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ECONOMIC PROSPECTS FOR A ONE-STATE SOLUTION IN PALESTINE-ISRAEL

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ABSTRACT

This paper explores the economic underpinnings of a one-state solution in Israel/Palestine, a dimension that has rarely been addressed in the growing literature on this subject. It seeks to demonstrate that economic developments since 1993 prove the demise of the two-state solution but without shifting the power imbalances in favor of a one-state alternative. This is largely because Israel has been able to dispense with the Palestinians, both economically and politically. The international community has inadvertently contributed to this situation but also holds the key to its reversal.

Introduction

The present impasse in the Israeli–Palestinian peace process and its failure to establish an independent viable Palestinian state, as stipulated by the 2003 internationally endorsed Road Map for Peace in the Middle East, have made the prospects for a two-state solution increasingly bleak. As a result, a growing number of scholars and political activists have been calling for a one-state solution in all of Palestine, inclusive of Jewish Israelis and Palestinians, as an alternative (Abunimeh 2006; Bisharat 2010; Benvenisti 2007; Siegman 2010; Farsakh 2007; Makdisi 2008; Sussman 2004; Tilley 2005). Resuscitating an old idea proposed first by Judas Magnus and Brit Shalom in the 1920s and reformulated by the PLO in 1971, the present day advocates of the one-state solution argue that the time is finally ripe to campaign for it again. They maintain that Israel's expansion of settlements in the West Bank, its transformation of Palestinian land into *de facto* Bantustans cut off from one another by a 709 km long separation wall and over a hundred checkpoints, and its siege and war on the Gaza Strip in 2008 and 2012 have created an apartheid reality rather than set the stage for viable independence (Farsakh 2005a). Within the Palestinian community, a number of politicians have threatened to reconsider the one-state option if Israel fails to give the Palestinians a viable Palestinian State.[1]

The aim of this paper is to analyse the economic underpinnings of the one-state solution in Israel/Palestine. It seeks to fill a lacuna in the growing literature on the one-state solution which so far has focused on its moral and political dimensions without addressing the extent to which economic dynamics will impinge on its ability to come into being. The paper argues that economic realities in Israel/Palestine since 1993, while proving the demise of the two-state solution, have not shifted the power imbalances in favor of a more egalitarian one-state alternative. This is largely because Israel has been able to dispense with the Palestinians, both economically and politically. As the analysis of the past 20 years will show, Israel has succeeded in separating economically from the Palestinians while keeping them under its economic and territorial domination. It has been able to do so without paying any political or economic penalties. The international community has inadvertently contributed to this situation but also holds the key to its reversal.

The first part of the paper reviews the economic premises of the various solutions proposed to the Arab-Israeli conflict since 1947. It will show how the idea of economic union has been, paradoxically, at the heart of the conceptual frameworks proposed for resolving the conflict through territorial separation. The second part analyses how Israeli-Palestinian economic relations form part of a single economic space controlled by Israel, rather than provide the basis for two separate national entities. It also explains the means by which the Oslo peace process changed the pattern of structural dependencies between Israelis and Palestinians in ways that emboldened Israel to become less reliant on Palestinian labour and markets. Finally, the paper assesses the role of globalisation and the international community in explaining the limited economic prospects for a democratic one-state solution and what alternatives are possible to change the continuing power imbalances.

1 See Saeb Erekat, Palestinian Chief Negotiator, quoted in 'Biden Visits Mideast to Push Peace Talks', *New York Times*, 9 March 2010 and Amira Haas, 'Senior Fatah officials call for single democratic state, not two-state solution', *Haaretz*, 17 March 2013.

The Economic Premises of the One-State Solution

The economic case for the one-state solution has been based on the premise that it can provide more justice and economic prosperity to the people living in Israel/Palestine. Although the concept of economic justice can be nebulous, it is generally understood to mean an equitable distribution of goods and resources according to pre-agreed criteria of rights. However, to talk about the notion of economic justice in the Israeli-Palestinian context is particularly difficult, given that we do not have clear criteria on which to base our discussion of economic rights for two peoples fighting over the same piece of land: are we talking about nations or about citizens, about resources confiscated or owned, about consumer or producers, workers or owners? It is all the more challenging given the difficulty of defining the boundaries and content of each of the Palestinian and Israeli economies. The two-state solution demarcates the boundaries of the former within the West Bank and Gaza Strip (WBGS). From a Palestinian nationalist point of view, though, this definition is problematic as it excludes Palestinian citizens of Israel as well as refugees outside Palestine. The Israeli economy, on the other hand, is usually understood to include all economic activities undertaken by Israelis, be they Jews or non-Jews, settlers in the occupied territories or citizens living inside 1948 boundaries. This too is problematic as it violates national boundaries and obfuscates how facts on the ground have eroded their economic and political validity.

Indeed, the porosity of economic boundaries between Israelis and Palestinians has led various scholars to argue that there is effectively one single economy in Israel/Palestine, a colonial one dominated by the Jewish state (Farsakh 2008, Sayigh 1986). Defenders of the two-state solution have claimed that only separation from the Israeli economy, through the establishment of a Palestinian state, would end this colonisation and ensure sustainable economic prosperity to the Palestinians. From their perspective, economic justice would entail separating the West Bank and Gaza Strip from Israel, which stalled its development and its own domestic sources of growth (World Bank 1993, Roy 1997).[2] It would mean ensuring equal access to material and social resources to two sovereign national entities, as well as redressing economic inequalities between them through the establishment of a compensation fund and enhancing investment in the disadvantaged economy. In a one-state solution, on the other hand, economic justice would entail giving equal economic opportunities to all citizens, irrespective of their ethnic, class or religious

2 In 1993, the Israeli GDP ($52,500 billion) was 12 times the size of the Palestinian economy ($3.2 billion) and its per capita income stood at $11,200 compared with $1,200 in WBGS in 1993 (Farsakh 2005b: 42).

background. The State would compensate disadvantaged members by giving them preferential access to resources and empowering them to compete equally with other citizens.

The question of economic separation or integration is key to understanding the viability of any political solution to the Israeli–Palestinian conflict, be it a two-state or one-state solution, as much as to the economic prosperity of Israelis and Palestinians. It is intrinsically tied to the nature of the political, *sic* territorial, solution proposed to the conflict. Interestingly enough, the international consensus has maintained, ever since 1947, that the optimal solution to the Israeli-Palestinian conflict is one based on *political, sic* territorial, *separation* but with *economic integration* between the two peoples. Indeed, UNGA Resolution 181 in 1947, which enshrined the principle of partition of Palestine into two separate states, a Jewish and an Arab envisaged an *economic union* between them. The underlying logic behind such an economic union is its ability to enhance complementarities between the historically labour intensive Palestinian sector and the more capital-intensive Jewish sectors.[3] It would thereby generate greater welfare and profitability to consumers and producers, as well as foster peace between the two peoples.[4] The UN partition plan's customs union proposal envisaged a single common tariff policy, a system of currencies with a common foreign exchange rate, and joint economic initiatives in areas such as irrigation, energy and transport. While this union gave each state the right to have its own central bank, control its own fiscal and credit policy, and conduct its international trade and financial operation, it sought to foster economic links between the two states by ensuring free movement of goods, capital and labour between them and allowing them to optimise on their complementarities. The partition plan also envisaged the formation of a Joint Economic Board at the head of the proposed Economic Union that would consist of equal representatives from both countries as well as from foreign countries. The responsibility of this board was to collect revenues from customs and other services and to allocate them equitably between the two states. The responsibility of the foreign representatives was to ensure effective implementation of the union and to settle disputes when they arose.[5]

3 Kimmerling (1983) and Metzer (1998) have shown that the Jewish sector in Palestine between 1926 and 1948 was more capital intensive then the mainly agricultural Palestinian economy.

4 A similar argument was used to explain the case for integrating poorer countries in Europe (e.g. Portugal and Greece) into the European Union in the 1980s.

5 United National General Assembly Resolution 181, at http://domino.un.org/unispal.nsf/0/7f0af2bd897689b785256c330061d253

Israeli–Palestinian Economic Relations: 1948–1993

The economics of the Israeli–Palestinian conflict have indeed been based on a dynamics of economic integration ever since 1948. However, it is a dynamic created through colonial domination, rather than territorial partition. Indeed, one of the strongest arguments for the one-state solution is based on the fact that Israel created, after the 1967 war, a single economic space between the river and the sea. This single economy, or de facto customs union, has been created by the Israeli military and state, not negotiated between two national groups. It is dominated by an Israeli, dynamic capital-intensive, sector controlling an enclaved Palestinian sector inside the 1948 borders, and exploiting a labour-exporting dependent West Bank and Gaza Strip.

In so far as Palestinian citizens of Israel are concerned, Israel has dispossessed them of their land, put them under military rule until 1966 and nationalised all industrial and agricultural resources. Despite giving them citizenship in 1966, the Israeli state limited their access to capital and any autonomous economic development. Palestinian citizens of Israel rather became a source of cheap labour for Israeli capital and a market for Israeli produce. They predominated in low skilled jobs, and concentrated in the construction and agricultural sectors, which absorbed 45 per cent of the Palestinian employed force in 1973. By 2008, only 6 percent of the Palestinian workforce living inside Israel were involved in business activities compared to 14 percent among Jews: (Rivlin 2011: 199). Only 2 percent of Arabs were in high tech jobs although they formed 10 percent of Israel's engineering graduates. Moreover, the average household income of Palestinian citizens of Israel remained half the Israeli national average. Unemployment among Palestinian citizens of Israel in 2008 was 18.5 percent higher than among Jews, and 58 percent were defined as poor compared with 15.2 percent among Jews (Rivlin 2011: 198–202). By 2013, Palestinian citizens of Israel faced over 50 laws discriminating against them and their access to less than 3.5 percent of the land (Adalah 2011).

After the 1967 war, Israel incorporated the West Bank and Gaza Strip into its economic space by imposing what some described as a one-sided customs union (Hamed and Shaban 1993). This imposed integration allowed the free movement of Palestinian labour into Israel and of Israeli goods into Palestinian areas, while preventing Israeli capital investment in the occupied territories. Israel became the destination for 70 per cent of Palestinian exports from the West Bank and Gaza. It was also the source of 90 per cent of imports going into the WBGS. The WBGS became the third largest market for Israel after the EU and the USA between 1967 and 1990.

Israeli policy eradicated the territorial base of any Palestinian economy by confiscating and directly appropriating 38 per cent of the West Bank land, building over 122 settlements between 1972 and 1990 and forbidding Palestinians from building industries or registering their lands and deeds. The Israeli military occupation helped transform the economy of the West Bank and Gaza from an agriculturally based one into a service oriented, labour-exporting economy. Industry represented less than 8 percent of WBGS GDP in 1991, down from 12 per cent in 1970, compared with 28 percent in Israel. Meanwhile, 40 per cent of Palestinian workers from Gaza and up to 33 per cent of those from the West Bank were employed in Israel between 1978 and 1988, mainly in low skilled construction and agricultural jobs. This structural dependency helped finance the Palestinian trade deficit with Israel (since workers' wages paid for Israeli goods flooding the local markets), estimated at 44 percent of WBGS GDP (Farsakh 2005b, World Bank 1993).

The Jewish sector of this single economy, created since 1948 and expanded since 1967, has been buoyant and industrial. It has been dominated by the Israeli military and a nationalist corporatist state. The military generated 8–25 per cent of Israel's GDP and employed 6–12 per cent of the Jewish labour force between 1948 and 1990.[6] The Histadrut, the Jewish Federation of Workers, together with over 160 public enterprises generated up to 30 per cent of Israel's GDP in the 1970s. Up until the early 1990s, the Histadrut was the major employer for Israeli workers, an important banker, main pension and health provider and insurer. Its industrial holding companies, such as Koor and Solel Boneh, were key to Israel's industrial development and the provision of well paying and secure jobs to Israeli-Jewish workers. Although it hired some workers from the West Bank and Gaza, the Histradrut did not provide them with the same benefits given to Jewish workers. The net daily income of a WBGS worker in Israel in unskilled occupations remained 30–17 percent lower than that of a Jewish worker doing the same job in agriculture and construction in the 1970s and 1980s (Farsakh 2005b: 123). While the hyperinflation of the late 1970s dealt a blow to the Israeli economy and brought about a harsh stabilisation period, Israeli workers still earned, on average, double what Palestinian citizens earned throughout the 1980s.

Since 1948, then, Israeli-Palestinian economic relations have been based on dispossession, domination and exploitation within a single territorial space controlled by the Jewish state. Palestinians needed the Israeli labour market to earn an income, albeit one-tenth to half the average Jewish wage. The Jewish sector meanwhile became dependent on the Palestinian sector as the third market for its goods as well as a source of income

6 Calculated from figures provide by Rivlin (2011: 120–124).

and cheap labour. This custom union arrangement that Israel imposed on the West Bank and Gaza enabled it to collect and appropriate tariff revenues on goods destined to Palestinian areas, which amounted to approximately 12–21 per cent of WBGS GNP between 1970 and 1987 (Hamed and Shaban 1993: 142). It is estimated that between 1970 and 2008 Israel accrued $16bn from the exploitation of Palestinian labour, markets and water resources. This is the equivalent to 10 percent of Israel's GDP in 2008 (Hever 2010: 62). Most importantly, Israeli capital in the construction sector came to rely on Palestinian labour. Although at the macro level, workers from the West Bank and Gaza represented less than 9 per cent of the employed force in Israel in the 1980s, they provided 30–45 percent of all those working in the Israeli construction and agricultural sectors. Together with Palestinian citizens of Israel, they formed between 48 and 70 percent of the labour force in Israeli construction between 1975 and 1992. This sector represents 9–12 per cent of Israel's GDP and is responsible for one third of investment in fixed capital formation since 1970 (Farsakh 2005b: 124–127). Above all, it is key to Israel's Zionist ideology of settlement.

The Oslo Peace Process: Restructuring Economic Domination

The Oslo peace accords between Israel and the Palestinians ushered in during 1993 brought hopes that it could end Palestinian dependency on Israel as well as allow Israel to liberalise and integrate in the global economy. Politically, they set the stage for separating Palestinians from Israelis in the West Bank and Gaza, but without promising the implementation of the two-state solution or the creation of a Palestinian state. Economically, the Oslo peace process sought to foster Palestinian economic growth, but without separating the Palestinian economy in the West Bank and Gaza Strip from Israel. Like UNGA Resolution 181, it relied on a peace formula that maintained that economic integration is beneficial for political separation.

The preamble to the Interim Agreement's Protocol on Economic Relations promises to 'lay the groundwork for strengthening the economic base of the Palestinian side and for exercising its right of economic decision making in accordance with its own development plans and priorities'. This was to be attained by reforming, rather than ending, the custom union imposed between Israel and the WBGS in 1967.[7] Oslo's

7 The Palestinian side wanted to have a free trade agreement (FTA) rather than a customs union agreement. However Israel rejected this as a FTA would have led to a *de facto* recognition of borders, a matter both parties agreed to settle in the final status negotiations.

reformed custom union allowed the Palestinians to trade directly with Arab and foreign countries for a limited list of goods. It also gave the Palestinians the right to decide on their economic priorities, to determine the nature of their employment, industrial and agricultural policies, as well as to tax and invest in areas under the PNA's control. Furthermore, it gave the PNA some leeway in monetary policy, allowing them to attract foreign capital, for the first time since 1993. However, unlike the UN partition plan economic proposal, Oslo's economic protocol did not allow the Palestinians to have their own currency or their own independent trade policy. Israeli tax rates (both direct and indirect), as well as Israeli standards and import regulations, remained in effect. Israel, though, agreed to remit to the Palestinian economy VAT and customs taxes collected on goods specifically destined to the WBGS, something it never did before 1994. These remittances were based on a micro rather than macro formula, which meant that they were prone to underestimate the amount of trade and VAT collected. A Joint Economic Committee was created (JEC) to deal with economic matters between the two parties. However, unlike the partition plan's proposal in 1947, this committee did not have foreign representatives who could monitor its work, ensure a fair and equitable calculation and distribution of customs revenues, or arbitrate in case of conflict. The economic protocol did not guarantee freedom of movements of goods and services into Israel nor end its military occupation.

Growth vs. Stagnation

Shimon Perez argued that the Oslo peace process ushered a 'New Middle East' that would allow the free flow of capital and labour and thereby cause standards of living to rise and violence to fall (Perez 1993:23). However 20 years of the peace process did not bring economic viability or justice to both parties. It rather enabled Israel to grow economically more prosperous and independent of the Palestinians while rendering the latter poorer and aid dependent.

The contrast between Israeli and Palestinian economic performance under the Oslo peace process could not be more revealing. Between 1993 and 2000, the Israeli GDP more than doubled, increasing from $61 billion to over $120 billion and per capita income increased from $12,000 to $19,000, despite the absorption of over 620,000 new immigrants from the former Soviet Union over the same period. Although Israel's GDP fell by 6.2 per cent per year on average between 2000 and 2003, after 2004 it grew by over 4 percent per annum on average, making Israel the 5th fastest growing economy among OECD countries. Its GDP rose to $230 billion in 2011 and per capita was at $31,000 (ICBS 2012: 2–4).

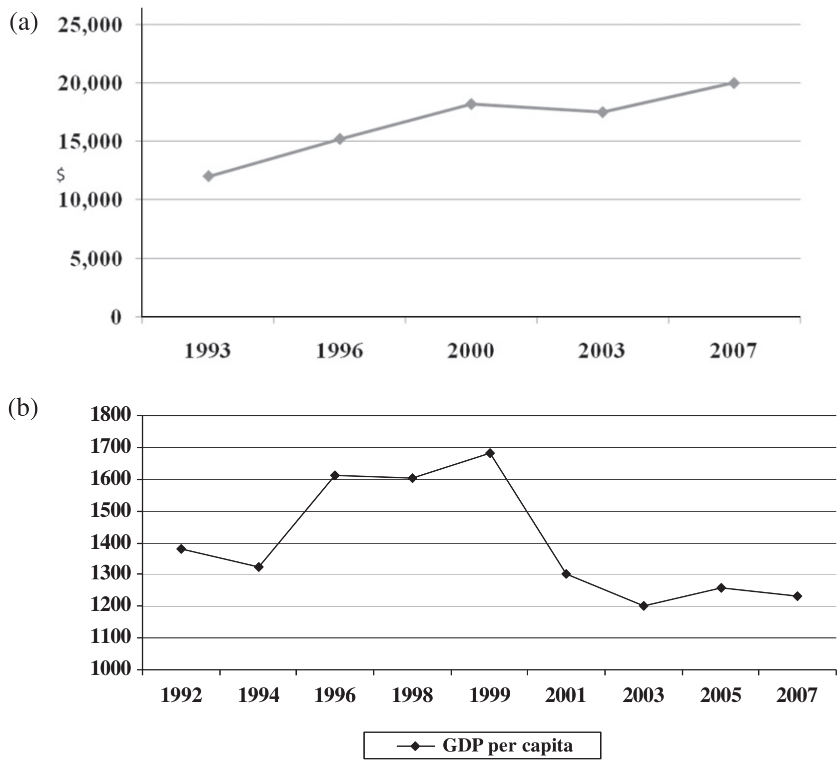

Figure 1. (a) Real Israeli GDP Per Capita, 1993–2007. (b) Real Per Capita GDP in the West Bank and Gaza Strip, 1992–2007.
Source: World Bank, *World Development Indicators*, database.
Botmeh (2010), *The State of the Palestinian Economy.*

The Palestinian economy, by contrast, saw its growth fluctuate and on average stagnate. Between 1992 and 1996 Palestinian GDP per capita income fell by 18 per cent, and although it then rose until 1999, it remained of the order of $1,683. It remained at less than a tenth of Israeli GDP per capita and increasingly volatile. Real GDP per capita of $1,250 in 2007 was 30 per cent lower than its level in 1999 (World Bank 2008: 7). It was 9 per cent lower than its level in 1992 (see Figures 1a and 1b). Moreover, the economies of the West Bank and Gaza Strip started sharply to diverge as real GNI (Gross National Income) per capita in the Gaza Strip was 30 per cent lower its levels in the West Bank in 1999.

Palestinian social indicators also worsened after 1993. Poverty, defined as those earning less than $2.1 a day, affected 46 per cent of the population in Gaza in 1998 compared with 15.4 per cent of those in West Bank. By 2008 it represented 67 per cent of the population, compared to 18% in

1992. Since the siege of Gaza in 2006, over 70 per cent of the population has been living under the poverty line, 30 percent of whom are food-insecure, and unemployment was over 45 per cent compared with 20 percent in the West Bank and under 8 percent in Israel (World Bank 2008: 7–9, Bank of Israel 2012:). Poverty in Israel, defined as a person earning less than $8 a day, was recorded at 22 per cent of the total population in 2009 (OECD 2009:7).

Meanwhile, the structure of economic dependency between Israel and the Palestinians started to change with the Oslo peace process. The WBGS did not see Israeli capital and foreign direct investment come its way, as was originally expected. Despite all the important steps that the Palestinian economy took to absorb its labour force, creating over 162,000 new jobs in the period between 1995 and 2000, it continued to need the Israeli labour market to keep unemployment down.[8] However, Israel has decided to sever its labour links with the Palestinian economy, especially with Gaza since 1993, i.e. 12 years before the actual disengagement from the Strip in 2005. Already since 1994, the flow of Gaza workers was curtailed to less than 29,000 workers. They came to represent less than 15 per cent of the total employed Gazans in the 1990s, and were stopped completely after the siege imposed on the Strip after 2006. West Bank workers, while still able to access the Israeli market in the 1990s, could not count on it. Nearly 22 per cent of West Bank employees worked in the Israeli economy in the 1990s, but their share has dropped to less than 12.5 per cent since 2001 (Farsakh 2005b: 210). In 2013 nearly 80,000 West Bankers, or 11 percent of the labour force, were working in Israeli markets, mainly in the settlements (see Figure 2).

By 2013, the economic space between the river and the sea was composed of 3 divergent but militarily tied economic sectors: a besieged Gaza Strip, an anemic economy in the West Bank and a buoyant economy in Israel. This divergent economic performance is the result of three main factors that the Oslo peace process institutionalised and which remodeled, rather than ended, Jewish domination within a single economic and territorial space. These include the increase militarisation of the conflict and the nature of Oslo's customs union arrangement that restructured Palestinian dependence on Israel, without giving it any leverage *vis-a-vis* the Jewish sector. They are also bound up with Israel's successful integration into the global economy. These three factors help explain in turn why the economic pressure for an equitable one-state solution remains weak.

8 The Palestinian labour force has been growing at an annual rate of 4.9 per cent since 2002. (Farsakh 2005b: 206–204)

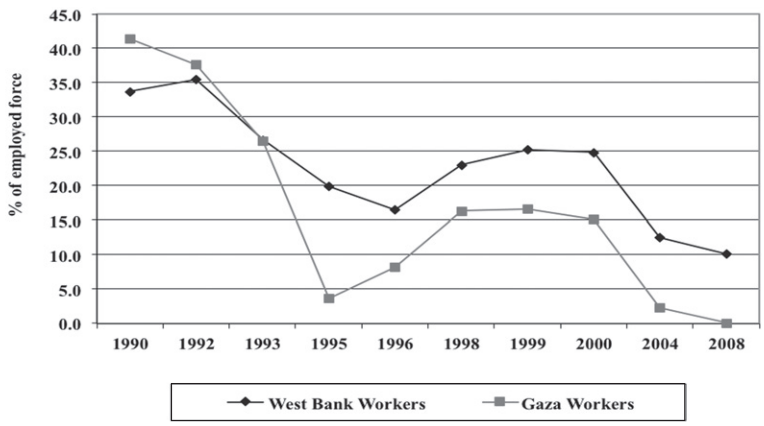

Figure 2. Palestinian workers employed in the Israeli labour market as a percentage of total Palestinian employed labour force.
Source: PCBS, *Palestinian Labour Surveys*, various years.

Increased Militarisation

The increased militarisation of the conflict since Oslo is best exemplified by the closure and permit policies that the 1995 Interim Agreement institutionalised[9] Imposed first in 1990, closures became an elaborate and frequent military tool that fragmented Palestinian land and severed it from Israeli and international markets. Israel imposed 443 days of closure on the Palestinian territories between 1994 and 1998 that brought to a halt all economic activity for nearly 3 months a year (Farsakh 2005b: 148). After the al-Aqsa Intifada in fall 2000, closures became permanent, causing unemployment and poverty to rise exponentially.

The closures' economic effects were compounded by the policy of checkpoints that consolidated the fragmentation of the West Bank and Gaza. These were part and parcel of Oslo's principle of phased disengagement that allowed Israel to remain in direct control of over 56 percent of the West Bank and 20 percent of Gaza by 2000 (area C). The Oslo Interim Agreement kept Israel in control of the West Bank and Gaza's exit points and their trade link to the outside world as well as between Palestinian areas and with Israel. Israel continued to have the right to intervene in areas A and B whenever it deemed it necessary, as it did in 2002 and 2003. At the height of the al-Aqsa Intifada, 456 checkpoints were implemented in the West Bank, cutting cities and villages from one another as well as from Gaza. Still in 2012, there were 58 permanent

9 See articles IX and XI of the Protocol on Redeployment and article 11.2 of the Protocol on Civil Affairs of the Interim Agreement. These gave to Israel alone the right to issue permits and control exit and entry points into declared Israeli areas.

checkpoints inside the West Bank and 256 flying checkpoints, thereby institutionalising the territorial fragmentation of the West Bank.[10]

The growth of illegal Israeli settlements since 1993 has been another component of the increased militarisation of the conflict. Israel built over 102 new settlement outposts since 1993, further depriving Palestinians of their land and water resources. The number of Israeli houses in the settlements has expanded at a rate of 4–6 per cent per annum since 1993 and the settler population doubled from 242,000 in 1993 to 520,000 in 2012 (including East Jerusalem) (FMEP 2013). These settlers and their products were not affected by Israeli checkpoints and closure policy in the West Bank, for they are fully integrated in the Israeli economy beyond the Green Line. While coming at an estimated cost of $15 bn in 2008 prices (Rivlin 2011:150), settlement construction has brought major economic and political leverage not only to the Israeli military but also to various interest groups, such as settlement building contractors, high tech security and industrial enterprises in the settlement industrial zones, as well as private security companies which man most checkpoint terminals in the West Bank and along Gaza Strip's borders. Settlements exports represented nearly 20 percent of all Israeli exports to the EU, amounting to a sum of nearly $2 billion, which amounts to third of the Palestinian GDP in 2008 (Profundo Economic Research 2009: 7).

Israel's violent military response to the al-Aqsa Intifada reduced the economic leverage that Palestinians tried, through their resistance, to gain over the Jewish sector. Although the wave of suicide bombings were effective in sabotaging Israeli tourism and foreign direct investment, causing Israeli GDP to fall by over 6 percent between 2001 and 2003,[11] by 2004 the Israeli military was able to seal the Jewish economy from Palestinian resistance. The Israeli military increased its budget by 12.5 percent between 2001 and 2004, intensified its closure policies, and started building a 709 km separation barrier at an estimated cost of $3.2 bn (Swirski 2008: 18). By 2013, 59% of the wall had been built, cutting Palestinian areas into ten main population enclaves separated from one another by cumbersome checkpoint terminals.[12] Upon completion the wall will absorb 11 per cent of the West Bank into Israel and all of it water resources. The World Bank (2008a:8) has described Israeli security

10 Figures taken from B'Tselem - The Israeli Information Center for Human Rights in the Occupied Territories at http://www.btselem.org/freedom_of_movement/checkpoints_and_forbidden_roads. Last consulted June 1, 2013.

11 Bank of Israel (2012) *Annual Report 2012*, Table 1.1.

12 The population enclaves include Jenin, Qalqilia, Tulkarem, Nablus, Tobas area, Jericho, Ramallah, Jerusalem, Bethlehem, Hebron. Btselem, '10 years to the Second Intifada', Press Release, Tel Aviv, at http://www.btselem.org/English/Press_Releases/20100927.asp

policies as not simply security restrictions but economic restrictions, since they impose restriction on economies of scale, restriction on access to resources and restriction on investment prospects and potentials. Their effectiveness explains the ability of the Israeli economy to grow steadily after 2004, despite a fall of 1.2 percent in GDP between 2007 and 2008 that has been attributed to the international financial crisis, not the war on Gaza.

Illusion of economic autonomy

The autonomy that Oslo promised the Palestinians did not bring them closer to sovereignty or improve their economic leverage *vis-a-vis* Israel. Trade with third countries, which the custom union agreement enshrined in Oslo's Economic Protocol, did not foster exports because of the closure policies and competition from cheaper produce from Arab countries. Trade with the EU did not increase as it was already available via Israel and remained dependent on Israeli trade regulations and restrictions, which often harmed previous Palestinian growing industries. Palestinians could not increase the size of their exports to Israel because of Israeli checkpoint policies. Still by 2008, Israel remained the market for 90 per cent of Palestinian exports and 70 per cent of imports (Kanafani et al 1998, World Bank 2008b:15).

In so far as Palestinian labour is concerned, the Oslo agreement did not promise to protect its access to Israel, despite its importance to Palestinian income and the Israeli construction sector. Neither did it facilitate the flow of foreign capital to employ Palestinian labour in the WBGS. Israel rather resorted to importing nearly 200,000 foreign workers who replaced Palestinians unable to cross the checkpoints. Meanwhile, the Israeli military and its civil administration retreated from being the direct manager of the Palestinian economy and became the gatekeeper of Palestinian finance and access to the world. Customs revenues, collected by the Israeli Ministry of Finance on goods imported to the Palestinian economy, became the most important source of finance for the Palestinian authority. They represented 70 per cent of the PA's revenues and up to 20 per cent of WBGS GNP in the 1990s (Naqib 1996; World Bank 2002). Israel often retained these revenues for political leverage, such as in 1996 or between 2001 and 2008, causing havoc in the Palestinian Authority finances.

As a result, the economy of the West Bank and Gaza became increasingly dependent on aid and an internationally financed public sector. The Palestinian National Authority sought to encourage industrial and financial development, but most of the investment went into housing and mortgage markets since these were the most profitable. The public sector became an important employer, rather than simply facilitator of private sector development. It absorbed up to 30 percent of total employment in Gaza and 18 percent of the employed force in the West Bank between 1995 and 2005. It thereby replaced the Israeli labour market as an employment outlet. Yet in doing so, the public sector reduced labour efficiency and endangered its fiscal stability. This stability was from the start threatened by its dependence on Israeli transfer of VAT and custom revenues. The Palestinian economy soon became dependent on international aid, a situation unfamiliar to it before 1993. Over $528 million in aid per year were given to the West Bank and Gaza between 1995 and 2000. This increased to over $1.1 billion per year since 2001, accounting for 25 per cent of Palestinian GDP (UNCTAD 2006: 37). This aid financed the PA's budget and its 172,000 employees in the police force and public administration.

The Cure of Globalisation

Since 1993, Israel has been able to integrate into the world economy, thereby reducing further its reliance on the Palestinians. Israeli exports have expanded at more than six per cent per annum since 1994, more than quadrupling in size from $15 billion in 1994 to over $72 billion in 2008 (Rivlin 2011: 260). They reached new countries, such as India and China, which up until 1993 boycotted Israel in solidarity with the Palestinian struggle for self-determination. These two Asian giants each absorbed over four per cent of Israeli exports by 2008, surpassing the UK as a trading partner. By 2012 Israeli exports to Asia had grown to 25 percent of total exports, with China's share growing to 8.9 percent. Trade with the EU and USA also expanded and changed in composition towards high-tech and security industries. They each absorbed 30 per cent of Israeli exports[13] Moreover, Israel became a full member of the OECD in 2010, a sign of recognition of its position as a fully developed and industrial country. It is the only non-European country allowed to sit on the EU Research and Developments Funds.

Although the EU signed a FTA agreement with the PNA, and various Asian countries attempted to foster trade links with the West Bank and Gaza, the Palestinian trade with non Israeli partners remain limited because of the unpredictability and high transaction costs imposed by the Israeli closure and checkpoint policies. Whatever trade took place, it was often mediated via Israeli middlemen, who reaped significant rent. Palestinian trade deficit with Israel remained of the order of two billion dollars, or approximately 34 per cent of Palestinian GNI (World Bank

13 Israeli Ministry of Trade, *Israeli Economy at a Glance*, 2010 (Tel Aviv): 3–7,

2008b: 6). Israel has recorded a balance of payment surplus since 2003 (ICBS 2012).

Israel's manufacturing sector also grew and diversified away from labour-intensive goods and into high tech manufacturing as well as security related products. This high-tech sector has grown at more than 7 per cent per annum since 1993. It accounted for 65 percent of the increase in the number of persons employed in industry, and nearly 80 percent of the increase industrial production growth between 2004 and 2010 (FOI 2011:16). Since 2003, it accounted for over 27 percent of Israeli exports and together with electronics and other industrial goods formed 80 percent of all exports.[14]

This growth was helped by the development of the military industry in the aftermath of Oslo and the al-Aqsa Intifada. Israeli defense spending continues to represent over 8 percent of the country's GDP, higher than the US (5 percent) or neighboring Egypt (2.2 percent). The military employed 20 percent of the industrial workforce in 1985, and up to 50 percent of Israel's scientists and engineers in 2010 (Rivlin 2011: 123–131). Israel's defense sales directory advertised 216 companies in 2008, up from 180 in 1988. Many of the major private high-tech companies have grown out of the military, which has provided them with a skilled labour force and managers from the core of retired generals.[15]

Moreover, the influx of foreign direct investment helped restructure and globalise Israel's financial sector. Between 1993 and 2000, a total of $22 billion came in FDI into Israel, mostly in the high-tech sector. The share of start-ups in Israel' growing GDP jumped from zero per cent in 1996 to 3 percent in 2000, higher than in the US where it stood at 0.7 percent (Zilberfarb 2006: 232). Currently there are more than 100 Israeli companies trading in the US NASDAQ. Since 1995 international companies, for a total of $25 billion dollars, have purchased over 150 high-tech companies. Venture capital industry has also developed, investing in local high-tech and security sector. The business sector grew at a 2 percent higher rate than the public sector, at 7.6 per cent per annum between 1990 and 1995, and by more than 5 per cent since 2003, becoming the main force pushing GDP (ICBS 2012: 21). The number of public owned companies in Israel dropped from 160 in 1985 to less than 100 in 2002, and many of the social benefits provided two decades earlier by the Histadrut have been dismantled to improve the growth of the private sector and foreign investment.

14 Israeli Ministry of Trade, *Israeli Economy at a Glance*, 2010, Tel Aviv, p. q5.

15 DIC, Israel's largest private holding company, cooperates closely with the Ministry of Defense. Employees of Israel Aircraft Industries (IAI), Israel's largest industrial company, set up their own subcontracted security company that grew to be independent and listed in Israel's lucrative and expanding stock exchange (Rivlin 2011: 132).

The Palestinian economy, meanwhile, failed to rely on global trade. It rather became dependent on international aid. Between 1994 and 2008 a total of $15.5 billion were disbursed in aid for the Palestinian economy. Its share in GNI increased from 14 per cent in 1994 to over 49 per cent in 2008 (UNCTAD 2009: 12). However, instead of becoming a vehicle for enhancing growth, aid became a means to finance over 60–100 percent of the PA budget deficit and contain unemployment through unsustainable short-term projects. It is estimated that 71 per cent of the aid covers the trade deficit with Israel, thereby effectively benefiting Israel.[16] The reforms initiated by the Prime Minister Salam Fayyad, after the Hamas take over of Gaza in 2007, helped improve the fiscal and institutional performance of the West Bank economy. Yet it remained dependent on over $1.8 billion dollars of aid transferred by the international community in 2008 (World Bank 2010: 23).

The Gaza economy meanwhile has become impoverished and had to develop autarkic strategies for sustaining its population. Operation Cast Lead on Gaza, cost over 3–4 billion dollars in damage, rendered 56 percent of the population food insecure and over 48 per cent unemployed (UNCTAD 2009: 3). It led to a total halt of manufacturing and collapse of the formal private sector. It directed the Gazans towards trading with Egypt, through the construction of over 3000 underground tunnels. These helped ease economic hardship and induce a 15 percent increase in the Strip's GDP in 2010. This growth though was concentrated in construction, not in industry or export growth (World Bank 2010:7). It remains highly volatile and unsustainable (Pelham 2012).

Can economics bring about a one-state solution?

The developments of the past 20 years have shown that in Israel/Palestine there is one single economy, and one that is fundamentally colonial[17]. The Israeli sector is the strongest economically and the one determining the pace of growth and prospects of each of other economies, be it the West Bank or the Gaza Strip. Despite the international support to the notion of a Palestinian state and the PLO's upgrade to non-member state status at the UN in 2012, the economic prospects of Palestinian sovereignty in 2013 are far worse than in 1993. Israel's disengagement from the Gaza Strip in 2005 did not end its control of the Strip's airspace, sea and access to the outside world. The fact that its economic prospects are being increasingly tied to

16 Nikki Tillekens, 'Aid to the Palestinian and Israeli Economy', *Alternative Information Center*, 2010, at http://www.alternativenews.org/english/index.php/topics/economy-of-the-occupation/2878-aid-to-the-palestinians-and-the-israeli-economy

17 For further discussion on how Israeli occupation has been colonial in its structure, see Farsakh 2008 and 2009.

Egypt does not change the reality of Israel's domination over Palestinian land and people living between the river and the sea.

However, arguing that we are in a single economy does not mean that economic forces are pushing for a viable one-state solution. The development of the past 20 years created rather an apartheid reality (Farsakh 2005a). This apartheid structure, though, did not give the Palestinians any of the economic leverage that Black South Africans have had historically in their country. The trade-off between political recognition and economic prosperity embodied in the Oslo peace process proved to be highly unequal for the Palestinians. It enabled Israel to prosper and reduce its reliance on Palestinian labour while the latter became impoverished and dependent on international aid. Israel has proven its ability to shelter itself from Palestinian resistance with the construction of the separation barrier, checkpoints and *de facto* imprisonment of the Palestinian population in the name of defending its own security. Just as alarming is the international community's *de facto* acceptance of this situation.

This being said, the economic developments of the past 20 years have proved yet again the centrality of politics and law in any attempt to reach a viable solution in the region. The success of Israeli globalisation proves its growing dependency on the international community. This might prove to be its Achilles' heel. The argument for economic sanctions has never been more pronounced and its likely impact most effective. The Palestinian Civil Society Call for Boycott Divestment and Sanctions (BDS) against Israel, launched in 2005 and signed by over 170 local organisations and trade unions, is proving to be an effective tool to put pressure on Israel to end its colonial domination. Although it is agnostic on whether the aim of Palestinian peaceful resistance should be a one-state or two-state solution, the BDS movement is using economic tools to shift power imbalances on the ground. It targets settlements' products as well as Israeli companies and institutions, which profit from the occupation and/or discriminate against Palestinians inside Israel. In other words, it deals with Israel/Palestine as a single economic and political space that is colonised by the Israeli state.

The BDS movement is gaining ground internationally and is increasingly supported by academics and grassroots organisations (Barghouti 2011; Giora 2010). So far major supermarkets in Italy, the UK and Norway have announced their boycott of Israeli produce from the settlements. In 2004 the Presbyterian Church USA started divesting from corporations doing business in Israel, causing a major uproar in Israel and the US. Since then, Deutsche Bank, a global financial institution, as well as Norway State Pension Fund, Sweden's largest Pension Fund, Foersta, Holland's largest pension fund and Denmark's

Danske Bank divested from Elibit systems, an Israeli arms and a large high tech company which provides surveillance equipment for Israel's wall. As a result of sustained campaigning, Veolia, a French-Israeli consortium, withdrew from construction of a light rail project intended to connect Israeli settlements in the West Bank with occupied Jerusalem (Cook 2013). Because of the efforts of the campaign, Veolia has lost a number of lucrative contracts in the United Kingdom and France. Most recently, New Zealand's Superannuation Fund divested from a settlement construction company in 2012.

Academically and culturally, the BDS has also garnered growing international support in a far shorter time than the BDS campaign in South Africa during the apartheid era managed to generate (Barghouti 2011). In 2009, Hampshire College in the US divested from a half dozen companies profiting from Israel's occupation of the West Bank and Gaza. By 2013, over 18 student councils in universities in the US, Canada, Europe and South Africa have supported the call for BDS, including at the University of Berkley, Cambridge, Oslo, Toronto, Sidney and Johannesburg. Despite vehement attack by pro-Israel groups, various academic associations endorsed BDS, including the American Association of University Professors, US association for Asian American Studies, The Teachers Union in Ireland, the UK University and College Union. Over 60 universities worldwide organised an Israel apartheid week in 2011 compared with 3 in 2006. Moreover, a growing number of cultural and scientific figures openly called for boycott of Israel or cancelled visits to official events in Israel (e.g. Desmond Tutu, Ken Loach, Judith Butler, Richard Falk, Naomi Klein, Roger Waters, Nigel Kennedy, Vincenzo Consolo).[18]

While it is still early to assess the economic impact of sanctions on Israel, it has so far worried Israeli policy makers and their supporters who launched major campaigns to 'improve Israel's image in the world'.[19] So far, this has not stopped Steven Hawking, the world renowned physicist and cosmologist, to refuse to go to Israel in 2013 in support of the academic boycott. His endorsement of the BDS movement was met, for the first time, with some understanding, rather than outright condemnation, from major US media, including The Boston Globe and

18 The list of universities and companies that have endorsed or supported the call for BDS has been compiled by the author, based on data provided by Palestinian BDS National Committee and consulting www.bdsmovement.net.

19 Lara Friedman, American Peace For Now on Criticism of Israel and BDS - New Policy Language, at http://peacenow.org/entries/apn_on_criticism_of_israel_and_bds_-_new_policy_language

Thomas Friedman of the New York Times.[20] Such media coverage, particularly in the US, is indicative of the success of the BDS movement in moving to the centre of the debate over the conflict and the means to resist Israeli violation of Palestinian rights. During his UN speech in 2012, the PA Chairman, Mahmoud Abbas, officially endorsed the BDS as an official Palestinian policy, and called on the international community to follow suit so long as Israel refuses to adhere to its commitments (Farsakh 2012).

The BDS is not the only economic strategy that can seek to dismantle Israel's colonial project. The increasing cost of the occupation and the militarisation of the conflict is a source of concern to many Israelis. It is estimated that the annual cost of maintaining the occupation is \$6.8bn, which is the equivalent of 3 percent of Israel's GDP (Hever 2010:70).[21] These include settlements' subsidies and security costs, such as checkpoints, the wall and internal security in WBGS, but excluding the military defense expenses. Israeli supporters of the two-state solution have long argued that the occupation deprives Israelis of much needed investment in education, housing and work inside 1948. The popular unrest in Israel in July 2011, following the Arab spring in Egypt and Tunisia, has shown the magnitude of growing inequality in Israel that resulted from the government's neoliberal policies of global integration in the 1990s. The poverty rate in Israel increased from 15% in 1996 to 22% in 2008 and the number of new houses in the Tel Aviv area has dwindled while it grew by over 4% per annum in the settlements.[22] By 2010, 20 business families own 30 percent of business market shares in Israel, further exacerbating income inequality (OECD 2011). Although the July 2011 protestors did not mention directly the occupation, they highlight the growth of a youthful social movement concerned with equal rights. They are questioning all the investment that has been put in the security apparatus and settlements instead of being invested for the welfare of the average Israeli inside Israel.

Meanwhile, the international community needs to rethink its whole paradigm of assistance to the Palestinian people. So far, international aid has sustained the Israeli occupation indirectly rather than help end it. It has not enabled the Palestinian economy to stand on its own feet. Unless the international community puts pressure on Israel to implement

20 Editorial, 'Stephen Hawking Makes a Peaceful Protest', *Boston Globe*, 13 May 2013; Isabel Kirshner, 'Stephen Hawking Joins Boycott Against Israel', *New York Times*, 8 May 2013; Thomas Friedman, 'Israel Lives the Joseph Story', *New York Times*. 5 June 2013.

21 Hever estimates the cost of the occupation between 1970 and 2008 at 381 NIS billion (circa \$100 bn), taking into account growing rather than static costs. Swirski 2005 estimates the costs of occupation, including the costs of Palestinian resistance, at \$23 billion, i.e. 15–20% of Israeli GDP in 2000.

22 Calculated from the ICBS, *Statistical Abstract of Israel*, various years, Tables O/4 at http://www.cbs.gov.il/www/yarhon/o4_e.htm

the Road Map or abandon it altogether for a one-state solution, this taxpayers' money will continue to be wasted. This in turn requires a change of direction taken by the Palestinian leadership. So far this PA has not officially pushed for a one-state idea, but it is has not excluded it. In April 2013 a number of Fatah officials called on the PA to endorse the one-state solution. Mahmoud Abbas, during his UN speech at the UN in 2012 clearly stated that the door on the two-state solution is closing (Farsakh 2012).

Conclusion

The economic rationale for such a one state solution is strong but the economic forces pushing it remain weak. The one-state solution might be indeed morally and politically the best solution ensuring justice and economic viability for all those living in Israel/Palestine. However, before the Palestinian national movement redefines itself in view of the failure of the Oslo peace process to protect the minimum of Palestinian rights, it is unlikely for the one-state idea to move much forward. The economic prospects for the one-state idea can only be strengthened by the Palestinian leadership adopting it, defining its new political platform and using the BDS campaign as a strategy, among others, in order to attain it. The international community has also a central role to play in this regard by upholding Palestinian rights and holding Israel accountable to international law.

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