

Summary

The PMA is honored to publish its annual report for the year 2004. This issue commemorates the tenth anniversary for the establishment of the PMA. The past ten years have been filled with accomplishments and challenges for both the Palestinian economy and the PMA itself. Over the past decade; the PMA has laid the grounds for a strong and sound pillar of the Palestinian economy, the banking and financial sector. This has been a monumental task considering the tremendous impact of both the global and local politics on this region of the world and the continued Israeli occupation.

The year 2004 had its highlights on the global economy; the growth rate, GDP and GNP have improved for most of the world economies. The unemployment rate has, generally for most of the world economies, fallen below those of 2003. In 2004, the international trade has seen a steady growth rate as well.

The local economic indicators for the Palestinian economy did not respond in the same manner as those seen at the global level. The uncertainty of the political future continues to hamper and impede any real attempts for a measurable improvement on the economic sector. The Palestinian local domestic indicators were by-in-large worse off than those measured during 2003. The continued Israeli closure and restrictions policies of the Palestinian cities have prevented attempts to improve the performance of the Palestinian economy. Furthermore, the Israeli authorities continued its partial and limited release of VAT collected on behalf on the PNA. This in turn dealt a blow to the ability of the PNA to pump-in any substantial amounts of liquidity, in terms of projects and emergency aid, to induce improvements within the local economy.

On the positive note, the Palestinian economy showed a higher resistance to closure policies and became better prepared to dealing with such adverse situations. The private investment and trade sectors of the Palestinian economy showed more resilience towards the Israeli policies. This was reflected in an increase in Palestinian exports to other countries. The trade and industrial sectors showed some signs of improvements. The banking systems did improved as well where the total deposits have increased and an increase in the amount of loans issued by the banking sector was visible.

The report contains three main topics spread over seven chapters:

- The Global Economic Development;
- Palestinian economy;
 - Economic Development;
 - Financial Development;
 - Foreign Sector;
 - The Development of Banking Sector;
- The Achievements of PMA;
- and the appendices.

The Global Economic Development:

Notwithstanding the fact that the year 2004 was the best of the past five years in terms of growth rate, the unemployment rate, and the international trade indicators were still lagging behind on the global front. Over the past five years, the two most significant events that impeded/continues to impede the recovery of the global economy remain:

1. Natural disasters as in the case of Tsunami which caused tremendous damage in the region extending from east Africa to Southeast Asia, causing losses in billions of USD, and a death toll close to a million people.
2. Wars and especially the Iraqi war, continues to escalate the oil prices which in turn negatively impacts the global economy.

The available data on the year 2004 shows that global economy enjoyed, on average, a growth rate equal to 5 percent, compared with 2.5 percent in the year 2003, which in turn, positively affected the international trade and the labor markets in many countries, specially the industrial nations. On the other hand, the volatile oil prices caused the prices of goods and services to go up, reflecting in an increase the inflation rates in those countries.

The interest rate witnessed a significant increase, especially in United States, where the Federal Reserve, for the first time in the US history, increased the interest rate five successive times during the past year. The same action was taken by the Canadian Central Bank, which increased the interest rate twice during the same period. The British Central Bank followed suit increasing the interest rate four times successively during the year 2004. On the other hand, the European Central Bank kept their interest intact.

The devaluation of the USD continued against Euro, Yen, and Sterling Bound. On the other hand the yield on the ten-year governments' securities showed an upward trend within the major industrial nations. The increase in the indicators of the stock exchanges of the industrial nations can be attributed mainly to the volatile oil prices.

The Main Developments of Palestinian Economy in 2004

1- The Economic Output

The available preliminary data for the year 2004 indicates some signs of recovery in Palestinian economy. This recovery, however, was not sufficient to put the Palestinian economy backs to its pre 2000 levels. The Palestinian economy in 2004 showed a growth rate in terms of nominal GDP equal to 6 percent, compared with 12 percent in 2003. Accordingly, the GDP was expected to increase to USD 4,462 million, compared with USD 4,222 million in 2003. It is worthy to mention that the overall performance levels of the Palestinian economy in 2004 remain lower than those in 1999 by 1 percent.

The growth in GDP positively affected income per capita, which also increased by 3 percent. The increase in the income per capita raised the individual income to USD 1,216. This increase in the income per capita is dismal compared with 8 percent increase that was achieved in 2003. In comparison to the income per capita levels

reached in 1999, it is safe to conclude that the standard of living in 2004 is still below what it used to be in 1999.

The GNI witnessed a growth rate equal to 4 percent, compared with 14 percent in 2003, to reach USD 4,950 million. As a result, the GNI per capita increased by 1 percent and reached USD 1,331, compared with 11 percent in 2003. The GNI levels are still below those of 1999 by 7 percent.

This situation requires gradual but contentious steps to solidify this growth, by encouraging more local and foreign investments, especially in the private sector, providing friendlier environment to encourage the role of the private sector, and improving the performance of the public sector by becoming more transparent and efficient.

2- The Labor Market

The labor force in 2004 increased by 4 percent to reach 790,000; of which 528,000 worked within the Palestinian territory, 50,000 are worked in the Israeli labor market and the rest, 212,000, were regarded as unemployed. The unemployment rate increased in 2004 to 27 percent of the total Palestinian labor force, compared with 26 percent in 2003.

3- Inflation

Despite the increase in unemployment rate, and increase in per capita income, the CPI in 2004 registered increase equals 3 percent, compared with 4 percent in 2003. On the other hand, it is evident that the closures and restrictions on the movement of people, goods and services, has negatively affected the poverty levels, which has increased by 4 percent in 2004. The poverty levels now affect at least 66 percent of total Palestinian families, or 2,682 million people of the Palestinian population living within the PNA territory. Following suit with the foregoing indicators, the economic dependency ratio increased to 6 persons per employee. .

Financial Developments in 2004

The PNA budget in 2004 was not different from that of the general economic outlook within Palestinian territory. The PNA budget was affected, besides the local environment, by the Israeli policies, changes in the economic activities, and institutional developments (including reform of the financial system) as well as the continued release of tax revenue, VAT (collected by Israel on behalf of the PNA) and the grants of the donor's country. The total revenue in 2004 has increased by 23 percent to reach USD 1,562 million {domestic revenues increased by 27 percent, compared with 19 percent increase in the external revenues (grants)}, compared with 22 percent in 2003. The total revenues in 2004 constituted 35 percent of GDP, and 89 percent of the total expenditures, compared with 30 percent and 84 percent, respectively in 2003.

The increase in population, continuous deteriorations of standard of living, the activating of the financial part of the civil service law, and the unperformed increased in the number of public employees has increased the pressure on the demand of the public services provided by the government. This increase was translated in an unprecedented expenditure. The government expenditures increased by 17 percent to reach USD 1,764 million (current expenditure increased by 20 percent, compared with

2 percent increase in the developing expenditure) compared with 21 percent in 2003. Total expenditures constituted about 40 percent of GDP, compared with 36 percent in 2002.

These developments not only affected the coverage level of revenues to expenditures, but also the budget deficit. The current deficit increased to USD 556 million (12 percent of GDP) in 2004, compared with USD 508 million (12 percent of GDP) in 2003. The deficit before the grants increased to USD 817 million (18 percent of GDP) compared with USD 765 million (18 percent of GDP) in 2003. On the other hand the deficit after grants decreased to USD 202 million (5 percent of GDP) in 2004 compared with USD 247 million (6 percent of GDP) in 2003.

The final figures of the budget, indicate a decline in the financial gap (deficit after finance) from a negative USD 202 million (5 percent of GDP) in 2004, to a positive USD 8 million (less than 1 percent of GDP).

In addition, the cumulative public debt has increased in 2004 by 13 percent to reach USD 1,450 million, which constitutes about 153 percent of domestic revenues and reflects a decrease from the figure of 171 percent in 2003. The public debt now stands at 265 percent of total export of goods and services, up from the 248 percent level of 2003, and 32 percent of GDP, verses the 30 percent reached during the 2003 fiscal year.

Foreign Sector Developments in 2004

Trade activity performance is regarded as one of the indicators used to monitor overall economic performance. This activity witnessed some recovery signs that mainly resulted from ease in the restrictions on the movement of people, goods, and services; all of which caused a measurable increase in Palestinian exports. The total exports of goods and services increased throughout the year 2004 by 8 percent, reaching USD 615 million compared to the year 2003, where there were no changes. While imports of goods and services also increased by 6 percent to reach USD 3,120 million compared to the 16 percent increase in 2003; all of which resulted in an increase of 5 percent in the trade deficit, putting it at USD 2,505 million, compared to a 20 percent increase in 2003.

The increase in the trade deficit put an added pressure on the financial resources, mainly net income from abroad and current transfers. However, net income from abroad declined by 9 percent to reach USD 488 million compared to a 41 percent increase in 2003. This decline was mostly attributed to the decrease in number of Palestinian workers in the Israeli labor market to 50,000; a number equivalent to 9 percent of the Palestinian labor force, all of which compares favorably with the 10 percent decline in 2003. At the same time, 2004 witnessed a substantial influx of money to the Palestinian Territory in terms of current transfers equaling 1,569 million (35 percent of the GDP), which exceeds 2003's value by 6 percent, all of which is distributed equally between both the public and private sectors. Net income from abroad and current transfers together helped to finance about 82 percent of the trade deficit, compared to 85 percent in 2003.

Banking Sector Developments in 2004

The performance of the banking system in 2004 is the translation of the PMA's efforts in developing a sound, credible, and effective banking sector; which in its turn resulted in a substantial increase in the assets/liabilities of the Palestinian Banking System.

The assets of the banks operating in Palestinian Territory¹ increased by 8 percent to reach a value of 5,114 million compared to an 11 percent increase in 2003. The share of customer deposits increased to 77 percent of the total money sources, compared with 76 percent in 2003. In addition the provisions and other liabilities increased to 4 percent compared to 3 percent in 2003; and 46 percent of the total assets in terms of balances with banks operating outside Palestine, compared to 48 percent in 2003. At the same time, the banks issued credit facilities and investments equal to 33 percent of their total assets, compared to 28 percent in 2003.

The clearinghouse at the PMA witnessed an increase in the number of cleared checks (consisting of US Dollars, Jordanian Dinars, New Israeli Shekels, and Euros) by 29 percent in numbers and by 26 percent in value in 2004 compared to only 12 and 20 percent respectively in 2003; and for the first time in the history of the PMA the clearinghouse witnessed many operations with the European Euro. At the same time, the percentage of the number of bounced checks and their values in 2004 remained the same as in 2003: about 14 percent of the total number of checks in the clearinghouse, consisting of 8 percent of the total value of the checks.

The Palestinian Securities Exchange also witnessed an increase in the number of dealing sessions, the amount and the value of the shares; which in turn contributed to the growth of the stock parameter "AlQuds" by 54 points, compared to only 19 points in 2003, reaching 278 points compared to 2003's total of 180 points.

The year of 2004, PMA's efforts were characterized with achievements, especially in terms of information-technology upgrades, whether through further development of existing infrastructure or in the development of new internal and external networks, and by the development of a system for collecting financial and statistical data to aid in improving the feasibility of studies concerning the payment system. These efforts were carried out in addition to PMA's traditional efforts in organizing the banking sector, serving the economy & its development, as well as, its role in developing the Palestinian Institute for Financial and Banking Studies.

Finally plans are underway to further develop the PMA's manpower and human resources, either by adding to the existing staff or through training and accumulative experiences in order to achieve the PMA's ultimate goals. These plans are going hand-in-hand with the efforts to establishing/strengthening ties with a number of financial institutions, both in the Arab world and globally.

¹ The 'banking sector' consists of the PMA as a supervisory authority, and all the banks operating within the Palestinian Territory, including both the foreign and national banks.

The key Economic Indicators In Palestine During (2000-2004)

Indicator	2000	2001	2002	2003	2004
Population (Thousand persons)	3,212	3,335	3,454	3,576	3,700
Growth rate (%)	4	4	4	4	3
Economic Development					
GDP at current prices (USD million)	4,442	4,136	3,780	4,222	4,462
Growth rate (%)	-2	-7	-9	12	6
GDP per capita (USD)	1,411	1,254	1,091	1,181	1,216
Growth rate (%)	-6	-11	-13	8	3
GNI at current prices (USD million)	5,275	4,622	4,161	4,760	4,950
Growth rate (%)	-3	-12	-10	14	4
GNI per capita (USD)	1,674	1,401	1,201	1,331	1,349
Growth rate (%)	-7	-16	-14	11	1
Unemployment Rate (%)	14	26	31	26	27
Inflation Rate (%)	3	1	6	4	3
Consumption Expenditure/ GDP (%)	126	130	134	133	135
Investment Expenditure/ GDP (%)	31	25	18	22	21
Local Saving / GDP (%)	-26	-30	-34	-33	-35
Public Finance					
Total Revenue (USD million)	1,364	1,053	1,037	1,266	1,562
Total Revenue/ GDP (%)	31	25	27	30	35
Of which: local revenues (USD million)	964	287	335	748	947
Local Revenue/ GDP (%)	22	7	9	18	21
Total Expenditure (USD million)	1,364	1,239	1,249	1,513	1,764
Total Expenditure/ GDP (%)	31	30	33	36	40
Of which: Current Expenditure (USD million)	940	1,016	1,049	1,256	1,503
Current Expenditure/ GDP (%)	21	25	28	30	34
Financial Position of PNA (Deficit After Financing) (USD million)	0	-265	0	27	8
Budget Deficit/ GDP (%)	0	6	0	1	0
Public Debt (USD million)	836	1,217	1,156	1,285	1,450
Public Debt/ GDP (%)	19	29	31	30	32
Public Debt/ Exports of goods & services (%)	96	182	202	248	265
Foreign Sector					
Export of Goods and Services (USD million)	868	670	572	572	615
Export of Goods and Services/ GDP (%)	20	16	15	14	14
Import of Goods and Services (USD million)	3,405	2,948	2,553	2,949	3,120
Import of Goods and Services/ GDP (%)	77	71	68	70	70
Trade Balance (USD million)	-2,537	-2,278	-1,981	-2,377	-2,505
Trade Balance/ GDP (%)	57	55	52	56	56
Remittances of Employees (USD million)	785	362	300	459	416
Remittances of Employees/ GDP (%)	18	9	8	11	9
Current Transfers (USD million)	586	671	1,109	1,477	1,569
Current Transfers/ GDP (%)	13	24	29	35	35
Current Account (USD million)	-1,118	-821	-491	-362	-448
Current Account/ GDP (%)	25	20	13	9	10

Indicator	2000	2001	2002	2003	2004
Banking Sector					
Assets/Liabilities of PMA (USD million)	412	373	397	520	569
Growth Rate (%)	17	-9	6	31	9
Assets/Liabilities of Banks (USD million)	4,594	4,422	4,266	4,729	5,114
Growth Rate (%)	19	-4	-4	11	8
Direct Facilities (USD million)	1,347	1,221	956	1,072	1,428
Growth Rate (%)	34	-9	-22	12	33
Balances with banks abroad	2,150	2,173	2,322	2,267	2,329
Growth Rate (%)	7	1	7	-2	3
Customer's Deposits (USD million)	3,508	3,399	3,430	3,624	3,958
Growth Rate (%)	22	-3	1	6	9
Equity (USD million)	244	209	192	222	307
Growth Rate (%)	-1	-14	-8	16	38



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