



Instability and Fragmentation Continue to Constrain Private Sector Growth in the Palestinian Territories

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Private sector is a key driver for economic growth and job creation but Palestinian enterprises have remained hostage to political instability, unresolved conflict, and continued restrictions on movement, access, and trade. "An active private sector is much needed to fuel economic and social progress in the Palestinian territories already faced with declining income and increasing unemployment, said Steen Jorgensen, World Bank Country Director for West Bank and Gaza. "Allowing mobility and access to resources is crucial to building investor confidence and developing industry and high value-added service sectors that would support a prosperous Palestinian economy and protect against future violence." A new World Bank report, Investment Climate Assessment: Fragmentation and Uncertainty, provides empirical evidence that political instability resulting from conflict, military rule, violence, political division, and lack of free movement and access to resources and markets remains the key obstacle to economic growth. The Palestinian private sector largely remains confined to primarily small-sized firms operating with low capital investment, in a fragmented domestic market, and in relative isolation from the global economy. The multiple layers of restrictions and complex rules imposed by Israeli authorities govern business activities. The severe fragmentation of the Palestinian markets, turned into "micro-climates" has led to different conditions and constraints depending on the location within the Palestinian territories. The business activities are burdened with additional time, financial resources, and capacity to navigate. In the West Bank, Israeli controlled commercial crossings, checkpoints, and other physical and procedural barriers impede business and trade. In Gaza, exports are nearly completely banned and imports restricted and severely delayed even when they are permitted. Panel data from Palestinian firms surveyed in 2006 and then again in 2013 show no significant growth in capital investment or employment due to the uncertainty and fragmentation. Engagement in innovative and business-upgrading activities has decreased, driven primarily by diminished level of activity among Gaza firms. On the Palestinian side, there is still work to be done to improve the business climate to get ready for the day when restrictions are released, of special importance is to ensure a unified system of economic and commercial legislation between Gaza and the West Bank. "It is imperative to alleviate the suffering of the Palestinian people and to provide new horizon for hope, said Jorgensen. "Unleashing the potential of the private sector could improve the living standards, create jobs and growth. It is in the interest of all parties to bring stability to the region and to abide by their commitments." The report also highlights positive findings and potential opportunities in the Palestinian investment climate. There is evidence of a nascent, but growing entrepreneurship ecosystem, a growing ICT sector, and a number of larger Palestinian investors who have successfully attracted FDI in recent years. Further positive aspects of the investment climate include a low incidence of petty corruption and a liquid and stable financial sector. Despite the political division between the West Bank and Gaza, most aspects of the Palestinian bureaucracy have remained functional. The Investment Climate Assessment shows that labor productivity of Palestinian firms is on par with comparator countries, while unit labor costs seem to be competitive within the region. This means there is a potential opportunity to increase labor productivity if firms invest more and resources shift towards high productivity sub sectors in manufacturing and services. "The report paints a gloomy situation of the investment climate but the productivity data and emergence of high-value sectors such as pharmaceuticals and information technology demonstrate the potential for growth that builds on the Palestinian entrepreneurial spirit, said Nabila Assaf, World Bank Senior Private Sector Development Specialist and lead author. "Although the political instability is the binding constraint to investment and business, it is crucial to identify ways of improving aspects of the business climate in the short term." The World Bank
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