
THE GEORGE WASHINGTON UNIVERSITY

**THE ELLIOTT SCHOOL
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**THE PALESTINIAN PRIVATE SECTOR:
CAPACITY DEVELOPMENT IN AN ERA OF SEPARATION**

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1 INTRODUCTION

Since the conclusion of the second *intifada*, the Palestinian economy and its underlying structure have become central to questions of peace-making and state building for parties on both sides of the Green Line. Israeli and Palestinian leaders have stated in certain terms that economic growth and developing economic capacity will play a large role in determining the future of a Palestinian state. In 2008, Israeli Prime Minister Benjamin Netanyahu (before his re-election) outlined the basis of his vision for “economic peace”:

"We must weave an economic peace alongside a political process. That means that we have to strengthen the moderate parts of the Palestinian economy by having rapid growth in those areas, rapid economic growth that gives a stake for peace for the ordinary Palestinians. Right now, if you look at the division of labor, maybe 99 [percent] of our efforts are going to into political negotiations, and less than one percent are going to economic development. I propose we change the proportions, not reverse it, but change the proportion, because economic peace will support and bolster the achievement of political settlements down the line." (Ahren)

Palestinian leaders are also intensely focused on “institutional development” with the release of Palestinian Prime Minister Salam Fayyad’s plan to build and declare a Palestinian state by 2011.¹ A functional and robust Palestinian economy is a central pill of the plan:

Liberating the Palestinian national economy from external hegemony and control, and reversing its dependence on the Israeli economy, is a high national priority. A capable state is built on the foundations of a strong, sustainable, active and efficient economy. In spite of all Israeli restrictions, and recognizing that sustainable development cannot be attained under the occupation, it is our national duty to do all that we can to pull our economy out of the cycle of dependence and marginalization. This is essential to our effort to build state institutions. (Palestinian National Authority)

Given this emphasis on development, capacity building, and economic growth from leaders on both sides, we think an investigation of capacity development and the private sector in

¹ In an April 14 interview with the Israeli English-language newspaper Haaretz, Prime Minister Salam Fayyad said “The time for this baby to be born will come and we estimate it will come around 2011. That is our vision, and a reflection of our will to exercise our right to live in freedom and dignity in the country [where] we are born, alongside the State of Israel in complete harmony.”

Palestine are particularly important at this time. To understand the dynamics of this reinvigorated interest in the Palestinian economy, we visited the West Bank in March, 2010 and met with those who would be essential to any future plans for economic development: entrepreneurs, business owners, business consultants, development professionals, and government officials. What we found was a disconnect between the purported importance and emphasis on economic growth and the facts on the ground.

In fact, the situation in which the Palestinian economy finds itself today is markedly different from any other time since 1967 (with the exception, perhaps, of the beginning of the first intifada). That is because there has never been such a concerted effort on both sides of the Green Line to forcibly divide these two economies. This “era of separation,” as we have deemed it, is putting extraordinary stress on businesses in Palestine, even considering the extraordinary circumstances of their everyday operation. For better or worse, Palestinians have been interdependent on the Israeli economy as a market for goods and as a primary place to earn wages. Now, the two economies are going through a divorce of sorts, physically split by the separation wall and Israeli policies to replace Palestinian labor with foreign or Israeli workers. At the same time, political risk remains high and the most important decisions about infrastructure, law and policy—which all have huge effects on the private sector—still remain under Israeli control.

In this paper, we argue that the business environment in the Palestinian territories is still so highly uncertain that institutional capacity development is difficult and unreliable; in response, the Palestinian private sector focuses on developing individualized (project, firm, or sector) capacity that is less susceptible to disruption by the political situation. Time after time, our interviewees lamented the inability of the Palestinian National Authority (PNA) or

international donor development projects to help develop the sustainable capacity needed to support their businesses. However, these same professionals went on to describe situations in which they confronted an obstacle to running their business and were able to develop capacity either within their firm or within their sector to overcome the barrier. Below, we take a closer look at the meaning of capacity development and its applicability to the Palestinian context.

1.1 Capacity in the Palestinian Context

The United Nations Development Program defines capacity development “as the process through which individuals, organizations and societies obtain, strengthen and maintain the capabilities to set and achieve their own development objectives over time” (Wignaraja). There are two key aspects to this statement. One is that capabilities must be obtained, strengthened and maintained. The second is that in order for capacity to be developed, there must be the opportunity to set and achieve objectives over time. This is not the case in the Palestinian territories.

In the West Bank and Gaza Strip (WBGS), capacity development as defined here is exceedingly difficult. The high level of uncertainty in which these people and groups operate makes it difficult for the society as a whole to maintain capabilities. Though individuals and organizations can obtain and strengthen capabilities, the ability to set and achieve objectives over time is the more difficult aspect of capacity development in WBGS. Uncertainty that can upset planning and the achievement of goals can come from any source: an extended Israeli closure or military incursion, fighting and gridlock between factions in the PNA, or violence that breaks out from fringe groups. Added to that kind of event-based uncertainty is the general uncertainty around the future status of the West Bank. In Gaza this isn't the case, as the borders are well entrenched and not disputed. In the West Bank, though, without a negotiated agreement to create

a Palestinian state, the future borders of such a state are unknown, the policies and decrees of the Israeli administration over Areas B and C are constantly in flux. Operating within such a business environment makes planning almost impossible—investments made today can be upset tomorrow by any one of these factors.

Simply put, there are too many uncertainties for widespread, society-based capacity development to be maintained. However, as we outline below in a number of case studies, individual firms have been able to develop capacity even when societal or institutional capacity development has lagged behind. Whether it is human capital and education, information communication technologies, or basic infrastructure, individual enterprises have focused on developing capacity that can be maintained even under the uncertainty of occupation. This type of capacity-building under occupation has three major aspects which we classify as spatial, temporal, and sectoral effects.

1.1.1 Spatial, Temporal, and Sectoral aspects of capacity development in Palestine

The spatial aspects of capacity development in WBGS are a result of the occupation, which limits movement of people and goods. Lacking this freedom of movement, the private sector has tended to produce either localized capacity or de-territorialized capacity. Localized capacity is done through investments to replicate resources in WBGS that would either need to be sourced from Israel or abroad. For example, a number of businesses spoke about developing educational programs for employees because it was difficult to attract Palestinians from the diaspora back to WBGS. De-territorialized capacity development attempts to circumvent the movement restrictions of the occupation, with the most prevalent example being a reliance on information technology systems and telecommuting for employees.

The temporal effects refer to the inability of Palestinian firms to effectively plan over time because of the high level of political risk and uncertainty. Lacking stability, these firms develop capacity through diversification and a broadening of activities to ensure that operations are sustainable regardless of the political climate.

Finally, sectoral effects are produced because “state” level capacity development is difficult and unsustainable. Thus, private sector tends to focus on small-scale capacity development within sectors, or carving out small slices of the economy that they can control. This effect can limit the size or scope of projects, as projects that are too large or touch on too many sectors are unlikely to sustain the capacity they develop.

1.1.2 The Occupation

Any discussion that touches on the lives of Palestinians must necessarily include the role of Israel’s occupation of the West Bank and Gaza Strip. For more than four decades, the dynamic of Israeli control of these territories has been a key factor in shaping social, economic, and political life within the territories. Still, the occupation is not the focus of our study. It is, however, the context within which the Palestinian private sector and economic development operate in the West Bank and Gaza Strip. To the greatest extent possible we have tried to present our findings about private sector reactions to this context without focusing squarely on the nature of the occupation or the political questions that invariably arise in any study that might touch on relations between Israel and the Palestinians. These questions have been researched and debated elsewhere, as they will continue to be for years to come.

1.2 Paper Organization

We begin with a discussion of the Palestinian economy since 1967, highlighting the major periods of change to show how the current situation of separation between the Israeli and

Palestinian economies is structurally different from past periods of the Palestinian economy under occupation. After that, we turn to case studies of capacity development under this context. First we look at five cases of private sector response to the current situation and attempts at capacity development. Second we look at institutional approaches to growth and capacity development. Finally, we conclude with a discussion of the implications of our findings.

2 REMAKING THE BOUNDARIES OF THE PALESTINIAN ECONOMY

The occupation and the “boundaries” of the Palestinian economy following 1967 are an important place to begin for two reasons. During this time, the physical boundaries of Palestine were in flux due to a lack of a clear articulation of Israeli intentions for the future of these territories. At the same time, the more abstract boundaries of what might be considered the Palestinian economy were undergoing a rapid structural shift. Though the West Bank and Gaza Strip were never fully integrated into either Jordan or Egypt, their agrarian-based economies looked outward toward the Arab world to export food and import other products. Fundamentally, the shape of Palestinian economic relations with the rest of the world changed in 1967—going from almost zero integration and cooperation with the Israeli economy to almost full integration within three years. The boundaries of economic activity for individual Palestinians also changed—with the primary location for economic production moving away from local farms and into Israeli industry located across the Green Line in Israel or on Israeli settlements in the West Bank or Gaza Strip.

2.1 The Palestinian economy since 1967

In his work covering the Israel’s occupation, Neve Gordon divides the occupation into five eras, based on the “modes of power” and “distinct forms of control” in effect under each era (18). Because many of these mechanisms of power and control were geared toward controlling

economic life in the territories, we will also use these eras to analyze the shifting dynamics of the Palestinian economy since 1967.

The military government in the Occupied Territories (OT) was instituted during Israel's capture of the WBGS during the 1967 six-day war and lasted until 1980. During this period, the Israeli military government in the territories undertook an intense effort to focus on the prosperity of the Palestinians now under their control (Gordon 62-69). The most important factor during this period was the rapid shift to using Palestinian labor within Israel. Gordon points out that just six percent of the Palestinian labor force worked in Israel a year after the six-day war, but "by 1974, 69,400 Palestinians worked in Israel, making up one-third of the workforce" (66). During the civil administration of the OT that began in 1980, the rapid economic changes of the military government period had redefined Palestinian life, transforming the economy from mostly agrarian to service-oriented. Leila Farsakh, in analyzing statistics of the early period of the occupation, shows that more than 38% of West Bank and Gaza Strip residents were employed in the agriculture sector in 1970, with less than 23% involved in agriculture by 1987 (41).

For its part, the Israeli government wanted to capitalize on this growing individual prosperity and put out numerous charts and statistics showcasing development statistics, such as the rise of personal income levels and rising levels of home appliances, like televisions, refrigerators and stoves in Palestinian households (Gordon 67). At the same time, however, measures of GDP or productive capacity within WBGS were declining.

The strange conundrum of individual welfare improving in the OT while overall capacity for production shrank pointed to the nature of the economic changes underway. Most importantly, the labor integration with Israel resulted in a circular path of capital. To clarify,

integration with the Israeli labor market meant that Palestinians were working on Israeli land, producing Israeli goods, and coming home to buy imported products usually manufactured in Israel or imported through Israel. There was little space in this system for any productive capital to remain within the occupied territories. Hamed and Shaban called the WBGS during this period a “dormitory region,” where “Palestinians work during the day in Israel and return at night to their homes, where they spend their earned income on imported consumer goods” (Hamed and Shaban 138).

In 1988, the first intifada, or uprising, began. While the intifada clearly had fundamental roots in the political aspirations of Palestinians to be free of the occupation, some have argued that it was economic factors that catalyzed the widespread mobilization of the Palestinians (Schiff and Ya'ari 87). In the 1980s, Israel's economy stagnated. Schiff and Ya'ari theorized that the government's response, which included high taxation, as well as the increasing unemployment among Palestinians, were key factors in the onset of the intifada. During the intifada, Palestinians attempted to disentangle themselves from the Israeli economy with a boycott of Israeli products and a new “development paradigm” that focused on local capacity. However, the erosion of the Palestinian economy that had already taken place in the previous period continued during the intifada and was exacerbated by the boycott, leading Palestinians to still rely heavily on wages earned in Israel (Roy 294). By the end of the intifada, however, these new goals for self-reliance hadn't been reached. The Palestinian economy was significantly weakened and actually ended up more reliant and interconnected with Israel's economy as efforts to create indigenous production failed.

The Oslo years (starting in 1993) were a sea change in the economic life of Palestinians. First of all, the creation of the Palestinian National Authority (PNA) finally wrested some control

and self-determination for the Palestinian public officially, if only partially, away from Israeli control. Second, the Oslo Accord's political framework paved the way for the Paris Protocol, a joint Israeli-Palestinian agreement on economic cooperation (signed April 29, 1994).

Referring to the Oslo Accords and the Paris Protocol, former Israeli prime minister Shimon Peres called it “a political divorce and an economic marriage” (Usher 35). The Paris protocol outlined the mechanisms for trade and economic cooperation between Israel and the Palestinians. However, the agreement was not without its flaws for the Palestinian economy. During our field research, we heard from multiple people about the inequity of the Paris protocol and its damaging effects on the Palestinian economy. Sami Abu Dayyeh, a businessman in East Jerusalem, had this to say:

“The needs that they put on us through the Paris protocol are really horrible if you think about it. They based us on the same standard of living like they have in Israel, which is not a reality. Somebody from a strong economy and somebody who is trying to have an economy—how could you have an agreement? The agreement is only based on things to their favor. It’s a joke, to tell you frankly.”

His sentiments are borne about by economic statistics of the period. In the two years following the signing of the Paris protocol, Palestinian unemployment reached record highs (28.4 percent in May, 1996) and GNP fell by 37 percent (Roy, *The Gaza Strip: the political economy of development* 334). This period also saw the beginning of Israel's closure policy, a system that limits movement within the OT and periodically closes off the OT completely from access to Israel, resulting in about 200,000 Palestinians being blocked off from their main source of income (labor in Israel) each day closure was in effect (Gordon 185). The closure policy became a major hindrance to Palestinian economic development during the period, and it continues until today.

2.2 The Current Period: an Era of Separation

We have deemed the current, second intifada and post-intifada period, an “Era of Separation” because the underlying economic structure of the Palestinian territories is based on separation, and is much different than at any other point since the beginning of the occupation. While much of the history of the occupation saw the creation of economic linkages and interdependency between Israelis and Palestinians (even during the first intifada), the current period of separation is reversing that trend. Palestinians are separated now on three levels: from each other, from Israel, and from the rest of the world.

Politically and economically, Palestinians are separated from each other. The election of a Hamas-led PNA government in 2006 precipitated a host of retaliatory actions and collective punishment by Israel with regards to Gaza. The West Bank and the Gaza Strip are now separated. Within the West Bank, Palestinians are also separated from each other. The creation of the Area A, B, and C systems under the Oslo Accords legitimized Israeli control in Areas B and C and has made shipping goods or moving people within the West Bank exceedingly difficult (Seibold). This, when combined with the closure policy, has had the effect of concentrating Palestinian economic activity in small clusters, with producers mostly focusing on city-size or village-size surrounding markets.

The split between the West Bank and Gaza has had major economic impacts on both territories. For Gaza, the complete closure and blockade of most goods by Israel and Egypt has greatly intensified poverty there and brought the economy to a standstill (ICRC). In the West Bank, the closure and separation from Gaza has also had an economic effect. The West Bank has lost about 30 percent of its potential market (i.e. Palestinians in Gaza) and has suffered from the loss of agricultural products from Gaza (Hezboun).

Israelis and Palestinians are now more physically separated than at any time in the past. Israel's disengagement in 2005 from the Gaza Strip cleared it of both Israeli settlers and permanent military installations. In 2002, Israel began construction of the separation barrier with the West Bank, improving its ability to control the flow of Palestinians coming from the West Bank (Weizman 161). Samir Hezboun, an economist based in Bethlehem, explains the economic impact of the separation wall on Bethlehem:

Now the situation is worse. Worse why? Because the volume of our trade with Israel has decreased. We are more dependent on marketing our products at the local markets. Our retail trade with Israel decreased because of the wall over the last 5 or 6 years. Even normal peddlers who had been selling products are losing this opportunity because of the wall. Stone and marble [exports] began to be more regulated. The other light industries for example, carpenters, goldsmiths, who had been working in Israel lost their job opportunities there, because for those people the cost of transportation is problematic.

The era of separation, which began during the second intifada, has increased in intensity. The Palestinian and Israeli economies, which for more than 30 years had been growing more intertwined and more interdependent, are being forcibly ripped apart. On the Israeli side, the removal of Palestinian labor has been compensated with increased numbers of foreign workers coming to Israel on temporary work visas or illegally (Sadeh). On the Palestinian side, there is no mechanism to replace the wages formerly earned in Israel.

3 CASES OF CAPACITY DEVELOPMENT IN THE PRIVATE SECTOR

We turn now to five present-day case studies of firms or projects in the WBGS and a discussion of their attempts at capacity development. By delving into the individual successes and failures of private sector firms in the OT, we aim to show the spatial, temporal, and sectoral effects that impact capacity development there.

3.1 PalTel: Developing localized capacity

Utilizing article 36 of the Accords, which nominally granted the Palestinians control of their own telecommunications, Sam Bahour and other investors developed the Palestinian Telecommunications Company (PalTel), Palestine's first national telecom provider. The PNA, under Yassir Arafat's command at the time, organized the sector as a monopoly and directly supported PalTel's development. However, even with monopoly status and institutional support, the company faced two major restrictions to growth: access to human capital and real control over the communication frequency spectrum. The case of PalTel illustrates how Palestinian lack of control over its own physical boundaries and policies for immigration forced the private sector to develop Palestinian human capital.

In describing the human capital challenge, Bahour explained "We didn't have the experience in country because there was never a telecom sector in this country. We have the expertise in our diaspora, we have it in Dubai, we have it in AT&T in the States, but we weren't able to bring these people to come back because we weren't able to give them the permanency to come back." What he referred to was the fact that Israel was not granting any more than three or six month tourist visas to Palestinian professionals who wanted to return to work on projects like PalTel. Bahour himself lived in Palestine for 15 years on a tourist visa before he was able to obtain a Palestinian ID. The inability to tap human resources resulted in a tremendous cost for PalTel, which was forced to rely on short-term international consultants who demand higher wages and leave along every few months, requiring additional training and disjointed accumulation of knowledge about the project.

However, Bahour and PalTel were able to eventually overcome the human resource challenge by developing the capacity to produce domestic telecom professionals. PalTel and the PNA focused on a mid- to long-term strategy of refocusing the education system to

include technical telecom curriculum and grant telecom-engineering degrees. Bahour explains that this strategy, which took years to implement, was successful because PalTel was a monopoly and had the government financed resources to initially carry the burden of hiring international contractors to establish the company.

Even though PalTel received tremendous support from the PNA, Bahour feels that they have been unable to effectively regulate the telecom sector. As a result, he left PalTel over concerns that the company was abusing its dominance and exploiting the lack of regulation to reap greater profits. Bahour felt that a company in such a position needed to impose a self-regulation in order to maintain and build the integrity of both the sector and the state infrastructure. Thus, by relying on institutional capacity development, the ability to actually create capacity in the telecom sector was diminished.

3.2 Bisan Systems: Developing localized, diversified and de-territorialized capacity

Seeking to reconnect to the Palestinian social fabric, Samiah Totah, an industrial designer, and her husband, a computer programmer, returned to Palestine during the first intifada and founded Bisan Systems in 1988. In order to develop the capacity to operate in a sustainable regardless of how the occupation, the intifada and the level of violence might impact the economy, she recognized the need to provide a service that would be vital to all sectors regardless of the level of violence. Therefore, Bisan developed an accounting software (which is needed by all businesses, regardless of their sector of the general business environment) and introduced the novel business model of a monthly service contract, which broke from the traditional model requiring Palestinian companies to make large upfront investments in new software. Bisan continued to adapt to changing technology and political realities. During the second intifada the company expanded into networking and telecommuting. In 2005, the

company introduced an Internet-based application that allows Bisan to serve their customers without needing to travel to clients, which helps to avoid being delayed by military closures in the West Bank. This response can be classified as de-territorialization of capacity, since the use of the service does not connect to a physical location or the necessity to move to a specific location to use it. The political situation has impeded Bisan's growth while at the same time prompting the company to innovate and adapt their business strategy. Bisan is now the oldest ICT company in Palestine and employs a team of 25, larger than the 10-15 employee companies that make up the majority of their clientele.

One interesting obstacle to their ability to develop human capacity is that Bisan Systems is actually undermined by the presence of internationally funded donor projects in the West Bank. These development projects employ the best and brightest IT professionals at wages typically twice the salary that Bisan could afford. According to Totah, Bisan "works by default" and is unable to develop 2-year, let alone 5-year, business plans because of unstable access to export markets. "We never had a five year business plan, never. You know if we had a one year business plan that would be excellent!" she told us. She doesn't believe that her situation is helped much by the PNA. Despite designing new integrated budget systems to link PNA ministries (which PNA ministers have touted as the basis of a new transparent government apparatus), the PNA has refused to extend tax breaks offered to new companies to established IT firms. Totah feels this has limited her firm, which is already established and successful. Her company's expansion is financed solely through profit reinvestment, and she feels she could do more with the tax breaks than new, unproven companies could.

The firm is also hampered by its location in the West Bank both domestically and internationally. Despite the absence of restrictions on providing IT services abroad, Bisan has

faced difficulty exporting their system to the rest of the Arab world and beyond. This is because potential clients are reluctant to invest in a system run by a Palestinian company for fear of the political risk that the Israeli government could interfere with the Palestinian telecommunications network. Domestically, the location of the business in Ramallah also creates challenges. Totah runs two data centers for Bisan Systems: one in Ramallah linked to the Palestinian telecommunications network, and one is in Jerusalem linked to the Israeli network. As of March 2010, Bisan had been unable to obtain travel documents from Israel to send a staff member to East Jerusalem in order to service one of company's data centers. If the data center were to stop working, there is no guarantee that Totah and her staff would be able to get it back online.

While the challenges of Palestine's international reputation and the ability to travel to Jerusalem are beyond Totah's control, she has focused on developing capacity within the West Bank in ways that would be beneficial to her firm. For one, Totah found that Palestinian college graduates were receiving largely theory-based degrees and little hands on training in accounting systems. She would end up training graduates for a long period of time before they could be productive employees. Now, she works with universities to develop curriculum that includes work in accounting systems so that graduates are prepared to use her software. Beyond developing resources for her own firm, this activity is also building a professional class of Palestinian accountants that know how to use computer-based financial accounting systems.

Totah also noticed another interesting phenomenon which she has been able to use to her firm's advantage. Because of the popularity of her software systems, other individuals and groups were offering training on her software. Totah decided that instead of having outsiders teaching her software, she would instead develop her own training programs to ensure that people actually know how to use the software correctly. She now provides free training programs

to accounting graduates and is working with the Birzeit continuing education center to establish a curriculum for a certification in Bisan Systems software.

3.3 Rawabi: Developing PNA capacity, internal capacity and state-building

Rawabi is a project to develop the first planned Palestinian city. The project receives some support from the PNA, but is financed mainly by Qatari investors, which will provide for 80 percent of the costs. The project was conceived by Bashar Masri, a Palestinian-American businessman who had completed successful residential projects in other countries of the Arab world and decided to try to repeat his success in Palestine. His company, Bayti real estate, runs the project out of Ramallah, and has teamed with RTI, an economic development consulting company headquartered in North Carolina, to build a strategy for employment and development for future Rawabi residents.

Currently, there are 135 Palestinian municipalities, all of which were in existence in some form prior to 1967. Rawabi would be the first totally new Palestinian city, designed from the ground up. The land for Rawabi is situated half-way between Ramallah and Nablus. It is strategically located in Area A land already under PNA jurisdiction, but would add physical structures in an area that is currently uninhabited specifically to build geographic contiguity between its surrounding population centers. As the first-ever planned city, the project has run into some major obstacles related to capacity.

We met with the Amir Dajani, the director of the Rawabi project for Bayti Real Estate. He specifically spoke to the issue of capacity development in dealing with the PNA:

“We are in the heart of Area A under PNA jurisdiction. That means you are really testing the Palestinian apparatus to approve a 300-page master plan, when they’ve never done a master plan for any city.”

The Rawabi project, in effect, is pushing for capacity development within the PNA. In addition to the effect of the master plan, Rawabi was able to pressure the Palestinian Monetary Authority to lower down payment requirements for mortgage borrowers, effectively making housing in the project more attainable for Palestinians within the West Bank.

As one of the largest private sector projects in Palestine, Rawabi has also taken on aspects of state-building normally reserved for the PNA. Rawabi would be the first totally new Palestinian city, designed from the ground up. The land for Rawabi is situated half-way between Ramallah and Nablus. It is strategically located in Area A land already under PNA jurisdiction, however access to the build site is only possible via a narrow roadway that travels through a number of crowded residential areas. Rawabi is currently directly lobbying Israel to re-classify a swatch of land running directly from Ramallah to Rawabi from Area C to Area A. Should this lobbying succeed, Rawabi will then work with the PNA to build a highway directly to the project.

Dajani also spoke about areas in which Rawabi and Bayti were developing their own capacity. Like other businesses, Rawabi faces a lack of skilled human capital for its project. For instance, for instance a lack of trained Palestinian landscape architects. One way they are trying to overcome the disconnect between project needs and the available human resources is to work directly with universities to develop their capacity:

“We have a steering committee including people from Rawabi, from RTI, from Birzeit and An-Nadjah universities in an effort to brainstorm what is needed, what kind of things do you need to revitalize the Palestinian economy, and how do we focus on priority sectors.”

Also, rather than relying on capacity to be developed elsewhere in the economy for the project to draw on as needed, Dajani is looking to build up capacity within the Bayti company to support Rawabi. For example, he told us about the architectural firm they were using in New

York to design their residential buildings on a software platform called BIM. The firm in New York was actually outsourcing the design to India. When he realized this, he thought that instead of paying for a US-based firm to outsource this service, he should have the work done in Palestine. Dajani discovered that an Egyptian company was supporting a BIM program at Birzeit University with 10 students to support his projects world-wide. “I’m already in the process of setting up a unit in-house to do BIM,” he told us. “I will then turn this service into a company and then will start giving services to the Palestinian sector in that respect. If the universities were engaging properly, they should understand what the needs are to adjust the curriculums, etc”

3.4 PADICO – Investing in a Palestinian State

Driven by the financial and political opportunities afforded by the Oslo Accords, a group of established Palestinian businessmen living primarily in Jordan and the Gulf, who felt committed to the coming Palestinian state, established the holding firm Padico. Through large scale, higher risk investments, the investment outfit used its initial \$150 million capital pool to invest in economic sectors by establishing new companies that would provide an opportunity for return on invest, create new jobs for Palestinians, and provide new services needed to build a new state.

In 1994, the company began operations with the establishment of the first Palestinian telecom company PalTel. From PalTel, Padico expanded to industrial companies in 1995, established the Palestinian stock exchange in 1997, and by 2000 the company had built 13 ventures, including five-star hotels in the West Bank and Gaza, real estate ventures, agriculture and other financial companies. However, Padico’s large scale invest strategy has proven to be extremely sensitive to the political situation. From 2000 to 2008, during the second intifada,

Padico did not develop any new companies and it shifted its financial investments out of Palestine in favor of international markets. With the relative smoothing of political tensions in 2008, Padico has begun to identify new growth sectors and begun new ventures. In addition to completing tourist ventures, the company is currently developing a waste water recycling system, a solid waste management project and a 400MW electrical generator to hopefully be fueled by the natural gas reserves off the Gazan coast.

For Business Development Manager Abdullah Sharawi, Padico's sits at the forefront of Palestine's shift from a nation dependent on international handouts to a stable and independent economy. "We act as a success story. Padico considers itself a model for investors who came to Palestine and made money." He sees Palestine as a "virgin territory" for investment, with its good market, educated work force and government incentives and to exploit this opportunity Padico is focused on enticing international private investment to share the risk of future large scale development projects.

In conjunction with the growing private investment opportunities, Padico has seen a dramatic increase in government support. With the rise of Prime Minister Fayyad's administration, the PNA has changed tax structures to allow Padico to register as a Palestinian corporation. In addition, the company has been able to participate and initiate international and municipal investment conferences designed to join private and public approaches to development. Moving forward, Padico sees the future of Palestinian economic development as a relationship in which the private sector attracts and directs economic development while the public sector works to provide the necessary infrastructure and institutional capacity necessary to facilitate economic growth.

3.5 Capturing Tourism Shekels: Sami Abu-Dayyeh and NET Tours

Sami Abu-Dayyeh was born in Jerusalem in 1953. After high school, he enrolled in college in North Carolina. Abu-Dayyeh returned from his studies in the US to join his family in running their business, a small tourism company focused on showing the holy land to religious and cultural tourists. Shortly thereafter, he set about expanding the business by diversifying its operations—expanding it to include a fleet of tour buses, hotels and restaurants. Over the years, he has had to react to the political situation, changing and adapting to fit the needs of the times. For instance, he says he has about 40 buses in his fleet now, but that number goes up and down depending on the political situation, which affects the number of tourists who come to the country.

Abu-Dayyeh has focused on developing sustainable capacity through a diversified tourism infrastructure all owned by his company. “The money is not in tour operation,” he told us. “The money is in infrastructure: hotels, restaurants.” He believes that this type of capacity should be developed not just by private businessmen but also by the PNA. As a business owner in Jerusalem, he feels particularly left behind by PNA initiatives. “They only talk about Jerusalem without physically supporting it,” he lamented. He sees the PNA as largely ineffective and wished that they would build physical structures in Jerusalem to help support the Palestinian economy there. For him, this includes tourism infrastructure like hotels as well as basic social infrastructure like schools.

He later made the point that private investors, (e.g. PADICO) should also focus on Jerusalem. Interestingly, he argued that the developed legal capacity within Israel is a benefit to Palestinian investors, with the implication that the same guarantees aren’t available in the West Bank:

It's Jerusalem that makes the money, it's not the West Bank. And also the reality of Jerusalem being under Israeli control where you have the law (not that I agree to it by the way, but it is a fact) but you know what your investment will go to. There is some sort of protection. The rule of law is something that you can depend on and it is fairly safe. They should have invested in Jerusalem. Jerusalem is the biggest Palestinian city. It's their duty to make investments in Jerusalem.

Abu-Dayyeh recognized that he has developed his own capacity through running his business, and believes that his experience and the experience of other businessmen working within Israel could be put to good use by the PNA. “If they will only make use of our know-how, of working with the Israelis, it will help them a lot. They should consult with us and not just do things as they see fit.” Without institutional capacity within the PNA to support the private sector, Abu-Dayyeh noted that the private sector must fight for itself to survive. “Anything that is my personal decision, I depend on myself and I don't depend on what the state or any government can give me,” he told us. “I purely base it on my gut feeling and calculation.”

4 INSTITUTIONAL APPROACHES TO CAPACITY DEVELOPMENT

4.1 Case Study: The Ministry of Planning, Prioritizing Development

In its own estimation, prior to 2008 the PNA and in particular the Ministry of Planning and Administrative Development (MoPAD) had no strategic plan to prioritize development projects. According to a high level government official in the PNA, the Palestinians simply presented the international community with a list of all possible donor projects, submitted by any budget agency or municipality, and then allowed donors to take up projects that aligned with their interests. In response, the development of the 13th government program under Prime Minister Fayyad has sought to assert a Palestinian identity and develop institutional accountability within donor projects in order to eventually build a Palestinian state.

The first attempt to better dictate project priorities came with Palestinian Reform and Development Plan in 2008, which coordinated efforts from the MoPAD and the Ministry of Finance for the first time to develop a single Palestinian solicitation for development projects between 2008 and 2010. The ministries solicited project proposals from the 53 budget entities within the Palestinian government and then identified the key projects in line with national goals and then presented those projects at the international donors' conference in Paris. The PNA itself admits that the initial plan, which the PNA rushed in order to meet the donor conference deadline, was a top-down approach focused on government capacity building and large-scale infrastructure projects.

The second PRDP, which will cover 2011 to 2013, is seen dominantly as a bottom-up approach. Informed by consultations with not only government offices and municipalities, but also NGOs, the private sector, and the international community, the MoPAD has identified 23 sub-sector development strategies within four overarching sectors: economic, government, social, and infrastructure. This PRDP is a move towards implementing Fayyad's national plan designed to give voice to all actors within Palestine.

Discussing the new PRDP, this administration official explained that the PNA is attempting to strengthen the policy initiatives of the 13th government plan through its development strategy. As the MoPAD is attempting to spread donations equally across the four sectors, the PNA recognizes Palestine as a developing country and thus has placed a strong emphasis on infrastructure development – roads, buildings, sewage, and water – as well as a focus on security and institution building within the government sector. In terms of economic development the PNA espouses support for the private sector, believing “you cannot have a functioning economy or a future state that depends on itself without a strong private sector.” The

PNA has designed this process to show the international community the Palestine is ready to become its own state and the government believes that it is making great progress towards that goal.

Defining the success of the PNA's policy shift, however, is still elusive. The official admitted that cannot determine if the recent surge in the West Bank's GDP is due to the work of the PNA, private sector growth, or an increase of international donors. Despite a boom in Arab business coming to Palestine, he is confident that the PNA will not be able to attract new business or establish a stable economy without addressing the political situation or the Israeli barriers to the movement of goods and services. At the same time, the West Bank's growth is widening the economic gap with the Gaza strip and "at some point when they are one unified land we are going to be faced with a major challenge for years of channeling money to rebuild Gaza."

4.2 USAID's Private Sector Development Projects

We are including two USAID-financed development projects in our case studies, since each focuses on reducing barriers to private sector development and increasing capacity in one way or another. However, both projects have faced the same capacity development issues that have been a barrier to large-scale institutional capacity development throughout the economy.

4.2.1 Trade Facilitation Project (TFP)

The Trade Facilitation Project (TFP) started in June of 2008 as a follow-on to an earlier USAID project. In this incarnation of the project, it is focused exclusively on developing capacity in the PNA and the Palestinian private sector. "We are attempting to facilitate product movement," we were told by Kelly Seibold, the project's director. "Moving goods out of the West Bank is expensive and time consuming and leaves Palestinian businesses with few

options.” The project aims to ease the restrictions placed on the movement of goods within the West Bank, between the West Bank and Israel, and between the West Bank and Jordan.

To do this, the project focuses heavily on research. While there are constant complaints by Palestinians about the difficulty of moving goods, it is difficult to change Israeli security policy based on anecdotes. Therefore, the TFP project relies heavily on producing research and analyses of trade issues to bring to the Israeli administration that controls the crossings. Having these facts helps to open up negotiations on certain policy changes. Beyond that, TFP has also brought together Israeli and Palestinian businessmen to discuss trade issues, which can move Israeli policymakers to loosen restrictions when the Israeli private sector is also advocating for improvements in trade.

The project’s ability to develop capacity is severely limited by Israeli control of all aspects of trade policy within the West Bank. “Frankly, you can’t do anything in trade facilitation without the Israelis, both for internal movement and access issues as well as the external,” we were told by the director. Most of the successes of the project—lengthening the time that crossings are open, removing internal checkpoints in the West Bank, or opening up the northern West Bank to more shoppers from Arab villages in northern Israel—can all easily be reversed by changes in the Israeli closure policy.

The project does focus on some sustainable capacity development with work that is not as easily hindered or reversed just with changes in policy. One small aspect of TFP is building better infrastructure at checkpoints, including the installation of electronic scanning devices, so that there is a staging area and better flow for shipments of goods. The TFP project also works with the PA to build capacity for customs to better regulate and tax imports and exports.

The biggest goal of the project seems to be changing Israeli attitudes about trade and movement in the West Bank, getting the authorities on the Israeli side to realize that economic growth is better for security. “There is a southern checkpoint near Be’er Sheva and there is nearly a thousand cars that come in to go to Hebron.” The director told us. “They are all spending money. Ultimately it is very good for security, because if you develop the economy it has a stabilizing influence. I think these are the easy things.”

4.2.2 Export Development and Investment Promotion (EDIP) project

Whereas TFP works on a macro-level to reduce trade barriers for all Palestinian businesses, the Export Development and Investment Promotion (EDIP) project targets individual firms and sectors to open export markets and encourage investment in Palestinian businesses from abroad. Carl Larkins, the chief of mission for the project, told us that the project really is geared to capacity development. It focuses on four sectors: ICT, Agribusiness, Stone and Marble, and Tourism. In each sector, the project works with a few “anchor firms”—established companies able to produce for export markets. The idea behind the export side of the project is that if a large firm sector can create an export market in a particular country abroad, other, smaller firms in the same sector will also be able to benefit from the path paved by the larger firm.

In agribusiness, for example, EDIP has worked with a few firms to get them certified to global standards for packaging. When those firms received orders for more than they can supply, they started sourcing from smaller farms to fulfill export requests. Agribusiness has also benefited from capacity development within Israel. Because Israeli firms are world-leaders in agricultural standards and technologies, the EDIP project has been able to help Palestinian firms acquire these technologies and learn from Israeli counterparts. The reputation effect can be used

on the investment side as well. EDIP was successful in convincing Cisco, one of the world's leading IT companies, to work with some Palestinian IT firms. This makes it easier for Palestinian IT businesses to find clients abroad, since the prior work done with Cisco gives them a "stamp of approval." Larkins is trying to repeat this by bringing in other firms if possible, such as Google, Microsoft, or Apple, to work with Palestinian IT businesses.

Even this strategy, which does focus on capacity development and is driven by market needs, faces obstacles. For one, the budgets for capacity building projects that focus on the private sector are quite small. In fact, Larkins was skeptical that development projects in general are focused on the needs of the private sector: "Sometimes it's the donors that are not business people and don't know business practices," he said. He also noted that the needs outlined by the PNA and the interest of international donors don't always align:

"I think part of it is that donors come in with their own agenda and they are not coordinated with the national plan. One concern is that the PNA does not have a 10 year plan for economic development, they just have pieces of it. They are trying to focus the plan through WTO ascension, which will require changes in tax laws, property rights, and other large scale policy adjustments. They need a focal point. Their list of priorities right now are just aspirations. They need to do something concrete."

Larkins also brought into the fore the fact that large-scale capacity development runs up against the very real barriers of the occupation. He gave the example of the PNA's ministry of information technology, which wants to implement e-government solutions and eventually create a knowledge economy by expanding broadband access.

You then have to look at the spectrum that Israel controls and is not giving up and you have to get the US and the quartet involved. They need spectrum concessions. Clearly its an economic development project, but with that comes the need for government development. People here are very capable, but are they missing the point of having a focal strategy. You go to each ministry and they have a plan and they have to convince the donors they have their act together and the donors choose where to focus and the PNA has little control over it.

In the end, for Larkins, it all comes back to questions of politics: “There could be development if there is some normalcy and free movement of goods. There is no precedent for how long it will take or for an economy to develop under occupation.”

5 IMPLICATIONS FOR THE PALESTINIAN ECONOMY

Summing up the state of Palestinian economic development, Sam Bahour called it “survival economics,” in which the “[government’s] priority is to have economic activity to employ as many people as possible,” without actually creating growth. Bahour argues that this emphasis on employment numbers rather than a focus on addressing the larger political problems have left the PNA and the Palestinian economy vulnerable to Israeli administrative pressures, which have led to a steady exodus of highly-skilled Palestinian talent.

However, as these case studies illustrate, the private sector has come to take the lead in transforming many government practices by undertaking individual projects in order to overcome challenges specific to an enterprise’s situation. In terms of education, older operations with direct ties to the Oslo-era government, such as PalTel, pushed the government to change the educational system by establishing a telecommunication program. Newer companies without government ties, including Bisan Systems and Rawabi, have moved to work directly with universities to change curriculum and develop students to fill needs specific to each company. Such individualized approaches, while addressing a short-term need, redefine capacity within the government and within the market by creating new practices and better trained labor that will be better able to fulfill future private sector needs.

Larger projects that attempt to create or transform entire sectors of the market are pushing the boundaries of the Palestinian government’s capacity and as a result have needed to take on aspects of state-building, with the Rawabi project being the most obvious example. Rawabi has

presented the PNA with an unprecedented master plan to construct an entire city and because Rawabi intends to build to an international standard, rather than to local zoning and construction standards, the project is forcing government agencies to learn international procedures for construction and to reconcile those procedures with the traditional Palestinian approaches to construction. Rawabi is also directly involved in the politics of state-building as it attempts to lobby Israel to reclassify a strip of area C to area A in order to build an access road from Ramallah to the build site. Should Rawabi succeed in their lobbying it will present a novel model for addressing the administrative conflict over land rights.

At the same time, USAID's Enterprise Development Investment Program is building capacity within existing small-scale Palestinian industries through a new emphasis on supply chain investment. The Trade Facilitation Project is building political capacity for negotiations and regulation as works on the specific goal of opening internal trade routes. These projects are attempting educate producers about the international marketplace, help establish international connections, and build a dependable trade system that will allow producers to develop their capacity within a more stable economic system.

Despite the capacity gains attained through the enterprises explored here, there is a realization that many of these gains are impermanent in the face of occupation. Large infrastructure projects are likely targets for closure or destruction during times of conflict and the projects that attempt to address political elements of state building aren't really developing capacity as they can be reversed through simple changes in policy. This reality shapes the long-term implications of both international development projects and private investment.

Donor projects related to economic development take on many projects that are unfeasible for the private sector or the PNA to finance, most importantly infrastructure

development. However, these projects create short-term enterprises that look to complete a limited number of specific projects and then dissolve. In the process, these projects crowd out much of the private sector by attracting the brightest people within industries through comparatively astronomical salaries. The international community's focus on finite projects, in fact, retards the private sector's ability to build its own capacity in ways that continue to engage the economy beyond the completion of a specific task.

The reality of impermanent growth also shapes the nature of private investment and its impact on the development of the market. The lack of a reliable export system has pushed private sector investment towards non-exporting industries, such as construction and ICT. The U.S. Commercial Service identifies the construction sector as the fastest growing sector of the Palestinian economy with output reaching \$300 million in 2002 (U.S. Commercial Service) and as the cases of Padico and Rawabi show, large-scale private investment is moving towards non-exportable services in construction, energy, and water management. ICT and Telecom continue to be another major source of private investment. In 2007, Wataniya International, a privately owned Kuwait company, paid a \$355 million licensing fee to the PNA in order to develop a competitor to the Palestinian telecom giants PalTel and Jawwal (U.S. Commercial Service).

Looking at the implications of these efforts, it is possible to say that even though the private sector cannot rely on political stability for long-term growth, individual efforts to address temporal, spatial, and sectoral effects can result in capacity development. Enterprises are not attempting to transform the entire political apparatus in order to build a stable marketplace. Rather they are creating niches of competence and innovation to resolve immediate concerns. Should the political situation change and avenues of growth be cut off, the examples of private development given in this paper show a commitment by the private sector to the people of

Palestine to remain engaged in the Palestinian economy. However, the realities of the political stage shapes the focus of Palestinian investment. Should investment continue to favor non-exporting industries there is a strong possibility that the private sector will carve out areas of stability within a local context and then cease to push the boundaries of development.

6 CONCLUSION

With international attention, the fate of the peace process, and the construction of an independent Palestinian state all seemingly resting on the state of the Palestinian economy, there is surprising little work done on the nature of capacity development under the occupation. In our exploration of the subject, we found that in the face of extreme pressures in the business environment, Palestinian firms were able to maneuver in such a way as to develop capacity in an individualized manner, responding to the spatial, temporal, and sectoral effects imposed on them. They responded in a number of ways, localizing their capacity or de-territorializing aspects of their business to overcome spatial restrictions. They also spoke about broadening their activities to overcome political uncertainty even while tightening their focus on specific sectors and markets.

Our analysis does not provide an answer for how development should be practiced under occupation, and it does not show that the private sectors are heroes able to overcome the difficulties that the PNA can't. Rather, we have shown how, under occupation, capacity development does take place in specific forms, and in ways that many may not expect.

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