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Could a Palestinian State Ever Be Economically Viable?

The West Bank and Gaza have some assets on which to build a thriving economy, but the liabilities are greater. The Biden plan fails to address that problem

If the Palestine's economy can't flourish, instability and violence won't go awayCredit: Photo: Andrii Zastrozhnov, Artit Wongpradu/ Shutterstock.com / Artwork: Anastasia Shub

David Rosenberg

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"Palestinian state." It's been a long time since those words have been on Israel's political and media radar screen. But U.S. President Joe Biden has put it there front and center with his ambitious plan for ending the Gaza war, freeing the hostages and normalizing Israeli-Saudi ties.

Prime Minister Benjamin Netanyahu has also been talking about a Palestinian state, albeit always prefaced by a "there will not be a," but how long will he be in power?

The logic behind the Biden plan is to create a political and security environment that might make the Middle East less strife-ridden than it is today. But political arrangements can only go so far to deter war, terrorism and dysfunctional government. The Arab Spring and the violence that has continued in the 13 years since then is Exhibit A for independence being no panacea.

By itself, ending the occupation would give a lift to the economies of the West Bank and Gaza Strip, which would no longer have to contend with, respectively, checkpoints and a blockade. UNCTAD estimates that the cumulative economic cost to the Palestinian economy, due to Israeli restrictions from 2000 to 2019, was about $58 billion (in 2015 dollars), or 3.5 times the size of the West Bank/Gaza economy in 2019.

UNCTAD tends to exaggerate how wonderful economic conditions were before 1967 ("The economy of the Occupied Palestinian Territory was thriving before the occupation in 1967") and how awful they have been since. But free of Israeli rule, the nascent State of Palestine could expect a year or two of growth as the arteries of economic life reopen.

Then, the real challenge would begin.

The history of post-colonial states making a go of it economically is quite poor, but there are some exceptions and each country should be judged on its own merits. The balance sheet of a future State of Palestine has assets and liabilities that can be examined much like a corporate balance sheet, albeit with less precision.

Let's look at the assets first.

Natural gas: The Gaza Marine field offshore Gaza is believed to contain some 30 billion cubic meters of natural gas that has yet to be exploited. More may be discovered. If peace comes to Palestine, there's no reason why it should not be put into production and become part of the East Mediterranean gas hub. How much the gas is worth would depend on the price, but an UNCTAD report using the average price for gas in 2012–2017 put the value at $4.6 billion after development costs.

Dead Sea minerals: Israel and Jordan earn billions of dollars every year extracting potash, bromine and magnesium from the Dead Sea, part of which borders the West Bank. In a 2013 report, the World Bank the potential value-added to the Palestinian economy from potash, bromine and magnesium production at least $918 million a year, or 9 percent of GDP.

Still, the amounts (or gas or minerals) are not enormous and Palestine cannot become a resource economy like Russia or Saudi Arabia. It will have to look elsewhere for a competitive edge. It has several assets it could put to work.

Access to the Israeli market: Palestinian nationalists will resent the idea of close economic ties with Israel, especially as Israel is by far the bigger (GDP of $522 billion in 2022 versus Palestine's $19 billion) and more advanced economy (No. 6 in the world, according to Global Finance). But that makes Israel a major market for Palestinian goods and even more for labor services. Sealing off the Palestinian from the Israeli economy would be fatal for Palestine.

Access to the Arab market: In theory, this could be quite significant since there are 465 million Arabs, many of whom might buy "Made in Palestine" as a show of support for their newly independent brothers and sisters. But the reality is that cross-border trade between Arab countries is paltry and Palestine will have no real competitive edge with which to break into Arab markets. It's an asset, but one Palestine will struggle to make work.

Large diaspora: About half the people who claim Palestinian identity live abroad, mostly in the Gulf. Many of them have built businesses and have accumulated capital, and regularly send money home to support household budgets. There was a brief flush of diaspora investment into Palestine in the wake of the Oslo Accords (Taybeh Beer perhaps being the best-known example). Independence might revive that, at least for a time.

Now, to a few of the liabilities:

Small domestic market: The population of the West Bank and Gaza is about five million, which is not enough to develop industry based on economies of scale. Singapore and Switzerland did so with populations that are not much bigger by becoming export powerhouses, but they are rare exceptions to the rule. Palestinians would have to demonstrate unusually strong entrepreneurial qualities to pull it off, and the odds are against that.

Lousy government: One reason the odds are poor for the above is that apart from entrepreneurial qualities, Palestinian businesses would also need good, proactive government behind them. They are unlikely to get that. Whether it is the Palestinian Authority or Hamas, the Palestinian political class has a history of corruption and inefficiency that independence is unlikely to cure at a stroke. In the Middle East, only the United Arab Emirates and in recent years maybe Saudi Arabia can boast of an economy-focused political leadership.

Small tech sector: For a small country with a relatively well educated labor force, high-tech is an obvious path for economic development. However, the many attempts to make Palestine into another Start-Up Nation have all failed. Independence might unblock the infrastructure problems Pal-tech faces, but for now fewer Palestinians get tech-related degrees than even Jordanians or Egyptians, the quality of tech education is poor and there is no start-up capital available, according to a Portland Trust paper.

Strangely enough, the destruction of Gaza is a liability that could turn into an economic asset, albeit at the cost of thousands of lives. Assuming the international community comes up with the funding, rebuilding the enclave will pump billions of dollars into Gaza's economy and create tens of thousands of jobs over many years.

Thus, Palestine's balance sheet arguably looks favorable. But that is only if you give equal weighting to each item. The absence of good and effective government can easily destroy much of the asset side, for example, by enabling corrupt officials to fritter away natural gas earnings or by putting politics before economics and spurning economic ties with Israel.

It's a pity that there is no real economic dimension to the Biden plan. And, the two components it does have that might give Palestinian economic development a boost – a "reinvigorated" PA (meaning one that is less venal) and demilitarized state (that would save Palestine a lot of wasteful spending) – are opposed by many Palestinans. Even before the State of Palestine is little more than a policy proposal, its asset side is being eroded.