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Palestine-Jordan-Israel: Economic Relations and Treaties - Realities, Constraints, and Prospects

Speaker: Professor Shimon Shetreet, former minister of economics (Israeli Labor Party)

Participants: Hanna Siniora, Dr. Nabil Al-Ja'bari, Professor Said Zeedani, Walid Alami, Sheikh Jamil Hamami, Mohammed Mustapha Tamimi, Antony T. Sullivan, Dr. Mohammed S. Dajani, Dr. Joel Peters, Layth Dajani, Clare Woodcraf, Safa' Abu Assab, Shlomo Shetreet, HE Manuel Cacho, David Viveash, Samir Huleileh, Peter Demant, Fernando F. Arias, HE Ethem Tokdemir, Hanna Daoudi, Dr. Munther Dajani, Muriel Aseburg, Deniz Aytali and Dr. Mahdi Abdul Hadi.



SUMMARY

Introduction by Dr. Mahdi Abdul Hadi

Let me welcome you, Professor Shetreet and all the guests to this roundtable in a Palestinian house. I am happy to host this meeting, and I hope that we can learn from your personal views on Palestinian-Jordanian-Israeli economic relations, on the various agreements and treaties signed in this field and the present standing of these documents. This roundtable meeting is aimed at promoting an exchange of ideas and increased understanding of the current situation.

At this point I would like to put on record that we, the Palestinians, are committed to what was agreed upon and signed in Washington on 13 September 1993. But since the Israeli elections last year, we have lost the Israeli partner; Mr. Netanyahu is not committed to 'what was agreed upon' or to the idea of separation. We would like to see, now, if the Labor party is still a partner in the peace process and if it is ready to work towards the implementation of 'what was agreed upon', in spite of the fact that it forms the opposition. The Americans are very aware of Mr. Netanyahu's policies, but are not, at the moment, putting pressure on him. The constraints on all of us, at this time, are severe; it is, however, time to build bridges between the parties in the region. I hope that we will be able to use this meeting to focus on what can be done.

Let me remind you that Chatham House rules apply to this meeting; we are here to speak in harmony and with understanding, not to score points or be quoted by the media.

Professor Shimon Shetreet

Let me start by saying that it is a pleasure for me to be here. I would have loved to see this meeting take place in better times, in an 'envelope' of peace and harmony, but unfortunately, the situation is not favorable. Nevertheless, I am an optimistic person, and I

hope that we will move on to better times and a more peaceful environment.

As an Israeli, I have to accept the democratic 'poll' that took place in 1996. The same people that supported us [the Labor Party] in the peace process, then voted for Netanyahu. Today, I want to talk about economic relations, but as you have already mentioned, Dr. Mahdi, they are only one aspect of the overall relations between Israel, Jordan and the Palestinians.

The economic relations between Israel and the Palestinians are now depending on the revision of the lists A1 and A2, which are part of the agreement signed in September 1995 between Israel and the PLO [Oslo II]; this agreement was the base on which the PA was established. These lists render it possible for the PA to import basic goods (food items and others) into the Palestinian areas, but they need to be revised in order to expand the number of items. The signing of the revision was supposed to take place in 1996; it was postponed following an Israeli bus suicide bombing and the document remains unsigned until now. With the revision of lists A1 and A2 it would be easier for the Palestinians to import food, consumer goods, cement, and other things that they are imported directly via the Allenby Bridge.

I think that, sometimes, pragmatic decisions must be taken. In the case of these lists, we are stuck without being able to move, and this affects the well-being of the people here. The items that are mentioned in these lists, such as rice, vegetables, corn, cement, iron for construction, oils, dish-washers, etc., are all items to be imported without customs. On this basis, bilateral Palestinian-Jordanian trade could be developed.

The 1996 level of trade between Israel and Jordan involved exports amounting to US\$8 million, and imports amounting to US\$2 million. The figures in 1997 were US\$6.57 million export and US\$6.12 million import. But there is a new phenomenon, which might be seen as reflecting negatively on the Israeli labor market: more and more Israeli textile companies, attracted by the low labor costs, are establishing factories in Jordan. Other textile companies, meanwhile, have displayed a similar tendency and moved to Egypt.

The trade between Israel and the PA in 1996 amounted to NIS 5.5 billion in exports and NIS 0.8 billion in imports.

There is a major conceptual difference between the Israeli-Jordanian trade agreements and the Israeli-Palestinian ones. The treaty with Jordan is based on the fact that Jordan is a separate entity; the relations are established according to the principle of most-favored nations with the goal of arriving at a free-trade agreement in the future. The relations are based on several agreements in different fields such as trade, water, transport, etc. The concept of the relations between Israel and the PA is a different one; it is a customs union, which implies that, throughout the whole territory of the union, exactly the same customs apply, including those on imports. There are only minor exceptions; the PA, for example, is exempt from paying taxes on its cars, and there is a slight difference in VAT of up to 2%. As you can see, this is a totally different concept in comparison to the Israeli-Jordanian relations.

The most important agreement with Jordan is the transport agreement. This consists of 'door-to-door' and 'back-to-back' arrangements, meaning that public transport and certain shipments are allowed to travel directly from Amman to Tel Aviv or Haifa (door-to-door), and other goods are transferred by reloading them at the border (back-to-back). In the future, the situation with the Jordanians will become similar - but not the same - as the one with the PA.

With the PA, customs taxes are applied according to the principle of residency, i.e., customs revenues from goods imported to the Palestinian Territories are transferred to the PA after the deduction of administrative costs. The amount of money that is transferred from Israel to the PA comes from various sources (import taxes, direct taxation of Palestinian workers [income tax], VAT, health insurance, petroleum taxes, etc.) and makes up a substantial part - some 60% - of the current PA budget.

An important feature of the customs union is the freedom of movement of goods and employees; this freedom, however, due to security considerations is often restricted by closure, which occurs far too frequently. In the 'high times', we had about 120,000 Palestinian employees officially working in Israel; today, the number is only around 30,000. Israel's decision to substantially decrease this number was, in my opinion, a grave mistake. The concept of separation is not compatible with a customs union. Separation is not right, but it is conveniently used to respond to situations such as bus explosions in the streets. Labor, at that time, thought about how to separate the people and decreased the number of Palestinian workers in Israel. But, as I said, the notion of a customs union is inconsistent with the concept of separation; on the contrary, it is embedded in a concept of integration. Israel replaced 90,000 Palestinian workers with 200-300,000 workers from abroad. Thus, we may have solved the problems of Thailand or Bulgaria, but we have aggravated our own situation. The idea of the closure is to make it more difficult for terror attacks to occur, but I do not think that this will be the result.

It is interesting to note that the doves in the Labor party supported the concept of separation, while the center and the hawks - and I consider myself as belonging to the center - supported integration. The Palestinians, from the point of view of sovereignty, of course, preferred separation, but they understood the economic necessity of integration. This is why, in the end, we agreed upon a customs union. The mistake of the Labor party was to bring in foreign workers and to replace the Palestinians.

Upon comparing the two treaties yet again, between Israel and the Palestinians we have a customs union with freedom of movement for goods and 'normal' movement of workers in normal times. From 1998 onwards, agricultural goods from the Palestinian Territories will be allowed to move freely into Israel. This is not the case with Jordan. The relations with Jordan are built on the principle of most favored nations and include various agreements and joint projects in the fields of water, tourism, trade, and transport, as well as the projects in the JRV [Jordan Rift Valley].

The customs union between Israel and the Palestinians can be seen as the beginning of a subregional trade structure, and can become the basis of a regional trade zone, which Egypt, and hopefully, Lebanon and Syria will eventually join. It is a step in the right direction for the development of regional trade. Generally speaking, the scope of trade that Israel has with the region is very limited; it is only about US\$70 million, not counting the oil transactions which amount to US\$420 million. Thus, it is only a small fraction of Israel's overall trade, and we are not talking about something significant from an economic point of view, but it might well become significant in the future. The customs union can develop into a regional customs union. It is a system that gives rise to cooperation; e.g., as I have already mentioned, all barriers in the agricultural field will be lifted in 1998, although there will remain certain standards to be fulfilled, such as in the area of hygiene. There is the possibility for a future new economic structures such as Middle East common market, a phrase which I prefer to a 'New Middle East', and the openings and avenues have already been laid down by Labor.

Another difference in the agreements is that Jordanians and Israelis did not face the same political problems in coming to an economic agreement. The Jordanian-Israeli agreement

was signed despite the incident at the Israeli-Jordanian border, in which seven [Israeli] girls were killed. I think that a combination of the two concepts would be most promising, but this can only happen when there is a positive political and economic climate to make things move in the right direction. At the moment, the economic situation is not too favorable; US and international investments are at a low in the Palestinian areas, despite the fact that the Palestinian economy shows great potential. Thus, there is hope for future positive developments.

Discussion

Dr. Mahdi Abdul Hadi: To what extent do the two treaties affect the Palestinians? Does their existence mean that, in this transitional phase, we are totally dependent on the Israelis, inasmuch as our economy is totally under Israeli control and domination? Is it true to say that Israel is winning in war and winning in peace?

Professor Shimon Shetreet: You tackled two major points in your question. The first one relates to the issue of sensitivity. Israel has a large and strong economy; we have reached a GNP per capita of about US\$17,000, which puts us close to the UK. This might lead to other countries in the region experiencing the feeling that they are in an unequal trade situation, or that they are being dominated. This is what you referred to with 'winning in war, winning in peace.' Israel may be regarded as a dominating power, and Israeli officials must be aware of that. I think it therefore better to conduct triangular projects involving the French, Spanish or Germans to alleviate Palestinian sensitivities. Israel has to be sensitive. On the other hand, I see the strength of the Israeli economy as an asset, a source of strength that can act as a locomotive for the entire region. If there is economic growth, all the parties - not only Israel - will profit. I think you should look at the positive aspects, but provided that Israel is not too insensitive.

Dr. Abdul Hadi: But there are so many constraints on the Palestinians; we feel that we cannot move in any direction without Israeli approval.

Professor Shetreet: It might be correct that from a national pride point of view, a total separation would have been better. But from a pragmatic viewpoint, this solution is much better. You are just starting to build up a new system; it is only natural that the efficiency during such a phase is low. Do not forget that, in 1996 alone, the sum of US\$520 million was transferred to the PA; your own collection system would have never been that effective. And this is in a phase where the money is badly needed for building up the country. The second issue related to this is that through what you call 'constraints', a culture of cooperation is created. I think, in the medium range, this is the best solution.

Professor Said Zeedani: I have three questions or comments. First, I think that political separation and economic integration are not necessarily contradictory. Look, for example, at the EU. The second question relates to your stand in Labor as you described it. You said that you are a centrist. What does this mean regarding your stand on the final status negotiations? The third issue I want to mention is the benefits of peace for Israel: tourism, investments, etc. I think there should be more emphasis on the fact that we, the Arabs, can create an environment conducive to peace but that Israel must pay the political price for it.

Professor Shetreet: You misunderstood me. I was talking about a contradiction on the economic level, about integration and separation in economics, about the customs union and the replacement of Palestinian workers. There is no discussion about political separation; this issue was agreed upon long ago. Now, there are 300,000 foreign workers in Israel, and we cannot easily expel them. The decision to replace the Palestinian workers is irreversible. I do not believe that these Palestinians now have good jobs that allow them to feed their families, and they are no longer contributing to a form of cooperation between

Israel and the Palestinians. It is a lost opportunity.

Professor Zeedani: How can there even be economic separation when there is no political separation, no political Palestinian sovereignty? The Palestinians are economically dependent on Israel.

Professor Shetreet: As I said before, if the Palestinian leadership had adopted another concept of economic cooperation, it might have been better from a psychological standpoint, but it would have posed many problems with regard to how to act effectively in the formative years, e.g., in the field of collecting taxes. With the current agreement, the ground has been laid for a subregional and a regional structure. Once peace is reached, such a structure can hold peace together. But I do not say that another option, that of separation, could not have been a solution.

Samir Huleileh: We now have three years' experience of the economic agreements between the PA and Israel. All the problems we witness are, at their core, not economic problems, but problems of control and domination. It has always been a question of who can force the other into an agreement, in the same way as Israel now uses all its power to force the PA to proceed directly to a final status agreement.

But there is another thing: in the economic agreement negotiations, all the options were discussed, including the idea of a free trade agreement. You did not mention that at all. The Palestinian economy is not yet mature enough for a customs union or relations based on the status of most favored nations. We were forced into this agreement for the interim period, as the Israelis were able to impose the conditions: they said, if you want separation, then you will get total separation, meaning you must take all your workers back and there will be no export or import at all between us.

The real reasons behind this, of course, are political: if you have a free trade agreement or the most favored nations status, you need borders. Israel did not want this, so it rejected the idea of a free trade agreement. But the idea was also rejected by the Palestinians as they feared that Palestinian Jerusalemites would thus be isolated from the West Bank economy. Therefore, the Palestinians accepted a semi-customs union that should evolve into a free trade agreement step by step through renegotiation of the lists A1, A2 and B every six months.

Israel is de facto losing with this agreement, e.g., with regard to VAT clearance, and because of this, it wants to stop the process from an economic point of view. But, as I said, most important is the issue of control; Israel wants to remain in political control and therefore always puts an emphasis on its security considerations. We have experienced no problems in negotiating and working with the civil ministries; the problems always come from the army. With the current closure, for example, our cargoes are not being cleared in the ports; today, there are 650 containers waiting to be cleared in Haifa and Ashdod. They have even canceled the back-to-back arrangements that we had at the Bethlehem checkpoint! This is not for security reasons: it is to exert pressure, to control. The problem is neither economic nor financial, but political.

Professor Shetreet: Your analysis of the different options for an agreement is an exact reflection of the deliberations that took place. I have just been trying to explain the considerations that led to this specific agreement that we have now. With regard to what you said about control, however, the Israeli side is mostly concerned with territory.

To be frank, I do not know what these containers have to do with security. Often regulations like these are adapted by bureaucrats, and often there is no visible connection between the

political decisions and the security arrangements made by the responsible security officer. But, Israeli control is first of all concerned with territory at this time. I know that the security measures often involve incidents in which VIPs are delayed or where the question arises as to whether sick persons will obtain a permit to travel to receive medical treatment, etc., and I am aware that this involves an element of humiliation and insult that cannot always be measured in money - not to mention the economic costs. But hopefully, when we pass this period, the rules of the game will be different; when we come to a permanent settlement, the whole situation should change. I think a joint lobby of Palestinian producers and Israeli importers having mutual interests will develop and put pressure on the authorities to stop the closure and import restrictions.

Dr. Joel Peters: I do not think that you can reduce the problem of security to one of bureaucracy. It is also a political problem as it reflects on the people and on policies. The closure effectively cancels economic integration. Also, I think that maybe you had a domestic lobby against the closure in the beginning, but the more you reduce Palestinian workers in Israel, the smaller this lobby becomes. Where is this lobby that says that the closure is counterproductive now?

Professor Shetreet: The domestic lobby, unfortunately, is not yet evident. But producers from the Palestinian side and Israeli importers will unite as the flow of products develops. Even today, the parallel economy brings goods into Israel from the Palestinian Territories, including meat. When you make this official, you will have the lobby.

The platform for the lobby is obvious. Look at the following comparison: there is a deficit in the balance of trade of US\$8 billion between Israel and the EU, and a deficit of NIS4.7 billion between the PA and Israel. This is the logical platform for the lobby.

Dr. Peters: I agree that this, logically, could be a platform for a lobby. But the sectors involved here are the least organized and the least structured. I do not think they will organize into a lobby.

Professor Shetreet: There have been a lot of changes in the Israeli economy over the last couple of years, including a major increase in imports. Maybe, some of the former Palestinian workers in Israel will find new jobs in the industrial parks. I am more optimistic in my outlook than you are.

Dr. Mohammed Dajani: My question aims at understanding the psyche of the Israeli decision maker. Where do Israeli decision makers think that the best interests of Israel lie - in a crippled, a dependent, an independent or a healthy Palestinian economy?

Professor Shetreet: If we assume that the Israeli decision maker is rational, and that is what I want to assume, he should think it to be in his best interest to have a healthy Palestinian economy. The relation now of GNP per capita is almost 1:10, with the Israeli economy moving towards a GNP of \$20,000 per capita vis-à-vis the Palestinian economy with a GNP of \$2,000 per capita. Such a big discrepancy is not good for Israel; it is not only uncomfortable and immoral, but it is also a matter of economic costs. Just consider the annual Israeli loss of NIS 2 billion that arises from the theft of cars; in a kind of 'joint venture', cars are stolen and taken to the Palestinian Territories to be 'slaughtered' and resold as parts. Bearing this in mind, a rational decision maker would not put obstacles in the way of developing the Palestinian economy.

Hanna Siniora: But the policy that is executed at the moment is meant to keep Palestinians dependent on Israel.

Professor Shetreet: With regard to the current withholding of revenues by the Israeli side, you are right. This is a new stage in the different means of economic control. But you have to understand that Israel does not regard the closure as economic control, but as a security measure. Anyhow, the closure is more a psychological measure; you all know that if you want to reach somewhere you will do so, with or without the closure.

Dr. Nabil Al-Ja'bari: What closure are you talking about? We have had a closure since 1991! Then, there has been a closure imposed on Jerusalem since 1993, isolating the city from the West Bank; now, we also have a new kind of closure, the 'inner closure', isolating villages and towns in the West Bank from each other.

Israel should also realize that the foreign workers are draining Israel of parts its capital. Palestinian workers used to spend the money here; the foreign workers do not spend it in Israel, but send it home to their families.

Walid Alami: I do not see how we can develop the Palestinian economy under the current circumstances. For example, we organized a business conference in Gaza, but businessmen from the West Bank could not attend. How can you build an economy under such circumstances? We are isolated and dependent on the Israeli economy. This is very well illustrated by the NIS 154 million that have not been transferred until now.

Professor Shetreet: I want to talk about a remarkable phenomenon. During the Labor government, terror attacks did not affect the peace process; of course, they led to a momentary break, but then, we went on with the negotiations and implementation of agreements, yet they led to Labor losing political and public support. Today, we have a completely different situation. Following a terror attack, Likud does not lose public support, but the peace process is stopped. Of course, also under Labor, closures were imposed as a reaction to terror attacks. But Labor leaders found themselves in a dilemma: even when they took measures, they lost support.

If any of the attendants here can exert influence on the people who take part in such terrorist activities, I want to ask you to do so in order to prevent further terror. Terror is counterproductive to peace. It leads to a chain of measures such as closure, etc. Our answer has to be to make joint efforts to go ahead with the peace process. Also, it would be useful to distinguish between the economic and the political field. Let us proceed in the fields of economics and culture. Perhaps, economic cooperation will give the political field a push in the right direction. I do not have any solution other than to move inch by inch. The important thing is that we try to compromise, that we sit together and talk and work for peace. Networking and joint thinking is necessary to influence leaders and decision makers.

Dr. Abdul Hadi: I hope that you are not defending Likud positions by what you are saying. I said in the beginning that we have lost our partner in the peace process. Is Labor still our partner in this process? What is your position as a member of the Labor center on the final status negotiations? We need this kind of exchange of ideas and other ways of building bridges. But let me ask you: Does the Israeli public understand our situation? Do they see us, humiliated, crippled, pushed into violence? Or do we need another Intifada to make them see and understand?

Professor Shetreet: The situation of the Palestinians is not well perceived at the moment in Israeli public opinion after the Mahne Yehuda attack. Israelis are worried about their own wounds. At this time, they are not able to see the plight of others. But when they are less preoccupied with mourning, they will have the capacity to see the Palestinians.

Concerning a permanent settlement, I share Mr. Beilin's view that we should go directly to

final status negotiations now, as both sides feel they are losing more and more as time passes. It is clear that the Palestinians should have a separate, independent entity. How its international legal status will be defined is another question about which, I assume, a lot of doctoral dissertations will be written. At this moment, it is important to pragmatically address the human needs of the people, of the Palestinian nation, parallel to the continued efforts to promote peace on the political level.
