Secretarial and Archive Unit

Oversight Payment Systems Unit

Public Relations and Communication Department

Protocol and Public Relations Division

Publications and Media Division

General Services Department

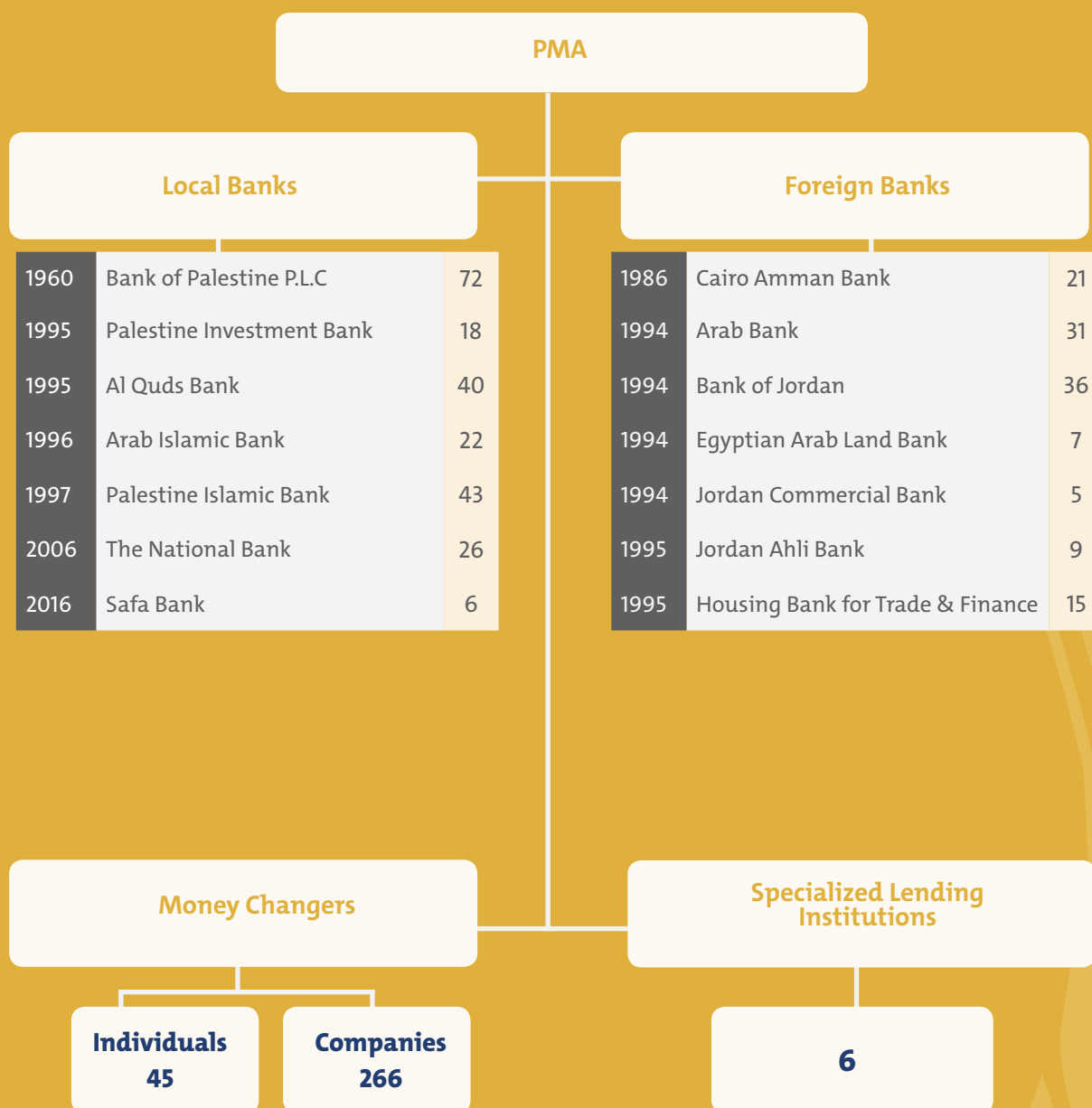
Procurement Division

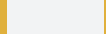
Administrative Services Division

Facilities Management Division

PMA organization chart

Palestinian banking system institutions 2018



 Year of establishment for local banks, or re-opening of the first branch for foreign banks.
 Number of branches and representative offices.



Executive Summary

The Palestinian economy suffered more risks and challenges in 2018 resulting in noticeable acceleration in growth slowdown pace, due to the developments in public finance and external sector. The Palestinian government suffered clear retract in clearance revenue and drop in grants leading to retracted revenue and grants by 4.1 percent compared to previous year to hit NIS 15,320.2 million.

Despite the government attempts to adapt to this challenge by rationalizing public expenditure –the government actually succeeded in reducing public expenditure by 3.2 percent compared to previous year to reach approximately NIS 14,137.1 million it was not sufficient. Consequently, the current deficit registered big increase by almost 49.2 percent on cash basis to approximately NIS 726.3 million compared to a deficit of NIS 486.8 million in 2017. This occurred alongside accumulating government arrears of 4.4 percent compared to previous year to reach USD 3,407.7 million.

Current account in the balance of payment also suffered noticeable increase in deficit, which reached USD 1,659.3 million at an increase of 6.1 percent compared to 2017 or 11.4 percent of the GDP compared to 10.8 percent in previous year. This increase in deficit is due to a big increase in the size of imports of goods (8.2 percent) and a 2.4 percent drop in current transfers.

These challenges contributed to continuation and entrenchment of slowdown in the growth of the Palestinian economy in 2018 (which was in line with the expectations of the PMA) to reach 0.9 percent compared to 3.1 percent in 2017. Real GDP (at 2015 prices) rose to approximately USD 13,810.3 million. The performance of the economy of the West Bank and that of Gaza Strip were clearly different (continued downturn in Gaza Strip and a loss of growth momentum in the West Bank in 2018).

In Gaza Strip GDP dropped by around 6.9 percent; a continuation of the retraction that occurred in 2017, which hit about 12.5 percent, mainly due to continued reduction in government spending and continued deterioration in the levels of investment as a result of the siege and closure that began in 2006 and the consecutive wars in Gaza Strip since then. In addition to the decline in foreign grants to development projects and to vital agencies such as the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) whose services benefit large percentage of families in Gaza Strip. In the West Bank, the political level confronted enormous challenges because of the successive American decisions concerning the Palestinian cause, which harmed different aspects of the economic situation; especially foreign grants (terminating Palestinian Authority's budget support and reducing development grants) and led to more concerns and exacerbated uncertainty. Subsequently, the West Bank economy continued to have average growth rates (3.1 percent) but lost the momentum it experienced in growth rate in previous year of approximately 8.5 percent.

The trend in the change of growth in per capita income was in line with the economic growth in Palestine and in both West Bank and Gaza Strip. The economic slowdown prevented per capita income in the West Bank from growing more than 0.8 percent to reach approximately USD 4,188.3. Per capita income in Gaza Strip experienced downturn again at around 9.5 percent to hit its lowest level ever (at USD 1,431.4) or one-third of the per capita income of the West Bank.

Consumer price in Palestine experienced slight downturn at approximately 0.2 percent (compared to price growth of approximately 0.2 percent in 2017). Inflation levels often vary between the West Bank and Gaza Strip because of different political and economic factors. In 2018, despite the minor acceleration in inflation rate in the West Bank, it stayed at low level of 0.4 percent compared to 0.0 percent in the previous year. In Gaza Strip, prices experienced deflation at approximately 1.3 percent compared to relative stability in the previous year at (0.1 percent).

Unemployment is still one of the biggest challenges that the Palestinian economy faces, especially in Gaza Strip. The

economic downturn in Gaza Strip negatively influences the market capacity to absorb the labor market newcomers and to create an adequate number of jobs as required. This leads to an increase in unemployment rates and low individuals' living standards. Unemployment rates in Gaza Strip rose to 52.1 percent compared to 44.5 percent in 2017. In the West Bank, on the other hand, unemployment rates dropped to 17.6 percent compared to 18.7 percent in 2017. Overall, unemployment rate increased in Palestine from 28.4 percent in 2017 to 30.8 percent in 2018.

Alternatively, Palestinian workers' nominal daily wage rose by 7.6 percent in 2018 to register approximately NIS 123.0. This occurred against the backdrop of an increase in average wage in the three work areas at close rates (7.6 percent for West Bank workers; 7.1 percent for Palestinian workers in Israel and in settlements; and 6.2 percent increase for workers in Gaza Strip). Price movements in 2018 were in favor of boosting purchase power, especially among Gaza Strip workers against the backdrop of consumer price deflation. Hence, the real wages of Gaza Strip workers grew more than the growth in nominal wages (7.5 percent compared 6.2 percent). The relative stability in consumer price level of the West Bank makes growth in real workers' wages in the West Bank and in Israel very close to nominal wages.

The Palestinian banking sector made more achievements in 2018 as the PMA continued its efforts to develop supervisory and legal framework that regulated the banking sector and supported its various supervisory systems. PMA also continued to strengthen the banking sector's Arab, regional and international relations, with the aim of deepening the ties between the Palestinian banking sector and its regional and international surroundings. These efforts covered many aspects, both at the regulatory and supervisory levels through supervisory instructions, and at the level of regulatory systems and their development, such as Basel III and the International Financial Reporting Standard (IFRS-9). At the level of payment systems, strengthening governance and transparency in the banking sector, as well as enhancing and improving access to finance, as the PMA's efforts culminated in the launch of the National Financial Inclusion Strategy (2018-2025) in December 2018. PMA also continued its efforts in combating money laundering and terrorism financing. In this context, and during 2018, PMA prepared the national strategy that addressed the weaknesses and shortcomings resulting from the national self-assessment of the risks of the crimes of money laundering and terrorism financing. It also issued several circular to institutions under its supervision related to combating money laundering and terrorism financing.

The outcome of these measures was positively reflected in the financial indicators of the banking sector, and the strengthening of public confidence in the safety and discipline of this sector in accordance with the highest international banking standards. The growing public confidence was reflected in a clear increase in the volume of deposits, with exploitation of these deposits inward rather than abroad.

In this context, the analysis of the financial statements for the banking sector (as at the end of 2018) showed that total assets in the banking sector increased by 1.7 percent to USD 16,124.9 million. The direct credit facility portfolio also increased by about 5.1 percent to reach about USD 8,432.3 million, or 52.3 percent of the total assets of the banking system. This is a sign of greater activation of the role of financial intermediation between surplus and deficit units in the local economy, providing more financing opportunities and contributing to the economic development process. Customer deposits also reached USD 12,227.3 million, increasing by 2.0 percent than it was in 2017. The banking sector's equity increased by 1.1 percent to reach USD 1,912.0 million.

On the other hand, PMA continued its institutional building and strengthened its capital in order to increase its ability to overcome the risks it faced in exercising its functions, mandates and responsibilities. The property rights of the PMA grew by the end of 2018 by 14.0 percent more than they were at the end of 2017 to reach USD 134.0 million, due to the increase in paid-up capital by about 19.3 percent. PMA's actions during 2018 also resulted in making a net profit of USD 20.8 million, which was entirely transferred to the capital account.

Main indicators of Palestinian economy, 2014-2018

Indicator	2014	2015	2016	2017	2018
Output and Prices	(Annual percent change)				
Real GDP (2015 market prices)	-0.2	3.4	4.7	3.1	0.9
Real Percapita GDP	-3.1	0.4	2.1	5.1	-1.7
Inflation rate	1.7	1.5	-0.2	0.2	-0.2
WB	1.2	1.3	-0.1	0.0	0.4
GS	2.9	1.8	-0.9	0.10	-1.3
Unemployment Rate	(Percent of labor force)				
Palestine	26.9	25.9	26.9	28.4	30.8
WB	17.7	17.3	18.2	18.7	17.6
GS	43.9	41.1	41.7	44.4	52.1
Consumption, Investment and Saving	(Percent of nominal GDP)				
Final consumption	117.2	120.2	118.2	113.2	113.7
Public	26.4	27.1	26.3	25.7	25.7
Private	90.7	93.2	91.9	87.5	88.0
Gross capital formation	20.0	21.1	21.2	22.6	23.7
Public	3.8	4.6	5.3	6.8	5.9
Private	16.2	16.5	15.9	15.8	17.7
Saving	5.3	4.5	5.1	10.8	11.6
Public Finance	(Percent of nominal GDP)				
Total net revenue and foreign aid	31.6	29.1	32.1	30.2	28.2
Total revenues (net), of which:	21.9	22.8	26.4	25.2	23.6
Tax	4.7	4.8	4.7	5.3	5.7
Non-tax	2.1	2.0	4.5	2.7	2.9
Clearance revenue	16.1	16.1	17.3	17.1	15.4
Foreign aid	9.7	6.3	5.7	5.0	4.6
Total expenditures, of which:	28.3	28.4	28.9	27.9	26.9
Wages and salaries	14.9	13.9	14.3	13.5	11.3
Non-wage expenditure	9.9	10.5	10.6	10.5	11.5
Net lending	2.3	2.4	2.0	1.8	1.8
Development expenditures	1.3	1.4	1.6	1.8	1.9
Overall balance (Excl. foreign aid)	-6.4	-5.6	-2.4	-2.7	-3.3
Overall Balance (Inc. foreign aid)	3.3	0.7	3.3	2.3	1.3
Government public debt	17.4	20.0	18.5	17.5	16.2

Indicator	2014	2015	2016	2017	2018
External Sector	(Percent of nominal GDP)				
Exports of goods and services	17.1	18.4	17.7	18.6	19.9
Imports of goods and services	56.7	59.5	56.8	55.6	59.7
Income from abroad, net	11.7	13.5	14.1	13.7	16.4
Of which: compensation of employees	11.4	13.1	14.1	13.6	15.6
Current transfers, net	11.1	11.2	10.5	12.5	12.1
Of which: to public sector	4.8	3.8	3.3	4.1	4.2
Current Account	-16.9	-16.3	-14.5	-10.8	-11.4
Monetary Sector	(Annual percent change)				
Pma assets	-0.6	10.0	9.8	8.5	3.2
Banks assets	5.6	6.6	12.7	11.6	1.7
Direct credit facilities	9.3	19.0	18.0	16.8	5.1
Of which: to the private sector	17.7	19.6	24.7	20.1	8.6
Customer deposits	7.6	8.1	9.8	13.0	2.0
Of which: from the private sector	6.9	10.4	10.4	13.2	3.3
Balances abroad	5.9	-16.5	11.1	-19.4	-7.2
Ownership equity	7.7	0.0	14.9	12.4	1.1
Of which: paid-up capital	5.2	-1.5	11.5	8.0	5.0
Memorandum Items					
Real GDP (USD Million, 2015 = 100)	12,252.9	12,673.0	13,269.7	13,686.4	13,810.3
Nominal GDP (USD Million)	12,715.6	12,673.0	13,425.7	14,498.1	14,615.9
Al-quds stock market index (point)	511.8	532.7	530.2	574.6	529.4
Exchange rate (USD/NIS)	3.57	3.89	3.81	3.61	3.59

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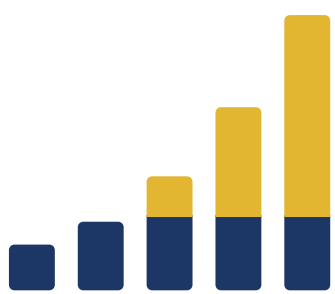
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Chapter One

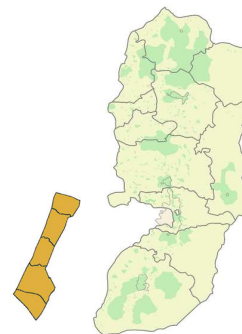
Macroeconomic Developments





2018

Economy



Population

4.85 

Million

Real GDP

13.81 

USD Billion

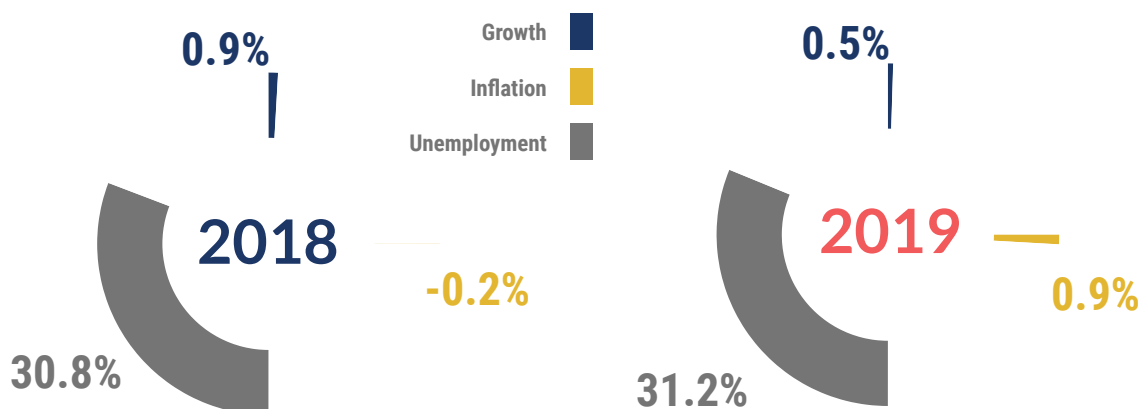
GDP per Capita

3.02 

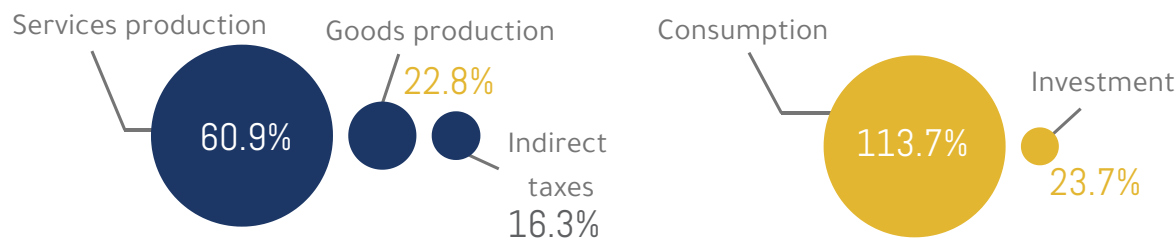
USD Thousand

Main Economic Indicators

PMA Forecasts



Production and Demand as a Percentage of GDP



Overview

2018 is described as a year of economic slowdown, following a series of events that cast a shadow over the performance of the major economies and the overall global economic activity. At the forefront of this is the escalation of trade tensions between the United States and China, the tightening of China's credit policies to curb lending in the shadow banking sector, the turmoil in Germany's automotive industry following the introduction of new emission standards, and the United States decision to reimpose its sanctions on Iran. Consequently, the global economy failed to maintain the momentum of the past year and early 2018. The second half of the year saw a marked slowdown following a slowdown in industrial production and trade.

So did the Middle East and North Africa, where conflicts and political unrest continued, and tensions between the United States and Iran that ended with sanctions against Iran. Overall, economic slowdown prevailed in the region, with the exception of some Gulf Arab countries that benefited from the relative recovery of oil prices.

Domestically, in 2018, the Palestinian economy faced additional obstacles and challenges, mostly due to external factors, starting with the United States administration's suspension of funding for the United National Relief and Works Agency (UNRWA), cut off its budget support, reduce development support, move the U.S. Embassy to Jerusalem, and close the PLO's Washington office and its bank accounts. Internally, the subject of the Social Security Law dominated the attention of the Palestinian citizens, which led president Mahmoud Abbas to issue a decree law to stop the enforcement of decree law no. (19) of 2016 about social security and its amendments starting from 28/01/2019.

In addition to previous developments, uncertainty and persistent political deadlock continued as the negotiation process stalled. As well as the economy's constant dependence on grants, which continued to dwindle, and its work within a multi-currency monetary of issuing countries, in addition of being affected by global prices of commodities, especially oil and food.

2018 ended with a further slide of the Palestinian economy into the trap of economic slowdown for the second year in a row, due to the large downturn in economic activity in Gaza Strip following the reduction of government spending, the decline in investment and the worsening of the trade deficit. This was accompanied by deterioration in construction and industry activities, record high unemployment levels, and price deflation. In addition, the slowdown in West Bank activity against the backdrop of slack public spending, investment and sluggish exports, along coinciding with weak industry and construction which was reflected in a marked slowdown in the GDP of the West Bank amid muted inflation as it was about three years ago. The PMA's forecast show a continued slowdown in 2019 and that the economy will not succeed in generating enough jobs, which will increase unemployment rates. This happens in conjunction with minor inflation.

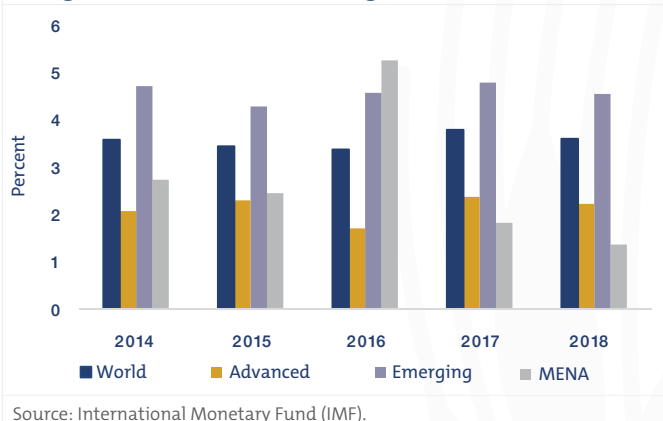


Global and regional economic performance

At the beginning of 2018, the global economy continued its strong growth, supported by improved industrial and trade activities worldwide. However, this recovery was short-lived in light of the events made by the world's largest economies. U.S. trade policy resulted in the introduction of tariffs, to which some countries, particularly China, responded with corresponding protection measures, heightening global trade tensions, and at the end of the year, the United States re-imposed economic sanctions on Iran. For its part, China moved towards tightening regulatory measures in the financial sector to rein in the shadow banking economy. Germany's automotive industry was also affected by the introduction of new emission standards. While the Japanese economy suffered from natural disasters. In light of these events, corporate confidence declined, uncertainty towards the economic policies of many major economies worsened, and the global economy experienced a marked slowdown, particularly in the second half of the year.

Both major groups of countries experienced slowdown. The slowdown in growth in China and India resulted in a declined growth of the emerging and developing countries from 4.8 percent in 2017 to 4.5 percent in 2018. Among the major economies of the advanced countries, the United States economy relatively accelerated due to strong consumption. Otherwise, growth slowed significantly in both the Eurozone and Japan, leading to slowdown in growth of advanced economies' group as a whole from 2.4 percent to 2.2 percent.

Figure 1-1: Global economic growth rates, 2014-2018



As a result, the global economy recorded a growth rate of 3.6 percent compared to 3.8 percent in 2017 (the best in nearly 7 years). Amid the declined investors' confidence, until the major economies begin to reverse the slowdown and move forward towards boosting growth, taking advantage of the easing of monetary policies in the absence of inflationary pressures, which would restore momentum to the global economy again. However, this will not be enough to accelerate the global growth rate, which is expected to stabilize at 3.3 percent by the end of 2019 as a result of slowing growth in both the advanced countries (1.8 percent) and in the emerging and developing countries (4.4 percent).

With the lack of momentum in growth in 2018, the majority of the major economies maintained the same level of low interest rates, particularly China, Japan and the Eurozone. On the other hand, in light of the strength and soundness of the recovery process, the Federal Reserve repeatedly raised the interest rate on the dollar during the year, raising it four times in March, June, September and December at 25 base point each time, to settle at 2.5 percent.

Regionally, the Middle East and North Africa region was subject to years of conflicts and geopolitical turmoil in many countries, particularly in Syria, Yemen and Libya, whose economies continued to slowdown, as well as internal tensions in Sudan at the end of the year following grassroots demonstrations against the political and economic system. The end of the year also saw the United States of America apply its sanctions on Iran, which clearly pushed the economy into downturn. On the other hand, the Gulf States, led by Saudi Arabia, have succeeded in accelerating growth rates, taking advantage of the surge in oil prices during the first three quarters of the year. With expectations of a further

rise in the light of the agreement concluded by the so-called “OPEC Plus”^[1], end of 2018 about reducing production by 1.2 million barrels per day starting next year for 6 months. Overall, and due to the downturn of the economy in countries such as Iran, Yemen, Sudan, or the sharp slowdown in countries such as Libya and Morocco, the entire group has seen the growth rate decline from 1.8 percent to about 1.4 percent, the lowest in about 9 years. Fears of increased oil price volatility remain against a backdrop of uncertainty, which could have a negative impact on the budgets of oil-exporting countries and may also extend to importing countries through a decline in remittances from expatriates. The pace of foreign trade and investment spending rates is also expected to decline, thus slowing the growth of the region as a whole to 1.3 percent in general 2019.

Box1 : Global Economy 2019: Close to Recession, Far from Growth

Despite a strong start of growth of the global economy in 2018, the whole year was full of market volatility, political turmoil and economic uncertainty. It seemed that 2019 would see a deepening of the turmoil into the global economy. The outlook for the global economy is more pessimistic in light of the rise in global indebtedness; the great fear of a recurrence of the global financial crisis in the euro zone; and a recession in the U.S. economy as a result of high rates of interest. In addition to the raging trade war between the United States and China.

In this context, a group of international institutions and organizations issued five desperate economic forecasts awaiting the world in 2019. However, these expectations should not be seen as inevitable, they at the same time paint a more objective picture of what the global economy may be witnessing during 2019 and the necessary precaution against these risks. And these expectations are:

First: Low Global Economic Growth Forecast

The International Monetary Fund (IMF) again lowered its global economic growth forecast for 2019 by 0.2 percentage points to 3.3 percent, most notably due to the U.S.-China trade war. “Christine Lagarde” IMF Manager Director warned world leaders of the outlook that the rapid growth of 2017, will not be back soon. She said that “the risks were starting to come true all over the world. Geopolitical threats were more pressing, activity was slowing almost everywhere, and markets seemed feverish”.

The Organization for Economic Co-operation and Development (OECD) also lowered its global economic growth forecast to 3.5 percent in 2019 from 3.7 percent in earlier forecasts. The Secretary-General of the OECD José Ángel Gurría Treviño said that trade conflicts and political uncertainty increased the difficulties governments faced in ensuring that economic growth remains strong, sustainable and inclusive.

Second: The Clouds of Trade War will Intensify Next Year

The new policy of the United States of America and its launching of a war of trade tariffs on world economies, primarily China, seems to have put the world economy on a volatile path. In the absence of signs of a breakthrough in this crisis, trade war clouds will intensify further during 2019. This will have negative effects on the global economy and markets, particularly emerging ones.

The Bank for International Settlements (BIS) warned that rising trade tensions between the United States and China could lead to a serious economic downturn. “Christine Lagarde” called during IMF and World Bank meeting in Bali-Indonesia, on world leaders to reform global trade regimes rather than seek to undermine them, she said “we need to work together to ease tensions and resolve current trade disputes, we need to come together to reform the current trading system, not destroy it.”

[1] Refers to OPEC's cooperations with non-OPEC producers to effect production cuts.



Third: Brexit

Brexit is the biggest event in the global economy in 2019, especially as the negotiations surrounding Brexit have played a key role in European politics throughout 2018. It will become even more important in 2019 with Britain targeting the exit on March 29, 2019 and extending it to October 31, 2019.

Although the date has expired (extending it to October 31, 2019) it remains unclear what the nature of Brexit process will be? What impact will this event have on domestic and global markets, and how this exit will affect the U.K. and the European Union? There is still little chance that secession will not occur at all, according to some optimistic experts.

Fourth: Oil... Expectations of a Surplus on Display and Enormous Stock Increase

The world oil markets may not have (for the past four years) experienced such a rapid change in circumstances in just one year, as they are now witnessing. Before the end of 2017, hopes were high about an increase in the level of global economic growth during 2018 and then the rising growth of oil demand. However, the picture of the situation now with respect to the growth forecast in 2019 is the opposite of the picture on which expectations were built before the beginning of 2018.

Fifth: Warnings of a New Global Financial Crisis

Fears of a new global financial crisis are growing nearly 10 years after the last financial crisis. Global financial markets are experiencing a slump and record declines, as well as a drop in oil prices, high levels of debt and other threats of a looming financial crisis. For its part, the World Bank warned that the world was not only waiting for a financial storm, but did not seem to be ready for it.

Despite all the previous negative indicators, economic analysts refuse to see all this as an indicator of a future financial crisis, or even comparing the current situation to the situation before the global financial crisis in 2008 for many reasons. The first of which was the crisis in the banking sector that occurred before 10 years and led to violent waves, while the current crisis is the inflation of the stock market and not in the financial markets.

To sum-up: These and other factors are likely to add to concern about 2019 and the global economy's transition to recession. In addition to the major economies, several countries such as Argentina, Brazil, Venezuela, Turkey and Russia will suffer from several economic problems.

As for the neighboring countries, the growth of the Israeli economy fell below expectations, and slipped to deceleration for the second consecutive year, due to weak export growth against the continued increase in imports, which pushed the surplus trade balance to unprecedented lows. On the other hand, in light of the continuous rise in inflation during the year, which reached close to the target level, the Bank of Israel raised the official interest rate at the end of the year for the first time after it was stabilized for more than three years (to 0.25 percent). On the whole, the Israeli economy's growth has declined by about 18 base point, to settle at approximately 3.3 percent with expectations that the economy will continue to slow in 2019 against the backdrop of the expectation of slowing private consumption and weak external demand.

Similarly, the recovery process in the Jordanian economy stalled as a result of the slowdown in agriculture, trade and the majority of services and industrial activities, as well as the continued downturn of the construction sector. In this context, Jordan faces many challenges in implementing its financial reform program signed with the IMF in mid-2016, which prompted the government at the beginning of 2018 to pass tax increases on many goods, particularly fuel, as



well as to lift subsidies on bread. Moreover, the Central Bank of Jordan raised the official interest rate on the dinar three times during the year in line with its rise on USD (Jordanian dinar is pegged to USD). As a result, preliminary findings indicate that the Jordanian economy slowed during the year, with the growth rate declining slightly by 0.1 percentage point and reached 2.0 percent-its lowest growth rate in years. However, it is expected to slightly accelerate to 2.2 percent in 2019.

In Egypt, which is also subject to an IMF reform program, its economy has recovered relatively in light of the improvement in both private investment and exports, accelerating its growth rate to its highest level in nearly a decade, to nearly 5.3 percent compared to 4.2 percent in the previous year. This was accompanied by a relative decline in its hyper inflation, especially at the beginning of the year, which prompted the Central Bank of Egypt to reduce the interest rate twice during the first quarter of 2018. This economic acceleration is expected to continue in 2019, with a growth rate of about 5.5 percent under the government's implementation of a series of economic reforms aimed primarily to access to global markets and attract more foreign investment.

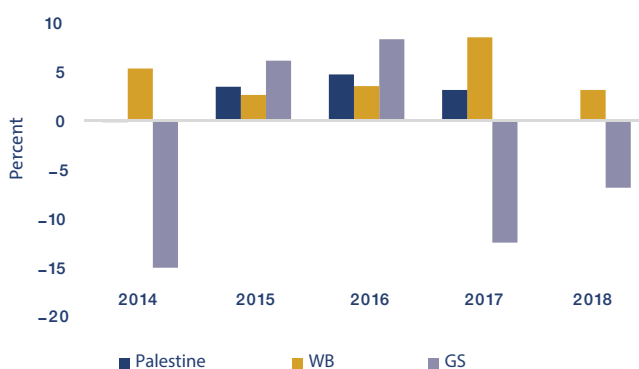
Local economic performance

As it was previously expected by the PMA, preliminary estimates of national accounts revealed a slowdown in the Palestinian economy in 2018, growing by 0.9 percent compared to growth of 3.1 percent last year, bringing real GDP (at 2015 prices) to about USD 13,810.3 million^[2]. The majority of demand components have slowed, as well as exacerbated leakage resulting from the acceleration of imports. In general, the overall slowdown in the economy was the result of a large downturn in the Gaza Strip economy, as well as continued loss of momentum in the West Bank economy.

The Gaza Strip economy has slipped into a recession after experiencing a decline in GDP for two consecutive years, influenced by continued decline in government spending following the stabilization of the Palestinian government's mid-2017 measures to stop the disbursement of some allowances on salaries of public sector employees in Gaza Strip. In addition to the continued deterioration in investment as a result of the continued blockade and closure since 2006, and the successive wars that have been experienced in the Gaza Strip since then. As well as the decline in external support, both for development projects and for some vital institutions such as the UNRWA, which benefits a large proportion of Gazan families. On the whole, Gazan GDP shrank by about 12.5 percent and 6.9 percent in 2017 and in 2018, respectively, to depreciate by the end of 2018 to an eight-year low, to settle at nearly USD 2,767.0 million (2015 prices).

In the West Bank, the political level faced major challenges in light of successive U.S. decisions against the Palestinian cause, which have affected the economic situation in many respects, particularly with regard to external financing (ending supporting the Palestinian Authority's budget and reducing development grants), and produced more anxiety

Figure 1-2: Real growth rates in Palestine, 2014-2018



Source: Palestinian Central Bureau of Statistics (PCBS).

[2] Palestinian Central Bureau of Statistics (PCBS), 2019, preliminary data subject to change.



and increased uncertainty. As a result, the West Bank economy continued to achieve moderate growth rates (3.1 percent) but missed the momentum it experienced last year with its growth at that time by about 8.5 percent. The size of the West Bank's GDP reached at the end of 2018 approximately USD 11,043.3 million (2015 prices).

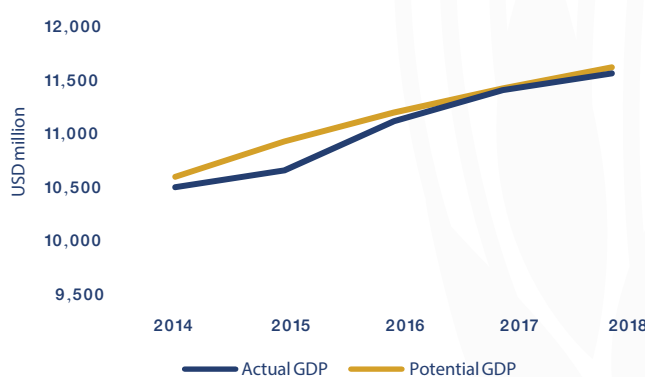
Since the establishment of the Palestinian National Authority in 1993, the Palestinian economy in both the West Bank and Gaza Strip has been subjected to many internal and external shocks that have greatly hindered its progress and development, causing apparent fluctuation in many main overall indicators. These shocks, for example, have resulted in a weak real GDP in both the West Bank and Gaza Strip, but to varying degrees depending on the different circumstances and economic and political factors. Over the past 25 years, the West Bank economy managed to double its size by about 2.5 times only, i.e. the GDP took about 10 years to double itself. The picture looks even worse in Gaza Strip, where the economy has not succeeded in doubling itself even once in all these years. Additionally, its total growth did not exceed 50 percent throughout this period growing at a rate of 2 percent only on average every year, which indicates that its growth is still below the rates needed to close the production gap, keep pace with the increase in population and the increase in the number of those joining the labor market.

These shocks have kept the Palestinian economy running below its potential level, i.e. the level of actual GDP is still below the potential level that would be achieved in a given period if the optimal employment conditions for economic resources were met. The actual deviation level can be measured (at factor cost) compared to the level of potential GDP^[3] through what's known as the output gap^[4]. Analysis of the output gap under the circumstances in Palestine shows that the potential GDP at factor cost in 2018 grew by 1.7 percent compared to 2017 to hit USD 11,610.6 million. At the same time, actual real GDP at factor cost grew by 1.4 percent leading to rise

below the potential GDP level (to about USD 11,554.6 million only) resulting in a negative output gap for the fifth year in a row. So, the actual GDP achieved over the years 2014-2018 was less than the economy could achieve, due to the unstable economic and political conditions that the economy experienced during those years, both in the West Bank and the Gaza Strip. This analysis also reflects the growing size of this gap, which hit USD 16 million in 2017 and rose to USD 56 million, or 0.5 percent of the potential GDP in 2018 but it remains below average in recent years, especially in the years following the Israeli war on the Gaza Strip in 2014.

On the other hand, per capita GDP is one of the channels through which the actual impact of economic performance is reflected, as enhancing per capita income levels directly contributes to improving social welfare. In 2018, the trend of change in per capita income was consistent with the growth trend of the Palestinian economy in both the West Bank and Gaza Strip. In light of the economic slowdown, per capita income in the West Bank has not been able to grow by more than 0.8 percent to hit approximately USD 4,188.3. In Gaza Strip, per capita income clearly shrank again by about

Figure 1-3: Actual and potential output in Palestine, 2014-2018



Source: Palestine Monetary Authority (PMA).

[3] GDP at real market prices excluding net indirect taxes.

[4] Production function methodology is used to estimate potential GDP.

9.5 percent to drop to an all-time low (USD 1,431.4). The average per capita income in the Gaza Strip currently accounts for about one-third of the West Bank' income, while it constituted 85 percent on average during the years between the establishment of the Palestinian National Authority and the outbreak of the Al-Aqsa Intifada in 2000. Overall, Palestine's GDP per capita was about USD 3,021.4, down about 1.7 percent from the previous year.

Economic activities

The Palestinian economy is predominantly service-oriented, with service production activities contributing for the most total value added. During 2018, there was no radical changes to this distribution, and service activities retained about 61.0 percent of the total value added. However, the components of service production activities undergone some minor changes, most notably the decline in the contribution of service sector^[5] in value added by 1.4 percentage point in favor of trade sector. Overall, service sector contributed approximately 30.9 percent followed by trade sector, which contributed about 20.7 percent of the total value added. The rest of the service production activities; transport and storage, financial and insurance, and telecommunications, have contributed by 1.8 percent, 4.0 percent and 3.5 percent, respectively.

Alternatively, goods production activities contributed about 22.8 percent of GDP, down about 0.5 percentage points from last year. Industry sector comes first (13.2 percent) followed by construction sector (6.5 percent) and finally agriculture activity (3.0 percent). In addition to the added value generated by both the service activities and goods production activities, net indirect taxes (customs and import taxes), which declined a little during 2018 to decrease its contribution to GDP from 16.7 percent to 16.3 percent.

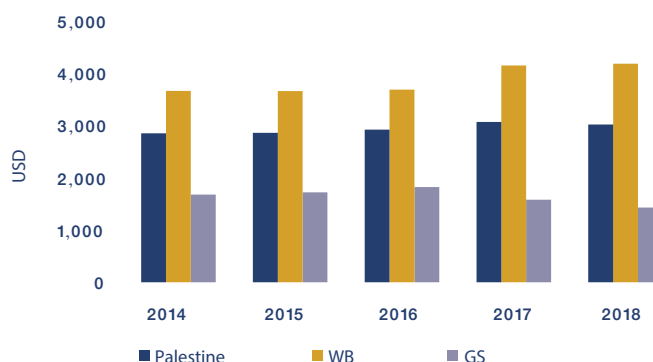
Looking at the level of the contribution of various economic activities to the growth rate, the contribution^[6] of goods production activities exceeded service activities by contributing more than two-thirds of the growth achieved in 2018 (0.7 percentage points in the growth rate) compared to service activities contribution of about 0.5 percentage points.

The remarkable contribution of goods production activities comes from agriculture which witnesses positive contribution for the first time in years (0.2 percentage points) and the increased contribution of industry (0.4 percentage points) despite a significant decline in the contribution of construction (0.1 percentage points). However,

[5] These include accommodation and catering services, real estate activities, professional technical services, administrative services, education and health, public administration and defense ... etc.

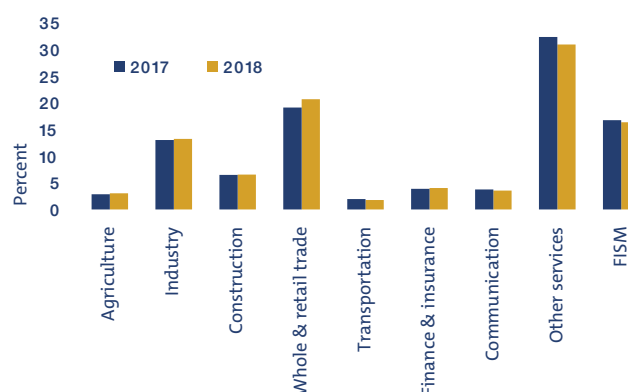
[6] Activity contribution to growth rate = growth rate in economic activity during the current year x the contribution of the economic activity in the GDP of the previous year.

Figure 1-4: Real GDP percapita in Palestine, 2014-2018



Source: PCBS.

Figure 1-5: Contribution of economic activities to GDP, 2017-2018



Source: PCBS.



the contribution of the majority of service production activities discouraged economic growth during the year. The performance of the services sector has negatively affected the Palestinian economy and weakened the rate of economic growth by 1.1 percentage point, along with another negative contribution from transport and storage, and communications of about 0.2 for each of them. On the other hand, the financial and insurance activities made a positive contribution to the growth rate of about 0.2 percentage points but declined compared to the past year. The most prominent contribution of the service production activities was the trade sector,

whose growth was the main driver of the growth of the Palestinian Economy during the year (1.7 percentage points) without it, the economy would have fallen into a shrink by about 1.0 percent. On the other hand, net indirect taxes contributed to discouraging growth rate by about 0.2 percentage points.

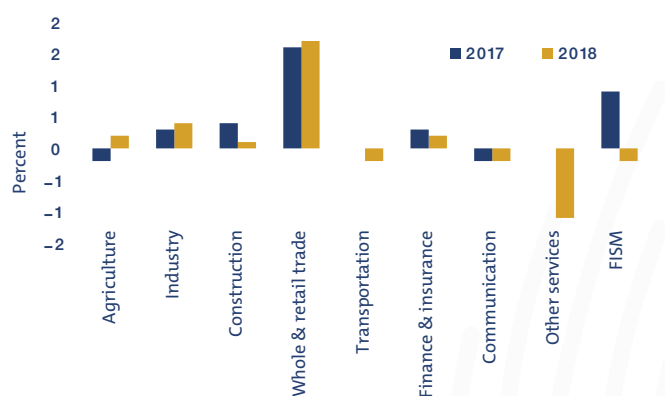
Aggregate Demand

Most real aggregate demand's components have experienced negative developments in 2018, primarily as the trade deficit increased to more than 37 percent of the GDP as exports continued to weaken and imports rose to a new record high (about three times as exports). Export growth of 7.9 percent failed to bridge the gap with imports, which in turn grew by about 7.0 percent. This comes under the continued negative influencing factors that directly affect foreign trade conditions such as import and export procedures, occupation control over trade ports, and other factors that increase the cost of production

and thus reduce Palestine's competitiveness compared to its trading partners. On the other hand, investment has slowed significantly, growing by 5.7 percent compared to 10.0 percent in the previous year, while government spending maintained its previous growth rate (0.9 percent). However, the most important change this year was the private consumption, which grew by about 1.4 percent, compensating its downturn by 1.7 percent in 2017 (1.8 percent). It is worth to mention the increase in the household consumption while the consumption of non-profit institutes serving households (NPISH) has dropped in light of the declined foreign funding.

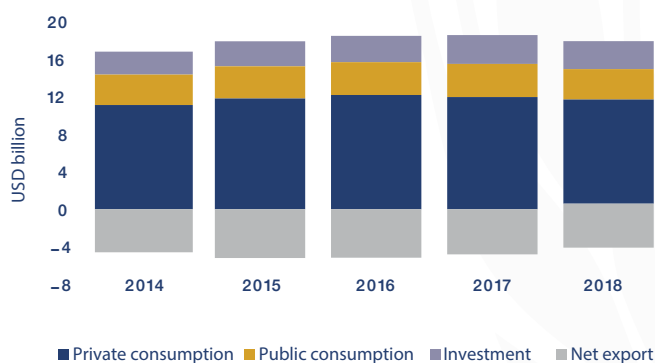
In the West Bank in particular, the foreign trade worsened as the export slowed down (grew by 7.7 percent compared to 12.3 percent in the previous year) and imports rose to set a new record (grew by 5.8 percent compared to a contraction of about 2.3 percent in the previous year), pushing the trade deficit to increase (grew by 4.5 percent compared to decline by 10.0 percent in the previous year). Against the backdrop of the many challenges witnessed by the Palestinian

Figure 1-6: Contribution of economic activities to growth, 2017-2018



Source: PCBS.

Figure 1-7: Real aggregate demand in Palestine, 2014-2018



Source: PCBS.

government during the year, as grants to support the budget shrunk, growth in government spending slowed to 2.6 percent from last year's leap of 22.7 percent. On the other hand, investment experienced some improvement as its growth accelerates to 8.7 percent compared to 6.1 percent in the previous year. Private consumption also succeeded in re-growing (about 1.9 percent) after shrinking at about the same rate in 2017.

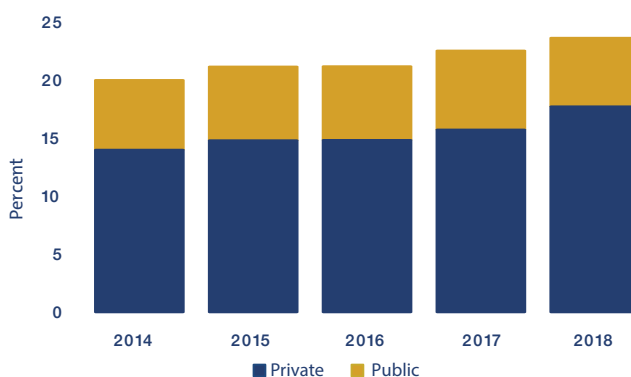
In the Gaza Strip, the majority of demand components declined for the second year in a row, putting the economy in a state of stagnation. On the one hand, government spending continued to shrink by 4.2 percent besides a bigger decline (34.2 percent) in 2017, in the wake of the continued actions taken by the Palestinian government in the middle of 2017 that included the suspension of some allowances for public sector employees in Gaza. Investment also experienced a new decline of 13.4 percent compared to a rise of about 44.4 percent in 2017. The level of investment in Gaza is constantly deteriorating in light of the continuing blockade and closure since 2006 and the successive wars suffered by the Gaza Strip, where the value of investment has shrunk by more than half compared to its pre-blockade level. In light of the decline in government spending, the decline in externally funded development projects and the scarcity of UNRWA funding that benefits a large proportion of households in Gaza Strip, private consumption failed to grow and remained at the low levels recorded in 2017. Despite the growth of both exports (11.4 percent) and imports (14.3 percent), the volume of foreign trade remains below pre-embargo levels, and the acceleration in import growth over exports resulted in an increase in the value of the trade deficit, reaching more than one third of the GDP.

Looking at the shares of the GDP components during 2018, it was relatively stable in the West Bank, unlike in Gaza Strip which witnessed notable changes. Final consumption in Gaza Strip continues to account for the largest proportion, exceeding the value of total GDP (about 126.4 percent) as a result of mainly the significant rise in private consumption (95.9 percent private consumption vs. 30.5 percent public consumption). The same applies to the West Bank, although the share of final consumption to total GDP is less than in Gaza Strip, it still exceeds the value of the GDP, constituting approximately 110.5 percent of the GDP (including 86.0 percent private consumption and 24.5 percent public consumption). On the other hand, the share of investment rose slightly in the West Bank from 25.0 percent to 26.3 percent whilst it fell in Gaza Strip to about 12.9 percent compared with 13.9 percent the year before.

Investment in Palestine is characterized by being weak under the unstable environment, especially after 2000. The blockade, the closures and the imposed restrictions imposed over the past years have all weakened the public sector and hindered the private sector's position as the leverage for the economy under the lack of incentives among investors, and therefore investment has mostly declined.

In general, the contribution of public investment to the total investment in Palestine is low, and in most cases does not exceed one-third of the total investment. During 2018, with the decline in the value of government development projects financed by foreign donors, public investment weakened, and its share to GDP declined to 5.9 percent compared to 6.8 percent last year. Conversely, the value of private investment increased, thus increasing its share of GDP to 17.7 percent.

Figure 1-8: Investment as a percent of real GDP, 2014-2018



Source: Estimates by PMA & PCBS.

As for the share of foreign trade, the increased exports'

share in the West Bank was undermined by a faster increase growing share of imports, which increased the trade



deficit to GDP to 36.8 percent. The same applies to the Gaza Strip, which suffers from a weak foreign trade contribution in the light of the blockade and closure. The modest growth in Gazan exports' share was not enough to counter the dramatic rise in imports, which have pushed the trade

In general, the Palestinian exports are much lower than imports, and particularly in Gaza Strip. This is linked to many factors, mainly the weak competitiveness of Palestinian products in foreign markets, due to high production costs in the light of obstructions and restrictions imposed by the Israeli occupation on

freedom of movement and access, as well as the destruction of infrastructure. In order to drive growth and sustainable economic development, plans must be adopted to increase the volume of Palestinian exports, increase the value added of these exports, and access to foreign markets other than the Israeli market, in order to enhance the position of the external sector in the Palestinian economy.

Doing Business

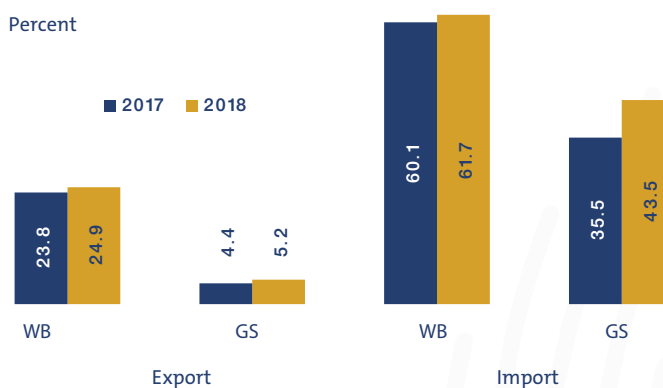
The World Bank Group annually publishes a report on ease of doing business in 190 countries around the world, based on a set of quantitative indicators related to the business environment in accordance with best practices. According to its latest report issued at the end of October 2018, Palestine has experienced a slight progress in the ease of doing business index. The value of the index rose by 0.39 point to 59.11 point against the backdrop of the progress of two of the 10 factors that make up the index; getting electricity, which measures the number of procedures, time and cost to get connected to the electrical grid; and registering property, which monitors the procedures, time and cost involved in registering property, assuming a standrized case of an entrepreneur who wants to purchase land and building that is already registered and free of title dispute. In addition, it also measures the quality of the land adminstration system in terms of its geographical coverage, transparency of information, land disputes resolution, ect.

On the other hand, there was a slight decline in factors measure the ease of starting a business, and the ease of dealing with construction permits, in terms of time, cost and procedures until the completion of the construction. As well as a slight decrease in the factor of paying taxes. While the remaining five indicators have maintained the same level since the previous report.

Palestine has a very advanced ranking in terms of the access to credit, which tests the strength of credit reporting system, and the effectiveness of collateral and bankruptcy laws in facilitating access to finance. Palestine also maintains its leadership in this index at the level of the Middle East and North Africa region, neighboring countries, and many European countries. This is achieved because gettingcreditin Palestine (in terms of system and legislation),the protection of rights, the growth in facilities and the low registered levels of defaults are evolving according to the best international standards.

It is worth noting that Palestine has obtained its highest mark in the subject of ease of cross-border trading, despite the difficulty of import and export movement. This is due to the methodology followed in the claculating thid index,

Figure 1-9: Net exports as a percent of real GDP, 2017-2018



Source: PCBS.

which taking into account the trade (import and export) with the main trading partner exclusively, which is Israel in case of Palestine. Accordingly, the associated time and cost from trading with Israel are very low compared to the majority of economies around the world.

Palestine ranked 116th out of 190 countries registered in this index, down from 114th. However, this is not due to the decline in Palestine's performance but it is due to the accelerated pace of progress made by some other countries, namely Brazil and Djibouti, which preceded Palestine in their rankings this year. Israel, the most prominent and geographically closest trading partner, is ranked 49 next to the world's advanced economies. However, Palestine reserves a middle position among the Arab countries, where it has been ranked 11 among the 22 Arab countries. The UAE, Bahrain, Oman, Tunisia, Qatar, Saudi Arabia, Kuwait, Djibouti and Jordan are ahead of Palestine.

Box2 : Entrepreneurship and Innovation and its Impact on Economic Development

The term entrepreneurship or business entrepreneurship is associated with the process of creating a new business or developing an existing one. The entrepreneur is an innovative and adventurous person who has the ability to take risks, looking for change and creating new opportunities for himself, his business community and the field in which he works. These people play a pivotal role in promoting trade and economic development through their practice of innovation.

Innovation is the most important pillar in enhancing competitive advantage in business and building and developing a competitive, strong and sustainable economic activity. Entrepreneurship and innovation have many advantages and benefits that benefit the individual and society as a whole, including:

1. Creating jobs and reducing unemployment: creating a new entrepreneurship or developing an existing enterprise aims first to creating job opportunity for the entrepreneur himself/herself and then creating job opportunities for others. Hence, enterprises reduce unemployment and boost economic development.
2. Develop new commodity and service products or develop existing products: Innovation is primarily aimed at providing new products or developing old products that are demanded by consumers.
3. Opening up new markets: Entrepreneurship creates new markets or expands existing markets domestically and internationally through export.
4. Entrepreneurship and innovation create a competitive business and production environment, thus improving quality of products and raise productivity and the transfer of technology, and development of industries and promote export.
5. Entrepreneurship and innovation raise the level of individual and community income, thereby reducing poverty and promoting development.

The central and important role of entrepreneurship and innovation in promoting economic development is evident, especially as innovation and technological development are key factors for economic growth. Innovation changes the structure of the economy and raises the level of technology in the production process, and the trend towards higher value-added economic activities (Szirmai et. al, 2011).



Growth theories (self-growth theory and developmental growth theory) emphasize that the return on production factors: capital or labor is a decreasing return. Meaning that the increase in capital or the number of workers increases the volume of production but the continuous increase in one or both of these factors increases the volume of production but at a lower pace and does not correspond to the pace of the increase in the number of workers or the increase in capital. However, investment in knowledge and innovation leads to a steady increase in production volume through the positive indirect effects of innovation on the production process (Romer, 1990).

The Endogenous growth theory suggests that developed countries benefit more from developing countries in terms of knowledge investment, due to their superior innovation system through two channels: first, that developed countries invest heavily in research and development; second, the rapid transfer of technology and knowledge in developed economies compared to developing economies.

On the other hand, evolutionary growth theory suggests that developing countries can catch up with developed countries in the field of development by taking advantage of innovative technology in developed countries without incurring the costs of their innovation and the risk of investing in it. The adoption of technology from developed countries by entrepreneurs in developing countries provides them with the ability to create new markets and create structural change in the economy.

Undoubtedly, there are entrepreneurs with more innovation capabilities than others, and there are successful entrepreneurs in more countries than in other countries. This is due to a number of factors and determinants, which can be summarized in three main points:

1. **Company or Entrepreneurial Characteristics:** The characteristics available in the entrepreneur such as the educational level, experience and characteristics of the company such as age and size are important factors in determining the success and superiority of the entrepreneur.
2. **Market Conditions:** In principle, the entrepreneur's incentive is profit (Schumpeter, 1934). But as Adam Smith says, the entrepreneur offers benefits to the community through his/her quest for profit. Therefore, there is a link between the entrepreneur's ability to engage in the innovation process and the size of the market and its work mechanism. That's why markets have an important role to play in the development process. Thus, markets in poor countries have failed to play their role in the development process, where the markets of developing countries are small, dispersed and incomplete (imperfect markets) as a result of weak infrastructure and low income, which limit entrepreneurs' capacity to innovate.
3. **Institutional Policies and Environment:** Government policies and institutional development play an important role in enhancing the role of entrepreneurs and encouraging innovation. Unsuccessful policies and institutional barriers (lack of political stability, transparency and integrity) which many developing countries have, inhibit entrepreneurial capacity to innovate and reduce returns on innovation. Foreign trade is a source of inspiration for entrepreneurs through new ideas and technology, so policies that place barriers to international trade limit innovation and thus development and catching up with developed countries. Property rights violations and weak contract enforcement are important institutional barriers in discouraging entrepreneurs and reducing innovation.

Finally, there is an important role for the government in motivating entrepreneurs and encouraging innovation by providing educational policies that encourage innovation and motivate entrepreneurs. Innovation is not only the presence of entrepreneurs, but also the availability of trained and highly skilled workers. Effective education policies and capacity building are therefore elements of encouraging innovation. In this regard, many governments of developed and developing countries have adopted "innovation policies" promoting innovation as an important factor in economic and social development.



At the local level, Palestine attained a remarkable achievement, the first of its kind, through the participation of a number of Palestinian companies and with the help of the Palestinian Trade Center (PalTrade) at the Halal International Exhibition held in the Malaysian capital Kuala Lumpur. One of the Participating Palestinian Companies received the Most Creative Product Award of the Year 2019 among more than 1,000 companies representing 40 participating countries.

The company received this award for its product derived from olive leaves, which was considered as a pioneering idea. Relying on scientific research and modern technology to extract the natural active substances needed to manufacture clinically proven nutritional supplements to the immune system, slowing down the absorption of sugars in the body, which positively affects diabetics, making its product unique as the world's leading product specialized in this field.

The jury (consisting of nine members from different government bodies in Malaysia) adopted in its decision a number of criteria related to: the creativity of the idea, in particular its positive impact in the fight against diabetes, the quality of the product, its compliance with the global specifications and standards, and its clear distinction from competing products, in addition to the way of presentation. The product is certified with Good Manufacturing Practice (GMP). Moreover, the product was able, in record time, to prove its effectiveness, and to invade several markets. It is worth mentioning that the Halal International Exhibition attracts huge numbers of participants and investors from all over the world annually to see the available investment opportunities. It is a platform for SMEs to showcase the brand and halal services to the world.

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Prices, inflation and purchasing power

Commodity prices in global markets experienced frequent rises during the first half of 2018, but the economic slowdown and weak global demand during the second half of the year led to lower levels of these prices, particularly oil and food. After oil prices gained momentum following production cuts by OPEC and non-OPEC producers, prices rebounded again in the fourth quarter in the context of supply uncertainty, amid U.S. sanctions on Iran and the suspension of oil exports (Prices during October rose to their highest levels in several years).

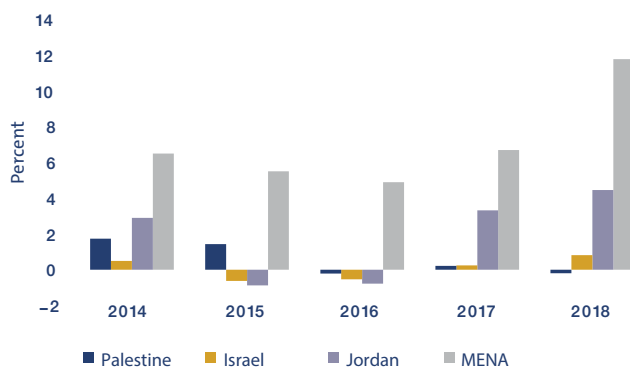
As a result, headline inflation rose slightly in most economies compared to the previous year, but remained below target levels in many countries. In developed countries, despite improved domestic demand over the past two years, wage growth and declining unemployment, inflation rates remain below central bank targets, particularly core inflation rates. These are rates that exclude changes in food and oil prices. Consequently, the overall inflation rate in developed countries was about 2.0 percent during 2018 compared to 1.7 percent the year before.

For its part, core inflation rates in some emerging and developing countries were close to the minimum target of central banks such as in India and Indonesia, but in others, they failed to climb sufficiently to approach these levels. As a result, overall inflation rates rose from 4.3 percent to 4.8 percent between 2017 and 2018. It is worth noting that the rise in inflation in part of the emerging and developing countries is mainly due to the effects of the fall in the exchange rate of local currencies, which in turn caused a rise in domestic prices, and mitigated the impact of the decline in commodity prices at the end of the year.



Political conflicts and unrest in the Middle East and North Africa region have also had an impact on inflation rates, which increased from 6.7 percent to 11.8 percent. This is due to so-called hyperinflation, which hit countries such as Iran and Sudan, where inflation doubled to unprecedented levels, and countries like Libya and Egypt faced very high inflation rates. As for the neighboring countries (Jordan and Israel), growth in consumer prices accelerated, as it grew in Israel from 0.2 percent to 0.8 percent close to the target level. While witnessing a higher acceleration in Jordan from 3.3 percent to 4.5 percent against the backdrop of the government's increased subsidies or tax increases on a range of goods, including bread and fuel.

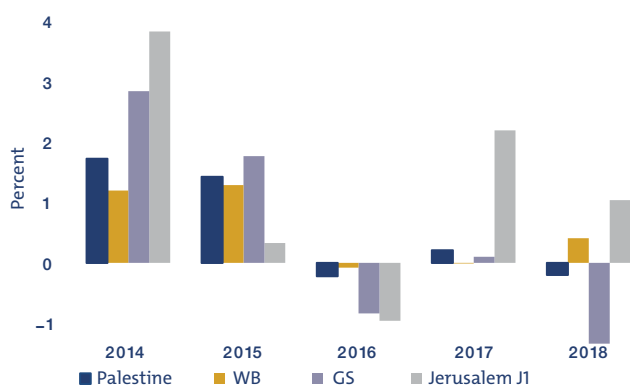
Figure 1-10: Inflation rates, selected countries, 2014-2018



Source: IMF & PCBS.

In Palestine, inflation is relatively low compared to regional and global rates. Its causes are also different in the West Bank than in Gaza Strip, while the former is mainly influenced by price trends in the world market and in Israel, the impact appears to be less in Gaza Strip, which suffers from poor in and out movement of goods. Price determinants also different in the Jerusalem area (J1)^[7], which is usually characterized by high rates. During 2018, with global commodity prices growing for most of the year, and the limited acceleration in the inflation rates of neighboring countries, the rate of inflation accelerated slightly in the West Bank but maintained low levels at 0.4 percent compared to about 0.0 percent last year. In Gaza Strip, prices shrunk by about 1.3 percent compared to relative stability in the previous year (0.1 percent). For its part, prices in Jerusalem maintained growth on average, so they grew by 1.0 percent compared to 2.2 percent.

Figure 1-11: Inflation rates in Palestine, 2014-2018



Source: PCBS.

As a result, these conflicting developments in Palestine resulted in a minor deflation by about 0.2 percent. It is worth noting that the overall level of prices in Palestine have continued to experience limited movements (up or down) for almost three years; hence, prices marginally fell in 2016 by 0.2 percent then rose at the same value in 2017 and dropped in the same value again in 2018. On the whole, average general prices in Palestine remained almost the same for nearly two years.

The twelve price groups experienced limited up and down movement throughout the year. On the one hand, the prices of clothing and textiles declined significantly by about 4.3 percent followed by a drop in tobacco and alcohol prices by 1.3 percent and education by 1.1 percent. The shrunk in furniture prices and food prices amounted to 0.9 percent

[7] This part of Jerusalem, which was forcibly annexed by Israel shortly after its occupation of the West Bank in 1967, includes East Jerusalem, and its extension in the north from Issawiya to Kafr Aqab.

and 0.7 percent, respectively. On the other hand, the prices of cultural and recreational

goods and services increased by nearly 1.5 percent. The prices of transport, medical services, telecommunications, restaurants and café services, and miscellaneous goods and services also increased, with each group growing by about 1.1 percent. This was followed by lower growth in housing prices at 0.8 percent.

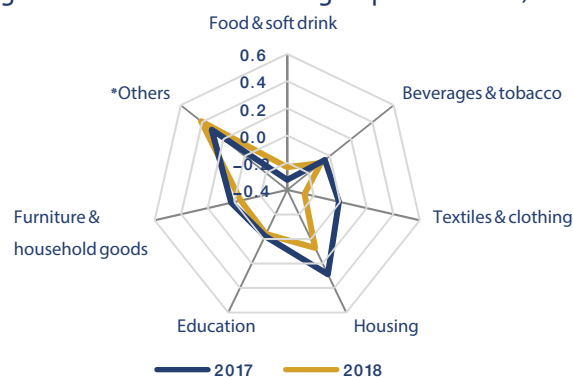
The contribution of price groups to the value of inflation varies depending on their relative weight in the consumer basket. In 2018, lower prices for both food and clothing were the most influential factors for the overall decline in prices, with a negative contribution of 0.23 percentage point for the first and 0.27 percentage point for the second. But it was met with a positive contribution from the transport group, and the group of miscellaneous goods and services by about 0.13 percentage point each. The contribution of the remaining goods and services groups was minor, either positive or negative.

Labor market

The Palestinian population in 2018 was more than 4.8 million (of which 2.9 million were in the West Bank and about 1.9 million in Gaza Strip) according to population projections based on the results of the Population, Housing and Establishments Census 2017. Despite the declining pace of population growth, particularly in the West Bank, which reached 2.3 percent compared to 3.0 percent in Gaza Strip. The population growth rate in Palestine is still high relative to global, even regional, ratios. According to the latest available data from the World Bank^[8], the population growth rate in both Arab countries and Israel has averaged by about 2.0 percent each in 2017 while the global average during the same year was about 1.2 percent.

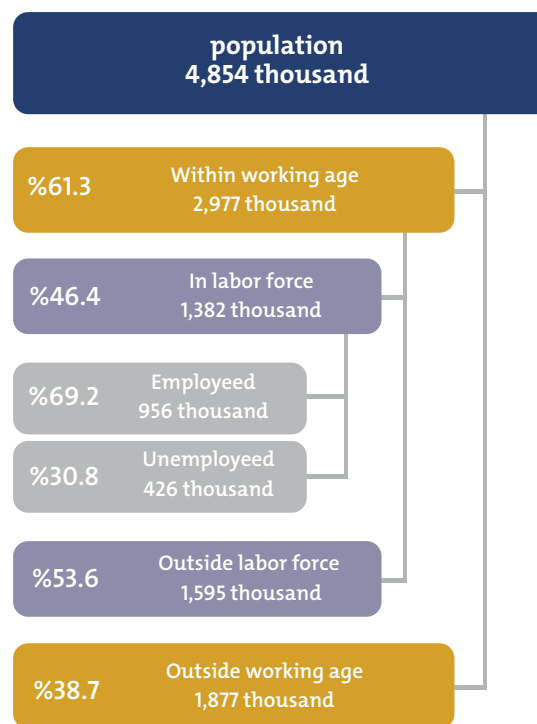
Countries with high population growth rates (due to natural causes), are often characterized by young communities, with a high proportion of school-age individuals. This applies to Palestine, where the population below the working age (under 15 years) is

Figure 1-12: Contribution of CPI groups to inflation, 2017-2018



* Includes medical care, transportation, communications, recreational, cultural goods and services, restaurants and cafes, and miscellaneous goods and services. Source: PCBS.

Figure 1-13: Labor force framework in Palestine, 2018



Source: PCBS.

[8] World Bank database.



approximately 38.7 percent of the total population. This ratio, in turn, is also higher than the global level of about 25.9 percent in 2017, and approximately 33.1 percent in the Arab world and 35.5 percent regionally, and 27.9 percent in Jordan and Israel.

The high proportion of the school-age population results in a high number of people outside the labor market, and therefore a low participation rate (46.4 percent). This means that more than half of the Palestinian society still does not actually contribute to economic activities. The labor market participation rate in Palestine is relatively low compared to global and regional rates, mainly due to the very low participation of females. Although it relatively increased during the current year to 20.7 percent, it was still one of the lowest rates in the world. Male participation was also relatively average at 71.5 percent in 2018. The female participation ratio is measured to the male participation rate to indicate the extent of the gap or convergence between them, which in Palestine was about 24.2 percent, higher than in Jordan (22.0 percent), but significantly lower than in Israel (85.6 percent) and global average (64.1 percent) during the same year.

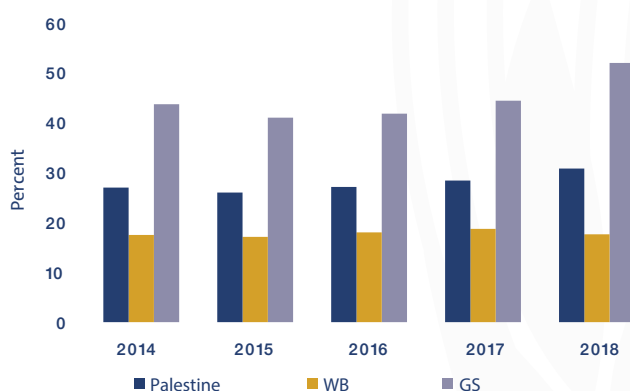
Employment and unemployment

Although the number of participants in the labor market (participation rate) is low, every year many of them become unemployed as the local labor market is unable to create enough jobs. The growth in the number of new workers in 2018 was less than 1.0 percent to bring their number to 956,000, compared to about 426,000 unemployed persons, of whom about 65 percent in Gaza Strip, which raised the unemployment rate in Palestine to about 30.8 percent. However, the labor market's capacity to absorb new laborer's is greatly lower in Gaza Strip compared to the West Bank because of the blockade, while the labor market in Israel and settlements contributes to the absorption of large numbers of workers from the West Bank.

In Gaza Strip, more than 28,000 newcomers in the labor market did not find job opportunities, in addition to 25,000 lost jobs due to the economic downturn, creating a wide gap within the labor market and pushing unemployment rates to 52.1 percent. In the West Bank, despite the economic slowdown, the local labor market, along with the labor market in Israel and settlements, succeeded in creating more jobs than the newcomers in the labor market (32,000 vs. 28,000), which slightly reduced the unemployment rate (from 18.7 percent to 17.6 percent).

The unemployment rate in Palestine, and in Gaza Strip in particular, is one of the highest in the world. This is evident when it compared with advanced countries, such as the United States of America (4 percent), Japan (2 percent), or with emerging or developing countries, such as China (4 percent), India (3 percent). On the other hand, with neighboring countries, such as Israel, where unemployment was around 4 percent, and Egypt 11 percent, and about 15 percent in Jordan, which is facing challenges to absorb the labor force, especially as it received large numbers of Arab refugees over the past years.

Figure 1-14: Unemployment rates in Palestine, 2014-2018



Source: PCBS.



It should be noted that unemployment rates in Palestine is significantly high among females, reaching 51.2 percent in 2018, due to labor market conditions, which are often a labor-repellent factor for women, especially those with a high academic level of achievement. (13 years of study and above). The unemployment rate among them is 54.3 percent. Unemployment rates in the refugee camps are also higher than in urban and rural communities, reaching an average of about 44.2 percent in 2018.

As for the distribution of workers in the local market to the sectors (public and private), and from the fact that the Palestinian private sector is the largest employer, about three quarters of the workers in the local market work for the private sector (excluding workers in Israel and settlements). About 63 percent of workers in Gaza Strip work for the private sector, while in the West Bank this percentage rises to about 81 percent, indicating that Gaza Strip is more dependent on employment in the public sector than the West Bank, which is why the government sector in Gaza became inflated after the division.

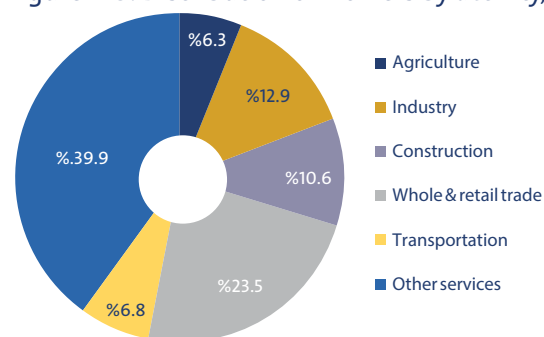
On the other hand, there were no substantial changes in the distribution of workers to economic activities during 2018. The overall structure of this distribution has been maintaining its relative stability for years, with the service sector maintaining a leading position in the absorption of workers at nearly 40 percent. The remainder is distributed across different sectors of the economy in varying proportions.

It should be noted that the contribution of sectors to the employment of workers is often inconsistent with their contribution to GDP. There are sectors that employ large numbers of workers due to their low value-added contribution, which in turn reflects the low productivity of a single worker, such as transportation, storage and construction. The contribution of value added generated by the industrial and service sectors exceeds that of these sectors in operation, reflecting higher effectiveness and efficiency, and a higher level of productivity.

Productivity

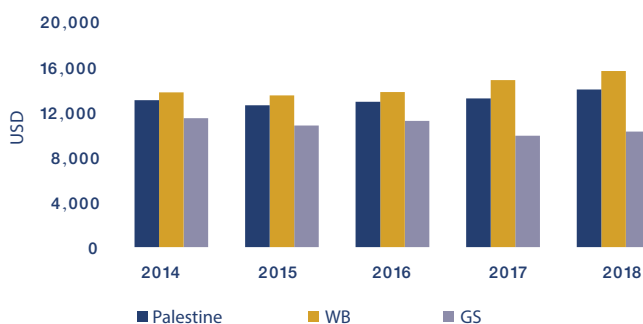
Worker productivity in the West Bank and Gaza Strip grew^[9] unevenly, continuing to grow steadily and strongly in the West Bank for the third consecutive year, while the level remains weak in Gaza Strip, increasing the gap between them, with worker productivity in Gaza still below 66 percent its level in the West Bank. As a result, the total productivity of workers in Palestine increased by about 6.0 percent to reach about USD 13,986 (2015 prices) per worker in 2018.

Figure 1-15: Distribution of workers by activity, 2018



Source: PCBS.

Figure 1-16: Worker's productivity in Palestine, 2014-2018



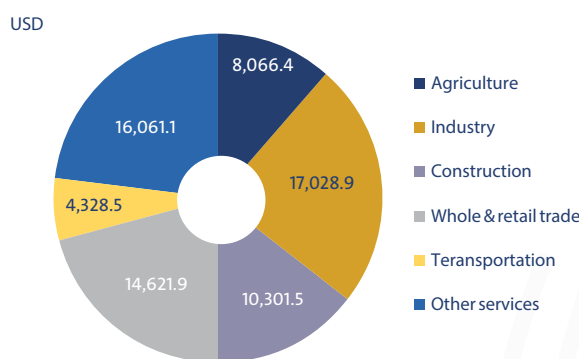
Source: PCBS.

[9] Productivity = GDP at the cost of production/ number of workers in the local economy.



Productivity varies greatly across different economic activities, depending on several factors, the most important of which is the ratio of employment to capital. Worker productivity in labor-intensive activities is often lower compared to capital-intensive activities. That was clear according to the year's data 2018, which showed the low productivity of workers in the transportation and storage sector (USD 4,328 per worker) and the agriculture sector (USD 8,066 per worker). Alternatively, productivity was higher in the services sector (USD 16,061 per worker). Productivity of the worker in the industrial sector increased to record the highest level at about USD 17,029 per worker.

Figure 1-17: Productivity by economic activity, 2018

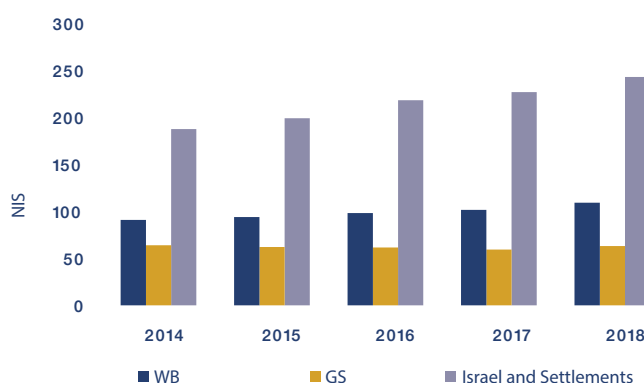


Source: PCBS.

Average daily wage

The average nominal daily wage for Palestinian workers increased by 7.6 percent in 2018 to NIS 123.0, due to the increase in average wages in the three areas of employment by a similar percentage: 7.6 percent for workers in the West Bank, 7.1 percent for workers in Israel and settlements, and 6.2 percent for workers in Gaza. However, this growth has not been sufficient to bridge the gap between wage rates in the three regions, as the average wage swelled to workers in Israel and settlements at 3.9 double the wage in Gaza, and 2.2 double the wage in the West Bank.

Figure 1-18: Average daily wages for Palestian workers, 2014-2018



Source: PCBS.

These differences in the level of wages reflected the outcome of different growth trends over the past years. For example, the average daily wage of workers in Israel grew by about 5.6 percent annually over the period 2010 - 2018. While this average in the West Bank grew by about 3.1 percent, in Gaza Strip, the average daily wage of a worker has barely grown at 0.2 percent annually on average during the same period.

For example, the average daily wage of workers in Israel grew by about 5.6 percent annually over the period 2010 - 2018. While this average in the West Bank grew by about 3.1 percent, in Gaza Strip, the average daily wage of a worker has barely grown at 0.2 percent annually on average during the same period.

Wage developments cannot be addressed in isolation from consumer price changes, because^[10] of their direct impact on the level of real pay or what is known as purchasing power. However, price movements during 2018 came in favor of strengthening purchasing power, specifically for workers in Gaza Strip, as consumer prices contracted, real wages grew beyond the growth in nominal wages (7.5 percent vs. 6.2 percent). With the relatively stable level of general prices, the growth in real wages for workers in both the West Bank, and Israel was very close to nominal wage growth.

Workers' wages are also affected by exchange rates, especially for those who are paid in currencies other than shekel, where workers in Palestine receive their salaries, in addition to shekels, mainly in US dollars and Jordanian dinars. During 2018, the average exchange rate of the dollar and dinar against the shekel remained relatively constant, at about 3.6 for the first, and 5.1 for the second; hence, the average purchasing power was not affected by exchange rate fluctuations compared to last year.

[10] The amount of goods and services that can be purchased through a specified amount of money.

Box3 : Living Standards in Palestine, 2017

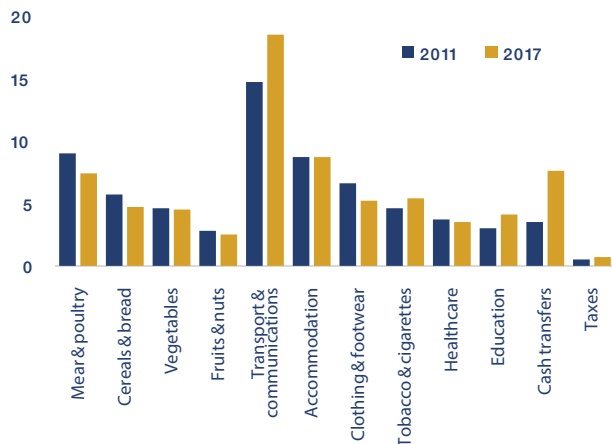
A 2018 report by the PCBS shows that an average Palestinian spends 170 dinars per month, 220 dinars in the West Bank and 91 dinars in Gaza Strip. The food share of spending is still the highest at 31 percent of total spending, followed by the share of transport and communications spending at 18.5 percent.

The report shows that average per capita monthly spending between 2011 and 2017 increased in the West Bank from 188 dinars to 220 dinars. While in Gaza Strip, it fell from 110 dinars to 91 dinars. The report also shows a change in the pattern of individual/family spending, where the share of spending on food fell from almost 35.9 percent in 2011 to 31.0 percent in 2017, and the share of spending on clothes and shoes dropped from 6.6 percent to 5.2 percent. While spending on transportation and communications increase in from 14.7 percent to 18.5 percent and an increase in spending on education from 3.0 percent to 4.1 percent, and an increase in the share of paid cash transfers from 3.5 percent to 7.6 percent during the same period.

Distribution of monthly household expenditure, 2017



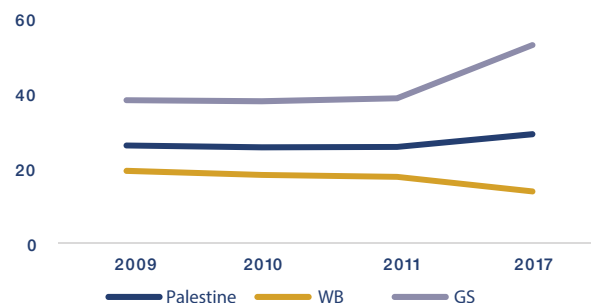
Household expenditure (percent), selected goods and services, 2011 & 2017



Geographically, the report shows that the average monthly household spending on food in the West Bank amounted to 29.1 percent of total spending, compared to 35.7 percent in Gaza Strip in 2017. The share of non-food cash spending was about 56.4 percent of total spending in the West Bank and about 49.4 percent in Gaza Strip.

With regard to poverty ratios according to consumption patterns, the report shows that in 2017 the poverty rate in Palestine reached 29.2 percent, including 13.9 percent in the West Bank and 53.0 percent in Gaza Strip. In comparison to 2011, the poverty rate in Palestine increased by about 13.2 percent (in 2011 it was about 25.8 percent). At the geographical level, poverty in the West Bank has decreased by about 21.9 percent (in 2011 it was about 17.8 percent), compared to a rise in the Gaza Strip of 36.6 percent (in 2011 it was about 38.8 percent).

Poverty rates in Palestine according to consumption patterns



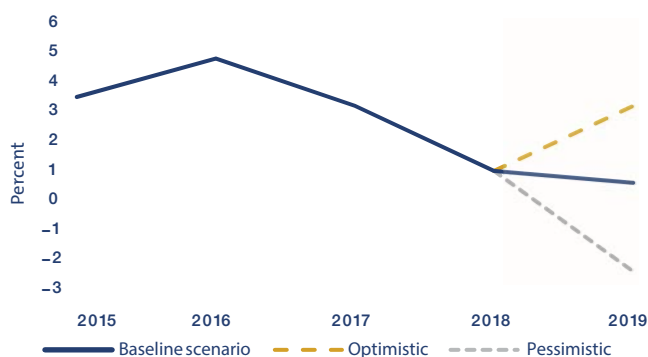
Source: PCBS, Standards of Living Report, 2017.



Palestinian economic outlook

The PMA's forecast for the performance of the Palestinian economy in 2019 indicates that the slowdown in the economy (according to the base scenario) will continue to be around 0.5 percent compared to 0.9 percent in 2018. This slowdown will have a negative impact on real per capita income (average real GDP per capita), which will shrink by about 0.8 percent compared to 1.7 percent in 2018. These predictions are based on a set of [11] underlying assumptions, including an analysis of various potential risks to varying degrees.

Figure 1-19: Economic outlook in Palestine (real growth forecasts), 2019



Source: Estimates of PMA.

This performance comes against the assumption that the financial crisis that the Palestinian government is going through will continue after Israel withheld part of the clearance revenues, which limited the Palestinian government's ability to cover its current spending in full, as this crisis was assumed to continue until the middle of 2019. Accompanied by the assumption of a decline in the amount of grants provided to support the government budget to USD 500 million in 2019. These forecasts are also based on the assumption that current transfers to the private sector will grow by 2 percent to USD 1,559 million, and credits for the private sector will increase by 8 percent. In addition, the cost of imports (inflation rate and exchange rates of trading partners) will increase by 1.5 percent beside an increase in the number of Palestinian workers in Israel by about 5.0 percent and that the Israeli economy will grow by about 2.3 percent in 2019, according to the Bank of Israel report.

With the expected slowdown based on the underlying scenario, final consumption is expected to decline slightly by 0.2 percent (including 0.2 percent for private consumption and 0.4 percent for government consumption), to fall to about 112.9 percent of the GDP estimated for 2019. Investment is expected to contract slightly (0.6 percent) with a drop to 23.4 percent of the GDP.

As for the external sector, in light of weak economic activity, foreign trade is expected to decline, with exports shrinking by 0.6 percent and imports by about 1.3 percent leading to a slight improvement in the trade balance (decreased deficit); its share will constitute about 36.6 percent of GDP. On the other hand, it is expected that the slowdown in economic growth will reduce the capacity of the labor market to generate enough jobs. Thus, unemployment rates will continue to rise gradually to 31.2 percent on average, and that inflation levels will reach about 0.9 percent against the backdrop of the forecasts of a slight rise in world food prices and a higher pace in the cost of imports to Palestine.

It should be noted that these forecasts remain subject to some different and potential shocks to varying degrees. Assuming that the economy will be exposed during 2019 to a positive shock (optimistic scenario) represented in a serious improvement in the political and security situation and Palestinian peace and reconciliation negotiations. In conjunction with easing the blockade and partial closures of the Gaza Strip, increasing the number of Palestinian workers in Israel, increasing the flow of donor funds to support the budget and g developmental spending, transferring clearing revenue entirely to the Palestinian Government, and increasing private sector transfers from abroad at a

[11] It is imperative to consider the sensitivity of these results to any change in the official actual figures issued by the PCBS and the Palestinian Ministry of Finance

pace higher than its annual average. Accordingly, real GDP is expected to grow by about 3.1 percent, and the average per capita GDP to rise by about 3.2 percent.

Based on this scenario, final consumption is expected to grow by about 3.4 percent (3.0 percent for private consumption and 4.6 percent for public spending) and investment by about 4.2 percent and that the trade deficit would increase by 5.2 percent due to export growth by 3.5 percent and imports by about 4.6 percent. Unemployment, on the other hand, is expected to fall slightly to 29.7 percent of the total laborforce.

In the case of a negative shock to the economy (pessimistic scenario), represented by a further deterioration in the political and security conditions, a further decrease in the volume of grants to support the government budget. In addition to the continuing disagreement with the Israeli side over the clearance revenue, and the decline in the number of Palestinian workers in Israel. Under this scenario, real GDP is expected to contract by about 2.5 percent and that the average per capita GDP would decline by 3.9 percent.

Based on this scenario, final consumption is expected to decline by about 1.7 percent (0.5 percent for private consumption and 5.6 percent for government consumption), and investment to decline by about 10.1 percent, and a decline in exports by about 5.4 percent and imports by about 4.5 percent, which will reduce the trade deficit by about 4.2 percent. This scenario will also lead to high levels of unemployment to 32.1 percent.

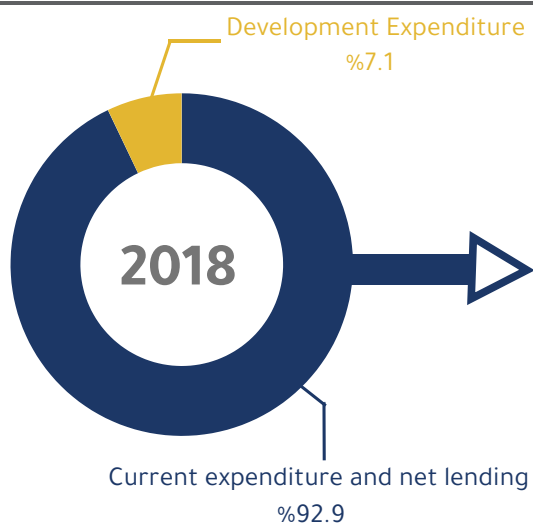
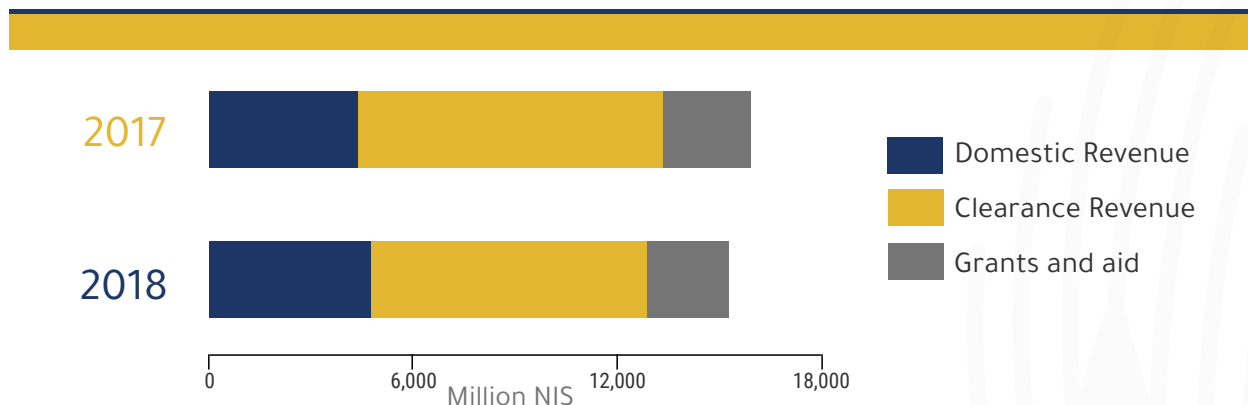


Chapter Two

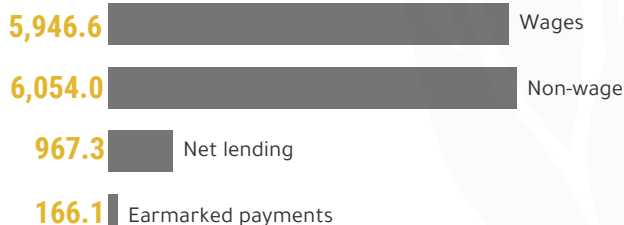
Public Finance Developments



Public Finance 2018



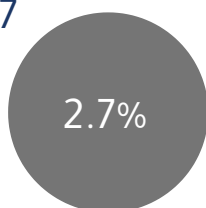
NIS million



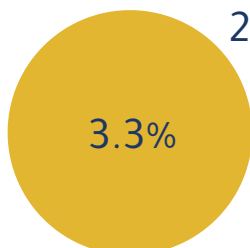
Overall deficit (Excl. grants and aid) as a percentage of GDP

Public debt as a percentage of GDP

2017



2018



2017



2018



Overview

The Palestinian government continued its efforts in 2018 to reduce the budget deficit by reforming the public finance management and regulating public spending, including the preparation of spending plans for locally funded projects. It also increased and strengthened revenues, by improving tax collection, continuing to adopt a stimulating and reduced tax policy, and continuing to pursue, develop and improve the mechanisms of clearance with Israel. These measures were reflected in the improvement in local revenue collection (tax and non-tax revenue). But on the other hand, 2018 witnessed significant decrease in clearance revenue, along with reduced grants. On the other hand, actual public expenditures declined due to the government actions to refer some staff to retirement and early retirement, as well as the suspension of some bonuses and allowances.

These developments led to drop in overall balance surplus, after grants, compared to previous year and drop in government public debt (domenated in USD) met with an increase in the government's accumulated arrears. The government continued to schedule private sector arrears, through the issuance of promessary notes, aimed at reducing the accumulation of such arrears and establishing a mechanism for payment and totally disposal of all arrears.

Total revenue and grants

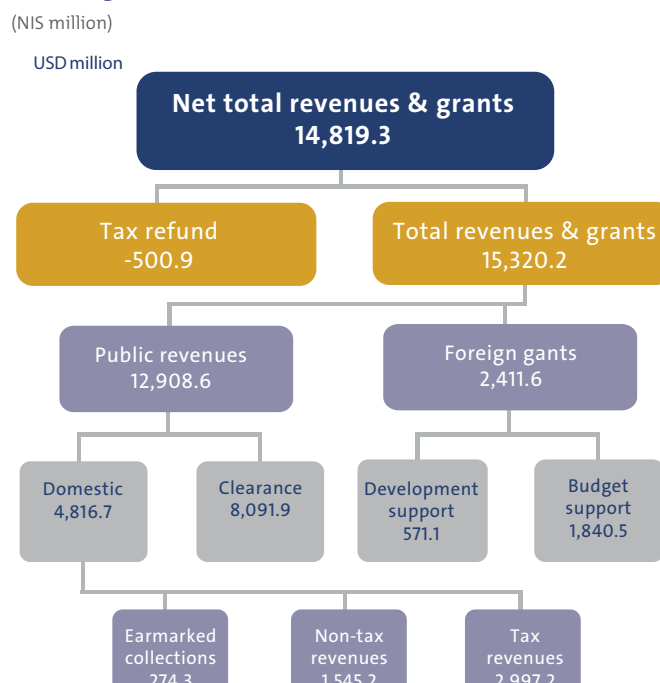
The year 2018 witnessed significant decline in clearance revenue, accompanied by a decrease in grants, against a rise in domestic revenue (tax and non-tax), which resulted in a decline in public revenues and grants by about 4.1 percent compared to the previous year, amounting to about NIS 15,320.2 million. Thus, actual public revenues and grants constituted approximately 93 percent of the target by the same year's budget, compared to about 97.9 percent in 2017.

In 2018, the volume of tax refunds doubled compared to 2017 to NIS 500.9 million, accounting for 267.9 percent of the target in the 2018 draft budget. In total, net public revenue and grants decreased by 6.2 percent in 2018 to NIS 14,819.3 million, or about the equivalent of 90.9 percent of the targeted amount in the draft budget.

Public revenue

Public revenue consists of clearance revenue at 62.7 percent, domestic revenue, which accounts for about 37.3 percent (of which 23.2 percent is the share of tax revenue, and 12 percent is the share of non-tax revenue, and 2.1 percent earmarked collections). Public revenues amounted to NIS 12,908.6 million, down 3.6 percent from the previous year,

Figure 2- 1: Public revenues framework, 2018



Source: Ministry of Finance.



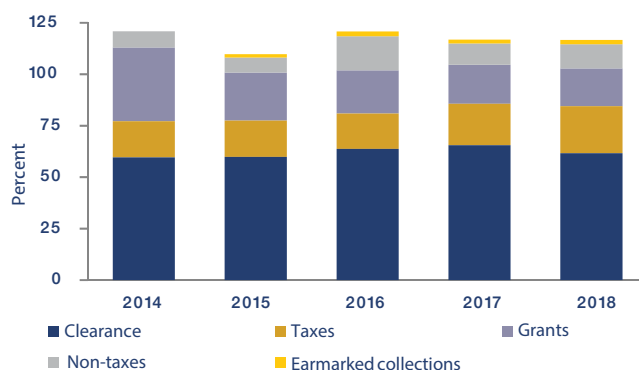
accounting for 94.3 percent of the budget target. The decline in public revenue reduced the ratio of the tax burden to GDP to about 24.6 percent compared to 25.6 percent in the previous year^[12].

The analysis of the components of public revenue indicates that the main reason for the decrease in this item is due to a significant decline in clearance revenue by about 9.8 percent compared to the previous year, to approximately NIS 8,091.9 million, accounting for about 15.4 percent of the GDP in 2018. Clearance revenue consists mainly of customs revenue that constitutes about 43.1 percent; fuel revenue at 30.8 percent; VAT revenue at about 24.9 percent; and income tax and purchase tax and other revenue at 1.2 percent of total clearance revenue of 2018^[13]. Clearance revenue contributed to the coverage of about 136.1 percent of the payroll bill, compared to about 126.9 percent in 2017 and about 61.6 percent of current expenditures and net lending compared to about 65.5 percent during the same period. These indicators underscore the great importance of clearance revenue, which is the government's safety net for meeting its obligations and paying dues.

Domestic revenue increased by 9 percent compared to the previous year, reaching NIS 4,816.7 million, due to the rise of all of its components, both tax and non-tax revenues and earmarked payments. The revenue of the domestic collection included tax revenue by about 62.2 percent, 32.1 percent for non-tax revenue, and about 5.7 percent for earmarked collections. Domestic revenue collection accounted for about 106.3 percent of the target amount in the draft budget and contributed to the coverage of about 36.7 percent of current expenditures and net lending, compared to about 32.3 percent in 2017.

In this context, tax revenues increased significantly (9 percent) during 2018 compared to the previous year, to reach about NIS 2,997.2 million, constituting almost 5.7 percent of the GDP and contributed to the coverage of about 22.8 percent of current expenditures and net lending, compared to about 20.1 percent in 2017. Government policies to reduce the tax rate and expand the tax base appear to have worked, with the past four years witnessing successive increases in this type of revenue. Tax revenues were distributed during 2018 between: VAT revenues at about 40 percent; income tax revenue at about 28.3 percent; the share of customs revenues amounted to about 23.3 percent; cigarette excise contributed by about 7.8 percent; and income from property tax and beverage excise contributed about 0.6 percent to tax revenues. Value-added tax revenue increased by about 18.5 percent to about NIS 1,198.2 million, and income tax revenue increased by 7.4 percent to hit NIS 848.7 million, cigarette excise revenues rose by about 21.4 percent to NIS 235.1 million. On the other hand, customs revenues decreased by about 5.4 percent to NIS 697.7 million, and beverage excise revenues and property tax revenues decreased to NIS 17.4 million compared to about NIS 18.4 million in 2017.

Figure 2- 2: Revenues and grants as a percent of current expenditure, 2014- 2018



Source: Ministry of Finance.

[12] The tax burden is the amount of taxes collected by the government in all its forms relative to GDP, usually higher in industrialized and developed countries than in developing countries.

[13] The contribution of taxes to clearance revenues is calculated on the commitment basis, as these details are not available on a cash basis.



Non-tax revenue in 2018 increased significantly (10.1 percent) compared to the previous year to about NIS 1,545.2 million, and to form about 2.9 percent of the GDP. As non-tax revenues increased, their coverage of current expenditures and net lending increased to about 11.8 percent compared to about 10.3 percent during the same period. This increase is mainly due to increased revenue from other fees^[14] by 29.6 percent compared to the previous year, to about NIS 646.6 million, and revenues from transportation fees increased by 4.8 percent to register NIS 138.9 million, as well as investment returns to nearly NIS 15.8 million. On the other hand, revenues from profession license fees, health insurance fees and sharia court fees decreased by 2.5 percent to NIS 743.8 million.

Finally, the earmarked collections in 2018 amounted to NIS 274.3 million compared to NIS 264.3 million in 2017, accounting for 5.7 percent of the revenues of the local tax, contributed to the coverage of about 2.1 percent of current expenditures and net lending.

Foreign grants

The volume of grants continued to decline for the sixth consecutive year, declining by 7.1 percent in 2018 compared to the previous year, to NIS 2,411.6 million. Thus reducing its share of total public revenues and grants to 15.7 percent, compared to 16.3 percent in 2017, contributing to cover about 18.4 percent of current expenditures and net lending, compared to about 19 percent during the same period. Foreign grants represent an essential tributary of the Treasury, and the bulk of it is used to support the budget, while a small part of it is used to support development projects. The volume of grants directed to support the budget hit approximately NIS 1,840.5 million or the equivalent of 76.3 percent of the total external support provided during 2018, compared to about NIS 571.1 million or the equivalent 23.7 percent of this support was allocated to finance development projects.

Foreign grants also contribute to reducing the government's fiscal deficit, often turning it into a surplus, as in 2013-2018. In this context, grants contributed during 2018 to transferring the government's overall balance from a total deficit of NIS 1,729.4 million (about 3.3 percent of GDP) to a surplus of about NIS 682.2 million (about 1.3 percent of the GDP).

Box4 : Economic and Social Implications of Stopping U. S. Aid to the Palestinian People

The United States of America was the main sponsor of the 1993 peace process between the PLO and Israel. Over the past years, USA has been providing aid to the Palestinian people as a means of advancing and sustaining the peace process between the two sides. This aid has been declining for the past two years until USA announced that it would suspend all aid as of 2019. The U.S. Agency for International Development (USAID) and the U.S. Department of State are the main source through which this aid flows.

Since Donald Trump won the 2016 US presidential election, he has been threatening to cut aid to the Palestinian people, with the aim of putting pressure on the Palestinians to accept what has come to be known as the Deal of the Century. In this context, many different segments of Palestinian society are wondering about the repercussions of the suspension of U.S. aid, and the positions are contradictory with regard to its repercussions, some believe that the impact of its suspension will have major repercussions on the economy, while others believe that its impact will be limited.

The figures indicate that this assistance is of great importance, particularly with regard to the support of the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA), where the USA is the largest supporter of the UNRWA budget. It accounting for nearly one-third of the total funding provided to the Agency with an average

[14] These fees consist mainly of the High Judicial Council fees, postage and telecommunications fees, Ministry of Economy fees, civil registration taxes and other fees.



of USD 300 million per year during 2008-2017. Thus, the suspension of U.S. aid has affected the performance of the UNRWA and its ability to finance its service and humanitarian activities. This will affect the Palestinian refugees both in the Palestinian territory (West Bank and Gaza Strip) or in the diaspora, and increase their suffering, thereby increasing the burden on the Palestinian government, which is already suffering from a budget deficit.

The threat to suspend U.S. aid (and start implementing these threats) will directly affect government performance, as the government receives direct support from the USA, which will worsen the government's financial situation and increase the deficit. There is also an indirect impact of stopping this assistance on the Palestinian government through the new unemployed who hold jobs in USAID projects who will join unemployment in the Palestinian labor market.

Data indicate that USAID is the main source of U.S. grants, with more than 70 percent of all grants provided to Palestine (West Bank and Gaza Strip) through this agency. While the remaining part is provided through the U.S. State Department of State. USAID has provided about USD 359 million in annual average during the period 2008-2018 to finance various projects in the West Bank and Gaza Strip. These projects varied from support to law and order in the Palestinian territory, direct support for the budget of the Palestinian government and the training and support of the security services. In addition to paying some of the Palestinian government's obligations to some hospitals operating in Jerusalem and supporting development projects related to education, health, water, social assistance, infrastructure projects and other projects. The U.S. Department of State has provided USD 169 million per year over the past 10 years, which has been mainly aimed at civil society and emergency assistance.

Table 1: Sources of American Grants and Aid to the West Bank and Gaza Strip

(USD million)

Year	Total American Aid	U.S. Department of State	USAID
2008	353.0	79.5	273.5
2009	918.3	345.5	572.8
2010	590.2	111.4	478.9
2011	828.7	275.5	553.2
2012	329.7	128.8	200.9
2013	802.9	249.1	553.8
2014	387.0	129.3	257.8
2015	456.6	101.2	355.4
2016	616.0	332.0	284.1
2017	375.2	107.7	267.5
2018	146.6	0.0*	146.6**
Annual average	527.7	169.1	358.6

*Data available by the end of 2018 Q1.

** Data available until the end of 2018 Q3. (The fiscal year in USA ends on 30/09 of each year).

Data Source: USAID^[15] website.

The following table shows the share of each of the key entities or sectors benefiting from U.S. aid from 2008 to 2018. The table shows that the share of sectors of this aid fluctuates, but it is clear that the share of security, protection and social assistance is fairly high, and the share of administrative costs is increasing, especially in 2017 and 2018.

[15] https://explorer.usaid.gov/cd/PSE?fiscal_year=2018&implementing_agency_id=1&measure=Disbursements
Data available until the end of 2018 Q3. (The fiscal year in America ends on 30/09/ of each year).



Table 2: Recipients of U.S. grants and assistance in the West Bank and Gaza Strip

(Percentages)

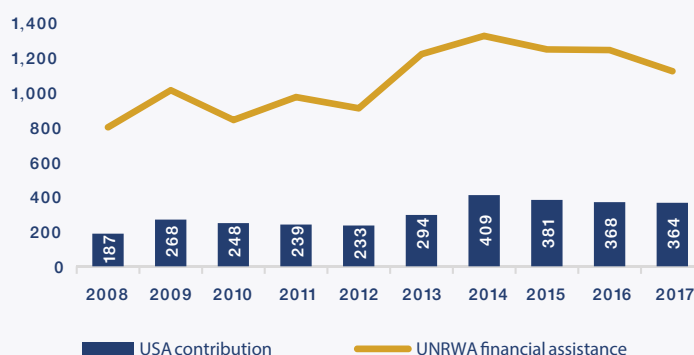
Item	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018*	Period Average
Admin costs	4.9	2.2	4.2	3.0	10.1	3.5	7.1	6.5	4.5	7.7	13.4	6.1
Infrastructure	0.9	3.7	11.8	7.9	2.6	1.8	12.1	7.9	3.6	2.7	10.4	5.9
Security & Protection	7.6	33.2	7.1	35.8	24.2	32.2	8.7	16.1	52.6	20.8	25.2	23.9
Rule of Law & H. Rights	16.1	8.9	19.5	5.9	30.7	3.8	34.0	14.7	4.8	21.0	2.1	14.7
Social assistance	42.6	39.0	29.6	25.5	5.8	45.6	7.1	30.6	17.9	26.3	8.4	25.3
Water & wastewater	9.0	2.7	10.7	6.5	7.3	3.7	10.4	12.5	9.2	7.0	16.6	8.7
Basic Education	0.8	1.8	1.6	2.1	2.0	1.1	1.9	2.6	1.5	2.7	6.2	2.2
Total (USD million)	353.0	918.3	590.2	828.7	329.7	802.9	387.0	456.6	616.0	375.2	146.6	527.7

* 2018 data are partial and does not cover the full year, but they are considered end of a fiscal year in USA.

On the other hand, UNRWA has played an important and essential role in reducing unemployment and poverty levels and raising the standard of living of many Palestinian families, sponsored by UNRWA, through relief programs provided by this agency. Due to the difficulty of separating the data of the UNRWA from other U.S. agencies assisting the Palestinian people, the UNRWA's data were obtained through its own website. UNRWA is known to be primarily concerned with providing education and health services to Palestinian refugees (at home and in diaspora) in addition to social and other emergency aid. Data from the UNRWA showed that the average volume of assistance to Palestinian refugees in the West Bank, Gaza Strip and the diaspora amounted to about USD 1.1 billion during the period of 2008 to 2017. U.S. aid has formed about 28 percent or the equivalent of USD 300 million per year[16]. The U.S. aid to the UNRWA reached about USD 60.4 only in 2018 or 4.7 percent of the total aid.

Consequently, the data show the amount of U.S. assistance provided through USAID and the U.S. Department of State, which is clearly and significantly influential in the Palestinian government's ability to meet its obligations, and in the capacity and effectiveness of the UNRWA. The analysis shows that the cessation of such aid will inevitably affect the government deficit directly and indirectly by increasing the financial burden of the government, which already suffers from chronic deficit. The direct impact is through the cessation of direct government subsidies that increase the government's fiscal deficit. While the indirect effect is through the suspension of social assistance and other development projects. In addition to the increase in the number of unemployed people as a result of the cessation of this support, which calls for increasing government spending and thus worsening the government's financial situation and increasing the burden of the Palestinian government with regard to the services of Palestinian refugees.

Financial assistance granted by UNRWA (USD million)



[16] <https://www.unrwa.org/how-you-can-help/government-partners/funding-trends/donor-charts>.



Public spending

In 2018, actual public spending decreased by 3.2 percent compared to the previous year, to NIS 14,137.1 million, mainly due to lower wages and salaries. Outstanding public expenditure (on commitment basis) fell by about 7.0 percent compared to 2017 to reach about NIS 16,104A million^[17]. Therefore, actual public spending formed approximately 87.8 percent of outstanding public spending, and about 78.2 percent of the amount of public spending targeted in the draft budget.

As in previous years, mostly current public spending (wages and salaries, non-wage expenditures, net lending, and earmarked payments) is about 92.9 percent of total actual public spending, compared to about 7.1 percent for development spending during 2018. The share of spending on wages and salaries was about 42.1 percent of total actual public spending, while non-wage spending accounted for 42.8 percent, net lending accounted for 6.8 percent, and the share of earmarked payments 1.2 percent. Actual spending in 2018 was about 27.0 percent of the GDP, compared to about 27.9 percent in 2017.

Current expenditure and net lending

Actual current spending and net lending in 2018 decreased by 4 percent compared to the previous year, to NIS 13,134 million, accounting for 81.2 percent of the target in the draft budget, and about 88.7 percent of the outstanding amount. The decline came against the backdrop of a decline in spending on wages and salaries, as the paid wage bill and salaries declined by about 15.8 percent compared to 2017 to approximately NIS 5,946.6 million, or the equivalent of 75.5 percent of the target amount according to the draft budget and about 92.6 percent of the outstanding amount. The payroll bill acquired about 42.1 percent of total actual public spending, and 45.3 percent of current spending and net lending compared to about 48.4 percent and 51.6 percent respectively in 2017.

Figure 2- 3: Public spending framework, 2018

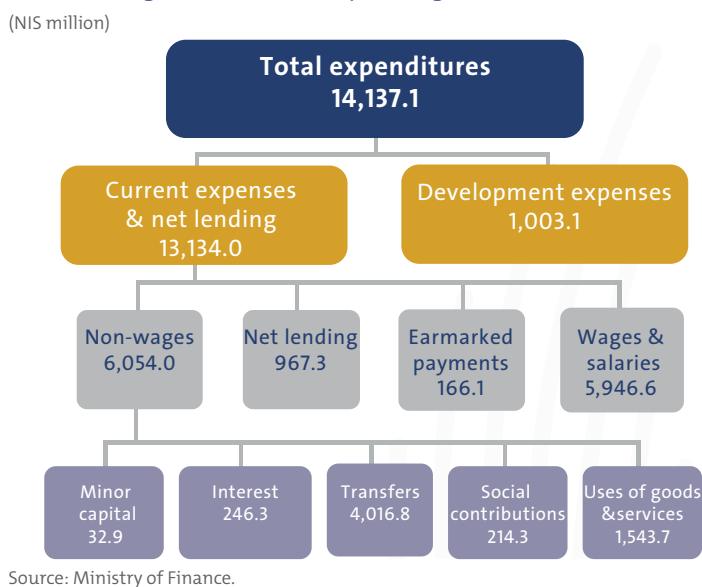
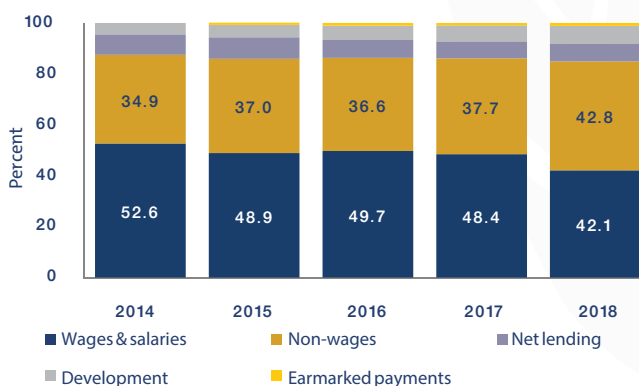


Figure 2- 4: share of expenditure items, 2014- 2018



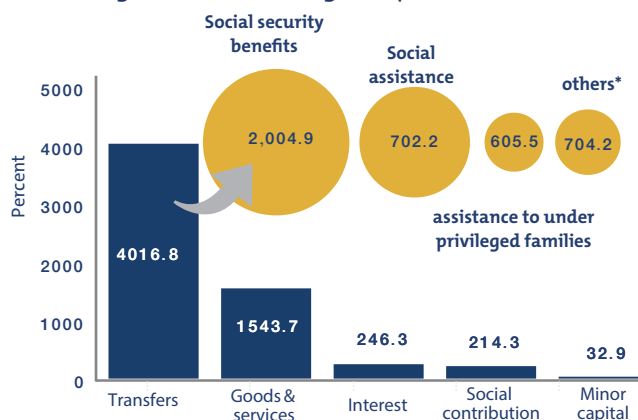
[17] The actual amounts represent what has actually been paid by the government, but the outstanding amounts (commitments) are the government's liabilities during a certain period of time (usually one year), which may not be paid in full by the government, but the target amounts are allocated by the government and targeted when it is budgeted.

According to an analysis of the wages and salaries by line ministry and agency, the security and public order sector (specifically the Ministry of Interior and security) accounted for the largest share of wages and salaries at 38.3 percent, while the Ministry of Education and Higher Education acquired 33.1 percent and the Ministry of Health accounted for about 9.8 percent. The share of the General Administration (Office of the President, PLO, General Personnel Council, Ministry of Local Government, Ministry of Finance, embassies) was about 9.4 percent of the wages and salaries. Economic affairs, environmental protection and housing accounted for about 4.8 percent, compared to about 4.6 percent for social services and religious and cultural^[18] services in 2018.

In contrast, non-wage expenditures increased by 9.9 percent in 2018 compared to the previous year to about NIS 6,054 million, accounting for 81.8 percent of the target amount in the draft budget and about 84.8 percent of the outstanding amount during the same year. This item constituted approximately 42.8 percent of public spending, and about 46.1 percent of current spending and net lending during 2018 compared to about 37.7 percent and 40.3 percent, respectively in 2017. The increase in non-wage expenditures was mainly due to increased transfer expenditures, as well as higher costs of the use of goods and services, and micro capital expenditures, while spending on social contributions and interest payments decreased.

With regard to transfer expenditures, it increased significantly (17.5 percent), to NIS 4,016.8 million –this item constitutes about 66.3 percent of non-wage expenditures. Spending on the use of goods and services increased by about 1.5 percent compared to the previous year, to NIS 1,543.7 million. Therefore, accounting for about 25.5 percent of non-wage expenditures, as opposed to a decrease in social contributions (retirement transfers) to NIS 214.3 million, compared to about NIS 260 million during the previous year, to form about 3.5 percent of non-wage expenses. Interest payments fell to nearly NIS 246.3 million compared to about 277.4 million in 2017, thus constituting 4.1 percent of non-wage expenses in 2018.

Figure 2- 5: Non-wages expenditures, 2018



* Includes unemployment benefits, local government support, payments to NGOs and civil society & universities, educational subsidies & scholarships, and compensation for damages & emergency expenditures.

Source: Ministry of Finance.

Transfer expenditure was distributed between social security benefits (civil and military pensions) of NIS 2,004.9 million (49.9 percent of transfer spending); social assistance of NIS 702.2 million (or 17.5 percent of transfer spending); and assistance to needy families of NIS 605.5 million (equivalent to 15.1 percent of transfer spending); unemployment benefits amounted to NIS 133.5 million (about 3.3 percent of transfer expenditure). Expenditure on support for local governments, universities and civil society, subsidies, scholarships, education, and emergency damage compensation; other transfers were about NIS 570.7 million (equivalent to 14.2 percent of transfer expenditure).

On the other hand, net lending in 2018 increased slightly by 0.8 percent compared to the previous year, to NIS 967.3 million, accounting for about 107.5 percent of the target according to the draft budget. Thus, this item acquired about 6.8 percent of public spending, compared to about 6.6 percent in general 2017. Earmarked payments amounted to NIS 166.1 million compared to NIS 149.9 million in 2017, accounting for about 1.2 percent of total public expenditure.

[18] The shares of line ministries and agencies in the payroll bill are calculated on the commitment basis, as these details are not available on cash basis.



Development expenditure

Actual development expenditures in 2018 increased by 8.9 percent compared to the previous year, to hit NIS 1,003.1 million, accounting for approximately 52.5 percent of the target amount in the draft budget, and about 77.3 percent of outstanding amounts, and accounted for about 7.1 percent of public expenditure in 2018. Note that the government received grants to finance development projects by about NIS 571.1 million, or the equivalent of 56.9 percent of development expenditures, while the remaining part was financed by the government treasury. Development spending during 2018 was about 1.9 percent of the GDP, which is a low percentage.

In general, this analysis indicates the continuing structural imbalance in the distribution of public expenditures, where the volume of spending on development projects remains modest, given the limited financial resources available, the limited sources and volume of revenues of the government, and the specificity of the Palestinian situation, as a result of the current political situation. On the other hand, most government spending is concentrated in consumer expenditures (wages, salaries, transfer expenses, use of goods and services, and other consumer expenditures) which is expected to have a weak impact on growth in the medium and long term.

Fiscal balances

Developments in both sides of the public finances during 2018 led to a significant increase in the current deficit (on a cash basis) to about NIS 726.3 million, compared to a deficit of NIS 486.8 million in 2017. This is mainly due to lower public revenues (clearance revenue in particular) at a rate higher than current expenditure and net lending.

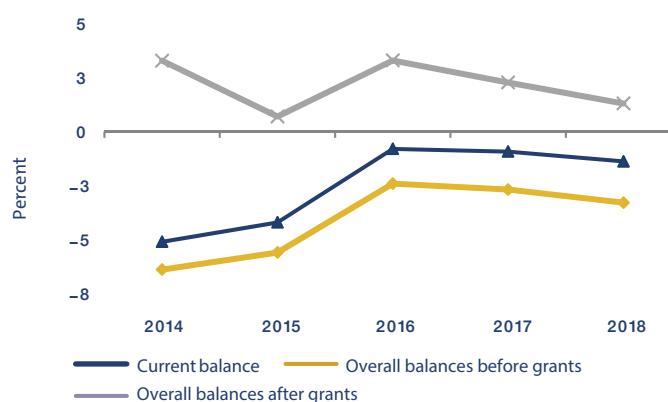
Overall balance before grants deficit (including development expenditures) increased to NIS 1,729.4 million, compared to a deficit of NIS 1,408.1 million in 2017. The total deficit before support was about 3.3 percent of the GDP compared to 2.7 percent in 2017.

On the other hand, the overall balance after grants had a surplus of about NIS 682.2 million (equivalent to 1.3 percent of the GDP) compared to a surplus of NIS 1,189.1 million during 2017 (equivalent to 2.3 percent of the GDP). Foreign grants contributed to the transformation of the deficit into surplus, thus demonstrating the importance and reliability on foreign grants, particularly when taking into account the volatility of public revenues and their irregularities, specifically clearance revenue (the safety net to cover a large and important part of the expenses) which is usually associated with the political situation.

Government arrears

In 2018, the government worked hard not to accumulate new arrears, but the lack of available financial resources and increased commitments prevented it. However, it was able to pay part of the arrears of previous years, particularly under the promessary notes program. In return, it delayed the payment of new payments and commitments that occurred in 2018. In 2018, the government was able to pay NIS 1,561.8 million in previous arrears. New arrears accumulated

Figure 2- 6: Budget balances as a percent of GDP, 2014- 2018

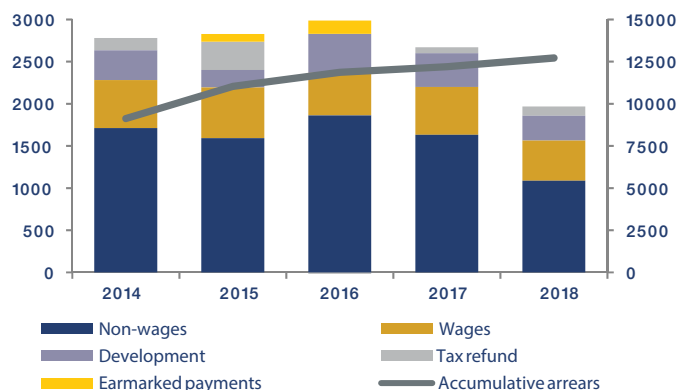


Source: Ministry of Finance.

during the same year of about NIS 2,076.6 million, which means the accumulation of about NIS 514.81 million in new arrears during 2018. The government's arrears at the end of 2018 amounted to NIS 12,719.1 million (about USD 3,407.7 million) or the equivalent of 23.3 percent of the GDP.

Most of the new arrears incurred by the government in 2018 (NIS 2076.6 million) were focused on a non-wage item, amounting to NIS 1,086.5 million, or about 52.3 percent of the total government arrears^[19]. Wage and salary arrears amounted to about NIS 476.9 million, constituting about 23 percent of the total arrears in 2018. The arrears of development expenditures amounted to about NIS 294.9 million, constituting about 14.2 percent of the total arrears. The arrears of earmarked payments also amounted to NIS 108.2 million, or the equivalent of 5.2 percent of the total arrears and the tax refunds arrears amounted to NIS 110.1 million, or 5.3 percent of the total arrears.

Figure 2- 7: Outstanding arrear payments (NIS million), 2014- 2018



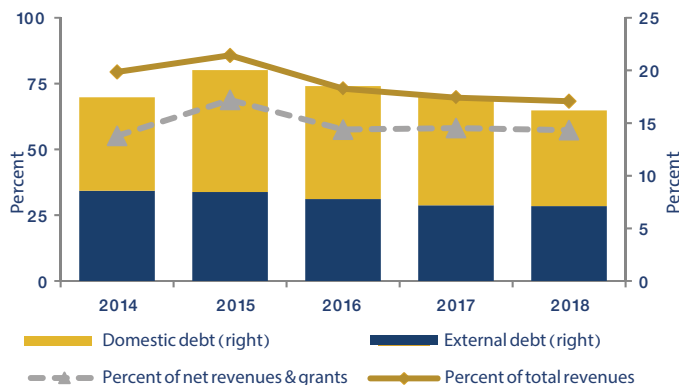
Source: Ministry of Finance.

Government public debt

It should be noted that the government public debt is provided in Israeli shekel, Jordanian dinars and the U.S. dollar in particular, so a large part of the changes in this debt are mainly related to the changes in the exchange rate of these currencies. So the rates of change may vary in this debt depending on the currency used. Data show reduced government public debt at the end of 2018 (measured in U.S. dollar) at about 6.8 percent compared to the previous year, to about USD 2,369.6 million (about NIS 8,916.1 million) or the equivalent of about 16.2 percent of the GDP^[20].

In terms of domestic government debt in 2018, it decreased by 10.9 percent compared to the previous year to about USD 1,337.9 million (about NIS 5,034 million) or the equivalent of 9.1 percent of the GDP, constituting 56.5 percent of the government's public debt and distributed among short-term debts of about 62.3 percent compared to 37.7 percent long-term debt. It should be noted that the bulk (about three quarters) of the domestic government debt

Figure 2- 8: Government public debt as a percent of revenues & GDP, 2014- 2018



Source: Ministry of Finance.

[19] Including use of goods and services arrears (operational expenditure arrears) at NIS 640.7 million, social contributions arrears at NIS 386.4 million, transfer expenditure arrears, including compensations for damage and emergency expenses and support for non-government organizations and local government at NIS 51.1 million. The arrears of minor capital expenditure were NIS 19.7 million. An amount of NIS 11.4 million was paid for public debt interest arrears.

[20] Having neutralized the impact of the dollar-shekel exchange rate, data show drop in public debt in 2017 by 2.5 percent compared to the previous year. This drop is what gives weight to domestic and foreign government debt being calculated after neutralizing the impact of the dollar against shekel exchange rate. The dollar-shekel exchange rate rose from USD 1=NIS 3.480 in the last working day in 2017 to USD 1=NIS 3.763 at the end of 2018. The value of public debt, measured in U.S. dollar, is directly and visibly affected by dollar shekel exchange rate since most of the debt is in shekels. Foreign debt is less prone to exchange rate fluctuation since most of it is in dollars.



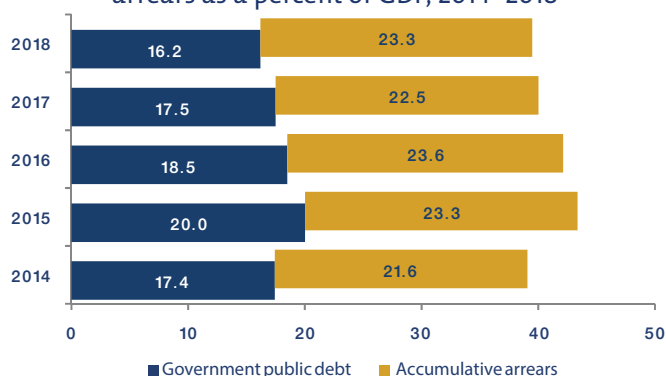
is dominated by the Israeli shekel currency, which makes it vulnerable to the impact of exchange rate fluctuations when calculating this debt in the U.S. dollar currency. The reason for the high rate of borrowing in shekels is that it is the currency of collecting revenues and paying expenses, so the government tries to avoid the risk of exchange rate fluctuations and to move as far away as possible from borrowing in other currencies. Banks operating in Palestine contributed about 99.0 percent of the total government domestic debt in 2018 or the equivalent of about USD 1,324.4 million according to the Ministry of Finance, compared to about 1.0 percent (equivalent to USD 13.5 million) funded by other public institutions, such as the Palestinian Pension Agency, zakat committee and others.

External government debt decreased by 1 percent during the same period, to USD 1,031.7 million (about NIS 3,882.1 million), or 7.1 percent of the GDP, accounting for about 43.5 percent of the government's public debt. In general, external government debt is akin to grants and donations, as well as mostly long-term. Arab financial institutions have contributed about 54.6 percent of external government debt at the value of USD 563.4 million, distributed among al-Aqsa Fund at USD 513 million; Arab Fund for Economic and Social Development at USD 14.2 million; Islamic Development Bank at USD 36.2 million. While international and regional institutions contributed about 32.9 percent of this debt, or the equivalent of USD 339.1 million, distributed among the World Bank by about USD 270.9 million; European Investment Bank USD 44.2 million; OPEC USD 21.9 million, and the International Fund for Agricultural Development contributed about USD 2.1 million. Bilateral loans also contributed about 12.5 percent of the government's external debt, equivalent of USD 129.2 million, distributed among Spain USD 79.8 million and Italy about USD 49.4 million.

The government's public debt ratio to GDP in Palestine is low (16.2 percent) compared to some neighboring countries, where this percentage in Jordan has reached about 94 percent, and in Israel about 61 percent at the end of 2018^[21]. The low rate does not necessarily reflect the strength of the government's financial position, nor does it reflect its ability to continue borrowing, due to a set of caveats that need to be taken into account when analyzing this ratio. Namely, the limited financial resources available to the Palestinian government and the lack of control over a large part of it, which is a real obstacle and challenge to its ability to pay and meet its obligations on time. As well as the risks of fluctuations in exchange rates in the absence of a national currency since a significant part of the government public debt is made in different currencies. This debt is used mostly to cover current expenditure (consumption expenses) rather the investment spending, which is expected to play a pivotal role in achieving sustainable development in the medium and long term. This indicates the weakness of the government's fiscal policy and its long-term unsustainability, especially in light of the decline in external support.

Government public debt indicators for 2018 show that this debt accounted for 57.3 percent of net public revenues and grants, and about 68.3 percent of public revenues. This is an indication of the government's weak financial position and its heavy reliance on irregular foreign grants, which contributed to reducing the debt-to-government revenue

Figure 2- 9: Government public debt and accumulated arrears as a percent of GDP, 2014- 2018



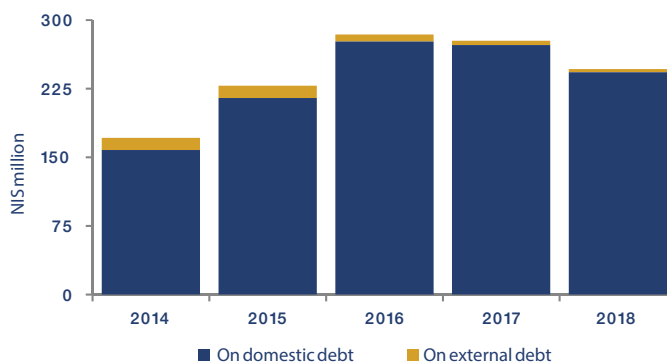
Source: Ministry of Finance.

[21] Jordanian Ministry of Finance (www.mof.gov.jo) and the Bank of Israel website (www.boi.org).

ratio by about 11 percentage point (from 68.3 percent to 57.3 percent). The fact that the government's accumulated arrears are considered part of the public debt to be paid raises the ceiling on the government's public debt, including accumulated arrears to 39.5 percent of GDP at the end of 2018 compared to about 40.1 percent in 2017. These ratios reflect the government's difficulties in obtaining the required funding and the difficulty of sustaining this debt, which leads it to fail to meet its obligations to the private sector, suppliers and others, thereby increasing its arrears.

The actual interest paid on government public debt in 2018 was about NIS 246.3 million, compared to NIS 277.4 million in 2017. Constituting about 104.7 percent of the outstanding interest in 2018, including NIS 242.8 million in interest payments on domestic debt, compared to NIS 3.5 million in interest payments on external debt, especially since the external debt is mostly considered closer to donations and grants than to debt.

Figure 2- 10: Interest payments, 2014- 2018



Source: Ministry of Finance.



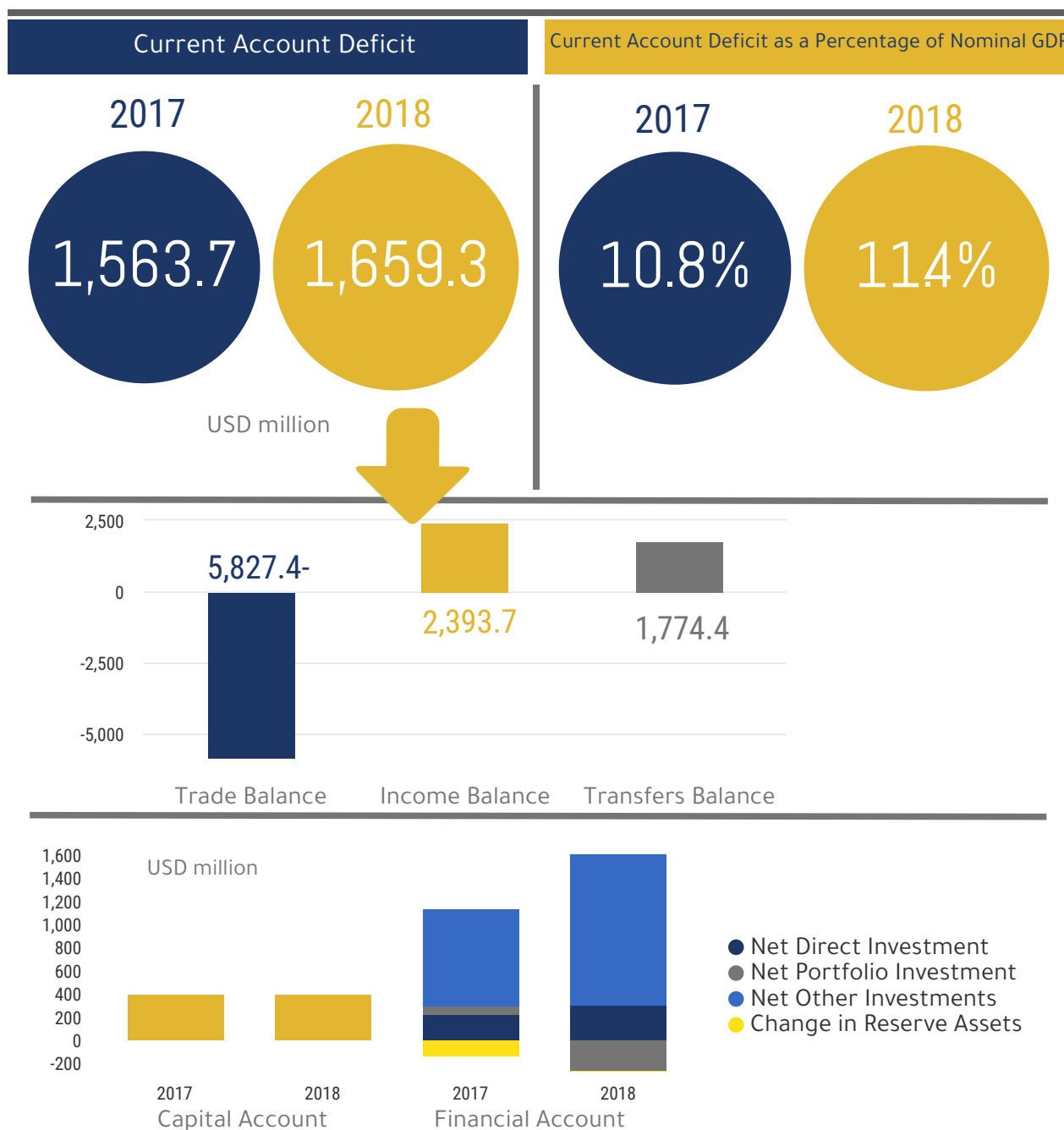
Chapter Three

External Sector Developments



Balance of Payments

2018



Overview

Foreign trade plays an important role in diversifying economic and trade activities, and constitutes an important tributary of the national economy in foreign currencies, and increases the employment volume of exporting companies and thus contributes to reducing unemployment and poverty. On the other hand, foreign trade is the channel through which external risks come to the economy, through trade and financial flows (business movement, workers' remittances, direct and indirect investment) which may affect the banking sector in particular, and financial stability in general.

During 2018, the current account situation in the Palestinian balance of payments witnessed a series of mixed developments. On the one hand, there was a marked increase in income transferred from abroad, due to the rise in compensation of employees in Israel, as well as a significant rise in other investments, as a result of higher currency and deposit flows, and higher direct investment flows. On the other hand, current transfers flows have seen (The most important source of trade balance financing) slightly drop. The outcome of these divergent developments was reflected in a slight increase in current account deficit. This part of the report reviews the most important developments in the external sector during 2018.

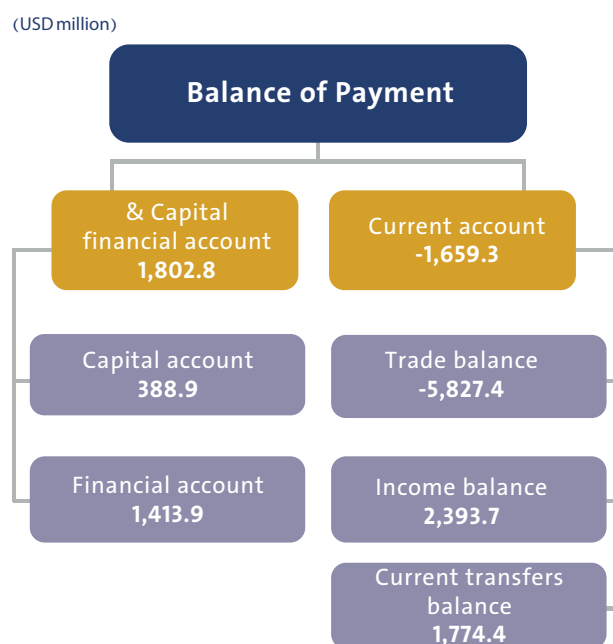
Balance of payments (BoP)

The balance of payments is one of the most important tools by which to measure the performance of the domestic economy compared to the outside world. In addition to its essential role in measuring the size of official foreign reserves and determining the competitiveness of the country compared to other countries. The balance of payments consists of two main accounts: current account, and capital and financial account.

Current account

The current account in the balance of payments consists of four sub-accounts: the goods trade balance; the service trade balance; the balance of income; and the balance of current transfers. In the Palestinian case, the current account suffers from a chronic structural deficit, mainly due to the trade balance, while the surplus in the income and current transfer balances is curbing the deficit. In 2018, the current account balance recorded a deficit of USD 1,659.3 million, up 6.1 percent from 2017, and accounting for 11.4 percent of GDP compared to 10.8 percent the previous year. The increase was mainly due to the marked increase in the volume of imports and the decline in current transfers. The following is an explanation of these developments.

Figure 3- 1: Palestinian balance of payments structure, 2018



Source: PMA & PCBS.



• Trade balance

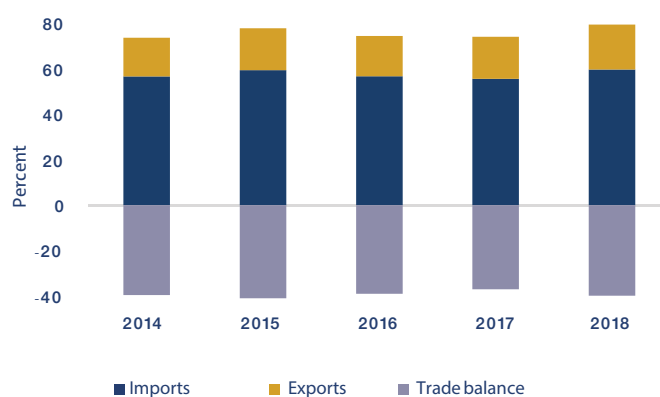
The Palestinian trade deficit in 2018 increased by approximately 8.4 percent compared to the previous year, to USD 5,827.4 million, or 39.9 percent of the GDP^[22], compared to 37.1 percent in 2017. The trade balance analysis is of great importance as it reveals weaknesses in the economy, its inability to meet domestic demand and its increased dependence on the outside to meet its needs, particularly those related to aggregate final consumption. The continuation and high growth of this deficit is indicative of low productivity and weak production base, which is offset by higher import volumes, which

on average accounted for about three times the volume of exports. The trade deficit is specifically linked to the large and chronic deficit in the goods balance (exports - imports), which during 2018 increased by 8.4 percent compared to the previous year to USD 4,813.2 million. Accounting for 33 percent of GDP due to an 8.2 percent increase in goods imports (to USD 7,105.1 million) compared to a 7.8 percent increase in goods exports (to USD 2,291.9 million).

Palestinian exports comprise a small number of commodity groups, primarily the basic manufactures group (wood, paper and metal manufactures, textiles, etc.), which account for about 36 percent of the volume of merchandise exports; and the variety of manufactures (furniture, clothing, shoes, etc.) by 23 percent. The food and livestock group by 17 percent. The raw materials group, excluding fuel accounted for 7 percent, the chemical group at 6 percent, the machinery and transport equipment group at 3 percent; and the rest of the other export groups accounted for about 8 percent of total merchandise exports.

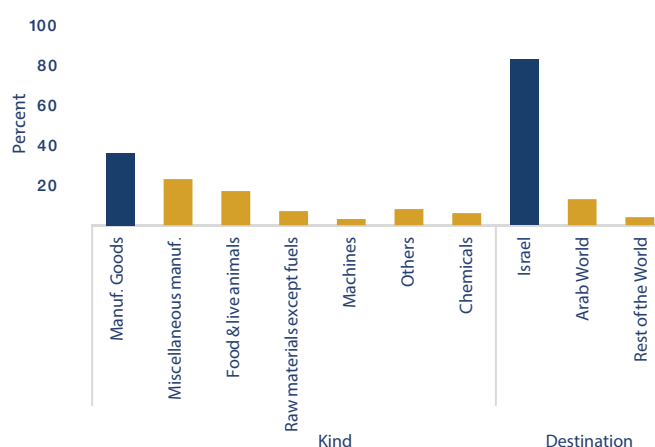
This analysis indicates that export of goods are restricted in a few commodities, with 10 commodities controlling 43 percent of the total exports, mainly stone, plastic bags, olive oil and marble (accounting for about 27 percent of total commodity exports), as well as shoes, tobacco and fresh cucumbers, scrap iron, living room furniture, dates. On the other hand, the analysis indicates that the majority of exports are concentrated in one geographical area, Israel in particular (due to the direct relation between the Palestinian market and its Israeli counterpart). Israel accounts for about 83 percent of the total exports, compared to 13 percent for the Arab world (bilateral trade), and only 4 percent go to the rest of the world.

Figure 3- 2: Trade deficit as a percent of GDP, 2014-2018



Source: PMA & PCBS.

Figure 3- 3: Major exported goods and destination, 2018



Source: PCBS.

[22] The difference in the deficit ratios in this Chapter from those in the first Chapter is due to the fact that the second is in real prices, while the ratios in this Chapter are at current prices.

Alternatively, the food and livestock group ranks highest on the import of goods with 22 percent, followed by the mineral fuel and energy group at 20 percent[23]. The basic manufacturing group at 19 percent, the machinery and transport equipment group at 16 percent; and the chemicals group with at about 9 percent, the range of various manufacturing, beverages and tobacco at 6 percent each, while other commodity imports amounted to about 2 percent.

This analysis also indicates that the bulk of commodity imports is concentrated in some geographical areas, mainly Israel, which accounted for about 57 percent

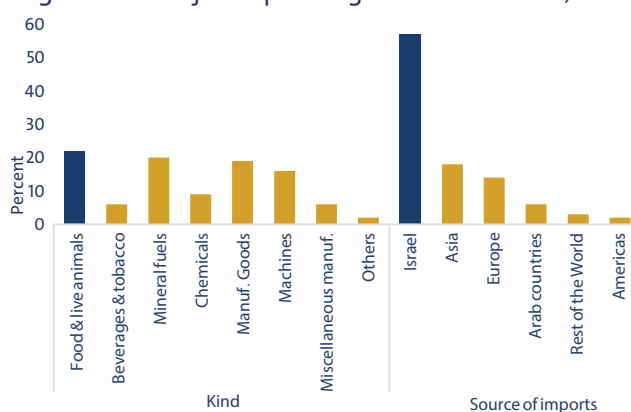
of total imports. While other Asian countries registered 18 percent, European countries at 14 percent, Arab countries (intra-Arab trade) at 6 percent, the Americas at 2 percent, while the rest of the countries with trade relations with Palestine registered 3 percent of total imports of goods.

This geographical concentration of both exports and imports underscores the extent to which the Palestinian economy is dependent on its Israeli counterpart, its dependence on Israeli products, the strength of the trade relationship with Israel and the weak relationship with its Arab neighbors. On the other hand, it emphasizes the ability of Israeli economic and trade policies to directly influence the performance of the Palestinian economy, as it is the primary exporter of goods consumed in the Palestinian market and the party controlling the movement of goods to and from Palestine. At the same time, this concentration underscores the benefit of the Israeli economy from its Palestinian counterpart.

On the other hand, the service trade balance (exports - imports) has not performed better than the goods trade balance. The balance of services ran a deficit of USD 1,014.2 million in 2018, up 8.5 percent from the previous year, against the backdrop of an 8.2 percent increase in services imports (to USD 1,625.8 million) compared to a 7.8 percent increase in service exports (to USD 611.6 million). Travel services account for the most important component since they account for about 70 percent of total exports and 60 percent of total service imports.

It can be concluded from the large trade deficit (both goods and services) that the agreements, trade protocols and preferential transactions that the PA has enjoyed with many countries and international groups have not contributed to facilitating the access of Palestinian products to foreign markets. The actions taken in this regard appear to have focused on considering foreign trade as a tool for financing the Treasury through reliance on customs duties and taxes rather than on fundamental transformations and changes leading to a reduction in the cost and competitiveness of the Palestinian product. Allowing increase the volume of exports to the world market, reducing their concentration in a dominant and non-competitive partner (security and geographical and its control of the movement and exit of goods). These measures have not helped to expand and diversify the domestic production base but have reduced the competitiveness of the Palestinian product compared to its Israeli counterpart and have made the productive sectors generating goods and goods dependent and unable to meet the needs of the Palestinian market. At the same time, it has made Palestine a market for the disposal of Israeli products, with its exports to the Palestinian economy occupying a leading position among international groups, and restrictions on production, import, export and severe Israeli competition have severely affected some production sectors (agriculture and industry).

Figure 3- 4: Major imported goods and sources, 2018



Source: PCBS.

[23] Imports of fuel, gasoline and gas are among the top 10 imported commodities, accounting for 11 percent of imports, while energy accounts for 9 percent of imports.



• Income from abroad

Income transferred from abroad (compensation of employees and investment income) is one of the main sources of financing for the Palestinian trade deficit. In 2018, the income account increased by 20.2 percent compared to the previous year, generating a surplus of USD 2,393.7 million and accounting for about 16.4 percent of the GDP. This account's contribution to the financing of the trade deficit increased to approximately 41.1 percent compared to 37.1 percent in 2017. This increase was mainly due to the increase in the number of Palestinian workers in Israel (127,200 in 2018 compared to 123,400 in 2017). As well as the rise in nominal wages (NIS 242.9 in 2018 compared to NIS 226.9 in 2017). In addition to the impact of the exchange rate USD/NIS (average exchange rate in 2018 decreased by 0.14 percent, from NIS 3.60 to dollar in 2017 to NIS 3.59 in 2018). In this context, compensation for Palestinian workers in Israel accounted for about 97.7 percent of the total compensation of employees. 2018 also saw a rise in returns on Palestinian investments abroad (direct investment, portfolio investment, and other investments) to USD 294.3 million, compared to USD 180.5 million the previous year, due to higher interest rates in many countries,

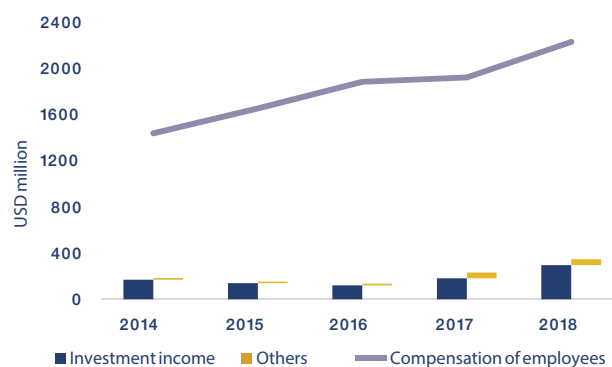
Especially on the USA. This analysis indicates that the bulk of the surplus in net income carried from abroad is mainly related to the compensation of employees in Israel, which accounted for about 93 percent of net income, while the rest is related to the returns on Palestinian investments abroad.

Although compensation of employees is important in reducing the current account deficit, they cannot be relied upon because of their unsustainability, due to their association with the political and security circumstances set by Israel. The surplus achieved in compensation of employees in Israel fluctuates depending on the number of workers, the average daily wage and the exchange rate of the dollar against the shekel. Although income account cannot be relied upon as a fixed source in reducing the current account deficit, it has a key role to play in stimulating the Palestinian trade movement and financing part of the consumption. During 2014-2018, compensation of Palestinian employees in Israel accounted for an average of 13.3 percent of GDP and about 11.7 percent of GNP.

• Current transfers

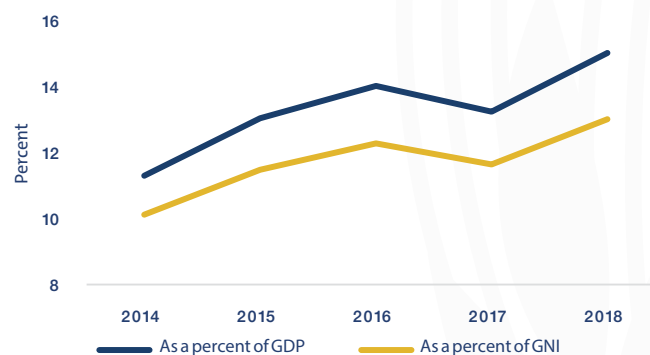
Current transfers include all funds (cash and in kind) provided to Palestine, whether for the public sector and the Palestinian government (budget support), or for the private sector (migrant remittances). These transfers are a key asset to the Palestinian balance of payments, and are of great importance, particularly private sector transfers,

Figure 3- 5: Income from abroad, 2014-2018



Source: PMA & PCBS.

Figure 3- 6: Compensation of employees from Israel, 2014-2018



Source: PMA & PCBS.

which are the basis for a consistent source of current account deficit reduction. Private sector transfers are a financial source without cost, and are not subject to political and economic pressures as the case of the transfers directed to the government. In addition to being a major financier of the trade deficit.

In 2018, the volume of inflows to Palestine increased by 1.4 percent compared to the previous year, reaching USD 2,143.0 million, while outflows from Palestine increased by 25.3 percent compared to the previous year, to USD 368.6 million. Net current transfers decreased by 2.4 percent compared to the previous year, to approximately USD 1,774.4 million. These transfers accounted for about 30.4 percent of the trade deficit, compared to 33.8 percent in 2017. It also reduced the ration of current account deficit-to-GDP to 11.4 percent compared to 23.5 percent if excluded.

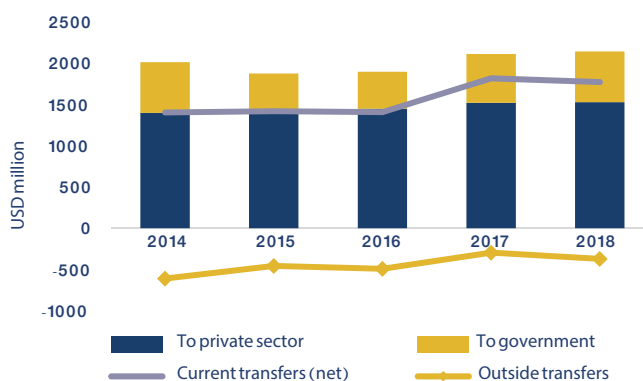
Previous ratios show the importance of current transfers to the Palestinian economy, as they are an important source of foreign currency reserve. They also contribute to reducing pressure on the balance of payments and in supporting the families of the expatriates, which has positive impact on their living standards, activating trade sectors and reducing the poverty and unemployment, providing a social safety net for recipient families, as well as contributing to economic growth. Current transfers, particularly those directed to the private sector, are characterized by continuity and are predominantly flowing (albeit increasing in turbulent political and economic situations, slowing down with political and economic calm) as they are sent by expatriates to assist their families in the face of crises, to ensure their basic needs such as education, housing, treatment, food, etc.

It should be noted that if this type of transfers is given sufficient attention, and organized well, they might constitute an alternative to transfers from donor countries, as they are a free source of financing at no cost to the Palestinian economy, far from political pressures, as well as contributing to increasing direct investment. They also contribute to expanding the deposit base, supporting liquidity in the banking sector, helping to finance the private sector, and supporting aggregate demand in the economy.

Capital and financial account

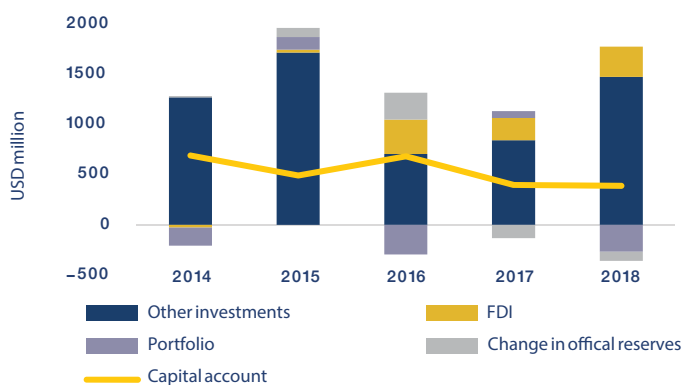
The capital and financial account in the balance of payments consists of two sub-accounts: capital account and financial account. This account (including reserve assets) generated a surplus of USD 1,802.8 million in 2018, up 29.2 percent from 2017, accounting for about 12.3 percent of the GDP. This increase was related to the huge increase in the financial account (41.7 percent) to USD 1,413.9 million, due to the backdrop of a 75 percent increase in net other investments (mainly currency and deposits) compared

Figure 3- 7: Current transfers, 2014-2018



Source: PMA & PCBS.

Figure 3- 8: Capital and financial account components, 2014-2018



Source: PMA & PCBS.



to the previous year (to USD 1,471.9 million). Also the increase in net direct investments of 35.6 percent (to USD 300.8 million), against a marked decrease in net portfolio investments to USD -267.4 million in 2018, compared to USD 68.6 million in 2017. Conversely, net capital account decreased by 2.1 percent in 2018 compared to the previous year, to about USD 388.9 million, mainly as a result of declining private sector flows.

As a result, the financial capital account (including reserve assets) financed about 86.2 percent of the current account deficit in 2018. The change in the reserve assets of the PMA increased by USD 91 million in 2018, compared with a rise of USD 133.5 million in 2017. These assets reflect the overall balance in the balance of payments and the amount of financing in the balance as a whole, given the lack of a national currency and other sources of financing for the Palestinian economy.

Current account sustainability

The sustainability analysis in the current account requires a review of a range of macroeconomic indicators. The most important of which is the trade balance index as a proportion of GDP. If the current account deficit is mainly the result of the trade deficit, this is a sign of structural problems related to the competitiveness and productive structure of the domestic economy, making it difficult to sustain the current account in the long term. In the Palestinian case, this percentage is high, averaging about 39.2 percent of the GDP over the past five years.

The national savings-to-GDP ratio is another important indicator in the process of analyzing the sustainability of the current account, which in the Palestinian case is about 7.4 percent of the GDP on average, which is low compared to other countries. The third indicator is net FDI flows as a proportion of GDP, which is very low, averaging about 2 percent over the past five years. The fourth indicator is the external debt and debt service index as a proportion of exports of goods and services, which amount to about 61.2 percent in Palestine, which is fairly acceptable. The fifth indicator is the reserve adequacy index (the proportion of official reserves covered by monthly imports), as the increase in the number of months of imports of goods and services covered by official foreign reserves, increases the sustainability of the current account deficit. According to international standards, the coverage must range between three and six months at a minimum, but in Palestine, this percentage is barely as high as a month. In general, these indicators indicate poor current account sustainability.

Other factors weaken the sustainability of the current account include: the restrictions and obstacles imposed by the Israeli occupation on the Palestinian economy; the lack of control over borders crossings; the lack of free trade movement; and the weakness of economic and trade policies necessary to activate economic agreements in order to achieve the desired goals of the national economy. The small size of the Palestinian market, and inability to meet the basic needs of the society and its weak structure are factors that reduce the sustainability of the current account. The sustainability of the current account is also affected by the poor financing provided to productive economic sectors (particularly the agricultural and industrial sectors), as well as the weakness of innovation, technology, research and development, which are the real drivers of competitiveness. In addition, the current account deficit has a relationship with the fiscal budget deficit, which shows that the government savings gap has a significant impact on increasing the current account deficit, while the private savings gap has rarely been one of the causes of the current deficit in the Palestinian balance of payments.



Previous analysis of the current account shows that the deficit of this account was financed by withdrawals from external assets of the banking sector and capital grants (the two items financed more than 100 percent of the current account deficit in 2018), while direct investment financing accounted for about 18.1 percent of the deficit for the same year. In the Palestinian case, external borrowing is not used to address the current account deficit, but rather to finance some current expenditures, namely salaries, most of which is long-term debt. Funding using the reserve assets of the PMA has no effect under the current situation.

International investment position (IIP)

The international investment position^[24] is increasingly important in the preparation and analysis of international account statements, as it is an indicator of the sustainability of financial conditions and vulnerability, and the relationship of such accounts to domestic sources of financing, interest rate and return. It is also an indication of the degree of economic openness, external debt and financial stability, and illustrates the relationship with the outside world and the development of external relations between countries, allowing for the facilitation of international comparisons.

The results on the status of Palestine international investment position in 2018 showed that there is still a significant disparity between the balances (investments) of the Palestinian economy invested outside Palestine, and the foreign assets (investments) invested in the Palestinian economy (foreign assets - external obligations) at USD 1,659 million. Deposits in outside banks, as well as cash in the Palestinian economy, accounted for the largest share of external assets and accounted for 59 percent of the total value of external assets.

On the asset side, the results showed that the total asset balances of the Palestinian economy invested abroad amounted to USD 6,597 million, spread among direct investment at 5 percent; portfolio investments of 22 percent; other investments (most notably currency and deposits) by 65 percent; and reserve assets of 8 percent. At the sectoral level, foreign investment at 69 percent of the total external assets of the Palestinian economy.

On the liability side, the findings showed that the total foreign balances employed in the Palestinian economy amounted to USD 4,938 million, distributed between direct investment by 55 percent; portfolio investments of 15 percent; and other investments (most notably currency and deposits) by 30 percent. At the sectoral level, foreign investment in the banking sector accounted for about 35 percent of the total foreign liabilities to the Palestinian economy.

[24] International investment position is defined as a statistical statement that shows, at a point in time, the value of financial assets of residents of an economy that are claims on nonresidents and gold bullion held as reserve assets and the liabilities of residents of an economy to nonresidents. See the Balance of Payments and International Investment Position Manual, sixth edition, IMF.

The difference between an economy's external financial assets and liabilities is the economy's net international investment position, which may be positive or negative. International investment position is strongly linked to the balance of payments; the latter registers all financial and non-financial transactions of nonresidents as they occur while the international investment position records the financial balances of nonresidents at a certain point plus the price changes and exchange rate and other adjustments. Hence, the transactions that contribute to changing the international investment position are those recorded in the financial account of the balance of payments. Assets and liabilities of the international investment position are divided into direct investment (10 percent or more of the capital of nonresident institution). Portfolio investments (less than 10 percent of the capital of a nonresident institution plus investment in bonds), and other investments (commercial credit balance, loans, currency and other deposits) in addition to reserve assets of the central bank that are used to address dysfunctions in the balance of payments.

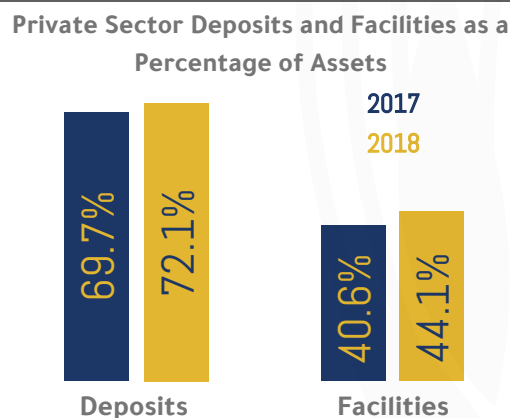
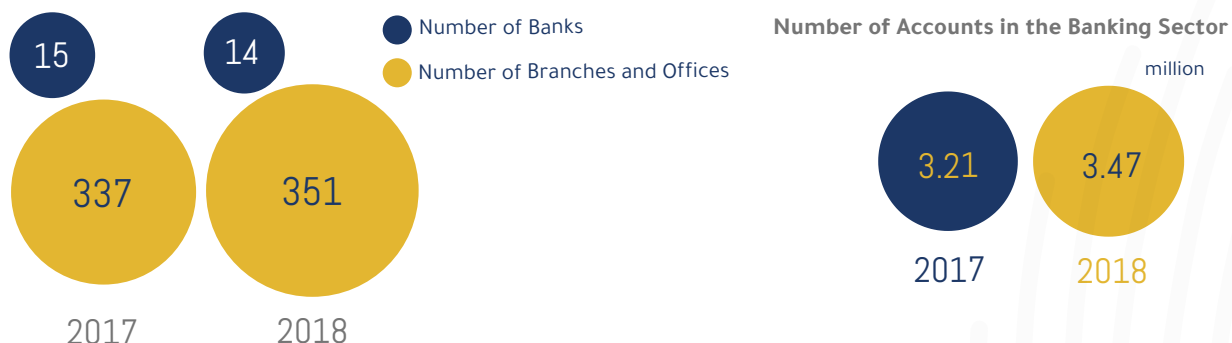


Chapter Four

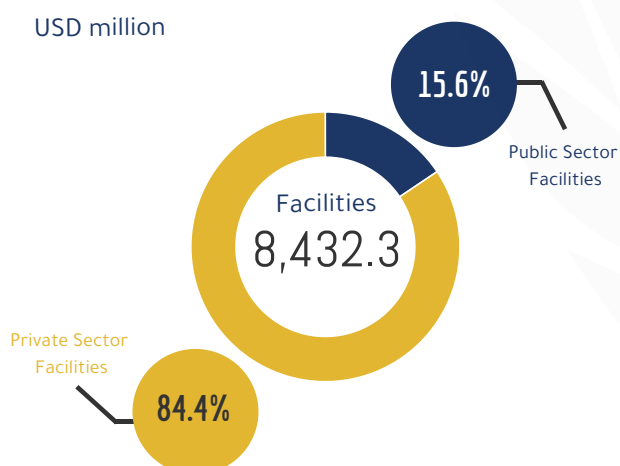
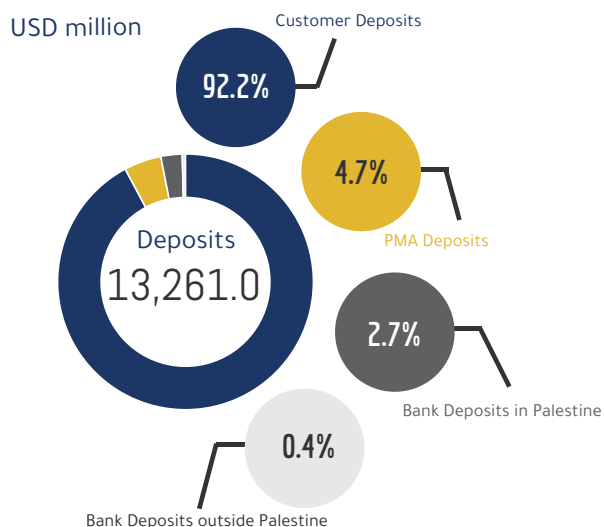
Financial Sector Developments



Palestinian Banking Sector 2018



Deposits and Facilities in the Palestinian Banking Sector 2018



Part I: PMA's Developments

Overview

PMA continued its efforts to develop the regulatory and legal framework governing entities under its supervision, and to support it with various regulatory systems. It also continued to strengthen its Arab, regional and international relationship, with the aim of deepening the ties between the Palestinian banking sector and its regional and international surroundings, and to ward off risks and concerns of the Palestinian banking sector in light of the current circumstances. PMA's efforts to promote financial inclusion in Palestine also continued and recorded many achievements in this regard.

This part of the report highlights PMA's most notable achievements in 2018, as well as the most significant developments in PMA, in terms of its oversight role, its domestic and international relationship as well as a review of its financial position in 2018.

Relations with entities under supervision

PMA has continued its efforts to develop its supervisory role aimed at enhancing financial stability, over the various entities under its supervision and control. These efforts have covered many aspects, both at the regulatory and supervisory level through regulatory instructions, at the level of regulatory systems and their development, or at the level of payment systems and the strengthening of governance and transparency in the banking sector. The following are the most notable of these efforts and actions undertaken by the PMA during 2018:

Strengthening the regulatory and supervisory framework

• Banks

PMA continued to develop the regulatory framework of the banking sector, in accordance with the global banking and regulatory developments, and in the context of continuing to follow up the implementation of the plan to develop the instructions for regulating banking in accordance with the requirements of the Banking Law No. (9) of 2010, the instructions that were issued during 2018 include:

- **Instructions No. (1/2018)** on cyclical fluctuation reserve, as one of the additional capital requirements (capital buffers), approved by the Basel Committee under the regulatory amendments associated with the Basel III Framework, with the aim of reducing the risk of fluctuations in the business cycle and granting credit. Under these instructions, banks are obliged to set up periodic fluctuation reserves between 0 percent-2.5 percent of risk-weighted asset as determined by PMA. In 2018, this ratio was about 0.57 percent of risk-weighted assets, deducted from the dividend/dividend account, and not recorded as an expenditure on the profit and loss statement. The reserve of periodic fluctuations is added within Teir 1 capital when calculating the base and capital adequacy ratio, and disclosed within the declared reserves, and it is prohibited to be used for any purpose without prior approval from PMA.
- **Instructions No. (2/2018)** on the requirements and guidelines for the application of International Financial Reporting Standard (IFRS-9) for the expected credit loss model. The instructions provided an explanation of the various aspects relating to the calculation of these losses and the associated allocations. It also included guidelines for banks, auditors and PMA supervisors.



- **Instructions No. (3/2018)** on the classification of credit facilities, and acceptable collaterals. Under these instructions the acceptance rate for the collateral for cars, machinery and equipment contained in instructions No. (1/2008) for the purposes of the formation of provisions, that was adjusted to 50 percent of the value of the policy or the market value, whichever is lower, for the first two years of the default date, and 25 percent for the third and fourth years for cars. As for the mechanisms and equipment, the ratio is 70 percent for the first two years, then 35 percent for the third and fourth years, provided that the mortgage procedures are completed in the register of security rights in the transferred funds and the insurance policies are endorsed for the bank.
- **Instructions No. (4/2018)** on the application of liquidity coverage ratio, which is a quantitative reform tool established by the Basel Committee on Banking Supervision. With the aim of enhancing the ability of banks to meet liquidity risks in the short-term by ensuring the availability of sufficient stock of high-quality assets (ratio numerator) to cover cash outflows (ratio denominator) that may occur under the stress scenario for a period of 30 days so that they must not be less than 100 percent in all cases. The instructions include a guide to how to apply and calculate the liquidity coverage ratio. The trial application of the ratio has been initiated for six months from the date of the issuance of these instructions (June 2018). With banks complying with the liquidity disclosure requirements from December 2018.
- **Instructions No. (5/2018)** on the application of the Net Stable Funding Ratio-NSFR, which aims to strengthen liquidity risk management in banks by maintaining more stable sources of financing to align asset benefits within and outside the budget and reducing banks' reliance on short-term and unstable sources of funding in the financing of their assets. The instructions include a guide to how to apply and calculate NSFR. Banks will comply with the disclosure requirements for the rate as of December 2018.
- **Instructions No. (6/2018)** on the security and safety requirements of ATMs, which aim to provide maximum protection to ATMs and locations and mitigate potential risks. Under these instructions, banks are obliged to prepare a security policy for ATMs, requirements when choosing ATM locations, implementation plan, cash safe protection, alarm requirements, surveillance and control, and card user protection, in addition to external and independent ATMs, and requirements related to high-risk areas.
- **Instructions No. (7/2018)** on clearing electronic cheques, which regulate all matters relating to electronic clearing. Such as, system ownership, membership, terms and currencies allowed carrying out clearing operations, acceptance of check data registered in the clearing system. Powers of PMA, and responsibilities of the beneficiary member, the responsibilities of the drawee, all matters relating to checks in circulation in the system, the collection of checks, the conditions for returning checks, the reasons for returning them (around 31 reasons). In addition to the clearing sessions, working hours, electronic clearing procedures, and other provisions that regulates the work of electronic clearing.
- **Instructions No. (8/2018)** on the application of regulatory capital requirements in accordance with Basel III (Islamic banks are excluded). With aim to redefine the components of regulatory capital in accordance with the decisions of the Basel Committee, so that the components of eligible capital are used along with risk-weighted assets in accordance with the provisions of Instructions (7/2016) for the purposes of calculating the ratio of the adequacy of the regulatory capital and the bank's hedge capital buffer. Under these instructions, banks must maintain a capital adequacy ratio, and a hedge capital of at least 13 percent of risk-weighted assets (credit, market



and operation), and the ratio is calculated quarterly. The ration for banks that exercise or wish to do banking outside Palestine is up 2 percent. These instructions will take effect from 31 March 2020, while requirements for the disclosure of the regulatory capital adequacy ratio and the hedge capital buffer will be introduced on 31 December 2020. The instructions give banks until the end of 2018 to prepare a plan to correct their situation as stipulated in these instructions.

- **Instructions No. (9/2018)** on the application of capital adequacy requirements for Islamic banks, which aim to apply capital adequacy requirements in accordance with the criteria issued by the Islamic Financial Services Council (IFSB), on capital adequacy and in accordance with Basel III requirements, especially the requirements of Standard No. (15). Under the instructions, Islamic banks must maintain a capital adequacy ratio, and a hedge capital of at least 13 percent of risk-weighted assets (credit, market and operation), and the ratio is calculated quarterly. The ration of a bank that exercises or wishes to do banking outside Palestine is up 2 percent. These ratios will be introduced from 31 March 2020, while requirements for the disclosure of the regulatory capital adequacy ratio and the hedge capital buffer will be introduced on 31 December 2020. The instructions give banks until the end of 2018 in order to prepare a plan to correct their situation as stipulated in these instructions.

As part of the PMA's concern for the integrity and stability of the banking sector and the continuity of its business based on the best international standards and practices. Banks have been asked to complete linking their headquarters with PMA's disaster recovery site using site-to-site VBN through the internet, in order to access critical PMA systems in times of disaster. On the other hand, in order to avoid any risks that may be incurred by dealing with bank checks, banks have been asked to prepare and adopt controls and procedures for the operation of bank checks, take due diligence measures, and provide PMA with periodic quarterly reports of bank check.

In the context of the PMA's great interest in Islamic banking, PMA's Board of Directors decided to establish the Supreme Sharia Supervisory Board to oversee banks and lending institutions engaged in Islamic finance. The Board is made up of a group of scholars of Sharia, jurisprudence and experts in Islamic banking and law, and consists of six members^[25]. The Board works to provide legal assistance and advice to the PMA, to indicate the sharia ruling in Islamic financial and banking transactions, and to express sharia opinion on the compatibility of new Islamic financial and banking products and services that banks or lending institutions wish to provide and the provisions of Islamic sharia. As well as expressing sharia opinion on the investments of Islamic banks in international products in accordance with the offer of PMA, and proposing criteria for determining the conditions for the appointment of members of sharia control bodies and sharia observers residing in banks or lending institutions. Provided that any new products are submitted to the Supreme Sharia Supervisory Board through the department of supervision and inspection after its approval from the Shariah Supervisory Board of the same bank or the sharia observer residing in the lending institution. The decisions of the Supreme Sharia Supervisory Board are binding on all Islamic banks and specialized lending institutions that engage in Islamic finance.

The Supreme Sharia Supervisory Board held its first meeting on June 3, 2018, during which it discussed a number of topics on its agenda, in particular the relationship between the Supreme Sharia Supervisory Board and the sharia oversight bodies at Islamic banks. The Board stressed the importance of the role of sharia oversight bodies in banks. The Board would work to coordinate the application of the sharia principles and provisions related to the banking

[25] The Supreme Sharia Supervisory Board includes Dr. Abdul Mun'im Abu Qahooq (Chairman), Dr. Mahir Khedair (Vice Chairman), Dr. Mohammad Hanini (Secretary), Dr. Na'eem Samara al-Masri, Dr. Abd al-Satar Abu Ghuda, Mr. Mahmoud al-Ram'a (financial expert in Islamic banking).



and financial transactions and various Islamic financing instruments and consider what is referred to them by banks whether to show sharia opinion or adjudication of different opinions.

Moreover, in order to enhance the transparency of the conduct of non-sharia compliant gains in Islamic banks. PMA issued a circular confirming that banks are obliged to determine the disbursements of these gains. So as to prohibit their spending in any matters that benefit the bank, and the need to get rid of the balance of non-sharia compliant gains during the year in the public interest permitted by Islamic law, and to provide PMA with a policy of addressing non-sharia compliant gains.

In another context, PMA issued circular, prohibiting banks, money changers and specialized lending institutions from dealing with financial institutions and their branches located in settlements.

In the area of raising the efficiency of field inspection on banks, a risk-based control approach has been implemented, and a number of field tours were carried out on the basis of this methodology and in accordance with a specific plan. The bank's solvency continued to be strengthened by supplementing its capital to meet the planned minimum of USD 75 million. In promoting bank governance practices, banks have been encouraged to appoint independent and representative members of small shareholders and to form effective committees of bank boards in line with international best practices in particular.

On the other hand, as part of the ongoing efforts to control the liquidity situation in the banking sector and to help banks to ship their accumulated shekel surplus. In 2018, around NIS 14,545.1 million were transferred from banks in the West Bank to Israel, of which NIS 8,764 million were shipped to the Bank of Israel through the Bank of Palestine, NIS 5,175.4 million shipped through Jordanian banks that ship directly to their corresponding Israeli banks, and NIS 605.7 million shipped through other banks.

• Money changers

PMA continued its efforts to promote the safety and stability of the currency exchange sector, as one of the important pillars in promoting financial stability, issuing the following regulatory instructions:

- Instructions No. (1/2018) on renewing the annual license of money changers. Specify the conditions for renewing the license, which is essentially the absence of substantive supervisory notes; the absence of checks returned on the money changers' account; the absence of unpaid fines; and the fact that the money changers is not listed on any of the lists of the perpetrators of the crime of money laundering and terrorism financing. The instructions also specify the procedures for renewing the license.
- Instructions No. (2/2018) on the license fees of money changers (license application fees, flat fees, annual fees), whether the license fees of new companies and their branch, or the annual license fees of existing companies, in accordance with the legal form of the company (ordinary general or limited company, joint stock company, a public shareholding company).

On the other hand, in continuation of PMA's efforts to regulate the currency exchange sector, control its conditions and raise the efficiency of its work, and to reduce potential risks, field inspection rounds on money changers continued during 2018 in both the West Bank and Gaza Strip. With the aim to enhance the commitment of money changers to the laws and the instructions issued by the PMA. Strengthening their commitment to the application of the accounting system and the commitment of companies to the instructions of transfers issued at the end of 2017. And to ensure that



the money changers do not get trusts and grant facilities to the public dealing with the banking sector, as coordinated with the relevant parties to develop the capabilities of compliance supervisors in currency exchange companies by informing them about the requirements of combating money laundering and terrorism financing.

In 2018, PMA issued several circulars regulating banking work, including a circular on the prohibition of dealing with financial institutions and their branches located in settlements. Another defining the procedures to be taken to deal with high risk countries that do not comply with standards of combating money laundering and terrorism financing. Also a circular concerning politically exposed persons, which identifies the categories of politically exposed persons, money changers were obliged to identify, understand and assess risks and apply a risk-based approach to due diligence procedures with politically exposed clients, in addition to take intensive care measures in dealing with these persons. Several circulars have also been issued to take precautionary and protective measures and to take the legal requirement in dealing with persons who are suspicious or listed on the freezing lists. In order to strengthen the principles of transparency and disclosure to customers and in order to preserve their rights with the banking sector, a circular has been issued regarding the delivery of the transfer to the beneficiary in the non-currency contained in it, unless the beneficiary requests in writing otherwise.

• Specialized lending institutions

In continuation of efforts to develop the regulatory framework for specialized lending institutions, the PMA has issued the following regulatory instructions:

- Instructions No. (1/2018) on scheduled, referred to, restructured or non-existent (loans/finances). These instructions are aimed at regulating scheduled, structured and non-performing loans and finances.
- Instructions No. (2/2018) on minimum disclosure requirements of the final financial statements. These instructions are aimed at setting minimum disclosure requirements required by specialized lending institutions in the final financial statements.
- Instructions No. (3/2018) on the requirements and guidelines for the application of the International Financial Reporting Standard (IFRS-9). These instructions provided an explanation of the requirements of the mentioned standard at the level of specialized lending institutions, including changes in the rules for the classification and measurement of financial instruments from IAS 39, as well as other requirements and guidelines.
- Instructions No. (4/2018) on regulating the IT environment in specialized lending institutions. The instructions included requiring lending institutions to adopt appropriate strategies and policies to develop the IT environment, which would be part of the strategies and policies of lending institutions. Under these instructions, lending institutions have also been asked to adopt plans for continuity of work and crisis management to avoid any losses to these institutions. These instructions also included controls and conditions to be observed by lending institutions when outsourcing information technology.

On the other hand, a strategy for specialized lending institutions (2019-2023) has been developed in partnership with the World Bank. This strategy mainly seeks to sustain services and products provided by specialized lending institutions, enhance financial inclusion, and expand the participation of lending institutions in the financing of small and micro enterprises to increase service coverage to 50 percent of the demand.



PMA's routine field inspection of licensed lending companies continued in 2018, with a number of field inspection rounds distributed between comprehensive tours, follow-up tours and special task tours on the new automated system of lending institutions.

Strengthening financial sector's infrastructure

PMA has continued its efforts to build and develop banking and financial systems in accordance with international best practices, supporting the creation of a robust and comprehensive banking structure, which contributes to reducing the risk to the banking system in particular, and the financial system in general. The following is a breakdown of the PMA's most important achievements during 2018:

1. Electronic Clearing System

PMA continued its efforts in 2018 to bring the electronic clearing system into operation. To this end, Instructions (7) for 2018 on clearing electronic checks was issued in accordance with the best practices in the field of electronic check clearing. The terms and mechanisms of linking banking systems with the electronic clearing system were also defined, in cooperation with banks, and the preparation of required documents such as the requirements and mechanisms of the system's work and the policies of the PMA in particular and other documents.

Procedures and mechanisms for clearing checks with old specifications were also developed through the electronic clearing system, and comprehensive system checks have been carried out within PMA as well as with banks, in accordance with the plan developed by the project management. Banks were trained on the system. The project is still under way.

It is worth mentioning that PMA has been keen to hold awareness campaigns for the electronic clearing system by organizing a number of workshops in Ramallah, Gaza, Nablus, Tulkarem and Hebron. These offers will be completed in the rest of the country in the coming period. Banks were also urged to immediately start communicating with their customers to replace old checks with new ones with security and technical specifications free of charge, with the campaign continuing until the end of June 2019.

In the same context, many seminars on electronic clearing were held for many parties such as economic journalists, some universities (Birzeit University, Palestine Technical University-Khdoorie, and Islamic University), and women entrepreneurs in collaboration with the Bank of Palestine. Other seminars will be held in the coming period for many different entities and sectors to raise awareness of this system and the economic implications of its launch on all economic sectors and citizens.

2. Credit Information Systems

PMA continued its ongoing efforts to develop credit operations systems, with a comprehensive questionnaire prepared for all key areas related to the system. The questionnaire targets system users from banks, lending institutions and lease financing companies to explore their views and development proposals, as well as hold an evaluation workshop for the system and to identify observations and suggestions for updating it in accordance with international best standards and practices.

In the context of the development of credit risk reduction instruments, a credit rating system was adapted the in line with the PMA 's future policy and aspirations in this area, and in accordance with the requirements of the



implementation of the national financial inclusion strategy. Including the empowerment of the small, medium, and micro enterprises access to sources of funding, and the possibility of allocating a credit rating system for the enterprise sector and the mechanisms and opportunities for classifying private sector data, which have been more than two years old in the disclosure of the system database. The team responsible for the development of the system was assigned to Prague during the period 18-21/12/2018 to carry out the modernization and development process in accordance with the terms of reference adopted with the developer. The procedures for the implementation of development and modernization by the team are currently being completed as agreed. The new version of the system is expected to be launched before the end of the third quarter of 2019.

On the other hand, proposed instructions were prepared for the PMA's Board of Directors about the bounced checks and consensual settlements systems. This comes within the framework to address the phenomena of bounced checks due to insufficient balance and excessive indebtedness, where some necessary developments were made on the bounced check and consensual settlements systems to reduce the risks of the two phenomena in order to preserve the social and economic fabric. A series of regulatory and statistical reports extracted from credit operations systems have also been developed with the aim of strengthening and developing the analysis mechanisms, with the first version of the reports received and is currently being reviewed and audited in preparation for approval.

As part of the effort to integrate banking systems with the PMA's credit systems, and in order to meet the requirements of financial technology services, measures are being taken to link banking systems with the credit systems of the PMA as the first stage of implementation of automatic credit enquiry using developed techniques. If successful, the trial will be circulated to all banks before the end of 2019. In the coming years, work will be initiated on the second phase, which will include disclosure, update and data exchange between the credit systems of the PMA and banking systems, directly without any manual interventions, which is more complex than the first phase.

3. Information System for Establishments Registered with the Ministry of Education and the Federation of Chambers of Commerce, Industry and Agriculture

This system comes as part of the completion of the implementation of the recommendations of the banking conference for 2013, which aim to enhance and empower the SME sector to access sources of financing, by allowing the PMA to develop a credit rating system for small SMEs based on the financial and demographic data collected on these enterprises. Two MoUs were signed with the Ministry of National Economy and the Federation of chambers of commerce, Industry and Agriculture to enable users of banks, lending institutions and lease financing companies to inquire about the data of these enterprises through the website of the Credit information. Business requirements of the system have been finalized and a contract has been signed with the developer to begin the development process, and is expected to be launched before the end of the third quarter of 2019.

4. Citizens Enquiry System

In order to reduce the risk of the bounced checks due to insufficient balance and to preserve the rights of the beneficiaries, as well as to preserve the legal status of the check paper, the development of a system of inquiry of citizens has been completed. The legal procedures required to launch it on the PMA website are currently being updated to be use by citizens in general, and its use is based on the maker line printed on the check paper, which is expected to be launched before the end of 2019.



5. Systems for Reporting and Disclosure of Deceased persons

In order to maintain bank secrecy and reduce operational risks to preserve the rights of the heirs of deceased persons, and in the absence of a unified database with the relevant official authorities, in this context the preparation of the business requirements including the working mechanism, and the proposed system screens were completed. Data on deceased persons will be collected from entities under PMA's supervision, and from various media and social media. The process of collecting and disclosing the data will be updated on a daily basis. The system is expected to launch in the beginning of 2020.

6. Bank accounts Systems (KYC Database)

In order to meet the requirements of the financial inclusion strategy and its plan to simplify the process of opening accounts for individuals and institutions, and to provide comprehensive data to users about bank accounts by building a unified demographic database for all bank accounts in Palestine, the Business Requirements were finalized, including the proposed working mechanism and system screens. A contract was signed with the developer to initiate the development process, which is expected before the end of the third quarter of 2019.

7. System for Allocating Sovereign Numbers to Legal Bodies

This system aims to fully automate the work and control and regulate the mechanism of allocating sovereign codes to institutions and entities that are not registered or without a license number or a unified registration number from the official authorities, for the purposes of disclosure, authorization and data exchange with the Credit Information System. In this context, the preparation of the business requirements, including the mechanism of work and the proposed system screens, and a contract was signed with the developer to initiate the development procedures. The system is expected to be launched before the end of the third quarter of 2019.

8. System for Calculating Annual Percentage rate (APR)

The pilot version of the annual borrowing cost calculation system was launched with the issuance of the system instructions and guidelines after being discussed with representatives of banks and lending institutions. The system aims to protect the rights of consumers and enhance confidence in service providers by promoting the principles of transparency and disclosure and fair competition among service providers, as well as enabling consumers to easily differentiate between offers from service providers and choose the least expensive and best offer for them. The system is expected to be formally adopted before the end of the third quarter of 2019.

9. Retail Payments System

Efforts to develop the retail payment system, launched the previous year, continued, allowing all personal transfers collected in detail and electronically to be implemented and their results settled definitively through a BURAQ system. In 2018, the system was better regulated, after salary agreements were separated from the system's transfers agreements, with five daily clearing breaks (three sessions for low-level personal transfers, and two others on salary payments). Banks are also executing all transfers of less than USD 10,000 or their equivalent in other currencies through the retail payment system only.



10. Updating SWIFT System

PMA adopted the latest version of the SWIFT system (7.2) after conducting the necessary tests and preparing the infrastructure. In addition to follow-up with all banks in this regard, in order to adopt this version and technical follow-up with the banks. All banks moved to work on the new version in accordance with the requirements of SWIFT as of 17/11/2018. All SWIFT requirements for the Customer Security Program adopted by SWIFT have been successfully completed in terms of the security aspects required to protect their customers, as well as the completion of all banks' security requirements as requested by SWIFT.

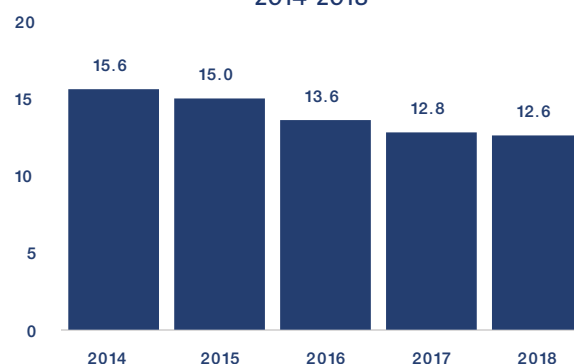
Improving Access to Financial Services

As part of the PMA's policy to strengthen and improve access to finance, the following was conducted:

- **Branching policy**

The year 2018 experienced a change in the structure of licensed banks due to the acquisition of Al Quds Bank of the Jordan Kuwait Bank in Palestine and the purchase of the bank portfolio of The Bank of Jordan Kuwait under the acquisition agreement signed between the two banks. Accordingly, the number of licensed banks decreased from 15 to 14 as of 26 August 2018, including seven local banks (three of which are Islamic banks), and 7 foreign banks (6 Jordanian and one Egyptian bank). However, 2018 experienced an increase in the number of branches and offices to 351 branches and offices compared to 337 in the previous year^[26]. Through its branching

Figure 4- 1: Population density per branch in Palestine, 2014-2018



Source: PMA.

policy, PMA seeks to reduce the population density to the number of branches, with the aim of increasing the efficiency of services provided to customers on the one hand, and to become in line with the internationally accepted rates (about 10,000 people per branch). In this context, the population index for each branch improved in 2018 to 12.6 thousand people per branch, compared to about 12.8 thousand in 2017^[27], and despite this continuous improvement in the ratio, there is still a space for further branching.

- **Financial Inclusion**

As part of the PMA's great attention to financial inclusion, the National Financial Inclusion Strategy (2018-2025) was launched in December 2018, after it was approved (with the composition of the National Committee for Financial Inclusion) from the Palestinian Cabinet in 2018. The launch of the strategy came after a three-year effort during which the document was prepared in accordance with relevant international practices and standards, funded by the Global Financial Inclusion Alliance (AFI) and technical support from the GIZ. It is worth mentioning that Palestine

[26] It is worth mentioning that three banks operating in Palestine have branches outside Palestine, namely: Bank of Palestine has a representative office in the Chilean capital Santiago and another in Dubai Financial Center, in the United Arab Emirates. The Palestinian Investment Bank has a branch in the Kingdom of Bahrain. The Arab Islamic Bank has a representative office in Dubai.

[27] The different value of the index for the years of the time series described in this report compared to the previous reports is due to the different estimates of the population according to the PCBS, and the series has adjusted according to the latest estimates issued for the population.



ranks second after Jordan in the launch of the National Strategy for Financial Inclusion, since the establishment of the financial inclusion initiative in the Arab region by the Arab Monetary Fund, GIZ, and the Global Financial Inclusion Alliance (AFI) at the Global Policy Forum in Sharm el-Sheikh in September 2017.

To implement this strategy, the National Financial Inclusion Committee was formed by a decision of the Cabinet, headed by PMA and Palestine Capital Market Authority (PCMA). The National Committee approved the formation of a technical committee for financial inclusion at its first meeting in May 2018 to be chaired jointly by PMA and PCMA. With a membership of: Ministry of Finance and Planning; Ministry of Social Development; Ministry of National Economy; Ministry of Affairs Women; Ministry of Education and Higher Education; Palestine Stock Exchange; Banking Association; Business Women's Forum; Birzeit University Media Development Centre; Palestinian Central Bureau of Statistics; Palestinian Insurance Companies Federation; Palestinian Network for Small and Microfinance (Sharaku); Federation of Chambers of Commerce, Industry and Agriculture, and the Palestinian Information Technology Association of Companies (PITA).

The chair of the Technical Committee for Financial Inclusion held its first meeting at PCMA headquarters to review the formation of the technical committee and the work committees and establish the terms of reference for their work. The meeting recommended the formation of the technical committee of the participating parties. These parties will play an important role in the implementation of the requirements of the strategic action plan in the implementation stages in the coming years, with the membership of the committee to be reviewed in accordance with the requirements of the stage specified in the strategy action plan. During this meeting, they also discussed the formation of working groups that will oversee the implementation of the strategic action plan, where the need to form six working groups was identified: gender working group, economic media, small, medium and micro enterprises, financial capacity building, and development of financial products and services and IT committee. Moreover, PMA has developed a website for financial inclusion, by contracting a specialized company to design a site for financial inclusion and financial awareness in accordance with the requirements of the National Strategy for Financial Inclusion Action Plan, and funded by GIZ. The site will be managed jointly by PMA and PCMA, and expected to be launched before the end of the third quarter of 2019. In the same context, following the adoption of the General Secretariat of the Arab Monetary Fund on April 27 of each year as a day of financial inclusion in all Arab countries, PMA launched the annual "Arab Financial Inclusion Day" event on 25 April 2018. During this day, lectures were organized at universities and a visit to students of some Schools to the PMA, the distribution of educational leaflets and the launch of an accompanying information campaign, with the aim of enhancing the levels of financial inclusion among the target groups of society in the strategy.

- **Financial awareness and social responsibility**

In continuation of PMA's efforts in promoting financial awareness, the Child and Youth Banking Week 2018 was launched from 11-15/03/2018 in the West Bank and Gaza Strip with the participation of banks, specialized lending institutions, the Ministry of Education and the UNRWA and other participants. This event aims to raise the level of financial and banking awareness among all segments of society, especially the children and young people. Prepare them to deal with financial and banking institutions in the future, through many activities, including organizing visits to school students to banks to inform them of their mechanism of work and banking products provided to customers. In addition, bank representatives visiting schools, giving educational lectures to students, distributing awareness leaflets, and the activities also included the establishment of an exhibition of the virtual bank in both Gaza and Bethlehem.



The last day of the bank week activities was allocated as national savings day, which comes as part of PMA's efforts to promote the idea of saving among Palestinian citizens, as saving is an essential investment pillar to improve living conditions and reduce poverty and unemployment and enhance economic development.

In the context of these major financial and banking outreach achievements, PMA received an international award from the Netherlands-based Global Foundation for The Financial Empowerment of Children and Youth (CYFI) for the best financial and banking awareness event organized in the Middle East and North Africa region to enhance the financial awareness of the children and young people. The award was in recognition of the high level achieved by the PMA in organizing the Child and Youth Banking Week 2018 in Palestine. This is the second time PMA receives such an award, having already received it in 2013.

Moreover, as part of the PMA's relentless follow-up of the crises in Gaza Strip and in light of the crisis in the salaries of government employees, banks and specialized lending institutions were asked not to exceed the discount rate of 50 percent with the possibility of scheduling arrears for those who wish from the public sector employees in the Gaza. So the new monthly installment will be in line with the salary of up to 50 percent of the salary that reaches the employee's account monthly.

PMA also continued its policy of strengthening relations and cooperation with universities, with training programs held within PMA for Palestinian university students. Awareness lectures were also given at Palestinian universities nationwide in various fields of banking, finance and economics.

In the area of strengthening the principles of disclosure, transparency and the protection of clients, specialized lending institutions have been obliged to provide PMA with all fees and commissions they charge their clients, either directly or indirectly, so that their values and proportions are determined in detail.

To deal with customers' complaints on some banks and specialized lending institutions not providing borrowers and sponsors with a copy of the contracts and documents signed by them as well as a copy of the summary facilitation/financing data, the PMA was emphasize that banks and lending institutions should be committed to providing borrowers with these documents. Banks and money changers have also been obliged to continue accepting and trading US dollars -all banknotes- and not to charge any fees or commissions when replacing old banknotes with new ones. With regard to citizens' complaints that they did not receive transfers in the same currency, it was confirmed that banks were obliged to hand over the value of the transfer to the beneficiary in the same currency as the one in which they were sent, unless the beneficiary requested in writing otherwise.

Strengthening local, regional and international relations

PMA has continued its efforts to strengthen and consolidate its local, regional and international relations. Participating in various meetings related to the economic and banking aspects, in the framework of working to connect the Palestinian banking sector with the global banking system in order to achieve the advancement and development of the services provided by this sector. In this context, PMA recorded several achievements in 2018:

- **Local relations**

PMA signed a memorandum of understanding with the Ministry of Tourism and Antiquities, with the aim of jointly cooperating to establish the Palestinian Museum for currency, reflecting the Palestinian economic history through



the ages, including the history of monetary circulation in Palestine and its economic, cultural, social, political and commercial implications. Like many central banks, it contributes to raising financial awareness for the public. Under this memorandum, the two teams will cooperate at all stages of the establishment of a modern interactive museum. That tells the history of currency in Palestine from its inception to the present, including the history and development of the work of the PMA and future prospects. This cooperation will cover all stages of the establishment of the design, supervision and establishment as well as operation at a later stage.

PMA has also signed a memorandum of understanding with the Ministry of National Economy for exchange of data, in cooperation with the Ministry of Communications and Information Technology, allowing banks operating in Palestine to inquire about the data of companies registered with the Ministry of National Economy. The MoU aims to govern the mechanism of linking government institutions and/or public institutions to ensure the security of information and the speed of electronic access, and to improve the quality and level of electronic services that rely on the service subject to the memo to its recipients. The memo also aims to reduce the costs of linking and exchanging information between government and/or public institutions, to achieve transparency and accuracy in the data provided by the information institution, and to improve the efficiency and performance of the service provider and supporting institutions. Under this memo, a joint technical committee was formed to discuss the mechanisms of cooperation between the Ministry and the banking sector. The committee includes the Ministry of National Economy, PMA and the Association of Banks in Palestine, with the aim to develop a mechanism for cooperation and the flow of information for the banking sector to serve this important sector to achieve its objectives, and reduce time and cost for the public and companies wishing to obtain banking facilities from banks.

As part of the PMA's constant communication and strengthening of its relations with the governorates and chambers of commerce in various governorates, it has signed a memorandum of understanding with the Federation of Palestinian Chambers of Commerce and Agriculture and Industry, which requires that the Federation of Chambers of Commerce provide PMA with demographic data for registered establishments. PMA discloses such to banks, lending institutions and leasing companies to facilitate the enterprise sector's access to credit sources.

In the same context, PMA continued to strengthen its relationship with private sector institutions by signing memoranda of understanding with many of these institutions, with the aim of giving them privilege and benefit from the Credit Registry System service, where memoranda of understanding were signed with a number of private sector companies, to benefit from this system. The system developed by PMA, which includes a database taken from the credit information system and relevant demographic data on borrowers and their sponsors, individuals or institutions, and their classification on the bounced check system.

These memoranda of understanding aim to ensure the safety and stability of private sector companies and institutions. Enhance their position and investment capabilities and protect them from exposure to liquidity or credit worthiness problems. Manage credit and operational risk in accordance with international standards, as well as promote economic growth and protect the sector from the risks of defaulting to ensure the continuity of the process of growth in the investment movement in Palestine as well as to protect citizens from overindebtedness. Under these memoranda of understanding, these companies will be able to identify the credit worthiness of the clients they deal with, based on credit sale under post-dated checks for a later maturity date and to make the right credit decision in dealing with these customers.

Moreover, PMA has signed a memorandum of understanding with the Palestinian Technology Park-Technopark, to collaborate and work together to implement, establish and operate fintech innovation laboratory within the first



park building. The Palestinian-Indian Technological Park project is a large Palestinian project with international specifications that contributes to building minds on modern foundations and establishes the rules of creativity and excellence.

As part of strengthening PMA's relationship with universities, PMA has signed several memoranda of understanding with a number of local universities, including Palestine Polytechnic University, the Arab American University, Istiqlal University, Bethlehem University and An-Najah National University. These memoranda of understanding aim at promoting scientific research in the financial field, promoting awareness, financial and banking culture and associated legislation among students of the Faculty of Administrative Sciences and Information Systems. Exchange expertise in several areas of joint interest, and allow Faculty students to train at PMA and the exchange of knowledge. Also, provide the academic sector and students with banking expertise and information, and provide universities with various publications and reports issued by PMA.

As part of the national plan to promote the use of electronic payment methods in Palestine 2018-2023, the PMA's Board of Directors approved Instructions No. (1/2018), on the regulation of the licensing of payment services companies, based on the provisions of Decree-Law No. (17), on the Palestinian National Payment Settlement Law. These instructions aim to develop and expand the use of retail payment methods by developing the infrastructure of electronic payment systems and tools in Palestine in a safe, transparent and effective manner. This is part of the PMA's efforts to carry out its tasks and responsibilities, which aim to achieve financial and monetary stability in Palestine, contribute to sustainable economic growth, reduce the risk to the banking sector in particular, and the financial system in general, and develop E-payment services system.

It should be noted that the provisions of these instructions apply to payment services and their providers and include payment system service, electronic payment services, under which the applications for licensing of payment services companies have been opened. All companies and providers of payment services in Palestine are currently required to begin to correct their legal status in accordance with these instructions.

- **Regional and international relations**

During 2018, PMA continued to develop its regional and international relations. In this context, a memorandum of understanding was signed between PMA and the Central Bank of Oman, to strengthen the relations between the two parties, exchange information and expertise in the field of banking control, bank supervision, financing of micro and small institutions and housing financing, macro prudential control and staff training on banking supervision practices.

PMA has also signed a technical assistance agreement with the European Bank for Reconstruction and Development for policies and partnerships. This agreement aims to enhance the resilience of the Palestinian financial system, help PMA manage assets and liabilities and benefit from the Bank's expertise and capabilities, especially in light of its extensive experience in this area. The agreement is Palestine's second cooperation with the European Bank for Reconstruction and Development (EBRD), the Bank's first investment in Palestine was in March 2018, a USD 5 million loan to Cairo Amman Bank in Palestine, sponsored by the PMA.

Additionally, PMA has obtained the PCI-DSS certification on compliance with the standards of payment card information. It is an international certificate for the application of data security standards stipulated by the PCI-SSC Electronic Payment Card Data Security Board, which is responsible for applying the highest security and protection standards for bankcard information. PMA's compliance with payment card information security standards is a basis for banks operating in Palestine to obtain such compliance, and as a basis for the launch of new payment services that enable



citizens to pay by relying on cards instead of banknotes. This achievement comes within the framework of PMA keeping up with the latest global banking developments and risk management in accordance with international standards. Raising confidence in the measures it takes to protect the banking sector, by providing the best ways and means to ensure the security and protection of the information and data of bank customers and strengthening the protection of bank cardholders' data.

As part of cooperation with the International Monetary Fund (IMF), the PMA hosted a two-week technical mission from the (IMF) to review and develop financial stability in Palestine (FSSR), in terms of the strength of the banking and financial sector and the extent of cooperation between its institutions, and its ability to withstand shocks and risks surrounding the economic environment. The delegation met with all relevant departments of the PMA, as well as various other Palestinian financial and economic institutions such as PCMA; a number of banks; the Ministry of Finance; the Association of Banks in Palestine; and Palestine Deposit Insurance Corporation. An IMF mission visits Palestine from time to time and meets with the most important decision makers and influencers in economic and financial affairs, in order to submit its report to the Ad hoc liaison committee (AHLC) on the West Bank and Gaza Strip.

As part of the PMA's keenness to deepen the links between the Palestinian banking sector and its Arab surroundings, the "Palestinian Banking Sector in its Arab Environment Conference" was organized by the Arab Banking Union, PMA, the Central Bank of Jordan, and the Association of Banks in Palestine, and its Jordanian counterpart. During 21-22 March 2018, the conference addressed a number of banking topics related to electronic payment systems and their impact on enhancing the role of the financial and banking sector; the effectiveness of the mechanisms and legislation of deposit guarantee institutions in protecting depositors' funds and the importance of increasing public awareness of the deposit guarantee system. The conference also addressed prudential control measures and sound anti-money laundering practices and mechanisms; the impact of money laundering on economic and banking activities; Basel III requirements, recommendations, principles and policies adopted in its application; as well as regulatory experiences Arab-Palestinian cooperation in this area. The conference also discussed the situation of Islamic banking in light of the development of the Arab banking sector and the sound practices of managing challenges in Islamic banking, the mechanisms for delivering them to a larger segment of enterprises and individuals, and the development of Islamic financing policies and programs.

PMA's anti-money laundering procedures and measures

PMA continued its efforts in 2018 in combating money laundering and terrorism financing. To this end, the national strategy was developed to address the weaknesses and shortcomings resulting from the national self-assessment of the risks of money laundering and terrorist financing. PMA also issued several circulars to the entities under its supervision, including Circular No. (36/2018), on training and development in the field of anti-money laundering and terrorism financing, under which banks are committed to providing PMA with approved training plans and budgeting for this purpose. Also providing PMA on biannual basis with training statistics in terms of the number of courses for anti-money laundering and terrorism financing officers, bank staff in general, courses held within the bank, number of staff beneficiaries and topics covered by the training.

In order to strengthen the anti-money laundering and terrorism-financing environment in Palestine, PMA issued Circular No. (209/2018), on politically exposed persons (PEPs). Accordingly, banks are required to provide PMA with policies and procedures adopted on strengthening identification and verification procedures of people and the source of their wealth and money. Due diligence and strictness on the financial operations carried out for them. The extent



to which the banking sector and anti-money laundering and terrorism financing systems are configured to determine the degree of risk of these persons and classify them as “politically exposed clients and those related to them” and to issue alerts when carrying out their transactions. Also, provide PMA with quarterly periodic statements of these persons and the persons related to them, and the total number of operations carried out on their behalf.

As part of strengthening banking sector immunity against the risks of money laundering and terrorism financing, PMA issued Circular No. (157/2018), on training courses obtained by compliance supervisors in companies and currency exchange businesses related to anti-money laundering and terrorism financing, and provide PMA with statements that demonstrate and illustrate the nature of these training courses.

Coordination and cooperation with the Financial Follow-up Unit continued. PMA circulating the Unit’s decisions to banks that are relevant to the list of high-risk countries that do not comply with the anti-money laundering and terrorism financing standards of the Financial Action Task Force (FATF). Updated on this list continuously on the website of the PMA and the Financial Follow-up Unit. It also issued Circular No. (74/2018) on providing PMA with the mechanisms, procedures and controls used on banking and transfers systems to ensure compliance with the decisions of the Financial Follow-up Unit and measures to be taken on enhanced due diligence and continuing due diligence towards working relations with those states.

PMA also issued Circular No. (177/2018), with the aim of ensuring the speedy reporting process in cases of suspected money laundering and terrorism financing offences. Money changers are obliged to report, send and receive conversations between the cashier and the Financial Follow-up Unit directly through the Unit’s website (GoAML), according to the guide provided to the money changers. As part of the implementation of the Financial Follow-up Unit’s instructions related to dealing with money changers and currency exchange companies operating and licensed in Israel, PMA issued circulars requesting banks and money changers to provide PMA with the measures and correction procedures taken by them to implement the mentioned instructions.

Moreover, a workshop was held to launch the final report of the work of the national team for the assessment of the risk of Money Laundering and Terrorism Financing. This workshop was held in the presence of the Director of the World Bank in Palestine, Mrs. Marina Weis, director of the Financial Follow-up Unit, members of the national team and specialized teams for assessing the risks of the crimes of laundering funds and terrorism financing, and a number of representatives of legal and official institutions.

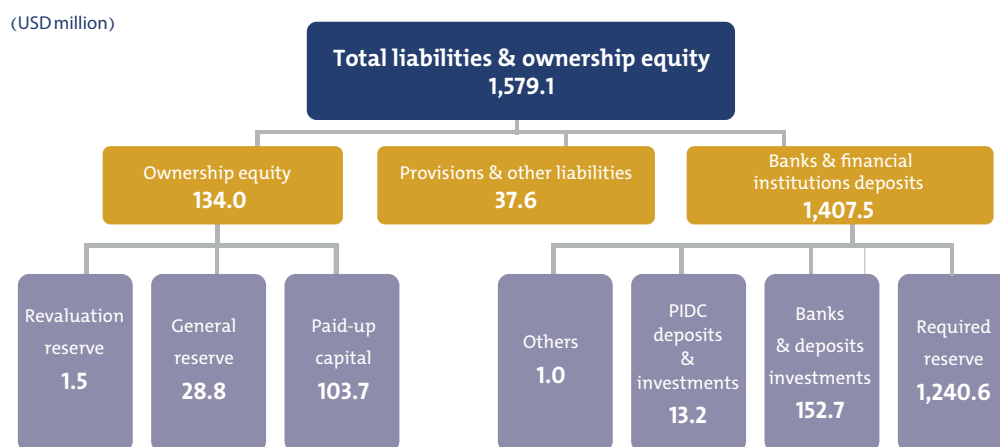
PMA also participated in the activities of the Joint Palestinian-Tunisian Forum of Counter-Money Laundering and Terrorism Financing, held in Tunis. Discussed the fight against money laundering and terrorism financing at the regional and national levels. Also discussed the role of regulatory authorities in the fight against money laundering and terrorism financing in both countries from the perspective of focusing on risk-based control, the importance of risk assessment in the international standard and the adoption of a risk-based approach by banks and financial institutions. At the end, the forum urged the regulatory authorities to put more pressure on financial and banking institutions to inject more financial and human resources into combating the crime of money laundering and terrorist financing. Hoping to enhance the control positions, in addition to strengthening cooperation by financial investigation units in Palestine and Tunisia, and the involvement of the largest number of countries in the upcoming forums. This event is a practical translation of the memorandum of understanding between the PMA and the Central Bank of Tunisia to exchange experiences at all levels, and a true indication of Palestine’s interest in applying international best practices and standards in the fight against money laundering and terrorism financing.



PMA's financial activities

PMA's financial activity in 2018 resulted in its assets/liabilities rising 1.5 percent from 2017 to USD1,579.1 million. The main source of the increase in liabilities was the increase in equity by about 14 percent to USD 134 million, against the backdrop of a 19.3 percent increase in the paid-up capital to USD 103.7 million, as its capital gradually strengthened to USD 120 million. While general reserve remained unchanged at USD 28.8 million, and reevaluation reserve fell 17.1 percent to USD 1.5 million. Also, bank and financial institutions' deposits with PMA, rose slightly by 0.6 percent, to USD 1,407.5 million, influenced by a 10.1 percent increase in required reserve to about USD 1,240.6 million, as customer deposits at licensed banks increased by 2 percent. Other provisions and liabilities decreased by 7.8 percent compared to the previous year to USD 37.6 million.

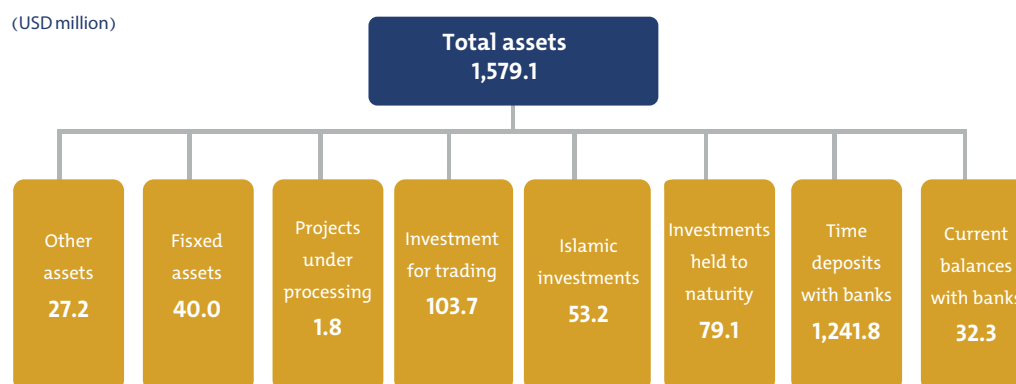
Figure 4- 2: PMA's liabilities structure, 2018



Source: PMA.

For the assets side, the main source of increase was the increase in time deposits (with domestic and foreign banks) by 2.9 percent, to USD 1,241.8 million. Current accounts of banks (domestic and foreign) increased by 46.8 percent to about USD 32.3 million.

Figure 4- 3: PMA's assets structure, 2018



Source: PMA.

At the level of investments, financial investments for trading increased by 1.5 percent to USD 103.7 million, while financial investments held to maturity decreased by 19 percent to about USD 79.1 million, and Islamic investments decreased by 9.2 percent to USD 53.2 million. Fixed assets of PMA (including net fixed assets, land, buildings and other property) also fell 4.5 percent to about USD 40 million at the end of 2018.

In terms of profit and loss, PMA's 2018 revenue swelled by 39.9 percent from 2017 to USD 41.9 million, as net interest earned increased by 43.0 percent, to USD 29.3 million, and other revenues increased by 12 percent, to USD 10.6 million. On the other hand, PMA's expenditure dropped by approximately 3.6 percent compared to 2017, to USD 21.0 million, due to the lack of expenditures to form provisions (approximately USD 3 million in 2017), and the 75 percent reduction in joint venture expenditures to USD 80.6.

Despite the decrease in total expenditure in general, staff expenses increased by 7.8 percent to USD 12.2 million. Also administrative expenses increased by 2 percent to USD 4.4 million, depreciation expenses increased by 99.6 percent to about USD 3 million. While contribution expenses of funding the budget of the Financial Follow-up Unit remained as it is at USD 1.3 million, unchanged from the previous year.

PMA's activity in light of changes in both revenues and expenditures resulted in a net profit of about USD 20.8 million, significantly higher (156.9 percent) compared to the previous year. It was fully transferred to the PMA's paid-up capital account.

Research and development

PMA continued its efforts to strengthen its research, analytical and informatics capabilities, and issuing numerous surveys and studies concerne with financial and monetary statistics. In this context, it continue issuing the monetary survey; the Banking Spread service Survey; and the Coordinated Portfolio Survey, which monitors data on the ownership of financial assets related to portfolio investments (equity and short-term debt), to provide a comprehensive information about the geographical distribution of the issuer and balance of equity, bonds and bonds acquired around the world. This survey contributes to improving the comprehensiveness of international investment status data and the balance of payments.

PMA also continued to issue many report and bulletin, including: Financial soundness Indicators; PMA Business Cycle Index; Annual Report; Standards for Data Dissemination; Inflation Report; Financial Stability Report; Economic Development Report; Public Finance and Government Debt Developments Report; Economic Monitor; Domestic Liquidity Developments bulletin; Balance of Payments and International Investment Position; FDI Survey; External Sustainability Report; Structural Model of the Palestinian Economy; Reduced Formula Model; Actual Exchange Rate Index; Production Gap; Financial Programming; and Mersa Magazine. Several specialized studies have also been conducted related to the functions and objectives of the PMA. All these statistics, research, reports and studies are published on the PMA's Website.

Staff and training

During 2018, PMA continued to develop its 339 staff, by involving them in many specialized professional programs, courses and workshops, which covered various aspects and disciplines of the departments of the PMA and were carried out in the most long-standing local and international institutions.



In this context, PMA's staff benefited from 177 training programs (course/workshop) in 2018 compared to 114 in 2017, where the Monetary Stability Group department staff receiving 30 training programs (including 18 for the Department of Research and Monetary Policy, and 12 for the Department of Monetary Policy and 12 for the Department of Monetary Operations). The Financial Stability Group department staff received 63 programs (of which 45 were for the Supervision and Inspection Department, 12 for the Market Conduct Department, and 6 for the Payment Systems Department). The Administrative Group received 55 training programs (including 18 programs for the IT Department, 6 programs for Human Resources Department, 9 programs for Public Relations and Communication Department, 8 programs for the Financial Department and 14 programs for General Service Department). Staff at independent offices received 29 training programs (including 4 programs for the Legal Office, 5 programs for the Security Office, 7 programs for the Internal Audit Office, 4 programs for the Risk Management Office, and 9 programs for the Governor Office).

This diversity of training programs and distribution mechanism is a sign of PMA's keenness to develop its human resources and keep pace with the latest global developments in banking, monetary and financial aspects related to its work and objectives.



Part II: Banking Sector Developments

Overview

There is a close relationship between the banking sector, economic growth and sustainable development, as it represents a driving force and an engine to stimulate economic activity in general and investment in particular. As an integral part of the economic system, the banking sector influences and is influenced by the economic system, and it has quickly suffered the effects of the slowdown in the Palestinian economy in 2018. Although growth in most key indicators of the banking sector has continued, their growth levels have been low compared to previous years, indicating how sensitive the sector is to economic and political developments and risks.

However, the banking sector, supported by the PMA's actions, has been able to deal with and compat with these risks. This is illustrated by its vital indicators, which generally indicate continued rise in assets, improved liquidity levels, enhanced public confidence, increased deposits, higher credit worthiness, and reduced volume of placements abroad, given the integrity and discipline of the banking sector to the highest international standards. The following is a review of the most important developments in the sector during 2018.

Domestic liquidity

Domestic liquidity levels and inflationary pressures are linked to the country's economic conditions, business cycle, interest rates, and the general price levels. Despite the economic slowdown experienced by both developed and developing economies in 2018^[28], central banks in many developed countries have continued to restrict the work of quantitative easing and expansionary monetary policies by raising official interest rates more than once during the year. Many central banks in the Middle East and North Africa region have also resorted to raising official interest rates as their growth slows^[29], especially those whose currencies are pegged to the US dollar, in order to keep these rates close to US interest rates, to maintain their monetary stability and their foreign currency reserves.

At the Palestinian level, 2018 saw a slowdown in the improvement of domestic liquidity levels to around 3.8 percent from 12.6 percent in 2017 to USD 11,411.9 million, influenced by weak economic performance on the one hand, and changes in liquidity components on the other. In terms of economic situation, the weakness was evident in the level of domestic demand, whose growth slowed to 2.6 percent from 6.8 percent in 2017, against the backdrop of drop in growth in consumer spending to 1.7 percent and investment to 7.0 percent compared to 5.0 percent and 16.9 percent respectively in 2017. This weakness in domestic demand was reflected in economic performance, reflected in a slowdown in the growth rate to 0.8 percent at current prices compared to 8.0 percent in 2017 (and 0.9 percent in real prices compared to 3.1 percent), which in turn slowed the pace of improvement in the level of liquidity in the economy.

[28] See Chapter One of this Report

[29] IMF report "World Economic Outlook" published in April 2019 indicates slow growth in MENA region since it fell from 1.8 percent in 2017 to 1.4 percent in 2018.



At the level of liquidity components^[30], the impact of movements in these components on the liquidity status varied. On the one hand, movements in net foreign assets had slight deflationary effects. After declining by about 0.2 percent (compared to an expansionary 4.3 percent in 2017), to decrease to USD 4,945.6 million, due to the deterioration of the current account position in the balance of payments (by 6.1 percent), against the backdrop of import volume increase of 8.2 percent, and current transfers decrease by about 2.4 percent, specifically. In this context, the balance of payments data (issued by the PMA and the PCBS), and the data available from the Palestinian Ministry of Finance, indicate that the volume of capital inflows to Palestine in form of grants to the public and private sectors have approached the two billion dollar mark, of which about USD 1.5 billion for the private sector. In addition, the amounts of income from abroad (workers' remittances and investment income) which exceeded USD 2 billion.

Movements in net domestic credit have had an expansionary effect on the domestic liquidity status, after rising by 7.9 percent (compared to 16.4 percent in 2017), to USD 8,274.3 million, due to a 9.2 percent increase in private-resident credit, compared with a 1.8 percent decline in net credit to the public sector.

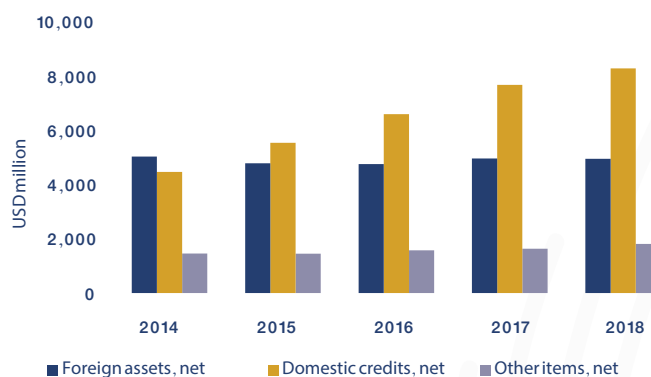
On the other hand, movements in other items net have had an expansionary impact on the domestic liquidity status of about 10.8 percent (compared to 3.8 percent in 2017). This was largely due to continued banking procedures as part of their measures to enhance their ability to compat and deal with the surrounding risks and in compliance with PMA's instructions in force, including continuing to strengthen the capital base and build up the cyclical reserve.

Banking sector performance

Although improvement and development are key features of the banking sector over the years, there is a real fear that the contagion of the slowdown will shift from the real sector to the banking sector, as it is part of the economic system, affecting it and being affected by it. Although the sector's vital indicators (assets, deposits, facilities, equity, and other indicators) continue to grow, but their growth levels in 2018 are lower than in previous years.

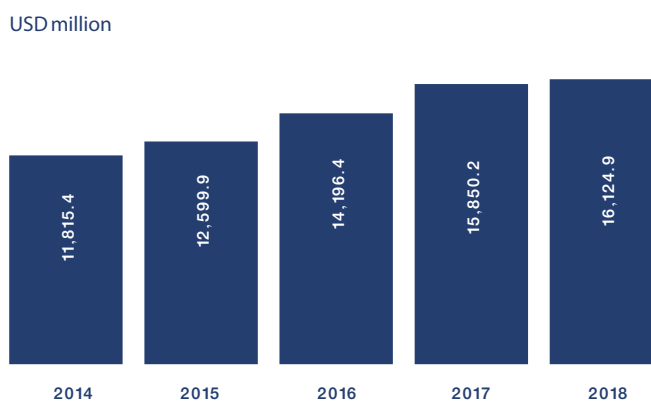
Analysis of the banking sector's consolidated balance sheet (as at the end of 2018) showed that total assets

Figure 4- 4: Domestic liquidity components, 2014-2018



Source: PMA.

Figure 4- 5: Assets of banks operating in Palestine, 2014-2018



Source: PMA.

[30] For more details about these components (Net foreign assets, net domestic credit, and other items net), you may refer to the Quarterly Monetary Development bulletin and the quarterly statistical bulletin posted on the PMA's website www.pma.ps.

increased by 1.7 percent^[31] compared to 11.6 percent at the end of 2017, to USD 16,124.9 million, influenced by changes in the main components of assets (and liabilities) in the consolidated balance sheet of banks.

From the perspective of liabilities (sources of funds), data indicate that the relative importance of customer deposits increased to 75.8 percent of the total available sources of funds compared to 75.6 percent at the end of 2017. On the other hand, the relative importance of PMA and bank deposits decrease to 6.4 percent (PMA has 3.9 percent, outside Palestine 0.3 percent, within Palestine 2.2 percent) compared to 7.2 percent (PMA has 3.8 percent, outside Palestine 1.3 percent, within Palestine 2.1 percent), while equity remained stable at 11.9 percent for the third consecutive year. The relative importance of the remaining liabilities^[32] increased to 5.9 percent compared to 5.3 percent during the same period.

From an asset perspective (use of available funds), data indicate that the share of the direct credit facility portfolio increased to 52.3 percent of the total funds available at the end of 2018 compared to 50.6 percent at the end of 2017. The share of investments and securities portfolio increased to 8.6 percent compared to 7.6 percent, and the share of fixed assets increased to 3.6 percent compared to 3.5 percent. Alternatively, the share of assets held by PMA and banks decreased to 23.3 percent (PMA has 8.8 percent, within Palestine 2.3 percent, outside Palestine 12.2 percent) compared to 24.7 percent (PMA has 9.0 percent, within Palestine 2.3 percent, outside Palestine 13.4 percent). The cash share decreased to 9.8 percent compared to 10.9 percent due to continued shipments of surplus shekels, and other assets to 2.4 percent compared to 2.7 percent during the same period.

To sum-up, this analysis indicates that the increase in banking sector assets during 2018 was accompanied by some changes in the uses of these assets. Banks retaining about 20.9 percent of their total assets in cash and deposits within Palestine compared to about 22.2 percent at the end of 2017, compared to a decline of banks hold balances outside Palestine to 12.2 percent compared to 13.4 percent. Banks also increased their credit portfolio to 52.3 percent compared to 50.6 percent, indicating the positive impact of the efforts and actions taken by the PMA in cooperation and coordination with the banking sector, which in turn led to more employment of funds in the local economy. Banks also increased their investment and securities portfolio to 8.5 percent compared to 7.6 percent. In contrast, banks reduced their holdings in the form of fixed assets and other assets to 6.0 percent compared to 6.2 percent of their total assets during the same period.

Analysis of the sources of fund (liabilities)

PMA's vigorous follow-up plays a pivotal role in maintaining the safety of the banking sector and keep it sound and reliable. This follow-up, together with prudent banking supervision, has also contributed to strengthening the most important component of its budget and attracting more funds, and strengthening its financial base, especially since deposits and equity are the main sources of liquidity and are the most important sources of funds available to banks operating in Palestine.

Banks and non-banks deposits

Analysis of deposits in the banking sector indicates that total deposits (bank and non-bank) at the end of 2018 increased by 1.1 percent compared to 11.7 percent at the end of 2017, to USD 13,261.0 million, influenced specifically by the increase in non-bank deposits, against decline in bank deposits. Bank deposits decreased by 9.0 percent, to USD 1,033.6 million,

[31] It should be noted that the growth rates referred to in this chapter reflect the impact of the change in the exchange rate of the dollar against the shekel.

[32] Including the items of the different provisions, implemented and outstanding acceptances, and other liabilities.



accounting for 6.4 percent of total banking liabilities and about 7.8 percent of total deposits at the end of 2018. The decline came against the backdrop of a significant decline (77.3 percent) in bank deposits outside Palestine, which fell to USD 47.5 million, compared to a 10.1 percent increase in bank deposits among them (within Palestine) to USD 361.4 million, where PMA has about 4.6 percent, which reached USD 624.8 million at the end of 2018.

Customer (non-bank) deposits, the largest and most important component, both at the level of total deposits (92.2 percent), and at the level of total liabilities (75.8 percent) continued to grow in 2018 by 2.0 percent compared to 13.0 percent at the end of 2017, reaching USD 12,227.3 million. In a sign of the continued flow of funds to banks, due to the PMA's policies in promoting financial inclusion, particularly those related to banking branching and their focus on rural and remote areas. During 2018, 14 new branches and offices were opened, to reach a network of branches and offices operating in Palestine of 351 branches and offices spread across the Palestinian governorates. In addition to the increased confidence of depositors in the safety and soundness of the banking system in light of the financial safety net adopted by the Palestinian Deposit Insurance Corporation; and the continued banking awareness campaigns by the PMA. Adding to that the gradual improvement in deposit rates for all currencies circulated in the Palestinian market.

The analysis indicates that the bulk of customer deposits (90.4 percent) is concentrated in the West Bank, with a limited part (9.6 percent) in Gaza Strip. Gaza Strip is suffering from difficult circumstances, in addition to the long-standing blockade, public employees in Gaza have suffered from some government measures (increasing salary deductions and early retirements), which have caused further declines in many economic and social indicators in the Strip, particularly with regard to fluctuating growth rates, and high recorded level of unemployment and poverty.

Figure 4- 6: Banks and non-banks deposits, 2014-2018

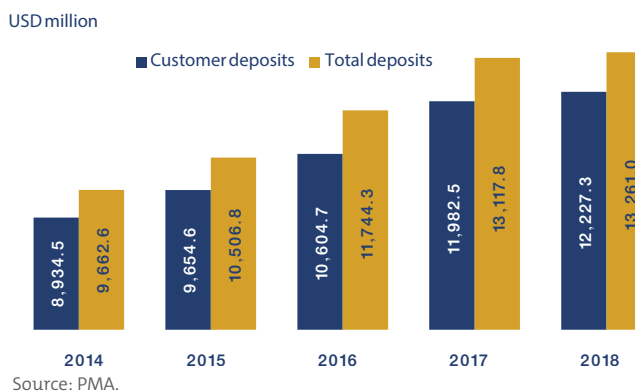


Figure 4- 7: Deposits structure, 2018

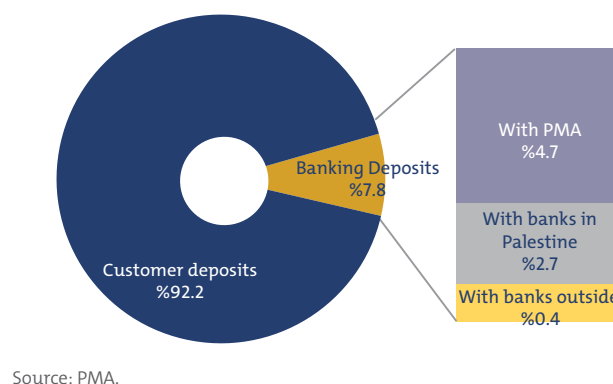
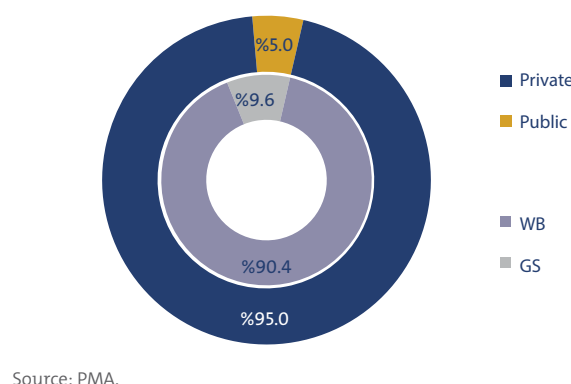


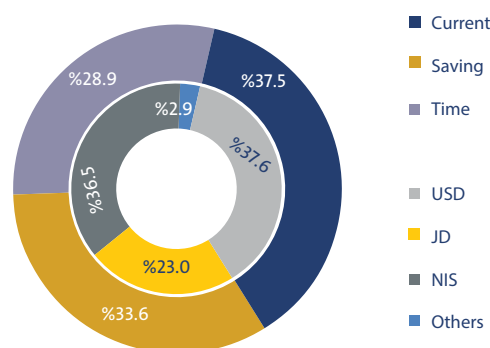
Figure 4- 8: Customer deposits by sector and region, 2018



Most of customer deposits are concentrated in the private sector, whose share has continued to increase over time, to about 95.0 percent (compared to 93.9 percent in 2017), compared to a continued decline in the public sector share, which reached 5.0 percent at the end of 2018 (compared to 6.1 percent in 2017). In this context, the vast majority of private sector deposits are for the resident, and non-resident deposits are still limited to 3.6 percent of total private sector deposits.

An analysis also indicates that although the relative importance of current deposits in favour of savings and time deposits has declined, it has remained at the forefront of the customers' deposit structure at 37.5 percent compared to 39.2 percent at the end of 2017. Followed by savings deposits, whose relative importance increased to 33.6 percent compared to 32.8 percent, and time deposits at 28.9 percent compared to 27.6 percent. Overall, the customer deposit structure in 2018 is the same as that of several years ago. The success of banks in attracting more savings and time deposits has a direct positive impact on their potential for use, particularly in the area of medium- and long-term finance and investment.

Figure 4- 9: Customer deposits by Type and currency, 2018



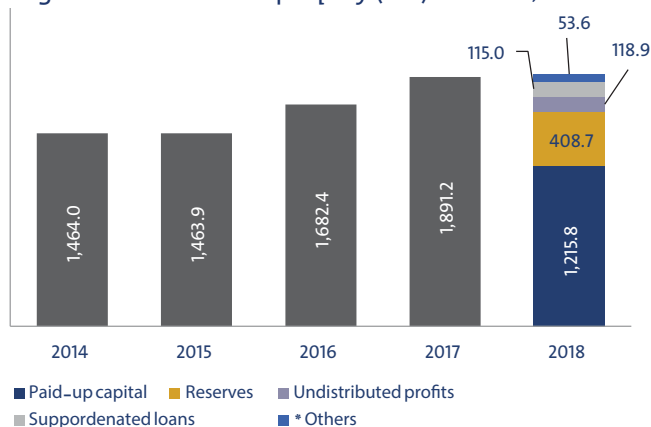
Source: PMA.

Although the Federal Reserve raised official interest rates on the dollar more than once in 2018^[33], the relative importance of dollar deposits fell to 37.6 percent of total customer deposits from 39.5 percent in 2017, yet the dollar remained the largest share. It seems that the weakening of the dollar against the Israeli shekel^[34] was among the reasons for the decline in the share of the dollar, and increase the share of shekel deposits (daily trading currency and settlement of clearing and trading with the Israeli side^[35]) to about 36.5 percent compared to 33.7 percent of total customer deposits at the end of 2017. The relative importance of dinar deposits decreased to 23.0 percent compared to 23.4 percent, and for the rest of the currency to 2.9 percent, compared to 3.4 percent during the same period.

Ownership equity

PMA has continued its efforts to build strong banking entities capable of countering and dealing with risks by strengthening the banking sector's capital base and continuing to grow. In this context, the data

Figure 4- 10: Ownership equity (net) of banks, 2014- 2018



Source: PMA.

[33] The Federal Reserve has effectively raised the official interest rate on the dollar four times in 2018, by 0.25 percentage points each time: from 1.50 percent to 1.75 percent on March 21; to 2.00 percent on 13 June; to 2.25 percent on 26 September; and to 2.50 percent on 19 December 2018.

[34] 2018 experienced a further decline in the exchange rate of the U.S. dollar against the Israeli shekel, albeit slightly and about 0.14 percent, with the average exchange rate of the dollar against shekel in 2018 reaching 3.5949 shekels per dollar compared to 3.5998 in 2017 (based on data from the Bank of Israel. The strength of the Israeli shekel is due to the fundamentals of the Israeli economy; good growth, with low unemployment rates and fiscal deficit, and surplus in the current balance. In addition to the Bank of Israel's purchases of the dollar, as well as the behavior of some speculators in order to make quick financial gains.

[35] Trade with Israel experienced a relative recovery in 2018, with Palestinian exports to Israel growing by 13.1 percent, compared with a 1.6 percent decline in imports from Israel.



indicate that net equity at the end of 2018 increased by 1.1 percent compared to 12.4 percent in 2017, to USD 1,912.0 million. Thus maintaining its relative importance from the total liabilities (sources of funds) of the banking sector at 11.9 percent for the third year in a row.

Paid-up capital is the most important component of equity, and is at the forefront of the line of defense against expected and unexpected risks. Paid-up capital grew by 5.0 percent compared to 8.0 percent at the end of 2017, to USD 1,215.8 million, accounting for 63.6 percent of ownership equity; The importance of various reserves by 21.4 percent^[36]; profit under approval at 6.2 percent; subordinated loans by about 6.0 percent; and other items in equity at 2.8 percent^[37].

The continued growth in equity has contributed to the improvement of the capital base of the banking sector, including capital adequacy ratios, which are a key requirement of PMA and international institutions concerned with standards to maintain the integrity of banking sectors.

Other items in liability

This is a group of items of small value independently listed in the liabilities side of the banks' consolidated balance sheet including implemented and outstanding acceptances (accepted to be paid in Palestine and abroad), which dropped in 2018 by 40.3 percent to hit USD 15.5 million. The group also includes tax provision, which dropped by 25.4 percent to register USD 62.9 million and provisions for loans, which notably rose by 106.5 percent to USD 224.2 million against the backdrop of banks starting to apply International Financial Reporting Standard (IFRS-9), which requires having more provisions, in addition to precautionary measure to face potential risks. Other provisions increased by 6.5 percent to USD 126.8 million. Other liabilities dropped by 1.0 percent to USD 254.0 million at the end of 2018.

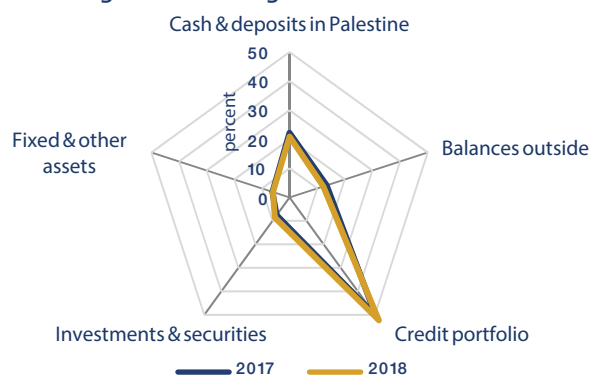
Analysis of the uses of fund (assets)

Central banks use a set of channels to transfer the impact of monetary policy to real economy, with the aim of influencing some of its key variables and bringing about the desired change in various fields and areas, including economic development. In this context, given the specific situation in Palestine, these channels are almost confined to the credit channel, which is becoming more effective as banks become more open to the local economy and provide more financing opportunities, and make them available to various economic sectors, especially the productive and development sectors.

Direct credit facilities portfolio

The credit policies, procedures and methodology of distributing funds available to banks currently play a pivotal role in shifting the impact of monetary policy to macroeconomics to stimulate growth and economic development, and to alleviate the problem of unemployment, as the main financing channel in the economy. PMA can influence

Figure 4- 11: Usage of funds, 2017-2018



Source: PMA.

[36] Includes legal reserves at 10.5 percent; declared reserves at 7.6 percent; general reserves of banking operations at 2.6 percent; and reevaluation reserves at 0.5 percent of net equity.

[37] Includes 2.2 percent capital surplus; undistributed profits of 1.5 percent; and profits (loss) of unrealized long-term investments of -0.9 percent of equity.

this channel and thus the size of credit, particularly provided to the private sector through some stimulus measures aimed at influencing the composition of lending portfolios. Such as strengthening the granting of facilities to certain areas (Jerusalem, Gaza) or for some active economic sectors (development sectors, high-productivity sectors, SMEs sector) or for some economic activities (technology, education, tourism, entrepreneurship, women, professions, handicrafts, etc.).

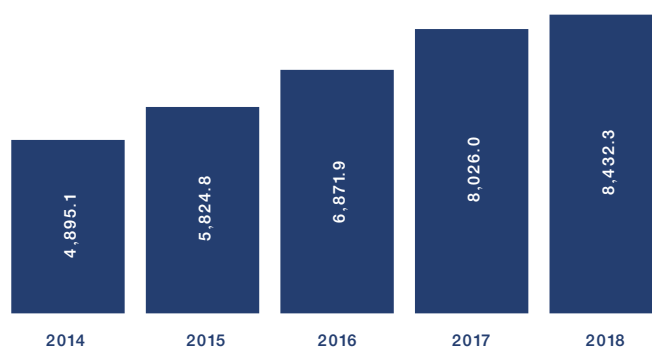
Over the past years, as part of its ongoing efforts to raise the rate of domestic investment of available funds and in cooperation with the banking sector, PMA has been able to inject increasing amounts of funds into the Palestinian economy, in various fields, areas and economic activities in the form of direct credit facilities. Thereby activating the role of the banking sector in the local economy and in the process of economic development.

In 2018, the credit portfolio accounted for 52.3 percent of the banking sector's total assets, compared to 50.6 percent at the end of 2017, up 5.1 percent, to approximately USD 8,432.3 million. The continued growth of credit portfolio, both in terms of volume and relative importance, is an indication of the continued trend towards further investment of Palestinian banking sector funds in the local economy despite the high risks involved.

With this increase, the West Bank's share increased to 88.7 percent of the total credit portfolio, up 6.3 percent from 2017 to USD 7,483.3 million at the end of 2018. This is a sign that the share of the Gaza Strip has declined to 11.3 percent. Influenced by the recent developments in Gaza Strip, and increased its potential risk, which pushed banks towards greater discretion in their credit policies towards Gaza. In turn, this caused the volume of facilities granted to Gaza to decline by about 3.8 percent from 2017, down to USD 949.0 million at the end of 2018. Despite the PMA's attempts and efforts to alleviate the suffering and difficult conditions in Gaza, and to strengthen the role of the banking sector in the Strip, where it has worked to promote banking penetration by opening more branches in Gaza, and the number reached 59 branches at the end of 2018. In addition, several banking awareness campaigns have been

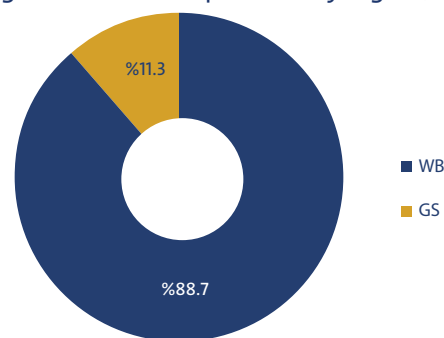
Figure 4- 12: Credit portfolio, 2014- 2018

USD million



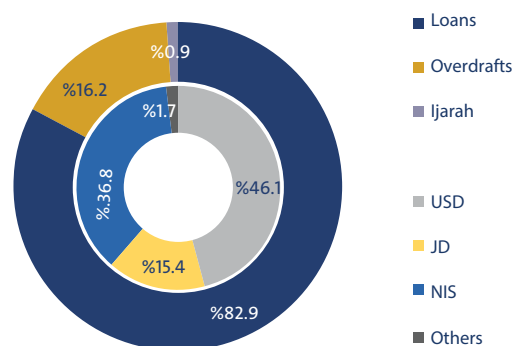
Source: PMA.

Figure 4- 13: Credit portfolio by region, 2018



Source: PMA.

Figure 4- 14: Credit portfolio by type and currency, 2018



Source: PMA.

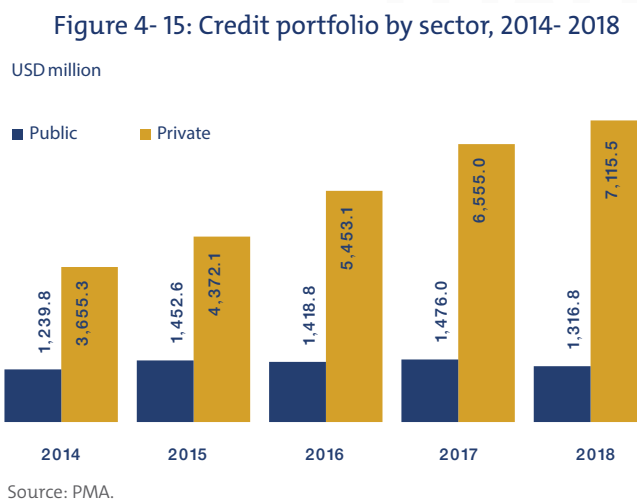


carried out in the Gaza Strip in conjunction with those in the West Bank, and other measures and arrangements to alleviate the difficult conditions and suffering in the Gaza Strip.

2018 also experienced an increase in relative importance of loans in the credit portfolio structure, as it continued to acquire the largest share of the portfolio (82.9 percent) compared to 82.2 percent in 2017. This increase came specifically at the expense of the overdraft account, whose share fell to 16.2 percent compared to 17.1 percent of the total portfolio in 2017, due to the current decline in the overdrafts granted to the government. The percentage of leasing that ends with ownership (Ijarah) remained marginal below 1 percent as in previous years.

2018 experienced further domination by the US dollar, with its share rising to 46.1 percent of the total credit portfolio from 44.7 percent at the end of 2017. In addition, the share of the JD increased to 15.4 percent compared to 14.1 percent of the total credit portfolio during the same period. In contrast, the share of the Israeli shekel fell to 36.8 percent compared to 39.7 percent of the total portfolio at the end of 2017. The share of the remaining currencies remained marginal below 2 percent of the total credit portfolio during the same period. Changes in lending interest rates in the domestic market^[38], as well as fluctuations in exchange rates and government facilities, appear to have been the most important factors responsible for changes in the shares of different currencies in the credit portfolio.

2018 also experienced an increase in funding granted to the private sector in terms of volume and relative importance, to about 84.4 percent of the total credit portfolio compared to 81.6 percent in 2017. Indicating a decline in the relative importance of public sector funding for the seventh consecutive year (the government accounts for the bulk of these facilities) to 15.6 percent, compared to 18.4 percent in 2017. Public sector funding declined by 10.8 percent in 2018 to USD 1,316.8 million, compared with growth of 4.0 percent at the end of 2017. Public sector funding fluctuates in size and importance from year to year, depending on developments in government fiscal



operations (revenues, grants and expenditures) and related liquidity conditions, and its need to borrow to pay off some of its immediate or accumulated obligations. This may affect the private sector opportunities to obtain the required funding, limiting its ability to direct this funding towards development projects.

In the same context, the portfolio of facilities granted to the private sector continued to rise by 8.6 percent compared to 20.1 percent in 2017, to USD 7,115.5 million. Distributed to various economic activities, productive and service, and in proportions ranging from 26.2 percent of the total funding granted to the private sector for real estate, construction and land activities, and 2.0 percent for agricultural activities and livestock. The relative importance of financing for the purchase of consumer goods as well as for the purchase of cars declined in 2018, in light of PM's measures to rationalize this type of financing. The relatively low importance of financing for agricultural activities is due to the high degree of risk associated with this activity as seasonal, on the one hand, and the fact that a large part of it is

[38] Dollar lending rates in the Palestinian market increased from 5.79 percent in 2017 to 5.92 percent in 2018, and in shekel from 7.09 percent to 7.18 percent, while decline for the dinar from 6.79 percent in 2017 to 6.75 percent in 2018.

unregulated on the other hand, limiting the ability of banks to finance such activity. In addition, there are other alternative sources of financing other than banks, represented by specialized lending institutions that are supervised by the PMA.

It is noteworthy that the PMA has made intensive efforts during the past period to strengthen and support the infrastructure of the banking sector, in order to deepening the financial depth in the Palestinian economy. Which contributed to the significant expansion of the credit granted to the private sector on the one hand (on average about 17 percent during 2010-2018), and on the other hand, increased the loan-to-GDP ratio from 32.4 percent in 2010 to 57.7 percent in 2018. However, the credit channel remains vulnerable to the impact of security and political developments on the overall economic activity and its direct impact on the environment and investment climate in Palestine.

Therefore, PMA is keen to follow up, monitor and control any developments in the risks related to the credit portfolio. Working on several precautionary measures and regulations that help banks to increase credit grants in the local economy, and to minimize the degree of risk associated to the lowest possible degree, through continuous development of credit information systems and effective risk-based supervision.

Placement abroad

As the level of domestic placements of funds available to the banking sector increases and financial depth indicators improve, placements abroad (the second source of funds available to banks operating in Palestine) is declining in volume and importance. It decline the fifth consecutive year, falling to 19.3 percent of the total use of funds available at the end of 2018 compared to 19.6 percent at the end of 2017, to approximately USD 3,113.5 million (roughly the same as in 2017), accounting for 23.5 percent of total deposits compared to 23.7 percent in 2017. That is, it is well below the maximum limits set on the PMA's instructions of 55 percent of total deposits.

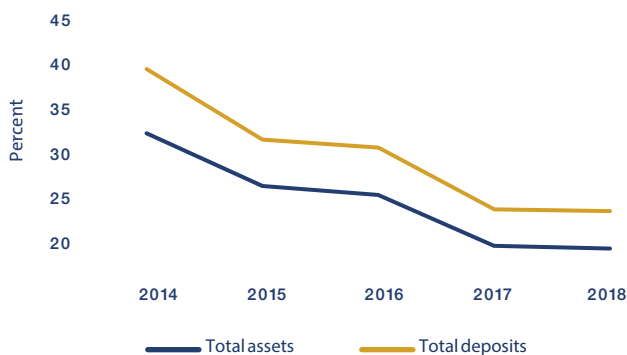
Balances of banks invested abroad are the main component of placements abroad, accounting for 63.3 percent of these placements, or equivalent to USD 1,969.8 million, down 7.2 percent from the end of 2017. Investment in some financial instruments is the second component of placements abroad, of which 30.9 percent, valued at USD 963.4 million, is up 13.8 percent from the end of 2017^[39]. Credit facilities granted outside Palestine account for the third

Figure 4- 16: Credit portfolio by economic activities, 2017-2018



Source: PMA.

Figure 4- 17: Placements abroad as a percent of assets and deposits, 2014- 2018



Source: PMA.

[39] In this context, it is noted that the external investments of banks in all types of securities are restricted by the need to obtain prior approval from the PMA, and to invest them in investments with a high credit rating. Taking into account the degrees of concentration, at the level of the single institution, and at the level of the state and currency as well, based on instructions No. (52008/, item 57/).



component of these placements, with a ratio of 5.8 percent, valued at USD 180.1 million, up 26.9 percent from the end of 2017. Consequently, the decline in the balances of banks placed abroad is the main reason for the decline in placements abroad, while the increase in investment in financial instruments and facilities granted outside Palestine has mitigated the decline in placements abroad.

In general, the continued decline in placements abroad reflects the effectiveness of the PMA's actions and policies aimed at encouraging banks to invest more money in the domestic economy, through the gradual reduction of the placements abroad.

Balances at PMA and banks

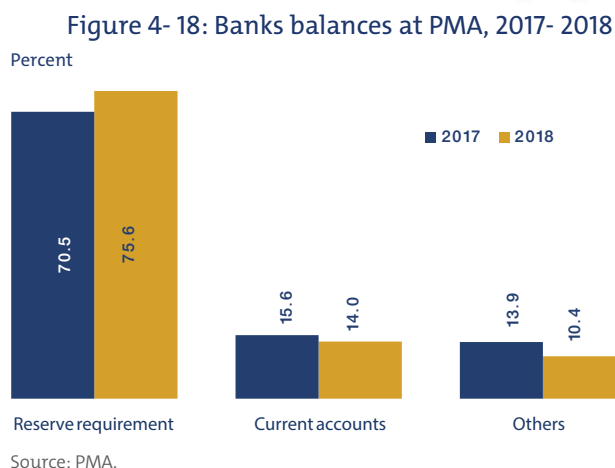
The analysis of the financial statements of banks operating in Palestine indicates that balances are the third component of the investment of available funds, including balances with PMA and other banks, both in Palestine and abroad. By the end of 2018, these balances accounted for 23.3 percent of total assets, valued at USD 3,763.7 million, down 3.8 percent from the end of 2017, against the backdrop of a decrease in assets held by PMA as well as those held by banks outside Palestine.

Balances held with banks outside Palestine (the largest and most important component of foreign investment) decreased by 7.2 percent from the end of 2017, falling to USD 1,969.8 million, accounting for 12.2 percent of total assets compared to 13.4 percent at the end of 2017.

The balances held with PMA also registered a slight decline (0.9 percent) compared to the end of 2017. It fell to USD 1,416.0 million, accounting for 8.8 percent of total assets compared to 9.0 percent at the end of 2017. The required reserve is the largest component of the bank balances at PMA, with approximately 75.6 percent of these balances at USD 1,070.1 million, up 3.4 percent from the end of 2017, against the backdrop of increased customer deposits. Current accounts accounted for about 14.0 percent of these balances, valued at USD 198.4 million, up 27.4 percent from the end of 2017, indicating that banks prefer to deposit these funds with PMA rather than use them in other areas. Other accounts accounted for about 10.4 percent of these balances, valued at USD 147.5 million, down 38.1 percent from the end of 2017.

Balances held with banks in Palestine (bank balances among them) increased by 5.3 percent from the end of 2017, reaching about USD 377.9 million, accounting for about 2.3 percent of total assets for the second year in a row, indicating that the interbank market is fragile, inefficient and weak.

Overall, this analysis indicates that about 104.2 percent of the decline in the balance item is mainly due to the decline in balances held with banks outside Palestine, and 8.6 percent is due to the balances held with the PMA. While the increase in the balances held by banks inside Palestine reduced this decline by 12.8 percent at the end of 2018.



Investment portfolio

Financing, investing, supporting productive projects, creating the appropriate environment and investment climate, are key and important factors in economic development. Some are related to internal aspects that can be managed and controlled, such as finance. While others are largely related to external aspects that are difficult to control, such as the investment climate. That is, in the Palestinian situation is basically related to the occupation and its control of borders, crossings, freedom of movement, access to personnel and goods, and the blockade Sanctions, and other measures that lead to increased political and economic uncertainty, increase the degree of risk to which different sectors of the economy are exposed. These factors negatively affect investment opportunities, and thus the size of the investment portfolio, which is one of the channels for the employment of available funds for banks operating in Palestine.

In this context, the data indicate that the slowdown in the Palestinian economy during 2018 did not have any negative impact on banks investment decisions. On the contrary, banks have increased their investments, both short and long-term. Securities-related bank investments (certificates of deposit, bonds and securities) increased by about 13.4 percent from 2017 to USD 1,123.3 million, accounting for about 6.9 percent of its total assets. At the same time, banks' long-term investments (investment in companies, financial and banking institutions, subsidiaries, affiliates and others) were up by 20.7 percent from the end of 2017, reaching USD 262.2 million, or 1.6 percent of their total assets. It seems that banks' assessment of the economic slowdown during the year, as a temporary event only appears to call for further precautionary measures, without having a direct negative impact on their investment decisions

Other items in assets

Represents a range of items independently listed on the bank's assets side. Such as: cash, which fell by 8.4 percent from 2017, down to USD 1,582.6 million, indicating continued shipments of surplus shekel; fixed assets, which rose 6.0 percent to USD 582.7 million; and other assets, down 10.5 percent from 2017, fell to USD 378.2 million.

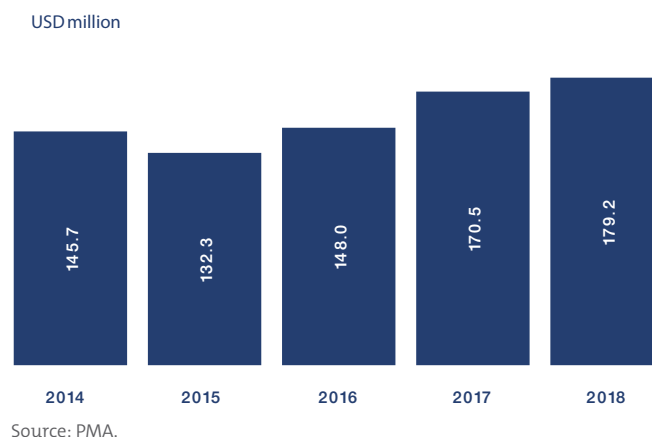
Profits and losses

Data from the profit and loss statement for the banking sector show net income at the end of 2018 of USD 179.2 million, up 5.1 percent from the end of 2017. In this context, the data indicate that the banks generated net income of USD 699.5 million from all operations, an increase of 6.2 percent, against expenses (other than interest) of USD 444.5 million, up 8.9 percent from the end of 2017.

Analysing the contributions of various activities to net realized income, shows that the largest contribution came from interest, with net interest income of about USD 507.1 million, up by 8.6

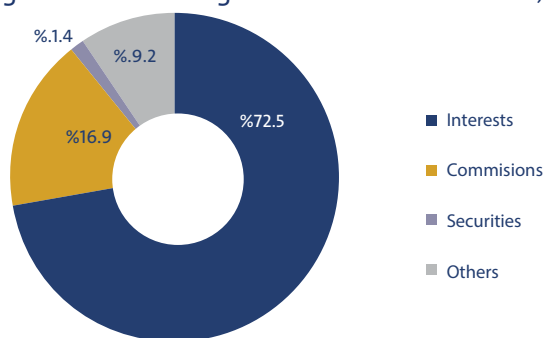
percent compared to the end of 2017, and accounting for 72.5 percent of net income generated, compared to 70.9 percent in 2017. The rest of the revenue came from net non-interest income, which rose slightly (0.1 percent), to USD 192.0 million, accounting for 27.5 percent of net income achieved compared to 29.1 percent during the same period.

Figure 4- 19: Net income of banks operating in Palestine, 2014- 2018



Non-interest income is related to the sum of the activities carried out by banks to generate income. That is, commissions of USD 117.9 million, accounting for 16.9 percent of total revenue generated at the end of 2018; securities and investments valued at 10.1 million at 1.4 percent; the rest of the other income is about USD 64.0 million, or 9.2 percent of the total income generated. This analysis generally indicates that banks continue to rely on their core function (financial intermediation among economic sectors) to generate income.

Figure 4- 20: Banking sector revenues structure, 2018

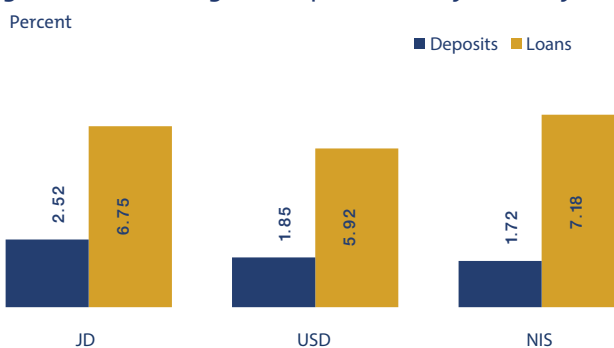


Source: PMA.

Interest rates in the Palestinian market

The prevailing interest rates (deposit and lending) in the Palestinian market are linked to market mechanisms, competition between banks and the degree of risk on the one hand, and the rates in the countries issuing currencies circulated in Palestine on the other hand (US dollar, Jordanian dinar, Israeli shekel). Data on the average annual interest rates of various currencies circulated in the Palestinian market indicate a gradual rise in the lending interest rates for both the dollar and the shekel, as opposed to a gradual decline in the interest rate of lending in dinars. While the average annual interest rates for deposits in all currencies in circulation have gradually increased compared to 2017.

Figure 4- 21: Lending and deposit rates by currency, 2018



Source: PMA.

At the deposit level, the average annual interest rate on dinar deposits increased by about 47 basis points to 2.52 percent; on dollar deposits by about 45 basis points, to 1.85 percent; and on shekel deposits by about 29 basis points, to about 1.72 percent. At the lending level, the data indicate that the average annual interest rate on the dinar has fallen by about 4 basis points, falling to 6.75 percent, against the increase in the dollar by about 12 basis points, to reach 5.92 percent, and on the shekel by about 9 basis points, to 7.18 percent in 2018.

These changes resulted in a decrease in the margin between lending and deposit interest rates on all currencies in circulation, with the margin on the shekel remaining higher in the Palestinian market. The margin on the dinar currency fell from 4.74 points in 2017 to 4.23 points in 2018, on the dollar from 4.40 points to 4.07 points, and on the shekel from 5.66 points to 5.46 points during the same period. Despite this decline, the margin remains high compared to that in the countries issuing these currencies. The reasons behind that related to the high degree of risk surrounding the banking and economic environment in general in Palestine, due to the political changes, as well as the impact of the volume of liquidity per currency and the cost of proving them, particularly with regard to Israeli shekels. Further reductions in the interest margin will undoubtedly have a direct impact on the efficiency of financial intermediation, the competitiveness of the banking sector, its role in activate economic growth, and the overall degree of financial stability.

Payments system

The national payments system is one of the main pillars of a strong and comprehensive banking infrastructure. It contributes to reducing the risk to the banking sector in particular, and the financial system in general, and helps to develop the banking and financial system, and contributes to increasing the ability of the banking sector to provide financial services and products in accordance with international best practices.

Settlements operations through BURAQ system

The total number of immediate settlements between banks operating in Palestine through the BURAQ system during 2018 was 122,722 transfers, with a total value of USD 58,925.7 million, a decrease of 33.8 percent in numbers, compared to a significant increase of 68.9 percent in value from 2017, influenced by the prevailing economic conditions. The settlements between member banks include personal transfers, bank transfers^[40], clearance settlement transfers resulting from check-clearing, exchange settlement transfers, and other settlement transfers related to the settlement of required reserve differentials, etc.

The bulk of these transfers are generally limited to bank transfers and personal transfers, both in number and in terms of value, with 81.2 percent in number and 94.8 percent in value. Data indicates that bank transfers accounted for 6.9 percent of the total number of executed transfers, compared with about 81.0 percent of their value, which more than doubled (108.7 percent) what it was in 2017, reaching USD 47.7 billion. Personal transfers accounted for 74.3 percent of the total number of executed transfers, and 13.8 percent of the value of executed transfers, down 3.8 percent from the end of 2017, to USD 8.1 billion. Personal transfers are relatively small compared to bank transfers, with an average volume of about USD 89,100 compared to USD 5.6 million for bank transfers in 2018.

Check clearing transfers accounted for about 5.3 percent of the total number of executed transfers and about 4.2 percent of their total value, down 20.4 percent from 2017 to USD 2.5 billion. Palestinian Stock Exchange transfers accounted 1.2 percent of the total number of executed transfers, and 0.1 percent of their value, significantly down 43.0 percent from 2017, to USD 67.2 million. National Switch System^[41] transfers accounted for 5.2 percent of the total number of executed transfers and 0.2 percent of their value, up 31.6 percent from 2017, to USD 99.4 million. Finally, other operations' transfers accounted for 7.1 percent of the total number of executed transfers and 0.7 percent of their value, up 62.7 percent from the end of 2017, to USD 399.6 million. At the same time, the number of transfers out of the system was 1,993, with a total value of USD 6.3 billion, down by about 20.0 percent from the end of 2017.

Clearance activities

The two clearing rooms of the PMA in Ramallah and Gaza operate on a daily basis to settle checks provided by banks operating in Palestine and in various currencies in circulation. In this context, the analysis of the data indicates that 2018 saw a slowdown in clearing movement in all currencies denominated in US dollars (checks are still among the most commonly used non-cash payment tools in transaction settlement). The number of checks submitted for clearing was 6,456,560, with a total value of USD 12.7 billion, indicating a 1.3 percent increase in the number of checks submitted for clearing, and a 15.5 percent decrease in value compared to the end of 2017. Shekel checks accounted for 93.4 percent of the total number of checks submitted for the clearing, and 77.7 percent of their value, the dollar 4.1 percent in number and 16.5 percent in value, the dinar 2.4 percent in number, 5.5 percent in value, and the euro at 0.1 percent in number and 0.3 percent in value.

[40] The parties of such transfers (the payer and the beneficiary) are banks. They result from operations and activities to do mainly with the internal money market among banks.

[41] The National Switch System 194 started in May 2015.



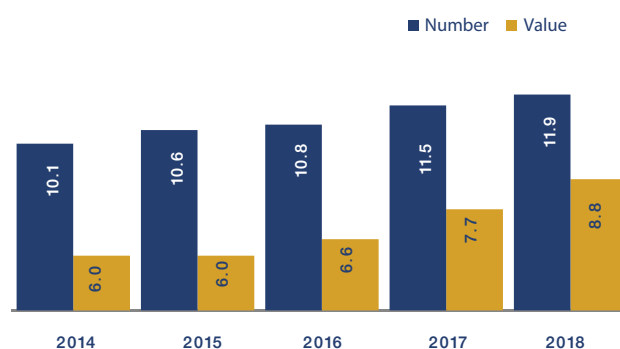
In general, clearing activity is largely linked to the overall economic situation and the prevailing level of economic activity. It is affected by growth rate, which is slowing to 0.9 percent (compared to 3.1 percent in 2017). As well as a 9.8 percent decline in clearance revenues with the Israeli side (compared to growth of about 1.1 percent in 2017, measured by In the shekel currency) and its irregularity, along with the slowdown in the Palestinian trade movement, and the decline of foreign grants obtained by the Palestinian government from donor countries.

At the same time, the bounced checks in all currencies (denominated in US dollars) increased by about 4.2 percent in the number of bounced checks, compared to a decrease of about 2.5 percent in value compared to 2017, to 766,151 checks with a total value of USD 1,125.5 million. The number of bounced checks are divided between the shekel currency, which accounted for 93.0 percent of the total number of bounced checks, 86.3 percent of its value, the dollar currency, which accounted for 4.5 percent in number and 19.5 percent in value terms, and the dinar currency at 2.5 percent in number and 4.2 percent in value.

This situation has resulted in an increase in the ratio of bounced checks to the total number and value of checks submitted for clearance, from 11.5 percent in 2017 to 11.9 percent in 2018 in terms of numbers, and from 7.7 percent to 8.8 percent in terms of value during the same period. It is worth to mention that the PMA had taken many measures to limit the continued increase in the proportion of bounced checks and maintaining the legal and operational status of the check as a highly credible commitment tool.

These include the development of an Integrated Credit Information System, which provided private sector institutions with the possibility of inquiring about the ratings of checks issuers and some credit data reflecting the client's status^[42]. In doing so, PMA protecting banking sector and lending institutions from granting loans to citizens beyond their capacity and financial solvency (overindebtedness). Also protecting private sector enterprises from dealing with insolvent citizens and refusing to sell goods and services through post-dated checks; reducing the phenomenon of bounced checks for insufficient balance; and maintaining the SME sector and micro-enterprises free from any credit or operational risks, especially liquidity risks that directly affect the continuity of the business of these facilities.

Figure 4- 22: Bounced checks as a percent of checks clearance, 2014- 2018



Source: PMA.

Part III: Non-Banking Financial Institutions Developments

[42] Some financial and demographic data derived from the bounced check, and credit information systems and uploaded to the Integrated Credit Information System database, to disclosure to users of private sector institutions not under the PMA's supervision.



Overview

Non-bank financial institutions in the Palestinian financial system are supervised by two supervisory bodies, with both specialized lending institutions and money changers under the control and supervision of the PMA. The securities, insurance, leasing and mortgage sectors are under the supervision of the PCMA.

Despite the development of some of these institutions, they still need more measures to continue to develop and progress, to enable them to play their required role effectively and contribute to the development of the Palestinian economy. This part of the report addresses the most important developments in these institutions during 2018.

Specialized lending institutions

Specialized lending institutions are a key pillar in enabling entrepreneurs and marginalized groups to break out of poverty, create jobs and reduce unemployment. Therefore, PMA is working hard to develop, control and regulate the conditions of these institutions to activate their role as a financing channel integrated with banks and as a key partner of the banking sector in fostering economy growth. To this end, in 2018, the PMA issued four instructions (1-4/2018).^[43]

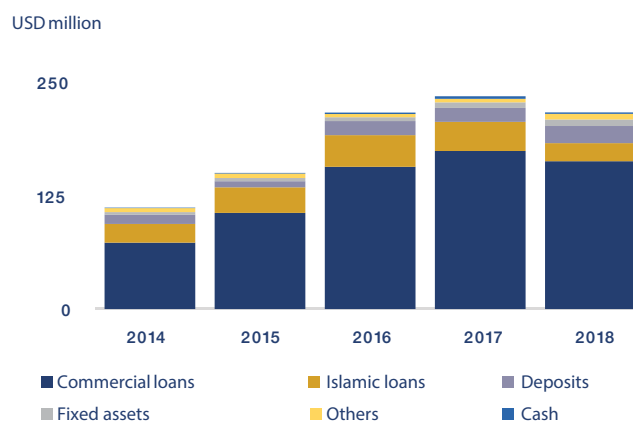
By the end of 2018, the number of institutions licensed by the PMA remained six institutions, four of which were profit institutions: Vitas Palestine; ACAD Finance; Al Ebdaa specialized lending; and Asala for Credit and Development Company. The other two are non-profit institutions: Palestine for Credit and Development Company (FATEN), and Reef Finance.

Analysis of financial statements of specialized lending institutions indicates that their performance was consistent with macroeconomic developments during 2018. The number of branches and offices of these institutions decreased to 81 from 84 in 2017, and the number of active borrowers decreased by 9.3 percent to 65,458. These institutions have 687 employees.

The assets of these institutions decreased by 7.6 percent compared to 2017 to USD 216.6 million, following a 38 percent decline in the value of Islamic and commercial loans by 6.5 percent, and a 47 percent decrease in cash. It is worth mentioning that commercial loans account for 75 percent of the total assets of specialized lending institutions, followed by Islamic loans at 9 percent, deposits at 9 percent, fixed and other assets account for about 6 percent, while cash only 1 percent of their assets.

On the liabilities and equity side, liabilities decreased by 6.6 percent from 2017, accounting for 67.6 percent (or USD 146.5 million) of total liabilities and equity (52 percent long-term liabilities, 33 percent short-term liabilities, and 2

Figure 4- 23: Asset's structure of specialized lending institutions, 2014-2018



Source: PMA.

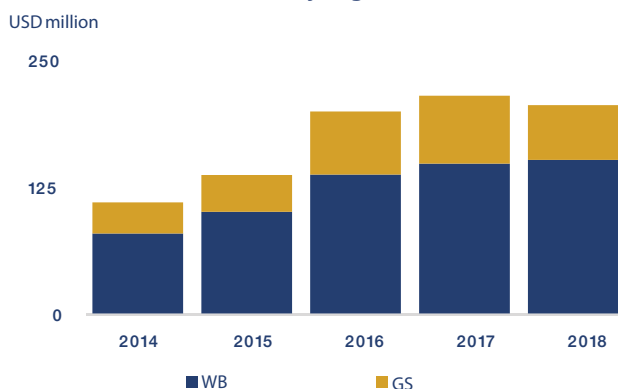
[43] For more detail on these instructions, see the first part of the Chapter Four of this report.



percent other liabilities). While equity dropped by 9.6 percent during the same period to USD 70.1 million, accounting for 32.4 percent of total liabilities and equity.

At the level of lending activity, the value of the loan portfolio decreased by 4.3 percent to about USD 205.7 million, distributed by 74 percent in the West Bank (equivalent to USD 151.7 million) and 26 percent in Gaza Strip (equivalent to USD 53.9 million). These loans were distributed among various activities and economic sectors related to the nature of the work and objectives of these institutions. Where the real estate sector dominated the largest share by 29.7 percent and valued at USD 61.1 million. Followed by the commercial sector with 27.7 percent and valued at USD 57.1 million, and the agricultural sector by 12.4 percent with USD 25.6 million, services sector 10.1 percent, consumer sector at 9.8 percent, industrial sector by 6.1 percent, and tourism sector at 4.0 percent. Nablus governorate controlled the largest share of the loan portfolio by 16.6 percent, followed by Ramallah and Al-Bireh governorate with 12.4 percent, and Jenin governorate with 10.9 percent. By the end of 2018, lending institutions had a net profit pre-tax of USD 2.6 million, down 19 percent from the previous year.

Figure 4- 24: Credit portfolio's of specialized lending institutions by region, 2014-2018

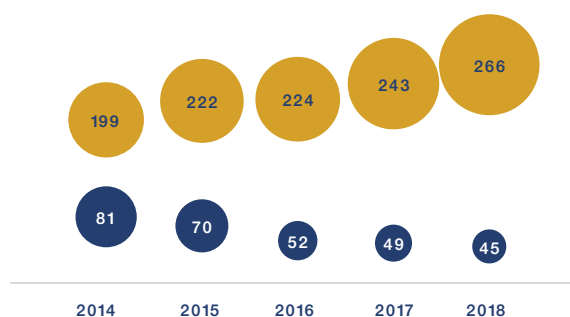


Source: PMA.

Money changers

During 2018, PMA continued its efforts to regulate this sector, control its conditions and raise its the efficiency, reduce its potential risks, strengthen its commitment to relevant laws and instructions, apply the accounting system, abide by the instructions of transfers, and ensure that there are no trusts and loans granted to the public. The relevant parties have also been coordinated with to develop the capabilities of compliance monitors in currency exchange companies by informing them of the requirements of combating money laundering and terrorist financing. In this context, PMA has issued instructions No. (1/2018, 2/2018), as well as several regulatory circulars for banking^[44].

Figure 4- 25: Money changers according to legal entity, 2014-2018



Source: PMA.

By the end of 2018, the number of licensed money changers increased by 19, bringing the total number of licensed money changers to 311, including 254 in the West Bank and 57 in Gaza Strip, of these, 266 are in the form of a company and 45 are individuals. Efforts appear to be geared towards turning individual money changers into companies.

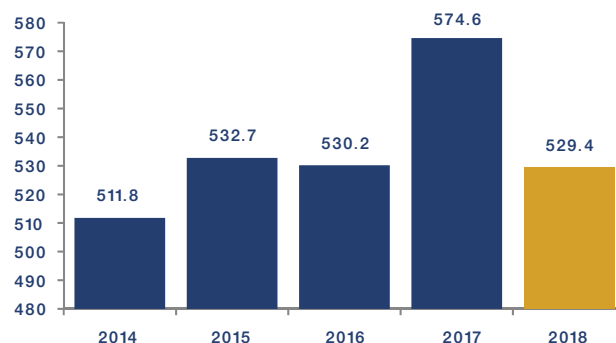
[44] For more detail on these instructions, see the first part of Chapter 4 of this report.

In terms of financial activity, the total assets of the money changers grew by 6.0 percent from 2017 to about USD 78.8 million, distributed among 93.0 percent of current assets, and fixed assets of 5.0 percent, while other assets accounted for about 2.0 percent. Equity in the sector increased by 7.1 percent to USD 71.3 million, accounting for about 90.5 percent of total assets.

Palestine Exchange-PEX (Securities sector)

The Palestine Stock Exchange serves as a gateway to domestic and foreign investment in a fully automated regulatory environment for trading listed securities. At the end of 2018, 48 companies were listed on the Palestine Stock Exchange, divided into: 7 banking and financial services companies; 13 industrial companies; 7 insurance companies; 10 investment companies; and 11 service companies. Their market value was about USD 3.7 billion (25.6 percent of GDP), down 4.0 percent from 2017. In 2018, the exchange held about 35,030 deals, for about 70,981 dealers of which 4.7 percent were foreign investors, mostly from Jordan.

Figure 4- 26: Al-Quds index of PEX, 2014-2018



Source: Palestine Exchange (PEX).

In terms of performance, the main index of the Stock Exchange “Al-Quds Index” decreased by about 7.9 percent compared to 2017, to close at 529.4 points, following the decline of the banking and financial services sector by 8.5 percent, the service sector index by 7.9 percent, and the investment sector index by 7.6 percent. The insurance sector index increased by 28.0 percent, and the industrial sector index by 0.5 percent.

Similarly, performance indicators indicate a lack of liquidity on the stock exchange, where trading volume decreased by 31.7 percent compared to 2017 to about 185.1 million shares, valued at USD 353.5 million, carried out through 35,030 deals in 243 trading sessions. The market value of listed companies’ shares fell by about 4.0 percent to USD 3.7 billion, influenced by political and economic tensions reflected in the stock market’s performance.

In terms of sectoral trading, the banking sector accounted for the largest share of the shares traded by 48.1 percent, valued at USD 1,143.5 million, or 30.6 percent of the total market value of listed companies. The investment sector accounted for 24.9 percent of the total number of shares traded, with a value of USD 803.9 million, or 21.5 percent of the total market value of listed companies’ shares. The services sector acquired 12.7 percent of the total number of shares traded, with a value of USD 1,185.6 million, or 31.7 percent of the total market value of listed companies’ shares. The insurance sector accounted for 11.9 percent of the total number of shares traded, valued at USD 206.8 million, or 5.5 percent of the total market value of listed companies. Finally, the industry accounted for 2.5 percent of the total number of shares, with a value of USD 395.2 million, or 10.6 percent of the total market value of listed companies.

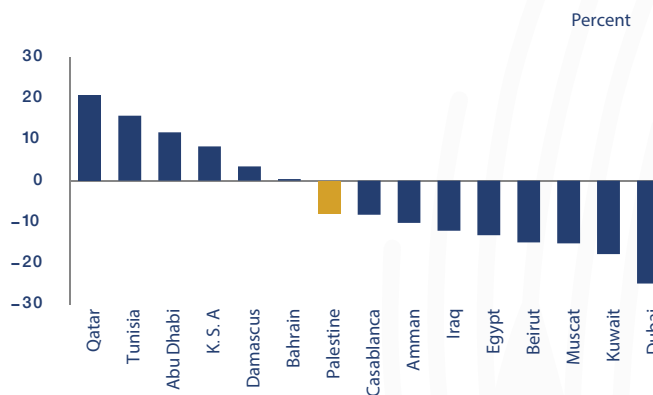
In 2018, the Palestine Stock Exchange ranked seventh in terms of the change in the value of the index compared to other Arab exchanges. Arab stock indices in 2018 have undergone changes in varying proportions, mostly due to oil price fluctuations, and political tensions in some countries in the region, as well as economic developments that concern each country individually.



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Figure 4- 27: Performance of arab exchanges, 2018



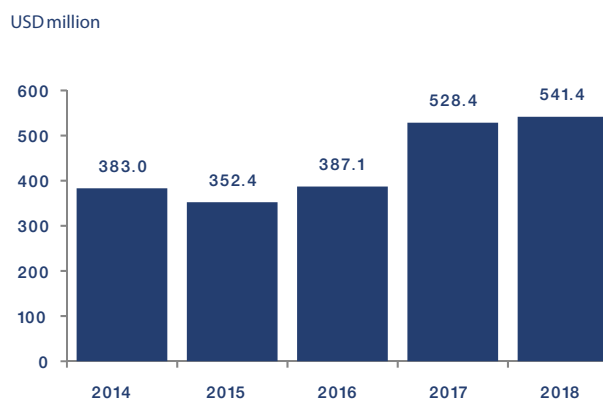
Source: www.arab-exchanges.org

Insurance sector

Ten companies were licensed by PCMA in 2018, after Tamkeen Insurance Company was licensed, bringing the number of companies engaged in takaful insurance to two companies. Insurance companies operate in various types of insurance through 151 branches and offices in the West Bank and Gaza Strip. The number of agents and producers licensed by PCMA was 271.

In 2018, total insurance company assets increased by 2.5 percent compared to the previous year, reaching USD 541.4 million, following a 7.7 percent growth in fixed assets (most notably real estate investments), compared with a slight decline in current assets of 0.7 percent. Although the paid-up capital of insurance

Figure 4- 28: Insurance sector's assets, 2014-2018



* Includes marine insurance, civil liability insurance, and other general insurance.

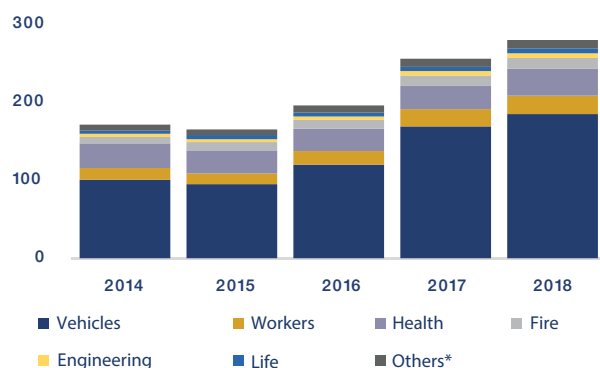
Source: PCMA.

companies increased by 26.4 percent to USD 90.0 million, due to the license of a new company in the field of Islamic insurance, shareholders' equity declined by 1.3 percent, to USD 186.2 million, and compulsory and optional reserves increased by 6.7 percent to about USD 27.6 million. Net profit for insurance companies after tax contracted by 40 percent to USD 15.4 million.

Total insurance premiums at the end of 2018 were USD 279.4 million, up 9.4 percent from 2017. In this context, the insurance portfolio is highly concentrated in favor of vehicle insurance (66 percent of the total insurance portfolio), followed by health insurance (12 percent), and workers' insurance (8 percent). Three companies operating in the insurance sector account for about 57 percent of gross premiums in 2018.

Figure 4- 29: Insurance sector's premiums by type, 2014-2018

USD million



* Includes marine insurance, civil liability insurance, and other general insurance.

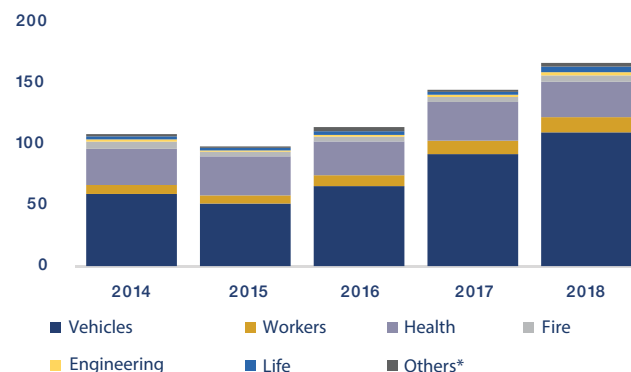
Source: PCMA.

This growth in insurance premiums was accompanied by a 15.2 percent growth in total compensation to USD 166.3 million. 65.8 percent of them paid for vehicle insurance, and 17.4 percent for health insurance, 7.5 percent for workers' insurance and 3.1 percent for fire insurance. Life insurance of 2.8 percent, and other types of insurance about 3.3 percent of the total compensation paid.

At the end of 2018, the per capita share of insurance premiums (insurance density = gross insurance premiums subscribed/ population) increased to about USD 58.5 per capita compared to USD 53.4 per capita in 2017. Also the ratio of gross premiums to GDP (Penetration ratio) increased to 1.9 percent compared to 1.8 percent the previous year. These indicators are similar to those in the region, with Jordan at USD 83.3 per capita and 2.1 percent respectively at the end of 2017. In Egypt, it was about USD 16 per capita and 0.7 percent respectively. In Israel, however, these indicators were higher, with a per capita premium of about USD 2,093 per capita, and premiums accounted for about 5 percent of GDP for 2017.

Figure 4- 30: Insurance sector's paid-up claim by type, 2014-2018

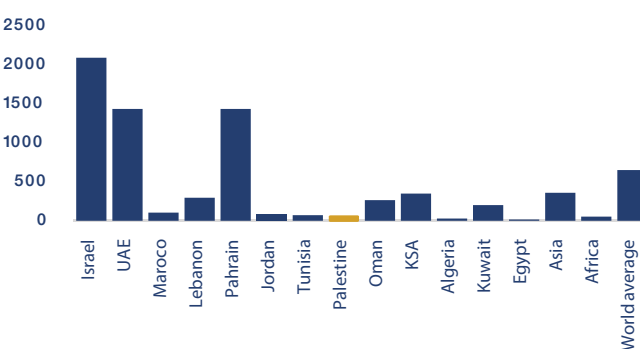
USD million



Source: Palestine Capital Market Authority (PCMA).

Figure 4- 31: Insurance density, selected countries, 2018

USD million

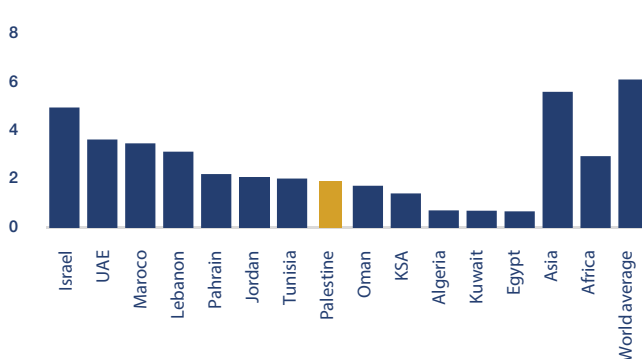


Data for 2017 except Palestine for 2018

Source: www.swissre.com

Figure 4- 32: Penetration ratio, selected countries, 2018

Percent



Data for 2017 except Palestine for 2018

Source: www.swissre.com



Lease financing sector

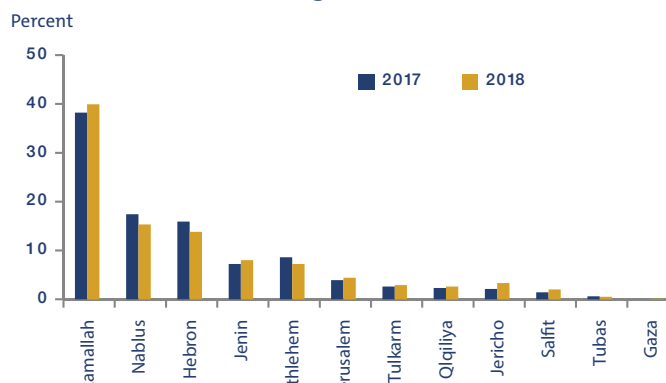
Lease financing sector consists of thirteen companies^[45] specializing in the field of lease financing. The total investment in contracts in 2018 was USD 92.1 million, through 1,645 contracts, representing a 9.1 percent increase in value and 20.2 percent in the number of contracts compared to 2017.

In 2018, PCMA continued to pursue corporate corrections (the deadline expired in August 2018). Also work with all relevant parties to ensure smooth funding, held several meetings with the Ministry of Transport to review and evaluate the instructions of leased vehicles issued by this ministry in 2017. A training program was also held for a group of judges, to emphasize the importance of the judiciary and the establishment of specialized courts in the development of the leasing sector and encouraging investment in it.

A consultative meeting was held between the PMA, PCMA, the Association of Banks in Palestine, and the International Finance Corporation (IFC), to encourage banks to invest in the leasing sector and to establish independent companies (usually these companies are either independent, resource-dependent, or bank-affiliated).

Overall, lease financing is still concentrated in Ramallah governorate with 39.9 percent, followed by Nablus with 15.3 percent, and Hebron with 13.8 percent, and the rest of the governorates together account for 31.0 percent of the total number of contracts. Vehicles continue to account for the largest share of the leasing portfolio, about 77.6 percent of the total value of contracts. This is mainly due to the ease of registration of vehicle ownership in traffic registration centers, and the low risk of renting them. While trucks and heavy vehicles accounted for about 12 percent, due to the decline in the value of their contracts, because of high risk of ownership. Money transferred accounted for 10.4 percent of the total leasing portfolio.

Figure 4- 33: Geographical distribution of the number of lease financing contracts, 2017-2018



Source: PCMA.

Mortgage sector

In 2018, the PCMA continued its review of the licensing instructions of real estate assessors issued in 2012, to ensure that they are adapted to the developments in the Palestinian situation and market changes, in conjunction with the intensive follow-up by PCMA with the Cabenit to approve a draft Real Estate Mortgage Law. In 2018, two new real estate assessors were licensed, bringing the number of licensed real estate assessors to 54.

Real estate assessors continue to face many structural problems in applying fully the available instructions, including the lack of a real estate assessors' database (records regulating real estate prices), which can be used to find out the comparative sales that took place in an area. The fact that banks oblige assessors to comply with their model of assessing also prevents adequate explanations in the reports that are not of interest to the banks. Hence, PCMA in cooperation

[45] Companies licensed by the PCMA in 2018 are: The Palestinian Company for Rental and Leasing PalLease; Arab Leasing Company; Ritz Leasing Company; Lease For You Leasing Company; Palestinian Leasing Company; Lease and Go Company; Easy Car Leasing; Mina Leasing Company; Murad Leasing Company; Good Luck Purchase Solutions; Jdeco Leasing Company; Al-Thuraya Leasing Company; and Mutakamila Leasing Company.

with the Association of Banks in Palestine is preparing to launch a unified real estate assessing model. The content of this model complies with the PCMA's instructions and the needs of banks as much as possible, and in a way that ensures the consolidation of foundations and practices in the real estate market, enhances the efficiency of licensed real estate assessors, and gives confidence to users of this report in accordance with the best international practices.



Statistical Appendices



Table (1- 1): Global real growth rates, 2014-2018

(Annual percent change)

Country	2014	2015	2016	2017	2018
World	3.6	3.4	3.4	3.8	3.6
Developed countries	2.1	2.3	1.7	2.4	2.2
United States	2.5	2.9	1.6	2.2	2.9
Euro area	1.4	2.1	2.0	2.4	1.8
Germany	2.2	1.5	2.2	2.5	1.5
France	1.0	1.1	1.2	2.2	1.5
Italy	0.1	0.9	1.1	1.6	0.9
Japan	0.4	1.2	0.6	1.9	0.8
United Kingdom	2.9	2.3	1.8	1.8	1.4
Canada	2.9	0.7	1.1	3.0	1.8
Israel*	3.9	2.6	4.0	3.5	3.3
Emerging and Developing Countries	4.7	4.3	4.6	4.8	4.5
Sub-Saharan Africa	5.1	3.2	1.4	2.9	3.0
Emerging and Developing Europe	3.9	4.8	3.3	6.0	3.6
Commonwealth of Independent States	1.0	-1.9	0.8	2.4	2.8
Emerging and Developing Asia	6.8	6.8	6.7	6.6	6.4
China	7.3	6.9	6.7	6.8	6.6
India	7.4	8.0	8.2	7.2	7.1
Middle East and North Africa	2.7	2.5	5.3	1.8	1.4
Egypt	2.9	4.4	4.3	4.2	5.3
Jordan	3.1	2.4	2.0	2.1	2.0
Lebanon	1.9	0.4	1.6	0.6	0.3
Saudi Arabia	3.7	4.1	1.7	-0.7	2.2
Latin America and the Caribbean	1.3	0.3	-0.6	1.2	1.0
Brazil	0.5	-3.5	-3.3	1.1	1.1
Mexico	2.8	3.3	2.9	2.1	2.0
Global GDP at purchasing power Parities	110,836	115,750	120,828	127,693	135,178

* Israel according to the WEO, that published by the IMF is classified within developed countries.
Source: World Economic Outlook, International Monetary Fund, April 2019.



Table (1- 2): Global inflation rates, 2014-2018

(Annual percent change)

Country	2014	2015	2016	2017	2018
World	3.2	2.8	2.8	3.2	3.6
Developed countries	1.4	0.3	0.8	1.7	2.0
United States	1.6	0.1	1.3	2.1	2.4
Euro area	0.4	0.2	0.2	1.5	1.8
Germany	0.8	0.7	0.4	1.7	1.9
France	0.6	0.1	0.3	1.2	2.1
Italy	0.2	0.1	-0.1	1.3	1.2
Japan	2.8	0.8	-0.1	0.5	1.0
United Kingdom	1.5	0.0	0.7	2.7	2.5
Canada	1.9	1.1	1.4	1.6	2.2
Israel	0.5	-0.6	-0.5	0.2	0.8
Emerging and Developing Countries	4.7	4.7	4.2	4.3	4.8
Sub-Saharan Africa	6.4	7.0	11.2	11.0	8.5
Emerging and Developing Europe	4.1	3.2	3.2	6.2	8.7
Commonwealth of Independent States	8.1	15.5	8.3	5.5	4.5
Emerging and Developing Asia	3.4	2.7	2.8	2.4	2.6
China	2.0	1.4	2.0	1.6	2.1
India	5.8	4.9	4.5	3.6	3.5
Middle East and North Africa	6.5	5.5	4.9	6.7	11.4
Egypt	10.1	11.0	10.2	23.5	20.9
Jordan	2.9	-0.9	-0.8	3.3	4.5
Lebanon	1.8	-3.7	-0.8	4.5	6.1
Saudi Arabia	2.2	1.3	2.0	-0.9	2.5
Latin America and the Caribbean	4.9	5.5	5.6	6.0	6.2
Brazil	6.3	9.0	8.7	3.4	3.7
Mexico	4.0	2.7	2.8	6.0	4.9

Source: World Economic Outlook, International Monetary Fund, April 2018.



Table (1- 3): Unemployment rates in developed economies, 2014-2018

(Percent of labor force)

Country	2014	2015	2016	2017	2018
Developed countries	7.3	6.7	6.2	5.6	5.1
United States	6.2	5.3	4.9	4.4	3.9
Euro area	11.6	10.9	10.0	9.1	8.2
Germany	5.0	4.6	4.2	3.8	3.4
France	10.3	10.4	10.1	9.4	9.1
Italy	12.6	11.9	11.7	11.3	10.6
Japan	3.6	3.4	3.1	2.8	2.4
United Kingdom	6.2	5.4	4.9	4.4	4.1
Canada	6.9	6.9	7.0	6.3	5.8
Israel	5.9	5.3	4.8	4.3	4.0
China	4.1	4.1	4.0	3.9	3.8
Egypt	13.4	12.9	12.7	12.2	10.9
Jordan	11.9	13.1	15.3	18.1	18.3
K. S. A	5.7	5.6	5.6	6.0	-
Brazil	6.8	8.3	11.3	12.8	12.3
Mexico	4.8	4.4	3.9	3.4	3.3

Source: World Economic Outlook, International Monetary Fund, April 2019.

Table (1- 4): Global Interest rates of major currencies, 2014-2018

(Period end, percentage)

Country	2014	2015	2016	2017	2018
United States	0.25	0.50	0.75	1.50	2.50
Euro area	0.05	0.05	0.00	0.00	0.00
United Kingdom	0.50	0.50	0.25	0.50	0.75
Japan	0.00	0.00	-0.10	-0.10	-0.10
Canada	1.00	0.50	0.50	1.00	1.75
China	5.60	4.35	4.35	4.35	4.35

Source: www.global-rates.com.



Table (1- 5): Growth rates in global trade, 2014-2018

(Percent)

Country	2014	2015	2016	2017	2018
Export					
Advanced countries	3.1	3.9	3.8	2.0	4.2
Emerging & developing countries	4.8	3.2	1.5	2.6	6.4
Import					
Advanced countries	2.3	3.9	4.6	2.7	4.0
Emerging & developing countries	5.2	4.2	-0.9	1.8	6.4
Goods export					
Advanced countries	2.7	3.5	3.1	1.8	4.4
Emerging & developing countries	4.7	2.6	1.1	2.6	6.4
Goods import					
Advanced countries	2.1	3.6	3.6	2.3	4.7
Emerging & developing countries	4.7	2.5	-0.5	2.3	7.0
Terms of trade					
Advanced countries	0.9	0.3	2.0	0.9	-0.2
Emerging & developing countries	-0.6	-0.6	-4.2	-1.4	0.6

Source: World Economic Outlook, International Monetary Fund, April 2019.



Table (1- 6): Global current account balances, 2014-2018

(Percent of GDP)

Country	2014	2015	2016	2017	2018
Developed countries	0.5	0.6	0.7	0.9	0.7
United States	-2.1	-2.2	-2.3	-2.3	-2.3
Euro area	2.5	2.9	3.2	3.2	3.0
Germany	7.5	8.9	8.5	8.0	7.4
France	-1.0	-0.4	-0.8	-0.6	-0.7
Italy	1.9	1.5	2.5	2.8	2.6
Japan	0.8	3.1	4.0	4.0	3.5
United Kingdom	-4.9	-4.9	-5.2	-3.3	-3.9
Canada	-2.4	-3.5	-3.2	-2.8	-2.6
Israel	4.3	5.3	3.7	2.6	1.9
Emerging and Developing Countries	0.6	-0.2	-0.3	0.0	-0.1
Africa- Sub-Saharan	-3.6	-5.9	-3.7	-2.1	-2.6
Emerging and Developing Europe	-2.9	-2.0	-1.8	-2.5	-2.2
Commonwealth of Independent States	2.1	2.8	0.0	1.0	5.0
Emerging and Developing Asia	1.5	2.0	1.4	0.9	-0.1
China	2.2	2.7	1.8	1.4	0.4
India	-1.3	-1.1	-0.6	-1.8	-2.5
Middle East and North Africa	6.0	-4.3	-4.2	-0.3	3.1
Egypt	-0.9	-3.7	-6.0	-6.1	-2.4
Jordan	-7.2	-9.0	-9.4	-10.6	-7.4
Lebanon	-28.2	-19.3	-23.1	-25.7	-27.0
Saudi Arabia	9.8	-8.7	-3.7	1.4	8.3
Latin America and the Caribbean	-3.1	-3.2	-1.9	-1.4	-1.9
Brazil	-4.1	-3.0	-1.3	-0.4	-0.8
Mexico	-1.9	-2.6	-2.3	-1.7	-1.8

Source: World Economic Outlook, International Monetary Fund, April 2019.



Table (1- 7): Global official foreign reserves, 2014-2018

(USD billion)

Country	2014	2015	2016	2017	2018
World	12,730	11,991	11,822	12,667	12,668
Developed countries	4,694	4,708	4,884	5,375	5,397
United States	130	118	117	123	126
Euro area	743	701	746	803	823
Germany	193	174	185	200	198
France	143	138	147	156	167
Italy	142	131	136	151	153
Japan	1,261	1,233	1,217	1,264	1,270
United Kingdom	124	148	135	151	173
Canada	75	80	83	87	84
Israel	86	91	95	113	115
Emerging and Developing Countries	8,036	7,283	6,938	7,292	7,271
Emerging and Developing Europe	372	338	349	367	361
Emerging and Developing Asia	4,751	4,290	4,030	4,294	4,211
China	3,869	3,405	3,098	3,235	3,168
India	323	352	360	410	396
Egypt	14	15	23	36	41
Jordan	14	14	13	12	12
Lebanon	50	49	54	55	52
Saudi Arabia	732	616	536	496	497
Brazil	364	356	365	374	375
Mexico	196	178	178	175	176

Sources: International Financial Statistics (IFS) database, May 2019.
Central Bank of Jordan.



Table (1- 8): Major real national accounts variables in Palestine*, 2014-2018

(USD Million)

Activity	2014	2015	2016	2017	2018
A) Productive Sectors	2,954.1	2,844.6	2,987.4	3,054.3	3,147.7
Agriculture and Fishing	485.2	450.1	413.5	390.0	418.2
Mining, Manufacturing, Electricity & Water	1,757.7	1,656.7	1,740.1	1,777.8	1,826.3
Mining and Quarrying	58.0	50.0	48.3	53.7	68.9
Manufacturing	1,461.0	1,347.7	1,431.1	1,457.0	1,492.2
Electricity, Gas, Steam and Air Conditioning Supply	158.7	156.2	153.8	155.7	149.4
Water Supply, Sewerage, Waste Mange. & Rem. Activities	84.6	102.8	106.9	111.4	115.8
Construction	711.3	737.8	833.8	886.5	903.2
Service sectors	7,531.2	7,804.8	8,118.4	8,342.9	8,406.9
Wholesale and Retail Trade, Repair of Motor Vehicles	2,260.8	2,415.5	2,404.1	2,613.4	2,852.2
Transportation and Storage	182.0	220.5	262.2	268.0	243.8
Financial and Insurance Activities	395.0	416.0	495.3	530.5	556.2
Information and Communication	510.0	515.7	542.1	511.3	488.5
B) Services	2,275.0	2,296.3	2,386.9	2,444.9	2,493.1
Real Estate Activities	613.2	642.9	644.4	672.6	720.2
Education	982.5	967.1	1,040.7	1,023.2	987.60
Human Health and Social Work Activities	405.6	404.0	426.0	407.2	382.5
Public Administration and defense	273.6	282.3	275.8	341.9	402.8
Others**	1,908.4	1,940.8	2,027.8	1,974.8	1,773.1
C) GDP At Factor Costs (A + B)	10,485.3	10,649.4	11,105.8	11,397.2	11,554.6
D) Net Indirect Taxes	1,761.0	2,023.6	2,163.9	2,289.2	2,255.7
Customs Duties	694.2	780.4	854.2	936.5	991.3
VAT on Imports, net	1,066.8	1,243.2	1,309.7	1,352.7	1,264.4
Real GDP (C +D) (2004 = 100)	12,252.9	12,673.0	13,269.7	13,686.4	13,810.3
Net Income Transfers from Abroad	1,440.6	1,712.3	1,694.2	1,597.1	1,829.9
Net Current Transfers	1,312.1	1,421.4	1,397.3	1,689.8	1,657.0
Real GDI	15,005.6	15,806.7	16,361.2	16,973.3	17,297.2
Memorandum Items					
Per capita Real GDP (USD)	2,852.4	2,863.9	2,922.9	3,072.4	3,021.4
Per capita Real GDI (USD)	3,493.1	3,572.1	3,603.8	3,810.1	3,784.5
Per capita Nominal GDP (USD)	2,960.1	2,863.9	2,957.2	3,254.6	3,198.4
Nominal GDP	12,715.6	12,673.0	13,425.7	14,498.1	14,615.9

* Quarterly estimates. According to the PCBS, the data lacks the summation feature (the sum of the sub-items are not equal to the main items) due to the conversion of the base year from 2004 to 2015.

** Includes Accommodation and Food Service Activities, Professional, Scientific and Technical Activities, Administrative and Support Service Activities, Arts, Entertainment and Recreation, Households with Employed Persons, FISIM, and Others.

Source: PCBS.



Table (1- 9): Expenditure on real GDP, 2014-2018

Activity	2014	2015	2016	2017	2018
USD Million					
Gross Domestic Expenditure	16,802.7	17,912.0	18,487.6	18,579.7	18,968.4
Aggregate Consumption	14,356.6	15,234.6	15,680.7	15,490.9	15,702.1
Private*	11,116.7	11,805.1	12,189.9	11,969.2	12,149.3
Public	3,240.3	3,429.5	3,490.8	3,521.7	3,552.8
Aggregate Investment	2,446.1	2,677.4	2,806.9	3,088.8	3,266.3
Private	1,712.3	1,874.2	1,964.8	2,162.2	2,449.7
Public	733.8	803.2	842.1	926.6	816.6
Change in inventories	-299.9	-317.4	-159.9	60.4	132.6
Net Export of Goods and Services	-4,598.0	-5,199.5	-5,170.6	-4,816.4	-5,127.8
Exports	2,277.8	2,338.1	2,383.1	2,678.1	2,889.1
Imports	6,885.3	7,537.6	7,553.7	7,494.5	8,016.9
Net errors and omissions	52.3	-39.5	-47.3	-76.9	-30.3
Real GDP	12,252.9	12,673.0	13,269.7	13,686.4	13,810.3
Percent of GDP					
Gross Domestic Expenditure	137.1	141.3	139.3	135.8	137.3
Aggregate Consumption	117.2	120.2	118.2	113.2	113.7
Private*	90.7	93.2	91.9	87.5	88.0
Public	26.4	27.1	26.3	25.7	25.7
Aggregate Investment	20.0	21.1	21.2	22.6	23.7
Private	14.0	14.8	14.8	15.8	17.7
Public	6.0	6.3	6.3	6.8	5.9
Change in inventories	-2.4	-2.5	-1.2	0.4	1.0
Net Export of Goods and Services	-37.5	-41.0	-39.0	-35.2	-37.1
Exports	18.6	18.4	18.0	19.6	20.9
Imports	56.2	59.5	56.9	54.8	58.1
Net errors and omissions	0.4	-0.3	-0.4	-0.6	-0.2
Real GDP	100.0	100.0	100.0	100.0	100.0

* Includes also NPISH final consumption.

Source: PCBS.



Table (1- 10): Consumer price index (CPI), 2014-2018

(Point)

Activity	2014	2015	2016	2017	2018
Main Expenditure Groups (Annual Percentage point)					
Foods and Soft Drinks	105.8	107.8	106.2	105.2	104.4
Alcoholic Beverages and Tobacco	143.9	159.6	166.0	164.8	162.7
Textile, Clothing and Footwear	104.3	109.3	112.4	112.2	107.4
Housing	114.8	108.3	105.5	109.0	110.0
Furniture, Household Goods	101.9	105.4	105.5	106.0	105.0
Medical Care	115.5	116.7	118.0	119.9	121.2
Transportation	103.3	102.2	101.4	101.3	102.4
Communications	97.8	95.7	94.4	94.7	95.8
Recreational, Cultural Goods & Services	100.1	102.2	101.8	103.8	105.4
Education	115.2	121.0	124.7	123.9	122.6
Restaurants and Cafés	119.2	121.9	125.6	126.1	127.5
Miscellaneous Goods and Services	117.0	118.2	118.3	120.2	121.6
All-items Index (2010 = 100)	109.4	111.0	110.7	111.0	110.8
Regions (Annual Percentage point)					
WB	112.4	113.9	113.8	113.8	114.3
GS	103.1	105.0	104.1	104.2	102.8
Jerusalem	113.6	114.0	112.9	115.4	116.6
All-items Index (2010 = 100)	109.4	111.0	110.7	111.0	110.8
Inflation Rates (Annual Percentage point)					
WB	1.20	1.29	-0.08	-0.01	0.41
GS	2.85	1.77	-0.84	0.11	-1.34
Jerusalem	3.84	0.33	-0.96	2.18	1.04
Palestine	1.73	1.43	-0.22	0.21	-0.18

Source: PCBS.



Table (1- 11): Labor market indicators, 2014-2018

Key Indicators	2014	2015	2016	2017	2018
individuals Over 15 Years (percent of polulation)					
Palestine	60.3	60.6	60.8	61.3	61.3
WB	62.4	62.8	63.1	63.0	63.3
GS	56.8	57.0	57.3	58.7	58.4
Participation rate (percentage)					
Palestine	45.8	45.8	45.8	45.7	46.4
WB	46.6	46.1	45.6	45.8	46.1
GS	44.4	45.3	46.1	45.6	46.9
Unemployment: Percent of Labor Force					
Palestine	26.9	25.9	26.9	28.4	30.8
WB	17.7	17.3	18.2	18.7	17.6
GS	43.9	41.1	41.7	44.4	52.1
Distribution of Palestinian workers by Region (percentage)					
WB	60.4	58.8	57.7	57.6	60.1
GS	28.0	29.7	30.5	29.4	26.6
Isreal and settlements	11.6	11.5	11.8	13.0	13.3
Distribution of workers by Economic Activity (Percentage)					
Agriculture and fishing	10.6	8.7	7.2	6.6	6.3
Industry (mining and manufacturing)	12.7	13.0	13.4	13.1	13.3
Constructions (build. & constructions)	8.9	9.1	10.1	10.4	11.0
Trade, restaurants and hotels	21.4	22.1	22.4	23.1	23.6
Trans., storage and communications	5.8	6.4	6.8	7.2	6.7
Other services and branches	40.6	40.8	40.2	39.7	39.1
Daily Average wage in NIS					
Palestine	102.1	104.0	109.3	114.3	123.0
WB	90.9	94.0	98.1	101.5	109.4
GS	64.0	62.0	61.7	59.3	63.1
Israel and settlements	187.6	199.1	218.1	226.9	243.1

Source: PCBS.



Table (1- 12): Economic forecasts, 2019

Indicators	2018	2019		
	Projection*	Baseline	Optimistic Scenario	Pessimistic Scenario
(Annual percent change)				
Real GDP	0.9	0.5	3.1	-2.5
Real Percapita GDP	-1.7	-0.8	3.2	-3.9
Private sector Real GDP	0.6	0.2	4.5	-3.2
Public sector Real GDP	0.4	-0.9	6.4	-4.3
Unemploument Rate (%)	30.8	31.2	29.7	32.1
Inflation rate (%)	-0.2	0.9	--	--
(percent of GDP)				
Aggregate Consumption	113.7	112.9	114	114.7
Public	25.7	25.5	26.1	24.9
Private**	88.0	87.4	87.9	89.8
Aggregate Investment	23.7	23.4	23.9	21.8
Net Export***	-37.1	-36.3	-37.9	-36.5
Exports	20.9	20.7	21.0	20.3
Imports	58.1	57.0	58.9	56.8
Memorandum Items				
Real GDP (USD million, 2015=100)	13,810.3	13,879.0	14,238.0	13,464.0
Real per capita GDP (USD)	3,021.4	2,298.0	3,095.0	2,974.0
Exchange rate (USD/NIS)	3.6	3.6	3.6	3.6

* Preliminary data from PCBS.

** Includes NBISH.

*** Negative sign means decrease in trade deficit.

Source: PMA estimates.



Chapter Two: Public Finance Developments

Table (2- 1): Fiscal operations (cash basis), 2014-2018

(NIS Million)

Items	2014	2015	2016	2017	2018
Total net revenues and grants	14,353.2	14,335.4	16,444.3	15,790.9	14,819.3
Total Domestic Revenue	3,114.3	3,542.2	5,023.2	4,418.9	4,816.7
Tax	2,148.7	2,354.0	2,391.2	2,750.6	2,997.2
Non-tax	965.6	968.4	2,309.1	1,404.0	1,545.2
Earmarked collections	--	219.8	322.9	264.3	274.3
Clearance Revenue	7,317.9	7,953.0	8,872.5	8,966.4	8,091.9
Tax Refunds (-)	481.3	264.5	372.2	191.6	500.9
Foreign aid	4,402.3	3,104.7	2,920.8	2,597.2	2,411.6
Budget Support	3,676.1	2,757.2	2,317.8	1,965.7	1,840.5
Development Financing	726.2	347.5	603.0	631.5	571.1
Total public expenditure	12,860.8	13,993.2	14,760.1	14,601.8	14,137.1
Current expenditure and net lending	12,274.4	13,306.4	13,935.9	13,680.5	13,134.0
Wages	6,766.5	6,837.0	7,332.2	7,063.4	5,946.6
Non-wage	4,485.5	5,173.3	5,409.2	5,507.6	6,054.0
Net lending	1022.4	1169.2	1029.3	959.6	967.3
Earmarked payments	--	126.9	165.2	149.9	166.1
Development Expenditure	586.4	686.8	824.2	921.3	1,003.1
Current balance	-2,323.5	-2,075.7	-412.4	-486.8	-726.3
Overall balance (Excl. grants)	-2,909.9	-2,762.5	-1,236.5	-1,408.1	-1,729.4
Overall balance (inc. grants)	1,492.4	342.2	1,684.3	1,189.1	682.2
Financing	-1,492.4	-342.2	-1,684.3	-1,189.1	-682.2
Net financing from local banks	-506.7	634.0	-486.3	307.0	569.4
Payments of previous years arrears	-1,003.8	-917.0	1,214.9	-1,495.2	-1,266.8
Balance	18.1	-59.2	16.9	-0.9	15.2
Exchange rate (USD/NIS)	3.57	3.89	3.81	3.61	3.59

Source: Ministry of Finance Database.



Table (2- 2): Government public debt, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Total Domestic Debt	1,128.0	1,466.5	1,439.8	1,501.2	1,337.9
Local banks	1,114.6	1,453.1	1,426.2	1,486.2	1,324.4
Loans	631.0	798.9	816.9	814	638.1
Overdrafts	302.7	433.5	382.7	424.9	448.3
Petroleum Authority ⁽¹⁾	180.9	220.7	226.6	246.9	238
Other Public Institutions Loans	13.4	13.4	13.6	15.0	13.5
Total External Debt	1,088.8	1,070.7	1,044.0	1,041.9	1,031.7
Arab financial institutions	620.9	618.4	606.0	564.4	563.4
Al-Aqsa Fund	517.4	518	512.4	513.0	513.0
Arab Fund for Economic and Social Development	56.9	56	56.1	14.3	14.2
Islamic Development Bank	46.6	44.4	37.5	37.1	36.2
International and Regional Institutions	347.7	337.4	329.8	342.3	339.1
World Bank	276.7	269.5	266.1	269	270.9
European Investment Bank	48.1	45.1	41.1	50.7	44.2
International Fund for Agricultural Development (IFAD)	2.7	2.5	2.3	2.3	2.1
OPEC	20.2	20.3	20.3	20.3	21.9
Bilateral loans	120.2	114.9	108.2	135.3	129.2
Total Government Public Debt	2,216.8	2,537.2	2,483.8	2,543.1	2,369.6
GDP (Nominal)	12,715.6	12,673.0	13,425.7	14,498.1	14,615.9

*Represents the value of loans provided by the Ministry of Finance to support the Petroleum Authority.

Source: - Ministry of Finance Database.



Table (2- 3): Government arrears, 2014-2018

(NIS Million)

Items	2014	2015	2016	2017	2018
Wages and salaries	569.8	602.7	505.3	568.1	476.9
Non-wage expenditures	1,711.9	1,591.6	1,861.3	1,631.1	1,086.5
Development projects	351.2	206.3	462.5	400.3	294.9
Tax refunds	146.5	334.8	16.9-	69.7	110.1
Earmarked payments	-	92.9	157.9	115.0	108.2
Total	2,779.4	2,828.3	2970.1	2,784.2	2,076.6
Repayments of arrears	1003.8	917.0	2134.3	2452.6	1561.8
Net arrears	1,775.6	1,911.3	835.8	331.6	514.8

Source: Ministry of Finance Database, and IMF.



Chapter Three: Foreign Sector Developments

Table (3- 1): Balance of payments, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Current Account (Net)	-2,149.0	-2,066.0	-1,941.6	-1,563.7	-1,659.3
Goods (Net)	-4,830.2	-4,300.5	-4,327.4	-4,439.1	-4813.2
Exports (Fob)	1,383.6	1,756.7	1,879.1	2,125.5	2,291.9
Imports (Fob)	6,213.8	6,057.2	6,206.5	6,564.6	7,105.1
Services (Net)	-206.5	-899.1	-918.8	-935.1	-1,014.2
Exports	788.6	581.4	501.4	567.1	611.6
Imports	995.1	1,480.5	1,420.2	1,502.2	1,625.8
Income (Net)	1,482.4	1,712.2	1,896.0	1,991.9	2,393.7
Receipts	1,618.4	1,803.0	2,014.6	2,150.3	2,572.5
Compensation of employees	1,449.4	1,663.9	1,894.5	1,969.8	2,278.2
Of which from Israel	1,435.3	1,650.7	1,880.3	1,918.6	2,226.1
Investment Income	169.0	139.1	120.1	180.5	294.3
Payments	136.0	90.8	118.6	158.4	178.8
Current Transfers (Net)	1,405.3	1,421.4	1,408.6	1,818.6	1,774.4
Inflows	2,013.2	1,875.4	1,897.4	2,112.8	2,143.0
To Public Sector	614.6	487.3	448.5	592.1	614.1
To Private Sector	1,398.6	1,388.1	1,448.9	1,520.7	1,528.9
Outflows	607.9	454.0	488.8	294.2	368.6
Capital and financial Account (Net)	1,765.4	2,451.1	1,701.5	1,395.2	1,802.8
Capital Account (Net)	690.9	491.0	682.3	397.1	388.9
Capital Transfers (Net)	690.9	509.8	694.7	397.1	388.9
Inflows	690.9	509.8	694.7	397.1	388.9
To Public Sector	447.5	260.6	436.8	146.2	148.0
To Private Sector	243.4	249.2	257.9	250.9	240.9
Outflows	0.0	0.0	0.0	0.0	0.0
Acquisition of Non-Produced Assets (Net)	0.0	-18.8	-12.4	0.0	0.0
Financial account (Net)	1,074.5	1,960.1	1,019.2	998.1	1,413.9
Direct Investment (Net)	-27.9	29.6	341.4	221.9	300.8
Portfolio Investment (Net)	-179.1	124.7	-295.4	68.6	-267.4
Other Investment (Net)	1,268.7	1,714.3	705.1	841.1	1,471.9
Change in Reserve Assets (- = Increase)	12.8	91.5	268.1	-133.5	-91.4
Extraordinary Financing	7.7	8.1	2.5	0.0	0.0
Net Errors and Omissions	383.6	-393.2	237.6	168.5	-143.5
Overall balance	-20.4	-99.6	-270.7	133.5	91.4
Financing	20.4	99.6	270.6	-133.5	-91.4
Current Account Deficit as a percent of GDP	-16.9	-16.3	-14.5	-10.8	-11.4

Source: PMA Database, PCBS, Balance of Payments Reports.



Table (3- 2): International investment position, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
International investment position (Net)	1,235.0	1,034.0	1,289.0	1,373.0	1,659.0
Total external assets	5,951.0	6,030.0	6,138.0	6,455.0	6,597.0
Foreign direct investment abroad	167.0	445.0	445.0	422.0	347.0
Portfolio investment abroad	1,183.0	1,088.0	1,110.0	1,055.0	1,451.0
Other investment abroad	3,929.0	3,916.0	4,270.0	4,532.0	4,261.0
Of which: currency and deposits	3,759.0	3,768.0	3,921.0	4,210.0	3,884.0
Official reserves	672.0	581.0	313.0	446.0	538.0
Total foreign liabilities	4,716.0	4,996.0	4,849.0	5,082.0	4,938.0
Foreign direct investment in Palestine	2,453.0	2,511.0	2,588.0	2,703.0	2,721.0
Portfolio investment in Palestine	710.0	821.0	658.0	664.0	726.0
Other investment in Palestine	1,553.0	1,664.0	1,603.0	1,715.0	1,491.0
Of which: loans	1,147.0	1,133.0	1,140.0	1,085.0	1,063.0
currency and deposits	404.0	530.0	496.0	603.0	417.0

Source: PMA Database, PCBS, Balance of Payments Reports.



Chapter Four: Palestinian Financial Sector Developments

Part I: PMA developments

Table (4- 1): Banks and branches by nationality, 2014-2018

Items	2014	2015	2016	2017	2018
Number of Banks					
Local Banks	7	7	7	7	7
Foreign Banks	10	9	8	8	7
Jordanian Banks	8	7	7	7	6
Egyptian Banks	1	1	1	1	1
British Banks	1	1	0	0	0
Total	17	17	16	15	14
Number of Branches & representative Offices					
Local Banks	142	155	187	209	227
Foreign Banks	116	119	122	128	124
Jordanian Banks	109	112	116	121	117
Egyptian Banks	6	6	6	7	7
British Banks	1	1	0	0	0
Total	258	274	309	337	351

Source: PMA Database.



Table (4- 2): Financial inclusion indicators, 2014-2018

Items	2014	2015	2016	2017	2018
Branches & Offices (number)	258	274	309	337	351
Deposit accounts (number)	2,766,635	2,940,575	3,072,923	3,208,783	3,471,849
Customer deposits (USD million)	8,935.3	9,654.6	10,604.7	11,982.5	12,227.3
Personals	6,468.9	6,805.9	7,341.0	8,316.1	9,065.4
Corporates	1,681.2	2,192.8	2,590.1	2,536.6	2,556.2
Public sector	785.2	655.8	673.5	736.2	605.7
Credit Portfolios (USD million)	4,895.1	5,824.7	6,871.9	8,026.0	8,432.3
Personals*	2,052.0	2,539.5	2,731.6	3,206.2	3,345.7
Corporates**	1,603.3	1,829.1	2,721.5	3,343.7	3,769.8
Public sector	1,239.8	1,456.1	1,418.8	1,476.0	1,316.8
ATM's machines (number)	549	592	622	644	690
Point of sales (number)	5,579	5,987	6253	5,579	5,660
Credit cards (number)	70,029	82,830	118,076	98,041	103,057
Deabt cards (number)	419,676	466,789	547,019	695,120	816,329
ATM withdrawal cards (number)	163,074	189,414	165,763	132,772	114,966

* Includes credit cards and non-residents.

** includes non-profits institutions and inactive overdrafts.

Source: PMA Database.



Table (4- 3): PMA assets and liabilities, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Banks & Financial institutions deposits	1,050.0	1,164.2	1284.1	1394.5	1,407.5
Required reserve	784.5	871.2	920.4	1034.6	1,240.6
Other accounts	265.5	293.0	363.7	359.9	166.9
Capital and reserves	100.7	103.6	109.5	117.6	134.0
Paid-up capital	70.0	72.9	78.8	86.9	103.7
Reserves	30.7	30.7	30.7	30.7	30.3
Provisions and Other liabilities	16.9	17.0	17.0	18.4	37.6
Total liabilities =Total assets	1,167.6	1,284.8	1,410.6	1,530.5	1,579.1
Domestic assets	132.0	295.5	642.4	592.3	623.1
Balances with banks in Palestine	132.0	295.5	642.4	592.3	623.1
Demand deposits	24.6	15.6	62.3	3.7	11.1
Time deposits	107.4	279.9	562.1	530.0	612.0
Investment deposits at Islamic banks	0.0	0.0	18.0	58.6	0.0
Foreign assets	1,007.3	955.4	726.5	886.6	887.0
Balances with banks outside Palestine	735.2	741.7	462.4	694.70	704.2
Demand deposits	68.9	47.5	38.3	18.2	21.1
Time deposits	666.3	694.2	424.1	676.5	683.0
Investments abroad	272.1	213.7	264.1	191.9	182.8
Fixed assets	3.1	4.0	3.4	41.9	41.8
Other assets	25.2	29.9	38.3	9.7	27.2

Source: PMA Database.



Table (4- 4): PMA profit and loss statement, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Revenues	22.7	18.9	23.2	29.9	41.9
Net interest and investment revenue	15.9	10.9	14.6	20.5	29.3
Other operating revenues	6.8	8.0	8.6	9.4	10.6
Expenditure	16.1	16.0	17.4	21.8	21.0
Personnel expenses	11.0	10.7	10.9	11.3	12.2
General and administrative expenses	3.0	3.2	4.3	4.7	4.4
Depreciation of property, plant and equipment	1.5	1.5	1.3	1.5	3.0
PMA's contribution to the Financial Follow-up Unit's expenditures	0.6	0.6	0.9	1.3	1.3
Others	-	-	-	3.0	0.1
Net comprehensive income of the year	6.6	2.9	5.8	8.1	20.8

Source: PMA Database.



Table (4- 5): PMA employee distribution, 2014-2018

Items	2014			2015			2016			2017			2018		
	Ramallah	Gaza	Total	Ramallah	Gaza	Total	Ramallah	Gaza	Total	Ramallah	Gaza	Total	Ramallah	Gaza	Total
Governor's Office	19	2	21	14	4	18	13	4	17	13	4	17	13	4	17
Security and Safety Office	13	10	23	12	11	23	12	12	24	17	12	29	20	11	31
Financial Follow-up Unit	10	0	10	12	0	12	0	0	0	0	0	0	0	0	0
Independent Offices	7	4	11	9	4	13	11	4	15	13	4	17	12	4	16
Legal Counsel	2	2	4	2	2	4	2	2	4	2	2	4	2	2	4
Internal Audit	5	2	7	3	2	5	5	2	7	5	2	7	6	2	8
Risk management	-	-	-	4	0	4	4	0	4	6	0	6	4	0	4
Core Departments	119	30	149	114	30	144	110	30	140	111	29	140	120	30	150
Monetary Stability Group	28	5	33	27	5	32	25	5	30	25	5	30	26	4	30
Research & Monetary Policy Department	16	3	19	15	3	18	16	3	19	16	3	19	15	3	18
Monetary Operations Department	12	2	14	12	2	14	9	2	11	9	2	11	11	1	12
Financial Stability Group	91	25	116	87	25	112	85	25	110	86	24	110	94	26	120
Supervision & Inspection Department	62	15	77	58	15	73	56	15	71	57	14	71	63	15	78
Payments System Department	12	4	16	12	4	16	11	4	15	11	4	15	13	4	17
Market Conduct Department	17	6	23	17	6	23	18	6	24	18	6	24	18	7	25
Supporting Departments	88	43	131	85	42	127	87	41	128	90	41	131	85	40	125
Public Relations Department	6	3	9	6	3	9	7	3	10	7	3	10	6	3	9
General Services Department	34	24	58	34	23	57	33	21	54	36	21	57	34	21	55
IT Department	23	5	28	21	5	26	22	5	27	22	5	27	20	5	25
Human Resources Department	11	3	14	11	3	14	12	4	16	12	4	16	11	3	14
Finance Department	14	8	22	13	8	21	13	8	21	13	8	21	14	8	22
Total	256	89	345	246	91	337	233	91	324	244	90	334	250	89	339

Source: PMA Database.



Table (4- 6): PMA staffing and training, 2014-2018

Items	2014	2015	2016	2017	2018
Governor's Office	11	6	6	10	9
Security and Safety Office	5	2	2	3	5
Independent Offices	5	9	11	12	15
Legal Counsel	2	3	3	2	4
Internal Audit	3	6	4	5	7
Risk Management	-	-	4	5	4
Core Departments	81	136	72	61	93
Monetary Stability Group	29	37	24	26	30
Research & Monetary Policy Department	19	22	17	13	18
Monetary Operations Department	10	15	7	13	12
Financial Stability Group	52	99	48	35	63
Supervision and Inspection Department	34	59	31	21	45
Payment System Department	5	13	5	5	6
Consumer Relations & Market Conduct Department	13	27	12	9	12
Supporting Departments	30	44	34	28	55
Public Relations Department	4	9	6	5	9
General Services Department	6	3	5	7	14
IT Department	10	16	9	6	18
Human Resources Department	5	10	8	5	6
Finance Department	5	6	6	5	8
Total	132	197	125	114	177

Source: PMA Database.



Part II: The Palestinian Banking Sector Developments

Table (4- 7): Domestic liquidity status, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Net foreign assets	5,023.9	4,781.3	4,751.2	4,957.4	4,945.6
Claims on non-residents	5,443.9	5,323.2	5302.4	5,657.2	5,478.0
Liabilities to non-residents	420.0	541.9	551.2	699.8	532.4
Net domestic assets	4,461.4	5,534.1	6586.9	7,667.6	8,274.3
Net claims on central government	629.4	969.9	940.0	912.6	895.8
Claims on central government	1,242.3	1,458.1	1,465.3	1,511.8	1,361.1
Liabilities to central government	612.9	488.2	525.3	599.2	465.3
Liabilities to other sectors	3,832.0	4,564.2	5,646.9	6,755.0	7,378.5
Other financial institutions	8.5	7.9	8.0	16.7	61.9
Local authorities	0.7	1.1	1.4	3.1	9.4
Non-financial institutions	0.0	0.0	4.4	0.0	8.8
Liability on private sector	3,822.8	4,555.2	5,633.1	6,735.2	7,298.4
Other items, net	1,449.8	1,447.9	1,772.2	1,631.8	1,808.0

Source: PMA Database.



Table (4- 8): Assets and liabilities, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Total assets	11,815.4	12,599.9	14,196.4	15,850.2	16,124.9
Cash and Precious Metals	658.5	1,083.2	991.2	1,728.2	1,582.6
Due from PMA and Banks (Total):	4,391.1	3,870.7	4,278.9	3,911.1	3,763.7
Due from PMA	1,041.5	1,134.1	1,305.7	1,428.7	1,416.0
Due from banks in Palestine	509.8	365.6	340.3	359.0	377.9
Due from banks abroad	2,839.8	2,371.0	2,633.0	2,123.4	1,969.8
Securities portfolio for trade and investment	985.6	953.3	1,007.1	990.4	1,123.3
credit facilities	4,895.1	5,824.8	6,871.9	8,026.0	8,432.3
Banking acceptances	6.0	4.1	4.8	4.8	0.0
Investment	145.0	164.3	205.2	217.2	262.2
Fixed assets	404.4	438.9	490.5	549.8	582.7
Other assets	329.7	260.7	346.6	422.7	378.2
Total Liabilities	11,815.4	12,599.9	14,196.4	15,850.2	16,124.9
Due to PMA and Banks (Total):	728.2	852.6	1,139.7	1,135.3	1,033.6
Due to PMA	134.6	299.2	644.5	597.4	624.8
Due to banks in Palestine	499.9	368.0	335.3	328.2	361.4
Due to banks abroad	93.6	185.4	159.9	209.7	47.5
Customer deposits	8,934.5	9,654.2	10,604.7	11,982.5	12,227.3
Executed and outstanding acceptances	11.3	13.8	30.9	25.9	15.5
Equity (net), of which:	1,464.0	1,463.9	1,682.4	1,891.2	1,912.0
Paid-up capital	976.0	961.3	1,071.8	1,157.7	1,215.8
Surplus capital	12.0	9.9	27.4	36.8	41.5
Legal reserve	138.0	151.7	165.8	183.8	201.5
Disclosed reserves	83.9	97.5	112.6	123.8	144.6
Undivided profits	4.7	4.2	14.3	33.3	27.8
Unrealized profit (loss) on long-term investment	-2.6	5.1	-1.2	-8.3	-15.7
Revaluation reserve	4.2	4.4	8.4	8.8	10.5
General reserves for banking operations	83.7	95.5	109.4	125.9	52.1
General reserves for non-banking operations	0.0	0.0	0.0	0.0	0.0
Qualified Subordinated loans	7.2	7.2	50.0	91.5	115.0
Current year Profits and losses	0.0	0.0	0.0	0.0	0.0
Profits and losses under approval	156.9	127.1	123.9	137.9	118.9
Tax provisions	61.1	43.5	60.7	84.3	62.9
Other provisions*	368.6	403.4	437.5	474.4	619.6
Other liabilities	247.6	168.6	240.5	256.6	254.0

* Includes provisions for securities, loans, overdraft, finance lease, investment, depreciation, and other provisions.

Source: PMA Database.



Table (4- 9): Profit and loss statement, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Interest received	423.1	438.4	484.2	571.9	631.5
Interest paid	63.2	64.1	78.0	105.0	124.4
Net interest income	359.9	374.3	406.2	466.8	507.1
Net commission income	86.1	90.2	96.4	115.9	117.9
Net debt securities and investments	6.5	6.2	11.0	14.3	10.1
others	44.7	45.7	47.3	61.6	64.0
Total non-interest income	137.3	142.1	154.7	191.8	192.0
Total income from all operations	497.2	516.4	560.9	658.6	699.1
Personnal expenses	154.1	167.6	178.8	216.1	238.6
Other expenses	144.9	158.5	172.4	192.0	205.9
Net Provisions	2.1	14.9	15.3	22.2	18.9
Total expenses	301.1	341.0	366.5	430.3	463.4
Net income before taxes	196.1	175.4	194.4	228.4	235.8
Taxes	50.4	43.1	46.4	57.8	56.6
Net income after taxes	145.7	132.3	148.0	170.5	179.2

Source: PMA Database.



Table (4- 10): Customer deposits, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Depositing Party					
Public sector, of which:	785.2	655.8	673.5	736.2	605.7
Palestinian National Authority	612.3	487.6	525.2	599.1	464.2
Private sector, of which:	8,149.3	8,998.4	9,931.2	11,246.3	11,621.6
Resident	7,840.6	8,653.8	9,594.7	10,852.6	11,186.7
Region					
WB	7,940.4	8,615.6	9,503.4	10,854.7	11,051.4
GS	994.1	1,038.6	1,101.3	1,127.8	1,176.0
Type					
Current deposits	3,505.7	3,776.0	4,207.5	4,698.4	4,581.1
Savings deposits	2,837.3	3,141.9	3,466.2	3,936.1	4,103.2
Time deposits	2,591.5	2,736.3	2,931.0	3,348.1	3,543.0
Currency					
USD	2,750.5	3,229.6	3,506.3	4,039.9	4,458.2
JD	2,299.4	2,477.2	2,643.7	2,805.2	2,814.8
NIS	3,550.4	3,578.6	3,956.1	4,732.4	4,597.3
Others	334.2	368.8	498.7	405.0	357.0
Total	8,934.5	9,654.2	10,604.7	11,982.5	12,227.3

Source: PMA Database.



Table (4- 11): Direct credit facilities, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Beneficiary					
Public sector, of which:	1,239.8	1,452.6	1,418.8	1,476.0	1,316.8
Palestinian National Authority	1,239.1	1,451.5	1,416.4	1,471.0	1,307.4
Private sector, of which:	3,655.3	4,372.2	5,453.1	6,550.0	7,115.5
Resident	3,631.2	4,352.9	5,387.7	6,470.7	7,029.0
Region					
WB	4,320.1	5,135.6	5,954.4	7,039.8	7,483.0
GS	575.0	689.2	907.5	986.2	949.0
Type					
Loans	3,853.8	4,639.9	5,632.5	6,594.1	6,990.3
Overdrafts	1,021.0	1,155.4	1,199.6	1,373.8	1,366.4
Leasing	20.3	29.5	39.8	58.0	75.6
Currency					
USD	1,443.6	1,984.7	2,460.9	3,182.7	3,099.2
JD	582.7	863.2	972.0	1,129.4	1,299.4
NIS	2,838.6	2,929.4	3,375.1	3,589.5	3,890.6
Others	30.2	47.5	63.9	124.4	143.1
Total	4,895.1	5,824.8	6,871.9	8,026.0	8,432.3

Source: PMA Database.

Table (4- 12): Direct credit facilities' provisions, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Loans	47.8	55.7	64.4	72.1	171.4
Overdrafts	28.8	28.3	35.7	36.5	52.4
leasing	0.0	0.0	0.0	0.0	0.4
Total Provisions	76.6	84.0	100.1	108.6	224.2
Direct Credit Facilities, net	4,818.5	5,740.8	6,771.8	7,917.4	8,208.0
Total Direct Credit Facilities	4,895.1	5,824.8	6,871.9	8,026.0	8,432.3
Outstanding interests	21.1	22.2	24.8	24.0	29.1
Non-Performing Loans	124.8	124.8	149.7	186.0	256.4

Source: PMA Database..



Table (4- 13): Sectoral distribution of private sector's loans, 2014-2018

(USD Million)

Items	2014	2015	2016	2017	2018
Real estate, constructions, and lands	831.2	1,081.0	1,369.6	1,620.7	1,861.1
Industry and mining	257.2	264.3	299.3	396.3	443.5
General trade	744.6	941.9	1,103.3	1,405.3	1,569.6
Agriculture and livestock	46.5	73.3	125.0	124.1	140.6
Services	374.4	402.0	605.6	868.4	864.0
Consumer goods financing	921.7	1,074.9	1,366.3	1,399.2	1,324.7
Car financing	165.1	200.7	229.3	292.9	302.9
Others	314.7	334.0	354.8	443.1	609.2
Total	3,655.3	4,372.1	5,453.1	6,550.0	7,115.5

Source: PMA Database.

Table (4- 14): Lending and deposit interest rates, 2014-2018

(Percent)

Period	Lending Rates According To			Depositing Rates According To		
	JD	USD	NIS	JD	USD	NIS
2014	7.20	6.05	9.09	2.15	0.83	1.46
2015	6.94	6.95	7.80	2.20	0.94	1.57
2016	6.34	5.87	6.94	2.28	1.02	1.50
2017	6.79	5.79	7.09	2.05	1.39	1.43
2018	6.75	5.92	7.18	2.52	1.85	1.72

Source: PMA Database.





Table (4-15): RTGS (BURAQ) participants total transactions, 2014-2018

Year	Bank to Bank Payments		Personal Payments		Clearing Settlement operations		National Switch Settlement operations		PEX CSD Settlements Operations		Other Operations		Total Transfers		Transfers outside the system	
	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value
2014	7,951	16,179.0	154,075	6,761.9	7,897	3,222.7	--	--	1,455	84.2	1,564	135.0	172,942	26,382.9	2,311	7,526.5
2015	7,271	23,440.0	172,677	7,648.5	7,681	2,780.2	810	0.4	1,464	56.1	1,568	146.0	191,471	34,072.1	2,272	7,450.1
2016	8,226	28,334.5	171,499	7,431.0	7,025	2,754.8	4,410	51.4	1,581	118.2	1,652	136.0	194,393	38,825.8	2,177	7,367.4
2017	8,954	22,872.7	159,796	8,447.3	6,864	3,125.1	5,405	75.5	1,463	117.9	2,957	245.6	185,439	34,884.1	2,278	7,844.6
2018	8,458	47,745.0	91,211	8,127.6	6,520	2,486.9	6,442	99.4	1,460	67.2	8,631	399.6	122,722	58,925.7	1,993	6,275.2

Source: PMA Database.

Table (4-16): Clearing activities, 2014-2018

Years	USD		JD		NIS		EUR		Total	
	No. of Checks	Value (USD Million)	No. of Checks	Value (USD Million)	No. of Checks	Value (USD Million)	No. of Checks	Value (USD Million)	No. of Checks	Value
checks presented for clearing										
2014	201,623	2,184.67	118,425	568.29	4,312,778	8,180.18	4,946	184.66	4,637,772	11,117.80
2015	212,523	2,199.55	119,776	610.04	4,758,872	8,239.27	5,225	82.54	5,096,396	11,131.40
2016	238,432	2,586.41	131,746	718.58	5,269,893	9,325.36	4,664	61.18	5,644,735	12,691.53
2017	264,449	2834.63	154,803	845.80	5,951,604	11,323.02	5,008	69.32	6,375,864	15,072.77
2018	262,066	2,094.33	160,156	699.18	6,029,461	9,890.99	4,877	45.54	6,456,560	12,730.04
Bounced checks										
2014	23,368	81.85	14,457	25.64	429,481	556.06	131	1.23	467,436	664.78
2015	21,478	73.61	13,824	31.34	502,622	563.94	121	1.42	538,045	670.31
2016	25,387	95.75	14,688	35.53	568,403	699.82	123	0.44	608,601	831.54
2017	32,385	142.40	17,283	45.73	685,687	965.70	124	0.36	735,479	1,154.19
2018	34,203	106.48	19,511	46.99	712,293	971.62	144	0.41	766,161	1,125.50

Source: PMA Database.

Part III: Non-financial Institutions Developments

Table (4- 17): Performing indicators of MFIs, 2014-2018

Items	2014	2015	2016	2017	2018
Institutions (number)	5	6	6	6	6
Branches (number)	58	64	85	84	81
Loans(number)	45,152	51,952	68,912	72,209	65,458
Credits portfolio (USD million)	97.0	136.7	199.4	215.0	205.7
By Region (USD million)					
WB	59.7	100.2	137.1	147.8	151.7
GS	37.3	36.5	62.3	67.2	54.0
Sectoral distributions of credits (%)					
Agriculture	14.0	14.9	12.6	11.7	12.4
Industry	10.9	5.0	4.9	5.6	6.1
Constructions	30.1	27.9	30.4	29.5	29.7
Trade	22.0	24.1	24.9	27.1	27.7
Services and public utilities	9.5	9.9	9.2	9.1	10.1
Tourism	0.6	5.1	4.6	5.0	4.0
Consumption	12.9	13.1	13.4	12.0	9.8

Source: PMA Database.

Table (4- 18): Money changers, 2014-2018

Items	2014	2015	2016	2017	2018
WB	237	238	225	233	254
GS	43	54	51	59	57
Total	280	292	276	292	311

Source: PMA Database.

Table (4- 19): Performing indicators of money changers, 2014-2018

(USD million)

Item	2014	2015	2016	2017	2018
Total assets	52.9	66.8	70.2	74.3	78.8
Ownership equity	45.8	47.2	47.5	66.6	71.3
Current assets	49.9	62.7	66.3	69.3	73.3
Fixed assets	2.8	4.1	3.8	3.7	3.9

Source: PMA Database.



Table (4- 20): Palestine Exchange- PEX, 2014-2018

Items	2014	2015	2016	2017	2018
Number of trading sessions	245	246	245	243	243
Banking and Financial Service Sector					
Number of listed companies (company)	8	8	7	7	7
Number of shares traded (share)	66,612,640	93,557,905	99,518,768	78,331,775	89,006,409
Value of shares traded (USD)	111,626,482	170,163,789	185,332,335	140,191,292	184,465,038
Number of executed transactions	8,099	10,852	9,482	14,220	9,759
Market value of shares traded (USD)	840,468,008	1,010,362,972	1,028,988,015	1,229,847,120	1,143,512,854
Insurance Sector					
Number of listed companies (company)	7	7	7	7	7
Number of shares traded (share)	6,387,299	6,329,064	11,871,187	25,461,516	21,996,471
Value of shares traded (USD)	4,273,400	3,084,350	29,288,370	11,807,880	22,829,535
Number of executed transactions	1,193	739	618	3,514	3,855
Market value of shares traded (USD)	105,346,000	110,496,000	150,912,500	159,688,000	206,766,000
Investment Sector					
Number of listed companies (company)	9	9	9	10	10
Number of shares traded (share)	73,144,267	50,418,739	88,912,257	126,481,172	46,098,997
Value of shares traded (USD)	109,532,601	56,384,917	114,562,485	188,589,019	67,202,307
Number of executed transactions	16,552	8,184	10,505	18,160	9,147
Market value of shares traded (USD)	545,274,304	512,422,052	564,056,509	854,427,042	803,889,873
Industrial Sector					
Number of listed companies (company)	12	13	13	13	13
Number of shares traded (share)	4,820,022	4,079,238	4,807,320	8,944,515	4,537,027
Value of shares traded (USD)	9,139,003	9,509,195	12,133,927	20,156,087	12,917,438
Number of executed transactions	2,773	1,845	2,135	3,111	2,274
Market value of shares traded (USD)	273,684,639	298,390,147	335,468,324	393,400,792	395,190,966
Service Sector					
Number of listed companies (company)	12	12	11	11	11
Number of shares traded (share)	30,580,926	20,844,517	27,514,575	31,944,772	23,432,156
Value of shares traded (USD)	119,345,638	81,245,961	103,835,252	108,325,943	66,061,701
Number of executed transactions	12,640	9,394	11,188	14,200	9,995
Market value of shares traded (USD)	1,422,586,673	1,407,525,208	1,297,269,627	1,254,132,578	1,185,561,326
Grand Total					
Number of shares traded (share)	181,545,154	175,229,463	232,817,327	271,163,750	185,071,060
Value of shares traded (USD)	353,917,124	320,388,213	445,152,368	469,070,221	353,476,019
Number of executed transactions	41,257	31,014	34,010	53,205	35,030
Market value of shares traded (USD)	3,187,359,624	3,339,196,379	3,390,122,335	3,891,495,531	3,734,921,019
Al-Quds index	511.8	532.7	530.2	574.6	529.4

Source: Capital Market Authority website, (www.pcma.ps)



Table (4- 21): Performing indicators of the insurance sector, 2014-2018

Items	2014	2015	2016	2017	2018
Companies (number)	10	9	9	9	10
Branches (number)	111	116	128	141	151
Employees (number)	1,175	1,156	1,192	1245	1401
Agencies (number)	215	206	224	262	271
Total insurance premiums (USD million)	171.0	164.8	195.6	255.4	279.4
Compensations (USD million)	108.1	97.9	113.8	144.3	166.3
Total assets/liabilities (USD million)	383.0	352.4	387.1	528.4	541.4
Paid-up capital (USD million)	69.7	58.7	59.5	71.2	90.0
Ownership equity (USD million)	136.7	124.6	137.7	188.6	186.3

Source: Capital Market Authority website, (www.pcma.ps)

