Economic Peace and the Israeli-Palestinian Conflict

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Abstract

"COMMERCE INVADES WHEN ARMIES FEAR TO TREAD"

The Israeli Palestinian conflict has used economic integration as a way of addressing the solution to peace. Historically; peace was achieved through using political gains to progress economic development. However, economic integration between the two opposing sides of Israel and Palestine has always served to highlight the asymmetry of power that exists. Applying the findings of economic peace theory to the Palestinian-Israeli conflict creates a contradiction between theory and reality. During times of economic integration, violence was still ongoing. This paper will attempt to explain such failures of economic peace from the 1967 war to the Paris Protocol and what lies ahead. Throughout the history of the Palestinian Israeli Conflict, economics has always been a vital part of any proposed solution. However, each proposed plan had similar dynamics in terms of economic policies. It seems to revolve around Israel remaining in control of macroeconomics in Palestine. As a result, Palestinian GDP suffered, which led to increased frustration from their side. With peace plans ongoing in the current political climate, it is crucial to highlight the past failures of economic policies of the conflict and explore new and creative recommendations. The first part will lay the theoretical framework of economic peace theory. It will define the supporting and opposing arguments that past researchers have made. Part two of the paper will highlight the limitations and failures of the economic peace policies imposed by Israel after the 1967 war as well as the joint Paris Protocol during the Oslo Accords. Finally, part three will give recommendations on the current economic prospects of peace.

Introduction

Economic Peace Theory articulates the notion that integrated and increased positive economic conditions between two countries can stimulate peace. Thus, the theory suggests that economic interdependence promotes peace and prevents conflicts. Economic interdependence is conducive to peace because national economic interests can be generated by economic cooperation between private actors. (Bijaoui 2014: 4).

Perhaps the most conventional explanation for economic peace is that it creates mutual value between two countries which then leaves them in a cost benefit analyses where destroying these economic benefits becomes more costly than engaging in conflict. Liberals argue that economic trade represents a good foundation on which to build agreements on more sensitive issues such as security and borders. Research conducted by Dorussen highlights that trade can create peace where there are conditions for minimal barriers to trade with few states in the trading system. (Dorussen,1995).

Realists would argue that the role of economics will be rather limited due to the residing memories of the conflict between two enemies. As a result, trust is less likely to exist with two societies and little familiarity is likely to be found. Realists would argue that peace is achievable through reconciliation between major political and security obstacles. In the case of South Africa, the defining element of their reconciliation was overcoming the political challenges. Economic cooperation, however, did not play a substantial role. (Press-Barnathan 2006: 262).

Another paradigm of the Economic Peace Theory is the economic involvement of the international community. Researchers, such as David Byrne, argue that economic intervention from outside parties promotes peace. For example, in the context of the Northern Ireland Conflict many studies found economic development not sufficient enough to reach peace. “Sustainable economic development on its own is not a panacea to de-escalate conflict and transform relationships" (Byrne and Ayulo, 1998). However, what played a big role in here was the external economic intervention by the European Union. Targeted external economic assistance may be an important tool in post-accord peace-building and reconciliation (Adam, Collier, & Davies, 2008; Byrne, et al., 2009; Byrne & Irvin, 2001).

The Root of the Beginnings 1967

Going back to the root of economic integration attempts between Israel and the Occupied Territories takes us to the end of the 1967 war. Israel won massively, gaining control of the Golan Heights, West Bank, East Jerusalem and Gaza. Discussions and debates began on the nature of the economic relations in West Bank and Gaza. It is imperative to outline that economic integration that developed after the 1967 war was between the established State of Israel and the Occupied Territories from what remained of Palestine. This economic integration wasn't between two states so the first element of The Economic Peace Theory definition is missing. To define clear parameters, the Palestinian economy will be defined as the areas occupied by Israel in 1967 (West Bank, East Jerusalem and Gaza). Additionally, Economic Peace Theory still was not articulated in academic research at this time, however it is imperative to look at its attempted implementation.

"Several economic processes began immediately after the war in 1967" (Kleiman 1990). The Israeli Minister of Defense, Moshe Dayan, argued for fully integrating both economies into one unit with freedom of movement, capital, goods and labour. On the other hand, Israel's Ministry of Finance had similar positions excluding the movement of labour. Naturally, the Palestinians had no voice or input in creating the economic dynamics of the region. At the time; the PLO leadership still was not strong enough in the region and resided its influence mostly from outside the territories. As the victorious super-power, Israel decided to integrate the economies of the

West Bank and Gaza to their own therefore creating one economic unit. Israel being the ultimate decision maker in the economics of what remained of Palestine, with zero input from the Palestinians created massive holes in rebuilding the Palestinian economy. From a Palestinian perspective, agriculture was the main sector. After the 1967 war, Palestine lost control of the land in West Bank and Gaza. This meant losing their main source of income, which laid the foundations of Palestinian dependency on Israel.

Moshe Dayan, created a new economic strategic vision called the Open Bridges. Within this new era, borders between the Palestinian territories, Israel and Jordan would be open. The reasoning behind including Jordan in this plan was the assumption that the West Bank would be controlled by Jordan in the coming future. This entailed freedom of movement and labour. Dayan envisioned that the bridges would serve as a basis for considerable trade to occur between the three parties. However, Israel imposed barriers to the import of Palestinian agricultural produce. Furthermore, “a myriad of administrative measures impeded Palestinian development, prevented local Palestinian competition with Israeli entrepreneurs, and further contributed to the economic asymmetry between the two sides” (Aix Group 2003).

According to a research conducted by Kubursi and Naqib, the size of Israel’s economy was ten times larger than that of the Palestinian economy. Israel’s manufacturing share in its GDP was four times larger. The paramount differences in size and structure between the Israeli and Palestinian economy developed the relationship as one between a giant, advanced and rich economy and another a small underdeveloped and poor economy. Theoretical as well as empirical studies show that that such a relationship generates two opposing forces that disproportionately shape the development of the smaller economy. (Kubursi & Naqib 2008: 16).

Israel had a developed manufacturing and agricultural sector with increased economies of scale due to its growing investments. This demanded labour that Palestinians supplied thus substituting Israeli labour. Instead, the Israeli workforce shifted away from traditional sectors transitioning towards modern industries. The Israeli economy was able to have an elastic supply of labour with relatively low wages. At the same time, there was an increasing effective demand for their modern sectors products. However, the Palestinian production of agriculture deteriorated. (Kubursi & Naqib 2008: 17).

The Open Bridges economic strategy created a circle of monetary transactions whereby wages earned in Israel by Palestinians were then spent on Israeli products. Due to the denial of Palestinian access to water and land; Palestinian agricultural output plummeted losing local employment potential. A study conducted by the United Nations showcased that 50% of Israeli exports were from Palestinian production prior to the occupation. Thus, creating a very high Palestinian dependency on Israeli economy composed mainly of employment opportunity with loss of its major economic segments.

The case of Jerusalem is slightly different from the characteristics of West Bank and Gaza. The 1967 war resulted in the unification of Jerusalem merging the East and West. In 1967, Jewish residents of Jerusalem's income were four times larger than Palestinian residents. After the unification of the city Palestinian residents of Jerusalem comprised of 26% of the population but represented only 16% of the work force. Unsurprisingly, they accounted for only 8% of Jerusalem's collective income. (Romann & Weingrod, 1991).

East Jerusalem was no longer under Jordanian rule resulting in an imperative loss of Muslim tourism. This negatively affected the Palestinian labour force in East Jerusalem, which shifted the employment into West Jerusalem's economy. The main sector that initially absorbed Palestinian Jerusalemites was construction. At this time, there were massive Israeli government investments in this sector because of the 1996 recession. In the early 1970s, many Jewish neighbourhoods started emerging that needed substantial manual labour, opening the door to Palestinian employment. (Shtern 2017:12) The Histadrut also played a major role in integrating workers from East Jerusalem to private and public employers of West Jerusalem. Its revised policies resulted in approximately 4,000

East Jerusalem workers employed in the Jewish sector year 1967. Within two years this number rose to 5,400.

It is imperative to highlight the major differences between the economic integration that was implemented between the West Bank and Gaza (WBG) and East Jerusalem. Firstly, workers from East Jerusalem were unionized. Secondly, there was unlimited trade between East and West Jerusalem. Third, the WBG sectors that suffered the most from the occupation were agricultural whereas in East Jerusalem tourism weakened substantially. Finally, East Jerusalem workers had basic social rights whereas WBG endured humiliating working conditions with lack of union oversight.

The framework of economic processes between the Israeli and Palestinian economy after 1967 created asymmetrical economic development. Even though the Palestinians had twice the GDP of Jordan and Egypt, and three times that of Syria, it still only represented 3.5% of Israel's GDP. The Palestinian comparative point was no longer the Arab world, it was replaced by Israel. Even though Palestinian workers from the West Bank and Gaza were approximately a third of the Israeli workforce by the 1980s; they were only blue-collar workers. While the Israeli perspective viewed the economic processes it had implemented as a positive occurrence and cooperation; Palestinians were far more reluctant to accept the dependence of blue-collar Israeli employment and deprivation of economic freedom as the status quo.

The fact that such an integration was imposed by one party to the other brings additional complexities, notably from an institutional point of view. Israel pursued economic policies that were not in the best interest of the Palestinian economy (Arnon and Weinbatt, 2000). On the other hand, the imposition of economic policies by Israel might have allowed Palestinian energies to concentrate on using market activities rather than the political system to generate income, as observed in comparable cases (Schiff, 2002). However, in reality Palestinian energies were still in shock of the aftermath of 1967. No clear leadership indicated the direction of Palestinian strategy. With no open communication between the two parties, and open integration being the imposed plan; the implementation was not favorably viewed by Palestinians.

Naqib (2000) distinguished two opposite sets of theoretical effects of the integration between a large, advanced and rich economy with a small, poor and underdeveloped economy: “Favorable repercussions are an increased demand for the products of the small economy, a diffusion of technology and knowledge, as well as other spread effects, resulting from the geographical proximity to a large market leading to subcontracting, joint ventures and coordination in tourism and other services. Unfavorable repercussions arise from the disappearance of many industries in the small economy, its confinement to producing low skill goods and the emigration of a sizable segment of the labour force to the neighbouring country, as well as to other countries.”

The failures of Israel’s economic policies following the 1967 war to achieve peace can be stated as follows. Firstly, hindering Palestinian agricultural capabilities heightened tensions. Secondly, being the only decision maker in creating economic integration and leaving out Palestinian voices dramatically influenced the asymmetrical economic development. Thirdly, relations between two dissimilar and unequal economies, whereby the large economy practices policies that keeps the small economy weak and dependent is not an effective way to sustain peaceful relations. As a result, I refute the Economic Peace Theory in the context of the 1967 economic integration imposed by Israel on the Palestinian economy.

The Paris Protocol

The economic dynamics between Israel and the Occupied Territories prior to the Paris Protocol can be described as a forced integration plan implemented by Israel without the consent of the Palestinians. The international community at the time did not play a significant role in outlining any of the policies; instead they were shaped unilaterally by Israel. Thus, creating an asymmetric trading paradigm with two hugely gaped economies. The asymmetry emphasized the dependence of the Palestinian economy on Israel. This dependency is attributable mainly to the high level of Palestinian employment in Israel. For instance, in 1992 Israel employed over one third of the Palestinian work force (approximately 116,000 people) meaning that 25% of the Palestinian Territories GDP was contributed to by Israeli employment. Moreover, the income generated by Israeli employment had an indirect affect in increasing the demand for locally produced goods. (Gross 2000: 1556).

The economic integration of 1967 continued reaching a peak from 1967 to 1987. However, the First Intifada hindered this integration. It led to a separation between the two markets, decreasing both the employment and trade of goods between the two economies. The failures of the first economic integration attempts and violent escalations gave a push for a new era whereby both parties entered negotiations for the first time.

During the 1993 Oslo Accords; the interdependency of economics of peace was still seen as a vital element during negotiations. The preparatory statement of the Paris Protocol gave evidence to this whereby it states "[t]he two parties view the economic domain as one of the cornerstones in their mutual relations with a view to enhance their interest in the achievement of a just, lasting and comprehensive peace"(Paris Protocol).

The Paris Protocol regulated all the Palestinian sectors, internal and external economic relations, and the Palestinian and Israeli economic roles. The Joint Committee was created for oversight of the implementation of the policies. As agreed during the negotiations, the Joint Committee had the authority to decide on any disagreements. Its functions included reviewing any issues requested by both parties. It was also responsible for deciding the quantity of goods that Palestinians could import and other import regulations.

It is crucial to highlight the Palestinian paradox within the Paris Protocol. Interdependency with Israel could improve economic prospects; however, enhancing a reality by which the Palestinian economy continues its dependency on Israel is counter-productive to achieving economic sovereignty. “Indeed the protocol did not focus on creating islands of cooperation or on searching for fields of mutual gain, as the interdependence peace logic would suggest. It was much more focused on establishing viable economic arrangements to deal with pre-existing interdependence and to help enhance Palestinian economic independence” (Lutmar, Miller 2016: 207).

The Paris Protocol enabled Palestinian economic performance to continue being linked to the monetary conditions of Israel. Even though, it gave the Palestinian Authority the right to establish a monetary authority with the basic functions of a Central Bank, even without a local currency. Several economists agree that this policy was set in place to keep the integration of the Palestinian economy in Israel. This policy created a window for Israel to obtain seigniorage revenue due to the circulation its currency in the Palestinian territories. The refusal of Israel to allow the creation of Palestinian currency can be seen as part of a strategy to perpetuate the Palestinian economic dependency on the Israeli economy. (The Palestine Israel Journal, 1999). A major limitation emerged due to this policy. Without an independent Palestinian currency, the Palestinian economy became automatically deprived from the mechanism of making monetary policies, particularly the determination of interest rates. As such, the Palestinian Monetary policy cannot effectively tackle issues such as inflation, aggregate output and employment.

There were loopholes in the Paris Protocol that were used to highlight Israeli control over economic logistics. Instead of shifting some of the asymmetry of power that might have enhanced equal economic integration; such practices only amplified by 1967 Palestinian economic frustrations. One way in which relations between Israel and Palestinian economies were shaped, is the practice of customs taxes on the goods imported to the Palestinian

Territories as well as VAT revenues of goods sold in Israel but consumed in the Palestinian Territories. They are collected by the Israeli government and then transferred to the PA. Israel has used this policy to withhold collected taxes in order to pressure the PA. When it accounts for 70% of the Palestinian Authorities revenues; it makes a substantial impact. The first purposeful delay was in 1997 which laid the groundwork for such practices to continue until today.

Other examples include the regulation regarding price control. This negatively affected the economic stability of Palestinians. In the Paris Protocol, the Palestinian VAT rate cannot exceed 2% lower than the Israeli VAT rate. In addition, the fuel prices in the Palestinian Territories cannot be more than 15% less than the Israeli fuel price. The implications of this regulation were illustrated in August of 2017. Israel increased its VAT and fuel prices, which imposed the PA to adjust its prices accordingly. The burden of the VAT affects Palestinians because they spend a larger portion of their income on basic goods.

The Paris Protocol was shaped by the political framework, instead of thorough economic analysis of alternative arrangements. As such, it ignored the issue of Palestinian sovereignty over land. Without clearly defined borders, an effective development strategy is unlikely to work. For example, the agricultural sector of Palestine that has the largest potential to develop cannot properly grow without Palestinian sovereignty over Area's C of the West Bank.

Another imperative element of the Paris Protocol was the affect that the escalating violence had during the second intifada. Several of the economic integration policies were not implemented because of the violence. Due to the escalating attacks, Israel imposed a relatively strict closure policy to the Palestinian territories. Israel also sealed off the West Bank from Gaza, which played a major role in the deteriorating economic conditions. For example, both the real GDP and real GNP per capita worsened during this period. Between 1992-1995 merchandize exports in the Palestinian Territories declined from 11% to 6%. Also, imports decreased from 64% to 38% of the total GDP. Studies show that the quality of life in the territories fell by 25%. The Paris Protocol failed to provide a foundation for the Palestinian economy to grow. It also failed to establish positive economic integration between Israel and the Palestinian Territories. One might even say, it kept the same level of dependency as of 1967.

It also highlighted the same frustrations the Palestinians felt during the 1967 era. The Palestinian struggle has been one of achieving, self-determination and emancipation. What is missing from most academic research is the importance of linking this to the economic limitations that Palestinians have. Having limited economic freedom only exasperates the core of the Palestinian struggle. The Paris Protocol failed to provide the foundation for economic independence of Palestinians because it continued to link regulations with dependency on Israel. This link is attributable to Israel's security concerns, which has always overpowered economic aspirations of Palestinians. For example, the establishment of a customs union with Israel based on Israel's trade regulations gave Israel the power to restrict specific quantities of goods that can be imported and exported that crippled many Palestinian business initiatives. As a result, the majority of the Palestinian public blame the deteriorating economic conditions to the Paris Protocol because of their lack of freedom to import and export without Israeli supervision.

Recommendations to What Lies Ahead

Firstly, for those who recognize that there has not been political progress, should understand that economic independence of Palestine will lay the groundwork for any future peace. Until the Palestinian economy is raised significantly with potential for future continued economic freedom, a sustainable political climate is unlikely. This can be explained through the failures of each economic integration attempt. Within the 1976 war era, Palestinians had no power or input in their economic well-being driving more resistance and opposition. The same story is painted during the Paris Protocol.

Albert Einstein defined insanity as doing the same thing over and over again whilst expecting a different outcome. In my opinion, he outlined the Israeli Palestinian peace process, particularly in regards to the economic aspects. Integrating the Palestinian economy in a framework that gives Palestinians blue-collar jobs in humiliating conditions will never enhance peaceful co-existence. This only heightens Palestinian frustrations. Instead, economic freedom should be the targeted vision.

Thinking outside the box should be the way to achieving economic freedom for Palestine. As there are no agreed upon political borders, deciding on economic borders will give space for the Palestinian economy to boom. It will lay the parameters for production, industrial zones and green house space. Another aspect is gaining international relations in the economic sphere. There is not one free trade zone in Palestine (excluding Israel's volatile trading policies). Opening easier tariffs and trade agreements will give Palestinians momentum and opportunities for shifting their way of thinking from a micro-economic level to a macroeconomic level.

Another element I would recommend is increasing relations with the European Union. There have been proposed ideas to give Palestine and Israel EU membership. Exploring such proposals is vital in reaching new circumstances of economic independence. In this aspect, Palestinian businesses will have the opportunity to export with no barriers to European member states. It will also allow freedom of movement within Palestinian and Israeli borders prompting more equal integrations between the two sides.

Another key element is the Middle East Market. Using the Middle East as an economic key is crucial. Economic conferences should be held with Economic Ministers in the MENA region for negotiating open market ideas in the Middle East. The United States is another major player that has influenced the Palestinian Israeli Conflict. Creating a lobbying strategy for Congress and the Senate can be imperative in directing the conversation towards creating economic independence in Palestine. Furthermore, using Palestine's allies such as Sweden, Northern Ireland and Norway in terms of strengthening Palestinian governance, Investment strategies, and Macro-economic development. Finally, it will shift the control power from Israel to a centralized regulatory framework. This will lessen the Palestinian frustration while still developing its economic vision.

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