



**LFI: *Policy Report***

**From Disengagement to an Economic Roadmap**

**January 2005**

*This policy report focuses on the economic repercussions of Israel's disengagement plan, offering guidance to policy-makers on how stability and prosperity may be promoted. The opportunity for Palestinian economic development created by disengagement is now even more pronounced, with the prospect of democratic elections and political and security reforms in the Palestinian Authority. This paper identifies the principal economic benefits that withdrawal from Gaza will bring the Palestinians and suggests that the Palestinians, Israel and the international community must focus on certain key areas of action in order to help the Palestinian economy to prosper in the disengagement era.*

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## Foreword

Israel's disengagement plan has direct implications not only for the future political and security relationship between Israel and the Palestinians but also for the state of the Palestinian economy and for the future economic relationship between the two entities.

This paper focuses on the expected economic repercussions of disengagement, with an emphasis on guiding policy-makers on how stability and prosperity may be promoted in the post-Arafat era. The analysis draws upon the lessons of past experience since the signing of the 'Oslo Agreement' Declaration of Principles in 1993, through the peak of business and economic relations just before the current *intifada* and on to the present day.

The report has been compiled from personal interviews of senior personnel at the **Aix Group, the Israel National Security Council, the Israel/Palestine Centre for Research and Information (IPCRI), the Palestinian Forum for Democracy, the Palestinian Ministry of Economy, Paltrade, and the Peres Centre for Peace**. It is also based on analysis of reports and statements by international and local agencies and experts including the **Aix Group, Business Data Israel, the Economist Intelligence Unit, the IMF, IPCRI, Israel's Ministry of Foreign Affairs, Paltrade, the Peres Centre for Peace, UNESCO, USAID and the World Bank**.

This research was conducted for Labour Friends of Israel by Coleman Becker Consulting (CBC), who provide expert and professional business services including economic and business research and analysis, business plans and competitive strategy development. CBC partner Jeremy Coleman has over a decade of practical, political and business experience in the Middle East, focused on building trade and business relations between Israel and the Arab World. Since 1996 he has worked closely with the world's leading authority on business and competitive strategy, Professor Michael E. Porter of Harvard Business School, with the aim of promoting regional stability and prosperity by strengthening competitiveness and cross-border business relations. Before moving to the region in 1993 he worked in both the UK Parliament and US Congress, and has a deep understanding of the perspective and requirements of international policy-makers. Mr. Coleman has an MBA from Tel Aviv University and also acts as a private business consultant for major companies in Israel and the region. An expert in global telecoms and hi-tech, he has brokered a number of Middle East cross-border trade deals, and has lectured on competitiveness and strategy at conferences and Business Schools across the region.

## **1. Executive Summary**

### **The Palestinian Economy & Israel-Palestinian Economic Relations**

Palestinian economic performance since 1967 can be broadly characterised by output volatility, dependence on Israel's economy, vulnerability to political factors, low productivity, and weak international competitiveness. As a result there has been generally high unemployment, widespread poverty and low standards of living.

Since 1994 Israeli-Palestinian economic relations have been formally governed by the 'Paris Protocol', a follow-up agreement to the 1993 'Oslo Accords'. The Protocol established a Customs Union and an open border policy between the two entities which allowed for the free movement of industrial and agricultural goods between Israel and the territories. It also enabled Israeli companies to hire Palestinians to work inside Israel – a far less expensive labour source for Israelis.

A deteriorating security situation and a subsequent sharp decline in Palestinian labour flows to Israel led the Palestinian economy into recession by 1996. That year the growth rate was estimated at a low 2% compared to 12% in 1997. Labour flow into Israel in 1996 was at a low of 15% compared to 22-23% in 1998-1999. The policy of closures, whereby the Israeli army controlled border checkpoints and restricted movement in the area, changed the spirit of the Oslo agreement which envisioned developing peace based on cooperation. Nevertheless, from 1997-2000 there was noticeable economic progress and the first three quarters of 2000 showed 8.4% growth compared to the corresponding period the previous year.

The outbreak of the *Al-Aqsa intifada* on 29 September 2000 caused economic crisis in the Palestinian areas. The Palestinian economy has lost an estimated \$4.5 billion in the period since then, with GDP per capita falling by 30%. Border closures and internal movement restrictions were set in place by Israel due to security concerns and unemployment in 2002 rose to a high of 31%, causing income reduction in all sectors.

Today's Palestinian economy relies heavily on international donor funding. Donor assistance to the Palestinians fell slightly in 2003, but at \$883m remains very high by international standards.

### **Overview of Disengagement**

In October 2004, Israel's Knesset ratified a plan for unilateral Israeli disengagement from Gaza and parts of the northern West Bank – Prime Minister Sharon's 'Disengagement Plan'. The plan calls for Israeli military and civilian withdrawal in phases, each to be discussed and voted on by the government, and requiring a majority in Cabinet for ratification. If it is fully implemented, there will be no Israeli military or civilian presence in Gaza, and the Palestinians will have full territorial contiguity in the northern area of the West Bank. However, Israel will continue to maintain full control of the border, airspace, and coastline envelope of the Gaza Strip.

In total, 21 settlements are slated for dismantling, of which 17 are in Gaza. The withdrawal is planned to be completed by the end of 2005.

### **The Economic Implications of Disengagement**

Disengagement would bring the Palestinians two principal benefits:

1. Bringing down some of the barriers to internal mobility. While the removal of internal barriers would bring immediate relief, its economic impact would be marginal. In order to have a significant effect on the economy of Gaza, the transport infrastructure would require wholesale redevelopment to improve the flow of goods and people.
2. The evacuation of settlements and military installations will grant 75 additional square kilometres of well-tended agricultural land to the Palestinians. But the economic potential of this land will

remain untapped unless there are markets for the agricultural produce, and a means of transporting goods in a timely and predictable way out of Gaza. Since 90% of exports from Gaza go either to or through Israel, this means a review of the border regime, not part of the disengagement plan.

According to the World Bank, disengagement alone will not deliver significant economic benefits. In fact, the difference between the Gaza economy under disengagement and the continuation of the status quo is negligible: High population growth and the reduction in work in Israel would result in a cumulative real GDP per capita decline of about 12% by 2006. Real GDI per capita would drop by some 22%. Forecast for poverty at 56% and unemployment at 34% is almost equal to the forecast under the status quo.

### **Policy Lessons**

It is important to all sides – the Palestinians, Israel and the donor countries – that the Palestinian economy prospers in order to support peace and stability. This paper discusses **three key areas of action** by which the chances of prosperity can be improved:

**The first, ‘Security and Stability’** is about providing the basic conditions required by any economy in order to attract investors with a safe and predictable business environment. The most important and long-term means of increasing security and enhancing the chances for peace and stability would be by an announcement that the Disengagement plan is the first step towards an end-game, perhaps by a return to the US Roadmap plan with its “Permanent Two-State Solution to the Israeli-Palestinian Conflict”. Accompanying this there should be a clear commitment by both sides to a ceasefire. In this way Disengagement would be made an integral part of a much wider vision for peace and reconciliation between Israel and the Palestinians.

**The second area, ‘Improving the Flow of Goods and Labour’**, is concerned with enabling Palestinians to trade normally with external markets and to move and transport goods freely within their own territories. World Bank projections indicate that facilitating Palestinian external trade would raise real GDP growth to 9.2% by 2006 compared with a negative 2006 growth rate under a status quo scenario. Exports would grow at 30% per annum by 2006, significantly higher than the 3.4% under the status quo scenario.

**Finally, ‘Industry Growth and Job Creation’** discusses ways in which the economy can be stimulated and businesses can be made more competitive. At the micro-economic level there are a series of measures by which Israel, the Palestinians and the international community can promote industry growth and job creation – these include launching large infrastructure projects, developing cross-border industrial parks, establishing more micro-financing programmes, improving the transparency of the PA’s financial affairs, establishing a more liberal credit regime and assisting specific Palestinian industries with international cooperation and expert know-how.

## **2. The Palestinian Economy & Israel-Palestinian Economic Relations**

### **The Nature of the Palestinian Economy**

#### **Volatility & Economic Dependence**

Palestinian economic performance since 1967 can be broadly characterised by output volatility despite an average annual economic growth rate of 5.4%. Economic development has broadly been based on dependence upon the Israeli economy. For example, between 1967 and 1994, on average 90% of the value of imports and 70% of the value of exports were to and from Israel. Underlying the volatility in output is vulnerability to political factors, low productivity, and weak international competitiveness.

#### **Small Businesses**

At the time of Oslo, the West Bank and Gaza Strip private economy consisted of some 50,250 individual establishments, approximately one-quarter of which were in the secondary sector (manufacturing, utilities and construction) and three-quarters in the tertiary sector (commerce and services). Total employment was estimated at 128,000 and the average employment size of establishments was about 2.5 people, hence the vast majority of private sector establishments could be characterised as small businesses. Small and medium businesses employing less than 25 employees, excluding enterprises operating in agriculture, contributed 24% of the Gross Domestic Product (GDP) in 1999.

#### **Services Heavy**

Roughly 80% of the Palestinian GDP is in the services sector. Industry is 12%, including 9% manufacturing. Agriculture is only 6% of total GDP. The services industry is based largely on Palestinians working in Israel. These workers benefit from larger and more modern Israeli productive capacities and receive higher remuneration than in jobs within the Palestinian areas.

#### **Corruption**

According to public opinion surveys, conducted regularly by the Center for Palestinian Research and Studies in Nablus, most Palestinians perceive a degree of corruption in the PA. Amid international pressure from donor countries, accusations of corruption and calls for Palestinian reform of leadership, the PA published in June 2002 a 100-Day Plan for Reform. The document included 39 items dealing with general institutional measures, public security, finances and the judiciary. Reform undertakings and transparency efforts included public disclosure of financial data for holding companies with PA investments, publishing of the terms of exclusive licenses to firms such as Paltel (Palestinian Telecommunications Company), creating regulatory bodies that are independent of policy ministries and publishing an annual report by the PA's Auditor General.

#### **Monopolies**

Import monopolies exist in the economy with PA involvement, namely for gasoline and cement. These monopolies were set up within the Paris Protocol framework to protect existing Israeli monopolies. In 2000, the PA announced plans to create a privatisation strategy aiming at gradually phasing out the PA's equity holdings and to privatise most public enterprises.

### **Oslo, the Paris Protocol and the PA**

In September 1993 with the signing of the Declaration of Principles ('Oslo Accords') and the jump-start of the peace process, morale and confidence were high, despite a lack of development and an under-provisioning of public goods and services. Alongside the political agreements forged in Oslo, a new economic relationship was born between the Palestinians and Israel. The 'Protocol on Economic Relations', formalising and defining this new relationship, was signed in Paris on April 29th 1994 (the 'Paris Protocol').

Under the Protocol, the Israeli and Palestinian sides recognised the need to develop progress towards a just and lasting peace in the region and the protocol laid the groundwork for a Palestinian economy to make and prioritise its own decisions. A Palestinian-Israeli Joint Economic Committee was created to follow up

implementation of policies regarding imports, financial and monetary issues, taxation rules, labour and agriculture standards, insurance coverage and others.

In May 1994, the Palestinian Authority (PA) was assembled to implement the Israeli-Palestinian agreements. The PA was expected to improve living conditions and adopt economic policies in favour of local development and it established various institutes to direct the Palestinian economy. The economic institutes established included a Palestinian Ministry of Finance with a Treasury and Budget Department, a Palestinian Monetary Authority and a Central Bureau of Statistics.

The PA sought to use cooperative relations with Israel to create a stable macroeconomic policy around its newly emerging financial sector. The infrastructure was set to improve through donor funds from international countries and private investment would foster growth.

### **Trade & Labour**

A Customs Union and open border policy were seen as the best way to establish the trade regime between the Israelis and the Palestinians. The Protocol allowed for the free movement of industrial and agricultural goods between Israel and the territories, making the Palestinians a captive and reliable market for Israeli products. The protocol introduced full tariff free exports in agricultural and industrial goods. The protocol also increased direct trade between the PA and other parties, which was highlighted by the signing of trade agreements between the PA and USA, EU, European Free Trade Association, Jordan and Egypt.

The protocol allowed for Israeli companies to hire Palestinians to work inside Israel - a cheap labour source for Israelis. The agreement was set to maintain the existing levels of Palestinian workers in Israel.

In discussions on the final status agreements in 2000, both sides agreed to move from a Custom Union regime to a Free Trade Area agreement. This meant a better opportunity for the Palestinians to create an independent economic policy.

### **Taxation**

Under the Paris Protocol, the Palestinian Authority is responsible for direct taxation and the implementation of a value-added tax system, while the Israel authorities are responsible for clearing tax receipts at Israeli ports for goods destined for PA areas. The protocol also created a revenue collection system for the Palestinian Authority. Increased tax revenues were partly responsible for the increase in Palestinian public expenditure from \$280 million in 1993 to \$818 million in 1997.

### **From Recession to Growth**

The tough task of economic management and governance along with a deteriorating security situation and a subsequent sharp decline in Palestinian labour flows to Israel forced the Palestinian economy into recession by 1996. That year the growth rate was estimated at a low 2% compared to 12% in 1997. Labour flow into Israel in 1996 was at a low of 15% compared to 22-23% in 1998-1999.

The policy of closures, whereby the Israeli army controlled border checkpoints and restricted movement in the area, changed the spirit of the Oslo agreement which envisioned developing peace based on cooperation between the sides. The deterioration of the security situation and the closures caused further separation, greater suspicion and a loss of confidence on both sides. Movements of businessmen and goods were restricted by security policies. Prior to the protocol, there had been virtually no borders with regards to movement of people, goods and vehicles.

Nevertheless, from 1997-2000 there was noticeable economic progress. The growth in the economy was slow but improvements in some areas were made. Infrastructure and buildings in the West Bank and Gaza Strip improved through substantial donor assistance. The PA solidified a strong revenue base and managed to balance the budget in 1998, despite continued strong increases in current expenditure. The unemployment rate in 1999 dropped to 11% compared to a high 20% in 1997. Between 1997 and 2000 the labour market grew. The first three quarters of 2000 showed 8.4% growth compared to the corresponding period the previous year. GDP growth reached an annual average of 5%. See Appendix B.

Israel's economy also benefited from the launch of the peace process with an average annual growth rate of 6%, partly as a result of rapid growth in foreign and local investment. Also, agreements with the Palestinians led to a direct easing of the Arab boycott and enabled Israel to develop diplomatic, economic and trade relations with several Arab and Muslim countries. Per capita income increased from \$12,500 in 1993 to \$17,000 in 1997. Israel also benefited from growing trade with the Palestinians which increased steadily throughout the period.

### **Al Aqsa Intifada**

The outbreak of the Palestinian *intifada* on 29 September 2000 caused an economic crisis in the Palestinian areas. The Palestinian economy has lost an estimated \$4.5 billion in the period since then, with GDP per capita falling by 30%.

### **Labour**

With the *Intifada*, border closures and internal movement restrictions were set in place by Israel due to security concerns. With border crossings closed and restrictions limiting movement, many stayed inside the West Bank and Gaza without work. Unemployment in 2002 rose to a high of 31%, causing income reduction in all sectors.

In 2003 the economy improved slightly. This was in part because of reduced levels of violence, fewer curfews and a rebound of the Israeli economy. In 2003, some 104,000 jobs were created for Palestinians. However, during the first half of 2004, 24,000 jobs were lost.

In 2004 the World Bank reported the number of Palestinian workers in Israel in Q3 2000 at 146,000 (116,000 from the West Bank and 30,000 from Gaza). After the start of the *intifada*, the number dropped in the next quarter to 43,000. The lowest level over the four years occurred in Q2 2002 when there were 32,000 (30,000 from the West Bank and 2,000 from Gaza). In Q1 2004 there was a slight increase to 55,000. In reaction to the loss of labour, Israel hired replacement foreign workers from the Far East.

### **Trade**

Between September 2000 and December 2002 Palestinian exports and imports contracted by around 30%, while total investment fell about 90% to \$150m. Over 3,000 buildings and infrastructure sites were estimated to be damaged or destroyed by the conflict and by Israeli military operations between October 2000 and July 2001. Palestinian economic losses during September 2000 until December 2002 were estimated at \$5.2 billion.

The Palestinians main trade partner is Israel. Trade is uneven, with imports from Israel far exceeding exports to Israel. In 1998, Israel accounted for 96% of Palestinian exports, while Jordan accounted for 2.3%, the United Arab Emirates for 0.4%, and the rest of the world for 1.3%. Palestinian areas imported 77.2% from Israel and a small percentage, 1.4%, from Germany and China. Jordan accounted for 2.4% and the rest of the world 17.6% of imports.

### **Revenue Transfers**

Under the Paris protocol agreement and up until the end of 2000, Israeli and Palestinian finance ministry representatives met on a monthly basis to agree the net amount to be transferred to the PA. However, after the *intifada* broke out Israeli authorities began to withhold the net transfers to the PA, claiming the PA was using the funds to finance attacks against Israel. Payment of these revenues only resumed again in late 2002 under considerable international pressure. The Joint Economic Committee (JEC) practically collapsed and has not convened since.

### **Investment**

One of the most damaging effects during the *intifada* period was the reduction in private sector investment, GDP and available jobs. Total investment flows fell from \$1.45 billion in 1999 to \$130 million in 2002. Today, the World Bank estimates the Palestinian GDP is 23% lower than in 1999 and the unemployment rate is at 25% compared to 10% before the *intifada*.

**Donors**

Today's Palestinian economy relies heavily on international donor funding, which provided approximately \$1.1 billion by the end of 2002 and averaged \$39 million per month for over two years up to May 2003. This funding was almost half of the total PA budget outlays during the period. The major share, \$738 million, was provided by the Arab League States, and the European Union provided \$214 million.

**Impact on Israel's Economy**

The *intifada* cost the Israeli economy an estimated \$12 billion over four years. In addition, the average risk level in the Israeli economy is now 33% higher than on the eve of the *intifada*. GDP per capita did not fall, but potential growth per capita was reduced by 11% - Israel's GDP per capita would have reached \$18,500, instead of the current \$16,700.

In 2000, Israeli exports to the Palestinian Authority were in excess of \$2.7 billion annually, and imports from the territories were in excess of \$800 million a year. This has now fallen to \$1.3 billion in exports from Israel to the PA and less than \$200 million in imports.

### **3. Overview of Disengagement**

In October 2004, Israel's Knesset ratified a Cabinet vote that set out a plan for unilateral Israeli disengagement from Gaza and parts of the northern West Bank – Prime Minister Ariel Sharon's 'Disengagement Plan'. The plan calls for Israeli military and civilian withdrawal in phases, each to be discussed and voted on by the government, and requiring a majority in Cabinet for ratification. If it is fully implemented, there will be no Israeli military or civilian presence in Gaza, and the Palestinians will have full territorial contiguity in the northern area of the West Bank. However, Israel will continue to maintain full control of the border, airspace, and coastline envelope of the Gaza Strip.

In total, 21 settlements are slated for dismantling, of which 17 are in Gaza. Responsibility for the re-housing of some 7,000 settlers has been handed to a Disengagement Administration, which will offer compensation and assistance in establishing new homes. According to estimates prepared by Israel's Ministry of Finance, the dismantling of settlements and compensation payments to 1,700 families will cost between NIS 2.5 billion and NIS 3 billion.

#### **Genesis of the Plan**

In December 2003, Ariel Sharon made a major policy speech in which he warned that Israel would take unilateral actions to dismantle settlements and redeploy troops out of areas currently under Israeli control if the Palestinians did not fulfil their commitments according to the US Roadmap plan. Following Knesset approval, he clarified that he envisaged the complete removal of Israeli civilian and military presence from Gaza, and that some isolated settlements in the West Bank would be dismantled.

The plan was conceived as a unilateral step that would protect Israeli citizens from terrorist attacks, and not as a substitute for the US Roadmap plan. The plans for withdrawal did not involve coordination with the Palestinian Authority, or a hand-over of power. With the death in November 2004 of Yasser Arafat, who was regarded by Israel as an obstacle to peace, there has been speculation that Israel may now have to reconsider the position it adopted in 2002. In the meantime, Sharon's public statements have reaffirmed his commitment to the unilateral implementation of the disengagement plan. Even if the new Palestinian government were more moderate, it may not be in their interest to be seen to work too closely with Israel.

When it was published in early 2004, the plan was enthusiastically received by the international community, with a statement from President George Bush on April 14 granting US approval. Prime Minister Blair and King Abdullah II of Jordan also gave their support to the initiative.

However, the plan met stiff opposition from within Sharon's own Likud party, which rejected it in May 2004. Some 60% of the party's Central Committee voted against the plan, forcing Sharon to issue a revised proposal, under which the implementation of each stage of withdrawal would require cabinet approval. There have also been a number of large-scale public demonstrations in Israel against the plan, with tens of thousands of opponents linking hands between Gaza and Jerusalem to protest. Yet polling data indicates that there is solid public support for disengagement, with 60% of Likud voters in favour.

Facing possible defeat in cabinet, Sharon was forced to dismiss his ministers of tourism and transportation in order to secure support for the plan. Following the vote, two further ministers resigned, leaving Sharon's government in a Knesset minority. In search of approval to widen his governing coalition by bringing in the Labor Party, Sharon once again took the matter to the Likud Central Committee. His request to start negotiations with Labor in August was defeated. He also saw his opening speech to the Knesset in October voted down, with a number of Likud "rebels" voting against him. However, at the end of October, the plan was passed by the cabinet by a vote of 13 to 6, and by the Knesset where the support of the centrist and left-wing parties secured a majority.

**Details of the Plan**

The full text of the plan adopted by the Cabinet in June 2004 and ratified by the Knesset can be found in Appendix C. The principal points are:

**Gaza**

- Israel will withdraw from the Gaza Strip, including all the existing Israeli settlements, and will redeploy in territory outside of the Strip.
- Israel will maintain a military presence in the area along the border area between the Gaza Strip and Egypt (known as the "Philadelphi Corridor"). Israel will retain the right to expand the area in which military operations are conducted. In addition, Israel will continue to control the airspace of the Gaza Strip, and will reserve the right to continue naval operations. Gaza will be demilitarised of weapons that are not in accordance with existing agreements between the sides.
- The future of the Erez Industrial Zone will be a subject for discussion, with Israel requiring suitable security arrangements and a clear recognition by the international community that the continuing operation of the industrial zone will not be viewed as a continuation of Israeli control of the area. Alternatively, the industrial zone will be handed over to the responsibility of agreed upon Palestinian or international authorities. Notwithstanding agreement on this issue, Israel will consider, together with Egypt, establishment of a joint industrial zone on the border of the Gaza Strip, Egypt and Israel.

**West Bank**

- Israel will evacuate the settlements of Ganim, Kadim, Homesh and Sa-Nur, and all permanent military installations in the Northern Samaria area, allowing for contiguous Palestinian control in this area, so long as security considerations permit. Israel will work towards reducing the number of checkpoints in the West Bank as a whole.
- Israel will continue building the West Bank security barrier.
- Israeli military activity will continue in the areas of the West Bank where Israel retains a presence. If circumstances allow, Israel will consider reducing its activity in Palestinian cities.

**Israeli Settlements**

- Israel proposes that the settlements to be evacuated will be taken over by an international body, agreed upon by Israel and the United States. Israel retains the right to ask for compensation to the value of all the economic assets that remain in areas from which it withdraws.
- Water, electricity, waste management and communications infrastructure that currently serve the settlements and the Palestinian population will remain in place.

**Other Matters**

- Other arrangements that are currently in place between Israel and the Palestinians will remain in effect, including the entrance of Palestinian workers into Israel and the flow of goods. Notwithstanding, Israel aims to reduce the number of Palestinian workers entering Israel in the long term. Existing arrangements governing international crossings between the Gaza Strip and Egypt, and the West Bank and Jordan, will remain in place.
- There will be no foreign military presence in the Gaza Strip and/or the West Bank, without Israeli agreement and coordination.
- Israel will maintain her right to self-defence, including armed pre-emptive actions and response, against threats emanating from the Gaza Strip and evacuated areas of the West Bank.

The withdrawal is planned to be completed by the end of 2005.

#### **4. The Economic Implications of Disengagement**

The Israeli plan for disengagement from Gaza and the northern West Bank provides the potential for positive development of the Palestinian economy. The implementation of the plan in Gaza - evacuation of the settlements and the redeployment of Israeli troops along the Philadelphi Corridor - would bring the Palestinians two principal benefits:

1. **Firstly, Israeli withdrawal would bring down some of the closure barriers to internal mobility that have been a feature of the last four years.** It would bring the reopening of the main north-south Erez–Rafah road and give Palestinians access to areas that are currently prohibited, such as the Al-Mawasi area between the Gush Katif settlements and the sea. However, whilst the removal of internal barriers would bring immediate relief, its economic impact would be marginal. To have a significant effect on the economy of Gaza, the transportation infrastructure would require wholesale redevelopment to improve the flow of goods and people. Such an undertaking would require both time and significant inward investment, both of which are in short supply given current security concerns.
2. **Secondly, if the settlements and military installations currently held by Israel were to be handed over to the Palestinians, some 75 additional square kilometres of well-tended agricultural land would provide an added resource for the densely-populated area.** However, the economic potential of this land will remain untapped unless there are markets for the agricultural produce, and a means of transporting goods in a timely and predictable way out of Gaza. Since 90% of exports from Gaza go either to or through Israel, this means a review of the border regime. Such a review is not part of the disengagement plan outlined by the Israeli government. In addition, the scarcity of water in Gaza places restrictions on agricultural activity. The sole water source in Gaza, the Gaza aquifer, is already over-exploited. However, if an additional source of water were to be made available, the agricultural sector could be an important building block in the post-disengagement economy in Gaza. All of this presupposes a negotiated handover of the assets connected to the settlements. Whilst the Israeli plan for disengagement provides for such a handover, it is conditioned on the appointment of an international third party to handle the assets and manage the contacts between the sides. If this is to work smoothly, both sides will need to display a greater level of cooperation than is currently the case.

According to the World Bank, disengagement alone will not deliver significant economic benefits. The Bank examined the likely impact of the disengagement plan, and compared it with the current situation. Their assessment makes a number of assumptions. Firstly, that Israel will implement its plan to gradually reduce the number of Palestinian labourers allowed to work in Israel. Secondly, that donor assistance remains stable. Thirdly, the Bank assumes that disengagement will result in free internal movement in Gaza and fourthly, that the Palestinians will produce a modest level of agricultural and industrial output from the areas handed over from the settlements. Even if these assumptions prove correct, the Palestinian economy will continue its decline. In fact, the difference between the Gaza economy under disengagement and the continuation of the status quo is negligible:

- High population growth and the reduction in work in Israel would result in a cumulative real GDP per capita decline of about 12% by 2006
- Real GDI per capita would drop by some 22%
- A forecast of 56% poverty and 34% unemployment is approximately equal to the forecast under the status quo

The World Bank analysis also warns that a disengagement process in which labour flows are cut abruptly, trade restrictions are widened, or electricity and/or water supplies are terminated would seriously worsen Palestinian economic, humanitarian and social prospects.

In order to bring long-term and sustained growth, the Palestinian economy will require an additional \$1.5 billion in foreign aid in the next two years - around \$380 per person per year. If such investment were made, it would produce a real GDP per capita growth of 26% by 2006. Unemployment would fall to a comparatively low 14%, although poverty would remain high at about 37%.

## **5. Policy Lessons**

It is important to all sides, the Palestinians, Israel and the donor countries, that the Palestinian economy prospers and supports peace and stability. There are three key areas of action in which the chances of this can be improved. The first, 'Security and Stability' is about providing the basic conditions required by any economy in order to attract investors with a safe and predictable business environment. The second area, 'Improving the Flow of Goods and Labour', is concerned with enabling Palestinians to trade normally with external markets and to move and transport goods freely within their own territories. Finally, 'Industry Growth and Job Creation', discusses ways in which the economy can be stimulated and businesses can be made more competitive.

### **1. Security and Stability**

Responsibility for security and stability lies with both Israel and the Palestinians. Ensuring this basic condition will increase the confidence of donors' and will encourage investors to establish productive businesses.

The most important and long-term means of increasing security and enhancing the chances for peace and stability would be by an announcement that the Disengagement plan is the first step towards an end-game, perhaps in the context of the US Roadmap plan with its "Permanent Two-State Solution to the Israeli-Palestinian Conflict". Accompanying this there should be a clear commitment by both sides to a ceasefire. In this way Disengagement would be made an integral part of a much wider vision for peace and reconciliation between Israel and the Palestinians.

Other important but more short-term steps include a variety of political and financial measures:

- The **peaceful transition of power** to a post-Arafat leadership that can demonstrate its commitment to renewing political negotiations with Israel. The holding of Palestinian presidential elections is an important step.
- **Implementation of promised reforms** in the Palestinian security services.
- Evidence of real effort to **stop the smuggling of weapons** into Gaza and the ending of Qassam rocket fire at Israeli towns.
- The **re-establishment of the Palestinian-Israeli Joint Economic Committee** created by the Paris Protocol would allow coordination of policies regarding imports, financial and monetary issues, taxation rules, labour and agriculture standards, insurance coverage and more. This might be achieved with the involvement of a third party sponsor.

### **2. Improving the Flow of Goods and Labour**

The current border regime places restrictions on the flow of labour and goods across borders. It adds considerably to transaction costs – an estimated extra \$150 for each 20 foot container – and makes it difficult to meet orders on time.

World Bank projections indicate that facilitating Palestinian external trade would raise real GDP growth to 9.2% by 2006 (compared with a negative 2006 growth rate under a status quo scenario). Exports would grow at 30% per annum by 2006 (significantly higher than the 3.4% under the status quo scenario); exports would spur job creation and reduce unemployment to 23% by 2006, compared with 34% if the current status quo continues. As a result, the poverty level would fall from 56% under the status quo scenario to 46% by 2006.

Improving the flow of goods and labour would be facilitated by the following steps:

- **Serious revision and upgrade of the current system of internal checkpoints.** Israel agrees to this but requires international assistance and finance.
- Utilising **new technologies** should help ease the border regime without compromising Israeli security, thereby removing the delays and unpredictability from transferring goods across borders that adversely affect competitiveness. Such technologies include container-sized scanners, appropriately scaled inspection gear and mobile positioning systems to track transport of goods. This should eliminate the need for fully unloading and reloading containers. For imports, improved inspection regimes at point of origin and bonded warehouses may reduce the need for Israeli inspection on arrival at Israeli ports. Israel is ready to install such technologies with international support.
- **Allowing a Gaza port**, at least initially as a ‘Roll-on, Roll-off’ (‘Ro-Ro’) shuttle service to Port Said or other nearby destination. Ro-Ro is simply an approach channel, a pier, an access road, warehouses, and transportation and security equipment. This would not preclude eventual expansion into a full-service port.
- **Removal of non-essential checkpoints and roadblocks** across the West Bank. An immediate easing of internal closures could lead to real GDP growth of 3.6% by 2005. Israel agrees in principle although the question is connected to a reduction in the threat of terror attacks and the completion of the security barrier.
- **More investment in checkpoint facilities** such as provision of additional forklift trucks to improve the efficiency of security checks.
- **Provision of a transport link between Gaza and the West Bank.** The current disconnect between the two seriously impedes economic development, growth and income. Initial proposals are being studied by Israel and the World Bank for cost, feasibility and security.
- **Continuing to allow Palestinian labour to find employment in Israel.** The Disengagement Plan foresees a halt in Palestinian labourers to Israel within approximately 2 years. The World Bank and Palestinian sources view this as a shock that the Palestinian economy will have great difficulty in bearing. The result is forecast to be increased unemployment and poverty, and reduced stability and standards of living.
- The best way for Palestinian goods to access third countries appears to lie in **partnerships with Israeli companies.** Israeli companies should secure market access for products wholly or partly produced by Palestinian enterprises. Examples of actual or potential cooperation include perishable agricultural products (flowers, strawberries) exported through Israeli outlets, and Israeli outsourcing to Palestinians of manufacturing processes and services. The example of Agrexco’s Coral brand for exporting Palestinian agricultural produce should be explored as a model for this kind of cooperation.
- **Standards:** When Palestinian goods to be traded require approval of the Israel Standards Institute and a technical inspection, the goods must stay at the port, costing further storage and demurrage charges. Israeli importers can have such tests conducted in their own warehouses.
- **Cargo:** Israel’s airport authorities do not allow Palestinian cargo to be dispatched on passenger aircraft. Hence, all Palestinian air freight shipments are dispatched by cargo aircraft and Palestinian exporters often have to pay additional air freight – e.g. to export to nearby Greece, Palestinian exporters must ship via France or Germany.

### 3. Industry Growth and Job Creation

Finally, at the micro-economic level there are a series of measures by which Israel, the Palestinians and the international community can promote industry growth and job creation.

- **Large infrastructure projects** such as developing a port, an airport, the road network and the sewage system would serve a triple purpose of rebuilding war-damaged property, creating jobs and kick-starting the local economy. This will boost the construction industry, a critical sector in the Palestinian economy. Construction of housing and public facilities will have a multiplier effect, stimulating other industries and encouraging the emergence of a private sector. With international support, the PA must begin to plan for this boom, zoning land for urban and agricultural

development and planning infrastructure projects. In order to encourage small businesses to take part in the rebuilding of Gaza, work should be done in the financial sector to provide financing options.

- Despite the policy of the current Israeli government to close the Erez Industrial Zone and halt the construction of other such areas, **cross-border industrial parks** allow both sides to utilise comparative and competitive economic advantages in complementary ways. When the atmosphere is more conducive to business cooperation such initiatives may be re-launched.
- **More micro-financing programmes** would assist Palestinian SMEs in getting off the ground and would help fight poverty.
- **Continuing to improve the transparency of the PA's financial affairs.** This is of fundamental significance for foreign investors. More can be done in the field of independent audits, and in more rigorously implementing public procurement regulations.
- **A more liberal credit regime.** Commercial bank lending is constrained by collateral requirements that rely excessively on land titles – scarce commodities in the Gaza Strip where only around a half of the land is registered. Allowing a wider range of assets to be used as collateral, expanding leasing and adopting more creative methods for assessing credit risk would all help expand credit opportunities
- **Agriculture** is a significant sector of the Palestinian economy, with much of the produce exported to Israel, or via Israel to Europe. The PA could capitalize on this potential by preparing a master plan for the agricultural sector in Gaza. Technology and know-how transfers from Israel and the international community could also improve the quality and value of Palestinian produce.
- **Fisheries:** The seas off Gaza are the primary source of sea-fish for the Palestinian and Israeli markets. With careful regulation, this could also become a source of produce for high-value European markets.
- The Gaza **tourism industry** would receive an enormous boost if Israel allows West Bank Palestinians or even Israeli Arabs to visit for tourist purposes. Israeli Arabs have a GDP of around \$10b, twice that of the GDP of all Palestinians in the West Bank and Gaza, and thus have significant spending power.

## Appendix A

### Political and Economic Chronology 1993 - 2004

- **September 13 1993:** The Palestinian National Authority (PNA) was established by the **Declaration of Principles** signed between the Palestine Liberation Organization (PLO) and Israel. The PNA governs Palestinian affairs in self-rule areas. It consists of the President, the appointed cabinet (Ministerial Board currently composed of 25 PNA Ministers) and the Palestinian Legislative Council (88 members).
- **April 29, 1994: The Paris Protocol**, a new economic relationship between the Palestinian National Authority and Israel was drawn up in the Protocol on Economic Relations, signed in Paris. The Paris protocol established the contractual agreement to govern the economic relations between Israel and the Palestinian Authority. The protocol laid the groundwork for Palestinians to control their economy and to improve economic relations with Israel.
- **December 1, 1994:** The **Palestinian Monetary Authority (PMA)** was created to secure the stability of the banking and monetary system and encourage economic growth in Palestine in accordance with general policy of the PNA.
- **September 28, 1995: The Israeli-Palestinian Interim Agreement** on the West Bank and the Gaza Strip was signed in Washington D.C.
- **October 31, 1995: The Beilin-Abu Mazen Document**, a Framework for the conclusion of a final status agreement between Israel and the Palestine Liberation Organization, was negotiated in secret in Oslo by a team of Palestinian and Israeli negotiators, under the supervision of Yossi Beilin for Israel, and Abu Mazen (Mahmoud Abbas) for the Palestinian side. Many of the ideas contained in this agreement were carried forward to other negotiations, and are reflected in draft agreements regarding refugee status and Jerusalem, as well as status of the settlements and the principle of territorial exchange.
- **November 4, 1995:** Israel Prime Minister Yitzhak Rabin was murdered by Israeli right-wing extremist, Yigal Amir.
- **January 1996:** Palestinians voted in their first presidential and legislative elections. Yasser Arafat secured 87% of the vote and his Fatah faction won 52 seats in the 88-member Legislative Council.
- **October 23, 1998: The Wye River Memorandum** aimed to facilitate implementation of the Interim Agreement on the West Bank and Gaza Strip of September 28, 1995 (the "Interim Agreement").
- **September 4, 1999: The Sharm el-Sheikh Memorandum** on an Implementation Timeline of Outstanding Commitments of Agreements Signed and the Resumption of Permanent Status Negotiations was signed by the government of the State of Israel and the Palestinian Liberation Organisation to commit themselves to full and mutual implementation of the Interim Agreement and all other agreements concluded between them since September 1993. The memorandum also called for the international donor community to enhance its commitment and financial support to the Palestinian economic development and the Israeli-Palestinian peace process.
- **July 25, 2000: Middle East Peace Summit at Camp David** was attended by US President Bill Clinton, Israeli Prime Minister Ehud Barak and Palestinian Authority Chairman Yasser Arafat in an effort to reach an agreement on permanent status.
- **September, 29, 2000:** The Palestinian **Al Aksa Intifada** (Uprising) broke out.

- **December, 23 2000:** US President Bill Clinton met privately with Israeli and Palestinian delegations in a last effort for a final status agreement. He presented **The Clinton Peace Plan**, his views for a final status agreement, but the meetings were ultimately unsuccessful.
- **January 27, 2001:** Israeli and Palestinian delegation had talks aimed at reaching a permanent and stable agreement between the two parties. The parties issued the **Israeli-Palestinian Joint Statement Taba**, committing themselves to the Sharm el-Sheikh implementation timeline taking into account the Clinton Peace Plan.
- **May 20, 2001:** **The Mitchell Report** was created by an American led inquiry into the ongoing violence between Israelis and Palestinians since September 2000. The immediate objective of the report was to build confidence and resume negotiations.
- **June 14, 2001:** **The Tenet cease-fire plan** (A Palestinian-Israeli Security Implementation Work Plan) was established for the two sides to commit to a mutual, comprehensive cease-fire, applying to all violent activities, in accordance with the public declaration of both leaders and to reaffirm their commitment to the Mitchell Report and Sharm el-Sheikh agreement.
- **March 28, 2002:** Prince Abdullah bin Abdul Aziz, crown prince of the Kingdom of Saudi Arabia, at the Arab State Summit in Beirut, presented the **Saudi Peace Initiative**. His initiative called for full Israeli withdrawal from all the Arab territories occupied since June 1967, in implementation of Security Council Resolutions 242 and 338, reaffirmed by the Madrid Conference of 1991 and the land-for-peace principle, and Israel's acceptance of an independent Palestinian state with East Jerusalem as its capital, in return for the establishment of normal relations in the context of a comprehensive peace with Israel.
- **July, 22 2002:** **The Nusseibeh-Ayalon Agreement** was created by Sari Nusseibeh, president of Al Quds University and Ami Ayalon, the former Director of Israel's domestic security service (Shin Bet). It is a set of principles for an Israeli-Palestinian peace deal. Often referred to as the "People's Voice", the petition supporting it has been signed by tens of thousands of Palestinian and Israelis.
- **August 2002:** The Knesset gave final approval to Stage A of a plan to build a security fence around the area of the West Bank. The completion date was set for July 2003.
- **April 30, 2003:** **A Performance-Based Roadmap** to a Permanent Two-State Solution to the Israeli-Palestinian Conflict was published. The U.S. State Department released the text of the "roadmap" to a permanent solution to the Israeli-Palestinian conflict. The roadmap specifies the steps for the two parties to take to reach a settlement, and a timeline for doing so, under the auspices of the Quartet - the United States, the European Union, the United Nations, and Russia.
- **July 21, 2003:** **The Economic Road Map** was created by an the IPCRI (Israeli/Palestinian Centre for Research and KAS economic working group composed of Israelis and Palestinians from the business and academic communities and officials acting in their personal capacities. The Economic Road Map document seeks to enhance the Road Map Process by integrating within it economic measures that will improve the lives of citizens and help to get the Palestinian economy moving once again.
- **October 12, 2003:** **The Geneva Accord (Beilin-Abd Rabbo)** was signed as a 'virtual' agreement that would be a final status for peace which both sides agree to. Israeli opposition leaders, led by Yossi Beilin and Palestinians led by Yasser Abd-Rabbo, took three years to negotiate the Geneva Accords which aims to offer hope both to Israelis and Palestinians that peace is possible as an alternative to the current violent impasse and diplomatic vacuum. The Accord demonstrates that there are answers to such issues like borders, settlements, security, refugee problems, and Jerusalem.

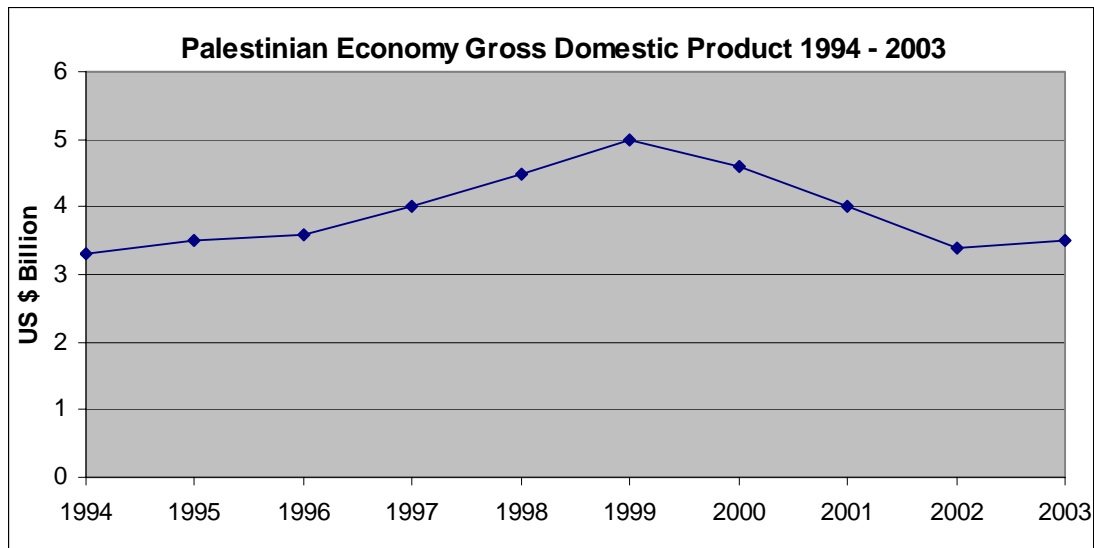
- **December 18, 2003:** In a speech to the Harelip Conference, PM Sharon unveiled his ‘**Disengagement Plan**’ stating that Israel would take unilateral actions to disengage if Palestinians were not capable of fulfilling their commitments under the Roadmap.
- **February-April 2004:** Sharon’s disengagement plan received wide approval from foreign leaders, including the UK Foreign Secretary Jack Straw (March 3), Prime Minister Tony Blair (April 7), the US State Department (March 2), Jordanian King Abdullah II (March 10), and President Bush (April 14).
- **June 6, 2004:** The Israeli Cabinet approved the disengagement plan by 14 votes to 7. The revised plan however, called for a further vote to be taken by March 2005, in which the government will decide on implementing the decision. The plan also noted the government’s intention to retain control of major settlement blocs in the West Bank.
- **June 8, 2004:** Israeli Minister of Industry and Trade Ehud Olmert announced that Israeli factories would be evacuated from the Erez Industrial Zone, a cross-border industrial park, leaving its future in doubt. Erez had been closed most of the time since the beginning of January 2004, following attacks by Palestinian militants.
- **July 25, 2004:** 100,000 Israelis took part in a ‘human chain’ demonstration stretching from Gaza to Jerusalem in an attempt to mobilise public support against the implementation of the disengagement plan and the evacuation of Jewish settlements.
- **October 26, 2004:** The Disengagement plan was passed by the Knesset.
- **November 11 2004:** Yasser Arafat died.

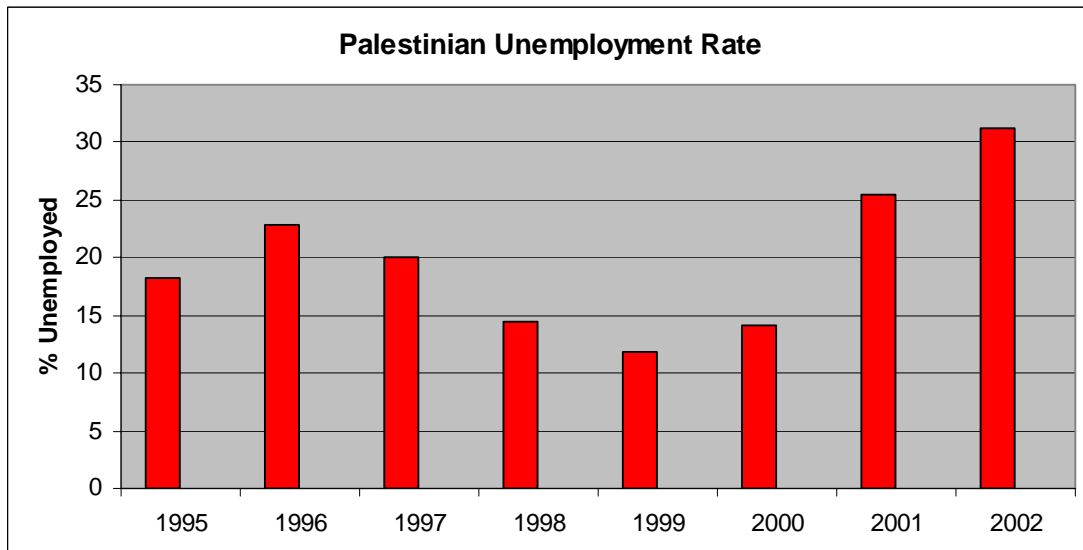
**Appendix B****Palestinian Economic Performance 1994-2003**

	94	95	96	97	98	99	00	01	02	03
<b>GDP</b>	3.3	3.5	3.6	4.0	4.5	5	4.6	4.0	3.4	3.5
<b>GDP Per Capita</b>	1.4	1.4	1.4	1.4	1.5	1.6	1.5			
<b>Growth Rates (%)</b>		6	2	12	12	9	-5	-14.2	-18.8	3.1
<b>Exports of goods and services</b>	0.7	0.7	0.7	0.8	0.9	1	0.9			
<b>Imports of goods and services</b>	2.6	2.6	2.8	3.0	3.4	4.1	3.5			
<b>Gross Disposable Income</b>	4.3	4.5	4.6	5.1	5.8	6.3	6.0			
<b>Inflation (%)</b>						5.6	10	7	17.2	7
<b>Unemployment (%)</b>		18.2	22.8	20.0	14.5	11.9	14.1	25.5	31.3	
<b>Output</b>	5.5	5.9	6	6.8	7.7	8.3	7.9			
<b>Private Final Consumption Expenditure</b>	3.6	3.6	3.7	4.0	4.4	4.8	4.6			
<b>Public Final Consumption Expenditure</b>	0.6	0.7	0.8	0.9	1	1.1	1.2			
<b>Gross Capital Formation</b>	1.1	1.1	1.2	1.4	1.6	2.2	1.5			

\*Statistics rounded to one decimal place and in US\$ Billion unless stated otherwise

Sources: World Bank, Palestinian Central Bureau of Statistics





**Appendix C****The June 2004 Revised Disengagement Plan****1. Background – Political and Security Implications**

The State of Israel is committed to the peace process and aspires to reach an agreed resolution of the conflict based upon the vision of US President George Bush.

The State of Israel believes that it must act to improve the current situation. The State of Israel has come to the conclusion that there is currently no reliable Palestinian partner with which it can make progress in a two-sided peace process. Accordingly, it has developed a plan of revised disengagement (hereinafter – the plan), based on the following considerations:

One. The stalemate dictated by the current situation is harmful. In order to break out of this stalemate, the State of Israel is required to initiate moves not dependent on Palestinian cooperation.

Two. The purpose of the plan is to lead to a better security, political, economic and demographic situation.

Three. In any future permanent status arrangement, there will be no Israeli towns and villages in the Gaza Strip. On the other hand, it is clear that in the West Bank, there are areas which will be part of the State of Israel, including major Israeli population centers, cities, towns and villages, security areas and other places of special interest to Israel.

Four. The State of Israel supports the efforts of the United States, operating alongside the international community, to promote the reform process, the construction of institutions and the improvement of the economy and welfare of the Palestinian residents, in order that a new Palestinian leadership will emerge and prove itself capable of fulfilling its commitments under the Roadmap.

Five. Relocation from the Gaza Strip and from an area in Northern Samaria should reduce friction with the Palestinian population.

Six. The completion of the plan will serve to dispel the claims regarding Israel's responsibility for the Palestinians in the Gaza Strip.

Seven. The process set forth in the plan is without prejudice to the relevant agreements between the State of Israel and the Palestinians. Relevant arrangements shall continue to apply.

Eight. International support for this plan is widespread and important. This support is essential in order to bring the Palestinians to implement in practice their obligations to combat terrorism and effect reforms as required by the Roadmap, thus enabling the parties to return to the path of negotiation.

## 2. Main Elements

### A. The process:

The required preparatory work for the implementation of the plan will be carried out (including staff work to determine criteria, definitions, evaluations, and preparations for required legislation).

Immediately upon completion of the preparatory work, a discussion will be held by the Government in order to make a decision concerning the relocation of settlements, taking into consideration the circumstances prevailing at that time – whether or not to relocate, and which settlements.

The towns and villages will be classified into four groups, as follows:

- 1) Group A – Morag, Netzarim, Kfar Darom
- 2) Group B – the villages of Northern Samaria (Ganim, Kadim, Sa-Nur and Homesh).
- 3) Group C – the towns and villages of Gush Katif
- 4) Group D – the villages of the Northern Gaza Strip (Elei Sinai, Dugit and Nissanit)

It is clarified that, following the completion of the aforementioned preparations, the Government will convene periodically in order to decide separately on the question of whether or not to relocate, with respect to each of the aforementioned groups.

3. The continuation of the aforementioned process is subject to the resolutions that the Government will pass, as mentioned above in Article 2, and will be implemented in accordance with the content of those resolutions.

#### 3.1 The Gaza Strip

- 1) The State of Israel will evacuate the Gaza Strip, including all existing Israeli towns and villages, and will redeploy outside the Strip. This will not include military deployment in the area of the border between the Gaza Strip and Egypt ("the Philadelphi Route") as detailed below.
- 2) Upon completion of this process, there shall no longer be any permanent presence of Israeli security forces in the areas of Gaza Strip territory which have been evacuated.

#### 3.2 The West Bank

- 3) The State of Israel will evacuate an area in Northern Samaria (Ganim, Kadim, Sa-Nur and Homesh), and all military installations in this area, and will redeploy outside the vacated area.
- 4) Upon completion of this process, there shall no longer be any permanent presence of Israeli security forces in this area.
- 5) The move will enable territorial contiguity for Palestinians in the Northern Samaria area.
- 6) The State of Israel will assist, together with the international community, in improving the transportation infrastructure in the West Bank in order to facilitate the contiguity of Palestinian transportation.

- 7) The process will facilitate normal life and Palestinian economic and commercial activity in the West Bank.

3.3 The intention is to complete the planned relocation process by the end of 2005.

B. The Security Fence:

The State of Israel will continue building the Security Fence, in accordance with the relevant decisions of the Government. The route will take into account humanitarian considerations.

**3. Security Situation Following the Relocation**

One. The Gaza Strip:

- 1) The State of Israel will guard and monitor the external land perimeter of the Gaza Strip, will continue to maintain exclusive authority in Gaza air space, and will continue to exercise security activity in the sea off the coast of the Gaza Strip.
- 2) The Gaza Strip shall be demilitarized and shall be devoid of weaponry, the presence of which does not accord with the Israeli-Palestinian agreements.
- 3) The State of Israel reserves its fundamental right of self-defense, both preventive and reactive, including where necessary the use of force, in respect of threats emanating from the Gaza Strip.

Two. The West Bank:

- 1) Upon completion of the evacuation of the Northern Samaria area, no permanent Israeli military presence will remain in this area.
- 2) The State of Israel reserves its fundamental right of self-defense, both preventive and reactive, including where necessary the use of force, in respect of threats emanating from the Northern Samaria area.
- 3) In other areas of the West Bank, current security activity will continue. However, as circumstances require, the State of Israel will consider reducing such activity in Palestinian cities.
- 4) The State of Israel will work to reduce the number of internal checkpoints throughout the West Bank.

**4. Military Installations and Infrastructure in the Gaza Strip and Northern Samaria**

In general, these will be dismantled and evacuated, with the exception of those which the State of Israel decides to transfer to another party.

**5. Security Assistance to the Palestinians**

The State of Israel agrees that by coordination with it, advice, assistance and training will be provided to the Palestinian security forces for the implementation of their obligations to combat terrorism and maintain public order, by American, British, Egyptian, Jordanian or other experts, as agreed therewith.

No foreign security presence may enter the Gaza Strip and/or the West Bank without being coordinated with and approved by the State of Israel.

**6. The Border Area Between the Gaza Strip and Egypt (Philadelphi Route)**

The State of Israel will continue to maintain a military presence along the border between the Gaza Strip and Egypt (Philadelphi Route). This presence is an essential security requirement. At certain locations, security considerations may require some widening of the area in which the military activity is conducted.

Subsequently, the evacuation of this area will be considered. Evacuation of the area will be dependent, inter alia, on the security situation and the extent of cooperation with Egypt in establishing a reliable alternative arrangement.

If and when conditions permit the evacuation of this area, the State of Israel will be willing to consider the possibility of the establishment of a seaport and airport in the Gaza Strip, in accordance with arrangements to be agreed with Israel.

**7. Real Estate Assets**

In general, residential dwellings and sensitive structures, including synagogues, will not remain. The State of Israel will aspire to transfer other facilities, including industrial, commercial and agricultural ones, to a third, international party which will put them to use for the benefit of the Palestinian population that is not involved in terror.

The area of the Erez industrial zone will be transferred to the responsibility of an agreed upon Palestinian or international party.

The State of Israel will explore, together with Egypt, the possibility of establishing a joint industrial zone on the border of the Gaza Strip, Egypt and Israel.

**8. Civil Infrastructure and Arrangements**

Infrastructure relating to water, electricity, sewage and telecommunications will remain in place.

In general, Israel will continue, for full price, to supply electricity, water, gas and petrol to the Palestinians, in accordance with current arrangements.

Other existing arrangements, such as those relating to water and the electro-magnetic sphere shall remain in force.

**9. Activity of Civilian International Organizations**

The State of Israel recognizes the great importance of the continued activity of international humanitarian organizations and others engaged in civil development, assisting the Palestinian population.

The State of Israel will coordinate with these organizations arrangements to facilitate their activities.

The State of Israel proposes that an international apparatus be established (along the lines of the AHLIC), with the agreement of Israel and international elements which will work to develop the Palestinian economy.

**10. Economic Arrangements**

In general, the economic arrangements currently in operation between the State of Israel and the Palestinians shall remain in force. These arrangements include, inter alia:

- One. The entry and exit of goods between the Gaza Strip, the West Bank, the State of Israel and abroad.
- Two. The monetary regime.
- Three. Tax and customs envelope arrangements.
- Four. Postal and telecommunications arrangements.
- Five. The entry of workers into Israel, in accordance with the existing criteria.

In the longer term, and in line with Israel's interest in encouraging greater Palestinian economic independence, the State of Israel expects to reduce the number of Palestinian workers entering Israel, to the point that it ceases completely. The State of Israel supports the development of sources of employment in the Gaza Strip and in Palestinian areas of the West Bank, by international elements.

### **11. International Passages**

#### **a. The International Passage Between the Gaza Strip and Egypt**

- 1) The existing arrangements shall continue.
- 2) The State of Israel is interested in moving the passage to the "three borders" area, south of its current location. This would need to be effected in coordination with the Government of Egypt. This move would enable the hours of operation of the passage to be extended.

#### **b. The International Passages Between the West Bank and Jordan:**

The existing arrangements shall continue.

### **12. Erez Crossing Point**

The Erez crossing point will be moved to a location within Israel in a time frame to be determined separately by the Government.

### **13. Conclusion**

The goal is that implementation of the plan will lead to improving the situation and breaking the current deadlock. If and when there is evidence from the Palestinian side of its willingness, capability and implementation in practice of the fight against terrorism, full cessation of terrorism and violence and the institution of reform as required by the Road Map, it will be possible to return to the track of negotiation and dialogue.



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