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The Economic and Social Costs of the War in Gaza

By Perrihan Al-Riffai

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EXECUTIVE SUMMARY

The Middle East region has a long history of geopolitical turbulence and conflict, which has had detrimental socioeconomic impacts on its economies. In addition to the tragic loss of life and livelihoods, rampant displacement, and the staggering cost of destroyed infrastructure and assets, the conflicts have also entrenched multidimensional poverty and inequality and unraveled decades of development gains. The Israel-Gaza war is a more recent flare-up of the longest running conflict in the world: the Israel-Palestinian conflict. The Israel-Gaza conflict has brought about tens of thousands of fatalities and injuries, displacement across three countries, and millions of dollars of destruction to infrastructure. Unless a permanent ceasefire is achieved soon, the involvement of other agents may quickly descend into a region-wide conflict, bringing with it a multitude of negative spillovers throughout the region and around the world.

To date, the Israel-Gaza war has had negative economic costs both globally and regionally. At the global level, the disruption in maritime routes due to the Houthi attacks in the Red Sea has had, and continues to have, economic and climatic implications. Longer transport routes and higher consumption of fuel has increased transportation costs, which may lead to higher consumer prices. Furthermore, the longer trade routes around the Cape of Good Hope increase emissions, further compromising the environment. At the regional level, the economies of the Middle East have had to deal with constrained growth, current account vulnerabilities, elevated fiscal costs, financial sector vulnerabilities, and various sectoral and labor market impacts.

The war in Gaza is imposing debilitating social costs on food security in the region's already fragile and conflict-affected states. Social vulnerabilities have increased in the Palestinian territories, Yemen, and Lebanon. Already net food importers, these fragile states must contend with sanctions and straightjacketed humanitarian aid flows that are crucial for survival.

If the conflict escalates and persists, it will bring heightened vulnerabilities and greater uncertainty to the region, including to its oil-rich economies. Political stability will be threatened, leading to greater economic uncertainty that deters foreign investment and redirects investor risk sentiment away from the region. Furthermore, commodity markets—especially given the oil production cuts decided by the OPEC+ countries—may bring about inflationary pressures and further tighten global financial conditions.

Moving ahead with a permanent ceasefire and a solid reconstruction plan is the only way forward for the socioeconomic benefit of the region. Peacebuilding efforts, mediated by the international community, have become an existential imperative, not just for the region's citizens, but for the rest of the world as well. In addition to the human toll, should the duration and intensity of the war in Gaza spread to other countries in the region, the impact on commodity prices, supply chains, and fiscal costs could undermine the fragile soft landing that is still emerging, after policy measures successfully brought inflation under control.

GLOSSARY

BoI	Bank of Israel
CAPMAS	Central Agency for Public Mobilization and Statistics
CBE	Central Bank of Egypt
CBS	Central Bureau of Statistics
COVAX	COVID-19 Vaccines Global Access
EFF	Extended Fund Facility
EMDE	Emerging Markets and Developing Economies
Epicenter countries	Israel and Palestinian territories
EU	European Union
FCS	Fragile and Conflict-Affected States
FDI	Foreign Direct Investment
FX	Foreign Exchange
FY	Fiscal Year
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GCC and Maghreb countries	Kuwait, Qatar, Saudi Arabia, UAE, Algeria, Morocco, and Tunisia
H1	First Half
H2	Second Half
ILO	International Labor Organization
IMF	International Monetary Fund
IRG	Internationally Recognized Government
MOF	Ministry of Finance
MOTA	Ministry of Tourism and Antiquities
MOU	Memorandum of Understanding
Neighboring countries	Egypt, Jordan, and Lebanon
NFA	Net Foreign Assets
OCHA	United Nations Office for the Coordination of Humanitarian Affairs
OECD	Organisation for Economic Co-operation and Development
OPEC+	Organization of Petroleum Exporting Countries +
PA	Palestinian Authority
PLO	Palestine Liberation Organization
Q1	Quarter 1
Q2	Quarter 2
Q3	Quarter 3
Q4	Quarter 4
SC	Suez Canal
UAE	United Arab Emirates
UN	United Nations
UN ESCWA	United Nations Economic and Social Commission for Western Asia
UNCTAD	United Nations Trade and Development
UNHCR	United Nations Refugee Agency
UNRWA	United Nations Relief and Works Agency
USA	United States of America
USD	U.S. Dollar
VAT	Value Added Tax
WEO	World Economic Outlook
y-o-y	Year on Year

I. Introduction

The Middle East and North Africa is a heterogeneous region. The MENA region is too often defined as one that consists of oil producers (and exporters) and oil importers because it is home to five of the world's top ten oil producers—Saudi Arabia, Iraq, the United Arab Emirates, Iran, and Kuwait—and six of the top twenty gas producers. That definition, however, is overly reductive. The region also includes high-, upper-middle, lower-middle, and low-income countries. In addition, it is home to six of the world's thirty-nine economically and institutionally fragile and conflict-affected states.[1] No single typology or classification can adequately capture the complexity of the region. For the purposes of this report, the countries in the region will be grouped into categories to better understand the socioeconomic impacts of the ongoing Israel-Gaza war: epicenter countries[2] (Israel and the Palestinian territories), neighboring countries (Egypt, Jordan, and Lebanon), other high- and middle-income countries not directly impacted by the conflict, and fragile and conflict-affected states (FCS).

The year 2023 was challenging for the region, and 2024 is proving equally challenging. The confluence of several shocks—high inflation and a cost-of-living crisis, unsustainable debt, population displacements, natural disasters, and the recent conflict in Gaza—have coalesced into a polycrisis.[3] The shocks are threatening the entire region by extinguishing lives, crippling livelihoods, entrenching multidimensional poverty and inequality, and unraveling many development gains.[4]

A. SOCIOECONOMIC IMPACTS OF CONFLICT IN THE MIDDLE EAST

The Middle East region has a history of geopolitical turbulence and is the site of the longest-running conflict in modern history: the Israeli-Palestinian conflict. Furthermore, over the past three-plus decades, the region hosted two wars that included the most international participants: the 1991 liberation of Kuwait (a coalition of forty-two countries) and the 2003 invasion of Iraq (a coalition of thirty countries). The region has also hosted one of the highest casualty interstate wars, the Iran-Iraq war (1980–88).[5] In addition, the unfavorable geopolitical dynamics that have persisted over the past fifteen years have significantly deteriorated the region's overall conflict profile.[6] The political turmoil and transition impacts of the Arab Spring linger to this day, disrupting growth and the economies of the region. The Middle East can easily be classified as one of the most conflict-prone regions globally.[7]

Conflict, insecurity, and fragility persist across much of the Middle East not only because of geopolitical tensions and flare-ups—but also due to a confluence of global, regional, and climatic shocks that serve to further disrupt growth in the region.[8],[9] Shocks like economic and climate vulnerabilities, the COVID-19 pandemic and the resulting supply chain disruptions, and the war in Ukraine added new layers of challenges to the ongoing conflict situations. This caused "complex emergencies" that continue in a global landscape of mounting geopolitical

1. Iraq, Lebanon, Libya, Palestinian territories, Syria, and Yemen.
2. International Monetary Fund, *World Economic Outlook: War Sets Back Global Recovery*, April 19, 2022, https://www.imf.org/-/media/Files/Publications/WEO/2022/April/English/text.ashx. Used in 2022 by the IMF to refer to the Russia-Ukraine war, this report adopts this categorization to refer to Israel and the Palestinian territories as the epicenter of an earthquake sending out socioeconomic shockwaves to neighboring areas and beyond.
3. United Nations Economic and Social Commission on Western Asia (UNESCWA), *Inequality in the Arab Region*, May 2024, https://www.unescwa.org/sites/default/files/inline-files/inequality-arab-region-crisis-key-messages-english.pdf. These crises combine to create a polycrisis: a devastating phenomenon in which separate crises combine to generate a level of harm that surpasses the cumulative impact of the individual crises.
4. UNECSWA, *Inequality in the Arab Region*.
5. Mirjam E. Sørli, Nils Petter Gleditsch, and Håvard Strand, "Why Is There So Much Conflict in the Middle East?," *The Journal of Conflict Resolution* 49, no. 1 (February 2005): 141-65, http://www.jstor.org/stable/30045102.
6. UNESCWA, *Arab Risk Monitor: Assessing Vulnerability and Resilience in the Region*, July 2023, https://www.unescwa.org/sites/default/files/pubs/pdf/arab-risk-monitor-assessing-vulnerability-resilience-region-english.pdf.
7. Sorli, Gleditsch, and Strand, "Why Is There So Much Conflict in the Middle East?"
8. UNECSWA, A*ddressing Climate, Peace, and Security in the Arab Region,* November 2023, https://www.unescwa.org/sites/default/files/pubs/pdf/climate-peace-security-arab-region-english.pdf.
9. The Middle East region is surrounded by other conflict zones: Afghanistan, the Caucasus, the Horn of Africa, and Sudan. This report, however, only focuses on the socioeconomic impacts of the Israel-Gaza war.

vulnerabilities, heightened geoeconomic fragmentation, and tightening financial conditions.[10] Consequently, growth in the region fell behind that of other emerging market and developing economies (EMDEs).[11]

The intensification of armed conflict and violence in the region during the past decade continues to have severe and adverse socioeconomic impacts. In addition to the tragic number of deaths, displacement, and the crippling loss of livelihoods, the cost of destroyed infrastructure and assets is perhaps the most obvious consequence of the ongoing conflict. But there are other forms of economic loss: the diversion of scarce economic resources toward increased militarization, capital flight, lost economic opportunities, and erosion of human capital.[12] In 2018 alone, the economic cost of violence in the Arab region varied between 3 percent and 67 percent of GDP.[13] Conflict generates economic losses that can persist for years, affecting all aspects of economic life—consumption, investment and firm production, government service delivery, and international trade.

Commentary on the extent of the adverse impacts of conflict differs depending on the nature of the conflict episodes, their duration, and the economic conditions of the affected countries. For instance, some estimate that civil conflicts continue to significantly influence growth up to four years after the conflict ends; the impact of non-territorial conflicts last up to one year and international conflicts up to two years.[14] Others suggest that the macroeconomic costs of conflict may result in GDP per capita being 28 percent lower for up to ten years after the onset of the conflict.[15] Furthermore, and as conflict severely impacts official trade, exports and imports may be 58 and 34 percentage points lower, respectively, ten years after the start of the conflict.

Most countries in the region are net food importers, increasing the region's vulnerability to external shocks. The MENA region's reliance on foreign trade and capital markets, coupled with a persistent fiscal deficit in many countries, exacerbates the region's vulnerability to the impact of shocks. Conflict raises food insecurity by reducing food availability when distribution systems, institutions, and physical infrastructure become adversely impacted.[16] Even before the Israel-Gaza war began, countries in the region showed a deteriorating debt profile and more challenging debt dynamics.[17] Amid the current landscape of ongoing conflict, legacy structural imbalances, unfavorable debt dynamics for some, maritime disruptions, and reduced oil production, uncertainty across the region is rising.

This report assesses the socioeconomic impacts of the ongoing Israel-Gaza war in the four aforementioned categories: epicenter countries (Israel and the Palestinian territories), neighboring countries (Egypt, Jordan, and Lebanon), other high-income and middle-income countries not directly impacted by the conflict, and fragile and conflict-affected states. A political and security analysis of the impacts of the Gaza war is beyond the scope of this report. The paper focuses on economic impacts as well as on the social, food security, and displacement impacts. It will, however, shed light on the potential global impacts of the ongoing war, including on maritime and trade disruptions, financial conditions, and the geopolitical risks for commodity markets. Finally, the report will consider possible outcomes should the war persist beyond this year and should more regional players become active participants. Though the report focuses on the social and economic impacts, it is important to note that the deaths, injuries, loss of human capital, and overall destruction of the underlying social fabric of societies facing conflict are an immeasurable cost of war. As of August 2024, at least 36,699 Palestinians had been killed and 91,722 injured,[18] and 1,670 Israelis had been killed and 17,881 injured as of September

10. Clemens Breisinger et al., *How to Build Resilience to Conflict: The Role of Food Security* (Washington, DC: International Food Policy Research Institute, 2014), page 38; UNECSWA, *Arab Risk Monitor*

11. Roberta V. Gatti et al., Conflict and Debt in the Middle East and North Africa, World Bank Group, April 2024, https://documents.worldbank.org/en/publication/documents-reports/documentdetail/099240104152411250/idu163f1f80915d9c149081a45f19ef4a6f9bae1. It fell by around 1.5 percentage points from 2010-19.

12. UNECSWA, *Fourth Arab Governance Report: Equality, Inclusion and Empowerment for More Effective Conflict Prevention*, February 2022, https://www.unescwa.org/sites/default/files/pubs/pdf/governance-arab-equality-inclusion-conflict-english_2.pdf; Thai-Ha, Le, Mang-Tien Bui, and Gazi Salah Uddin, "Economic and Social Impacts of Conflict: A Cross-Country Analysis," *Economic Modelling* 115 (October 2022), https://www.sciencedirect.com/science/article/pii/S0264999322002267.

13. UNECSWA, *Fourth Arab Governance Report*.

14. Olaf de Groot et al., "The Global Economic Burden of Violent Conflict," *Journal of Peace Research* 59, no. 2 (February 2022): 259–76, https://journals.sagepub.com/doi/10.1177/00223433211046823.

15. Natalija Novta and Evgenia Pugacheva, "The Macroeconomic Costs of Conflict," *Journal of Macroeconomics* 68 (June 2021), https://www.sciencedirect.com/science/article/abs/pii/S016407042100001X.

16. Breisinger et al., *How to Build Resilience to Conflict*.

17. Gatti et al., *Conflict and Debt*.

18. "'Another Day of Horror': UN Rights Office Condemns Israeli Strikes at Gazan School," UN News, August 10, 2024, https://news.un.org/en/8story/2024/08/1153041.

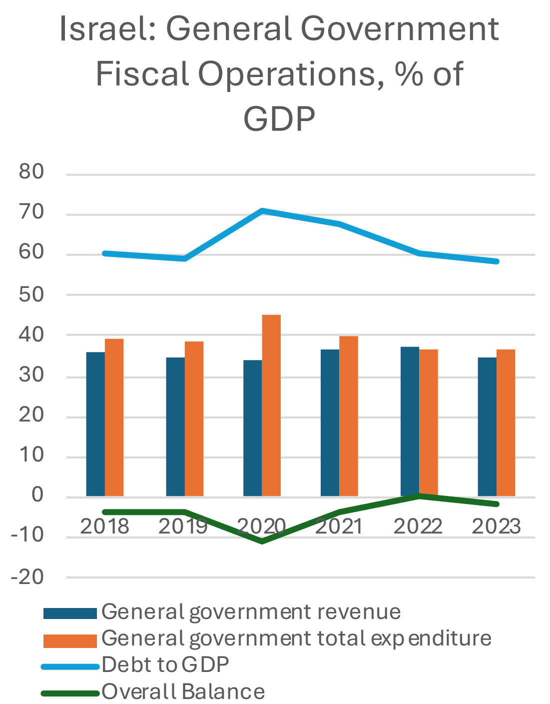
2024.[19],[20] The number of fatalities and casualties is expected to rise as the conflict expands and intensifies.

B. ECONOMIES OF MIDDLE EAST PRIOR TO THE ISRAEL-GAZA CONFLICT

1. Epicenter countries

Israel

Unlike other economies in the region which still suffer long-term scarring from the COVID-19 pandemic, the Israeli economy recovered strongly. This was primarily driven by the high-tech sector and robust exports. Between 2017 and 2022, the high-tech sector was responsible for 32 percent of the growth in economic output. In 2022, the economy grew by 6.5 percent, and higher growth was projected by the International Monetary Fund (IMF) (around 9 percent) for 2023. The fiscal support measures put in place during the pandemic helped mitigate cost-of-living increases for Israeli citizens. Emerging from the pandemic, the authorities wound down the support measures and successfully reversed the country's fiscal deficit[21] from just over 11 percent of GDP in 2020 to a surplus of 0.6 percent of GDP in 2022. As a result, the overall balance was projected to fall to -0.9 percent of GDP in 2023. Over the medium term, growth was projected to stabilize around 3.8 percent in 2028. Fiscal prudence and consolidation helped rebuild fiscal buffers and reduced debt-to-GDP ratios from just over 70 percent of GDP in 2020 to about 61 percent of GDP in 2022. Debt-to-GDP was projected to fall further to 55 percent over the medium term. After peaking in 2022, inflation began a downward trajectory. The Israeli economy's overall external position was strong in 2022 and was projected to improve even further in 2023. It is worth noting that the war in Ukraine had not directly impacted Israel's economy as a result of minimal direct trade with either Russia or Ukraine. Furthermore, Israel's energy dependence is moderate with local production covering more than half of domestic needs.



Source: [IMF: WEO 2023 Database](https://www.imf.org) *Figure 1*

Even prior to the pandemic, long-standing challenges in the labor market were limiting the growth potential of Israel's economy. While economic activity in the construction and high-tech sectors exceeded pre-COVID levels, the overall labor market recovery remained uneven.[22]The high-skilled, high-tech sector accounts for 12 percent of total employment, 17 percent of GDP, half of exports, and 25 percent of income tax revenue, existing alongside lower-productivity, lower-wage sectors. Domestically, a shortage of skilled labor constrained supply, contributing to a nominal wage increase of approximately 7 percent in 2019.

Palestinian territories

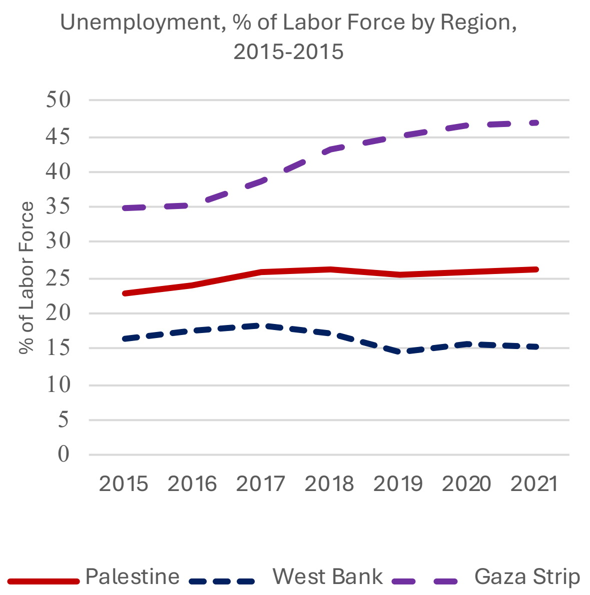
The Palestinian territories include Gaza and the West Bank. Prior to the war in Gaza, approximately 5.5 million Palestinians were living in Gaza and in the West Bank. They were governed by a mix of authorities. Officially, the Palestinian Liberation Organization (PLO) represents the Palestinian people globally. A faction of the PLO (Fatah), through a newly formed entity (the Palestinian Authority), governs most of the West Bank, and, prior to June 2007, governed Gaza, but de facto, Israel exercises significant control over the Palestinian territories. Israeli forces withdrew from the Gaza Strip in 2005, Hamas (formally created in

19. *Hostilities in the Gaza Strip and Israel | Flash Update #83*, United Nations Office for the Coordination of Humanitarian Affairs (OCHA), January 3, 2024, https://www.unocha.org/publications/report/occupied-palestinian-territory/hostilities-gaza-strip-and-israel-flash-update-83.

20. Institute for National Security Studies, *Israel at War: An Overview*, September 13, 2024, https://www.inss.org.il/publication/war-data/.

21. Figures reflect the General Government fiscal operations.

22. International Monetary Fund, *West Bank and Gaza: Report to the Ad Hoc Liaison Committee*, September 13, 2023, https://www.imf.org/en/Publications/CR/Issues/2023/09/12/West-Bank-and-Gaza-Report-to-the-Ad-Hoc-Liaison-Committee-539149; Michelle Koelle, "Addressing Labor Market Challenges for Sustainable and Inclusive Growth in Israel" (working paper, OECD Economics Department, Paris, 2023), https://www.oecd-ilibrary.org/economics/addressing-labour-market-challenges-for-sustainable-and-inclusive-growth-in-israel_dcdb1283-en;jsessionid=8CK4BFd_xfMHE832uz3AlWRkfjKorG1y9M7D21bX.ip-10-240-5-80.



Source: [Palestinian Labor Force Survey 2022] *Figure 2*

1987)[23] won a majority of seats in Palestinian legislative elections in 2006 and in 2007, and then took over Gaza after ousting Fatah forces loyal to Palestinian President Mahmoud Abbas.[24,25] A series of fatal clashes have been taking place between Hamas and the Israeli military forces in the Strip ever since.

Gaza's economic development has lagged behind the West Bank's due to years of isolation and ongoing conflict. Even prior to the Gaza war, the government of Israel had imposed restrictions on Gaza and the West Bank regarding movement, access, trade, and investment. Although these restrictions affected around 61 percent of the West Bank—referred to as Area C under the 1995 Israeli-Palestinian Interim Agreement on the West Bank and Gaza (also known as the Oslo II Accord)—they were more severe for Gaza than for the West Bank. Over the past fifteen years, Gaza's economic productive capacity has been not only anemic but also accompanied by a deterioration in its social indicators. [26]

Until the outbreak of the Gaza war, economic growth relied predominantly on government consumption. Weak investment levels, stunted financial intermediation, and insufficient wages were unable to spur growth or provide basic services such as electricity.[27]

The divergence between the economies of Gaza and the West Bank had been growing since Gaza split from the Palestinian Authority's (PA) control in 2007.[28] Between 2007 and 2022, the Israeli-imposed blockade, four wars with Israel (2008–09, 2012, 2014, and 2021), and deeply rooted political opposition to the PA took a heavy toll on the Gazan economy, resulting in the prolonged stagnation of real GDP.[29] Gazan unemployment hovered around 45 percent, and 53 percent of the population lived below the national poverty line. Moreover, data from 2019-20 indicated that 0.8 percent of children under five in Gaza suffered from acute malnutrition.[30] In contrast, the West Bank experienced an unemployment rate of 13 percent, with about 14 percent of residents living in poverty. [31]

Additionally, in Gaza, growth was driven by government consumption, whereas household spending led growth in the West Bank. Blockades and trade restrictions severely reduced access for the Gazan economy, and Gaza has been highly dependent on imports and food aid to meet consumer demand, with 63 percent of imports coming from Israel and the remainder from Egypt.[32]

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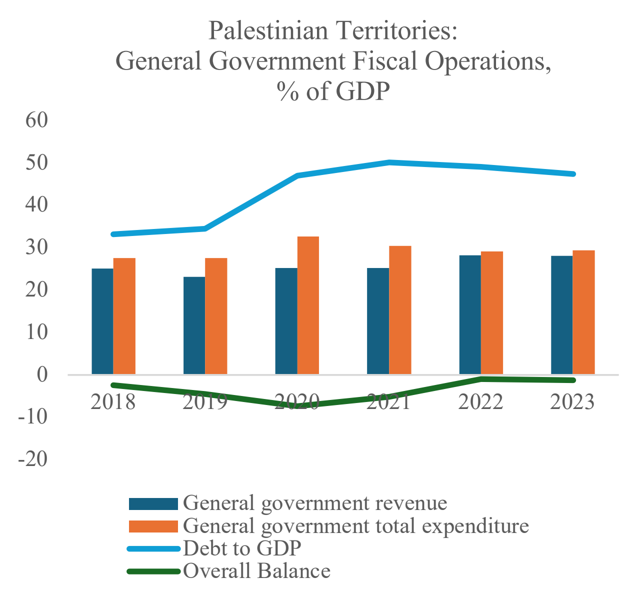
23. Kali Robinson, "What Is Hamas?," Council on Foreign Relations, updated August 19, 2024, https://www.cfr.org/backgrounder/what-hamas. Hamas was founded by a Palestinian cleric in the late 1960s and became a grassroots movement performing charitable work in the West Bank and Gaza after Israel occupied both areas following the 1967 Six-Day War.
24. Kali Robinson, "Who Governs the Palestinians?" Council on Foreign Relations, updated May 28, 2024, https://www.cfr.org/backgrounder/who-governs-palestinians.
25. Reuters, "Hamas and Israel: A History of Confrontation," May 14, 2021, https://www.reuters.com/world/middle-east/hamas-israel-history-confrontation-2021-05-14/.
26. Area C was to "be gradually transferred to Palestinian jurisdiction in accordance with this Agreement." Niksic, Eddin, and Cali, *Area C and the Future of the Palestinian Economy*, 1; International Monetary Fund, *West Bank and Gaza*. Relatedly and under the 1995 Accord, Israel is responsible for levying and collecting income tax and VAT on Israeli individuals and corporations in Area C (other than those in the settlements and in military locations) and submitting the receipts to the Palestinian Authority.
27. Ajamieh et al., *West Bank and Gaza*.
28. Haggay Etkes and Wifag Adnan, *Gazan Workers in Israel: Implications for Employment Regulations*, Institute for National Security Studies, August 9, 2022, https://www.jstor.org/stable/resrep42585. Before 2000, employment in Israel constituted an important source of income for the residents in Gaza, and 46 percent of the Gazan labor force were working in Israel.
29. International Monetary Fund, *West Bank and Gaza: Report to the Ad Hoc Liaison Committee*, September 2023.
30. Famine Early Warning Systems Network, Gaza Strip Targeted Analysis, November 28, 2023, *https://fews.net/sites/default/files/2023-12/Targeted-Analysis-Gaza-Strip-11282023.pdf*.
31. Etkes and Adnan, Gazan Workers in Israel. Unofficial employment of Gazans in Israel ceased temporarily with the outbreak of the COVID-19 and resumed in October 2021 as the pandemic ebbed.
32. Famine Early Warning Systems Network, Gaza Strip Targeted Analysis.



Source: [IMF: WEO 2023 Database] *Figure 3*

The growth momentum in the Palestinian territories had already been falling prior to the Gaza war. Escalating violence and casualties alongside frequent security operations by the Israeli military in the West Bank have been eroding socioeconomic and political stability. At the same time, increasing fiscal pressures and humanitarian and development agencies grappling with significant funding shortfalls resulted in compromised government service delivery to the Palestinian people.

The economic outlook was already concerning. Real per capita income was projected to fall over the medium term amid a widening of the already large gap in living standards between the economies of the West Bank and Gaza. Preliminary assessments indicate that, prior to October 7, 2023, more than 63 percent of the Gazan people were living in poverty and 80 percent of the population was dependent on aid.[33] Amid entrenched challenges and limited policy space, the unresolved fiscal crisis and liquidity squeeze were undermining government service delivery, social support, and the full payment of wages and salaries.[34] In fact, wages in Gaza have remained unchanged since 2000, leading to a consistent erosion of purchasing power in the region compared to the West Bank. [35]

The humanitarian situation in Gaza was precarious even before the COVID-19 pandemic, which drastically affected lives and livelihoods across all the Palestinian territories. Infections in the Gaza Strip accounted for two-thirds of all the COVID-19 cases in the Palestinian territories.[36] Testing capacity was very low and access to vaccines sparse. Until vaccines became available through the COVAX International program (in March 2021), only 3 percent of Palestinians had received a first dose of the COVID-19 vaccine.[37]

2. Neighboring countries

Egypt

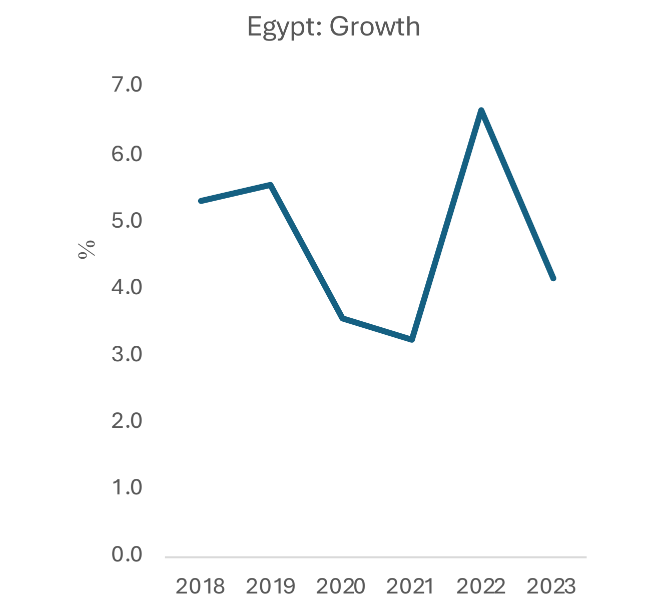
Having successfully achieved macroeconomic stability after the 2016-19 reforms supported by the IMF's program, Egypt was one of the few emerging market economies that experienced positive growth in 2020.[38] Supported by the Extended Fund Facility (EFF), the authorities had implemented bold economic measures, including liberalization of the exchange rate, removal of most fuel price subsidies, and substantial fiscal consolidation to ensure public debt sustainability. From 2017-18 to the first half of 2019-20, real GDP growth had reached an average of 5.5 percentage points, official unemployment rates fell to 8 percent, and 12-month consumer price inflation fell to 5 percent in March 2020 (from 14 percent the previous May).

Furthermore, by the end of February 2020, international reserves stood at $45 billion. The overall fiscal balance was deteriorating, while the primary fiscal balance improved from a deficit of over 3 percent to a surplus of just under 2 percent of GDP, indicating a sustained downward trajectory for public debt.

At the same time, financial market conditions had improved, and Egypt was regularly accessing international capital markets until investors withdrew more than $15 billion in a flight to safe-haven countries in March and April 2020.

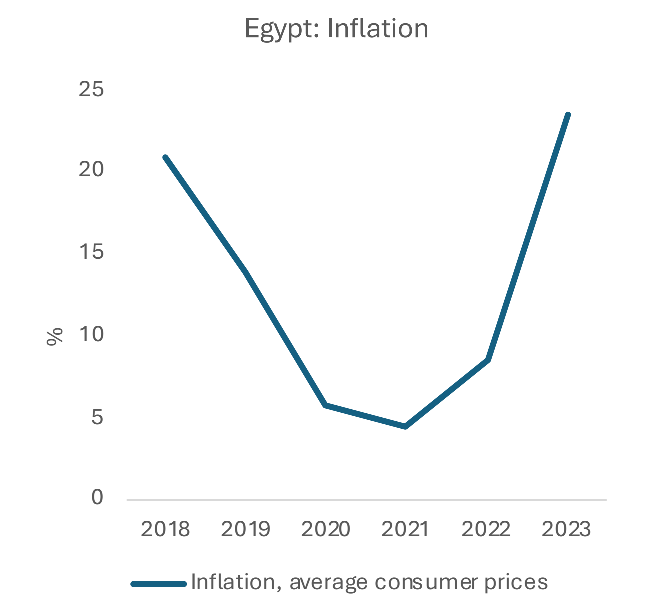
In May 2020, Egypt received $2.8 billion in emergency financing from the IMF, part of a two-part financing plan aimed at maintaining economic stability and helping the authorities

33. World Bank, Gaza Strip Interim Damage Assessment, March 29, 2024, https://thedocs.worldbank.org/en/doc/14e309cd34e04e40b90eb19afa7b5d15-0280012024/original/Gaza-Interim-Damage-Assessment-032924-Final.pdf.
34. International Monetary Fund, West Bank and Gaza: Report to the Ad Hoc Liaison Committee.
35. Gaza Strip Targeted Analysis, FEWS Net, December 21, 2023, 5, https://fews.net/sites/default/files/2024-01/Targeted-Analysis-Gaza-Strip-20231221.pdf.
36. Sharmila Devi, "COVID-19 Surge Threatens Health in the Gaza Strip," *The Lancet* 397, no. 10286 (May 8, 2021): 1698, https://www.thelancet.com/journals/lancet/article/PIIS0140-6736(21)01055-2/fulltext.
37. Devi, "COVID-19 Surge."
38. IMF Country Focus, "Egypt: Overcoming the COVID Shock and Maintaining Growth," *IMF News*, July 14, 2021, https://www.imf.org/en/News/Articles/2021/07/14/na070621-egypt-overcoming-the-covid-shock-and-maintaining-growth.



Sources: IMF, Arab Republic of Egypt: First and Second Reviews Under the Extended Arrangement Under the Extended Fund Facility, Monetary Policy Consultation, and Requests for Waiver of Nonobservance of a Performance Criterion, and Augmentation and Rephasing of Access

Figure 4



Sources: IMF, Arab Republic of Egypt: First and Second Reviews Under the Extended Arrangement Under the Extended Fund Facility, Monetary Policy Consultation, and Requests for Waiver of Nonobservance of a Performance Criterion, and Augmentation and Rephasing of Access

Figure 5

mitigate the adverse impacts of the pandemic. To that end, a Stand-By Arrangement was approved by the IMF in June 2020 for the remainder of the $8 billion in financing.[39] At the time, it was projected that growth would exceed pre-COVID levels in 2021-22 and the country would preserve macroeconomic stability and resume economic reforms.[40]

Legacy structural imbalances—in the face of successive, overlapping crises, falling donor funding, and higher borrowing costs amid policy slippages—worked to unravel Egypt's hard-won macroeconomic stability. While the economic consequences from COVID-19 on the Egyptian economy were more or less contained (except for the tourism sector) as a result of expanded social assistance and a brief lockdown period, the supply chain crisis closely followed by the war in Ukraine and the resultant commodity price hikes and higher borrowing costs severely tested the resilience of Egypt's economy. The war in Ukraine exacerbated Egypt's preexisting external pressures stemming from the lack of exchange rate flexibility and high public debt vulnerabilities.[41]

In December 2022, a 46-month IMF-supported program was approved in the amount of $3 billion, aimed at implementing a comprehensive policy package to preserve macroeconomic stability, restore buffers, and pave the way for sustainable, inclusive, and private-sector-led growth. At the time, the total projected financing needs came to $14 billion, far exceeding financing through the program. The rest was projected to come from Egypt's international and regional partners, through an ongoing divestment of state-owned assets, and from traditional forms of financing from multilateral and bilateral creditors. The authorities also requested access under the IMF's recently established Resilience and Sustainability Fund in the amount of $1 billion. At the time, the current account deficit was financed by a drawdown of banks' net foreign assets (NFAs). By the end of February 2022, banks' NFAs stood at a historic low of -$11.8 billion, a decrease of more than $18 billion since the peak in February 2021. Activity and the economic outlook continued to be hampered by the drop in imports, an impaired FX market, and tightening global financial conditions. Exchange rate and monetary policies focused on restoring external resilience and maintaining price stability.

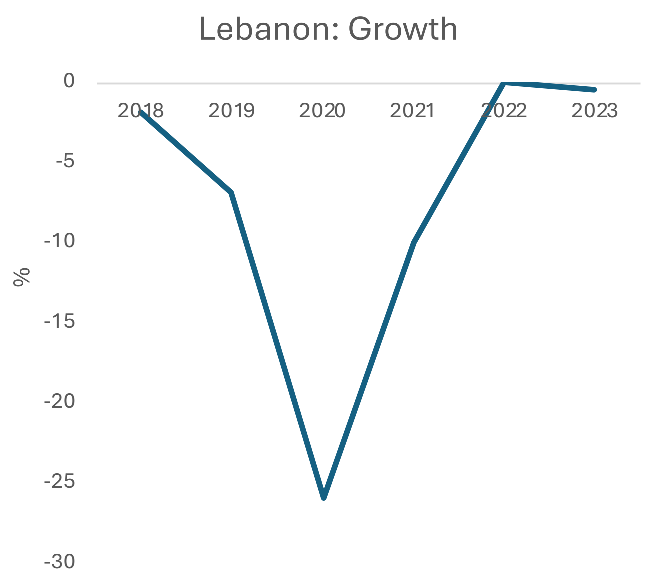
Lebanon

Lebanon's financial crisis in 2019 triggered a severe and multifaceted socioeconomic crisis. Extensive deposit outflows caused the country's first external public debt default. Since the onset of the crisis, the economy has contracted by about

39. IMF Country Focus, "Egypt: Overcoming the COVID Shock."

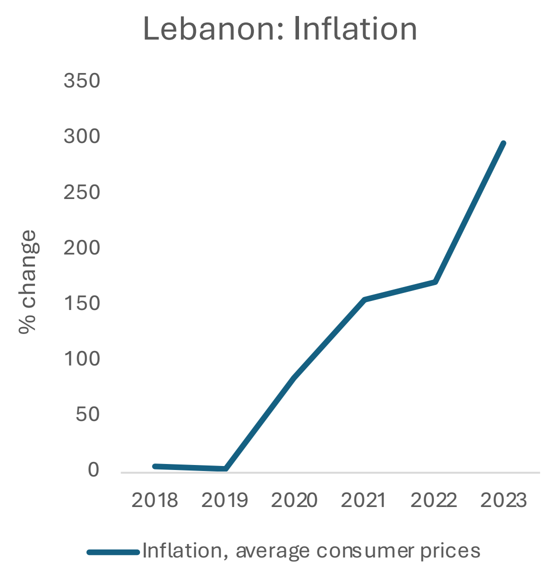
40. International Monetary Fund, *Arab Republic of Egypt: Request for Purchase Under the Rapid Financing Instrument*, IMF Staff Country Report, September 1, 2020, https://www.imf.org/en/Publications/CR/Issues/2020/09/01/Arab-Republic-of-Egypt-Request-for-Purchase-Under-the-Rapid-Financing-Instrument-Press-49724.

41. International Monetary Fund, *Arab Republic of Egypt: Request for Extended Arrangement Under the Extended Fund Facility and Staff Report*, IMF Staff Country Report, January 10, 2023, https://www.imf.org/en/Publications/CR/Issues/2023/01/06/Arab-Republic-of-Egypt-Request-for-Extended-Arrangement-Under-the-Extended-Fund-Facility-527849.



Sources: *IMF, Lebanon: 2023 Article IV Consultation*
IMF WEO October 2023 Dbase

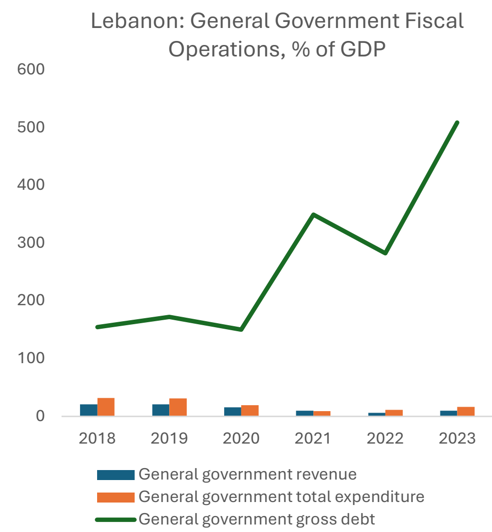
Figure 6



Sources: *IMF, Lebanon: 2023 Article IV Consultation*
IMF WEO October 2023 Dbase

Figure 7

40 percent, the local currency has lost 98 percent of its value, inflation reached triple digits, and the central bank has lost two-thirds of its foreign reserves.[42] The socioeconomic impacts of the crisis continue to be severe. Real incomes collapsed, and unemployment and poverty sharply increased. Following the dramatic exchange-rate depreciation in the first quarter of 2023, dollarization increased, and inflation sharply accelerated to 270 percent year on year (y-o-y). As a result of collapsing revenue, the fiscal deficit is estimated to have widened to 5 percent of GDP in 2022. Public service delivery has all but collapsed, as has the banking sector. The current account deficit is estimated to have widened to almost 30 percent of GDP because of rising imports, and foreign domestic investment (FDI) has remained depressed alongside other financial inflows.[43]



Sources: *IMF, Lebanon: 2023 Article IV Consultation*
IMF WEO October 2023 Dbase

Figure 8

To help mitigate the adverse impacts of the financial crisis, the authorities requested IMF support in April 2022, and reached a staff level agreement which included a package of policies aimed at tackling the macroeconomic and structural imbalances.[44] The reforms would focus on fiscal rationalization, capital controls reform, and restructuring and strengthening the banking system. Unfortunately, internal political complexities prevented implementation of the agreed-upon reforms.

Lebanon, once a middle-income economy, has since 2018 been classified as a fragile and conflict-affected state. It hosts the second largest number of refugees relative to its population (1 in 7).[45] Lebanon is among the largest refugee-hosting countries in the world, with 9 out of 10 refugees living

42. International Monetary Fund, *Lebanon: 2023 Article IV Consultation*,June 29, 2023.

43. International Monetary Fund, *Lebanon: 2023 Article IV Consultation*,June 29, 2023.

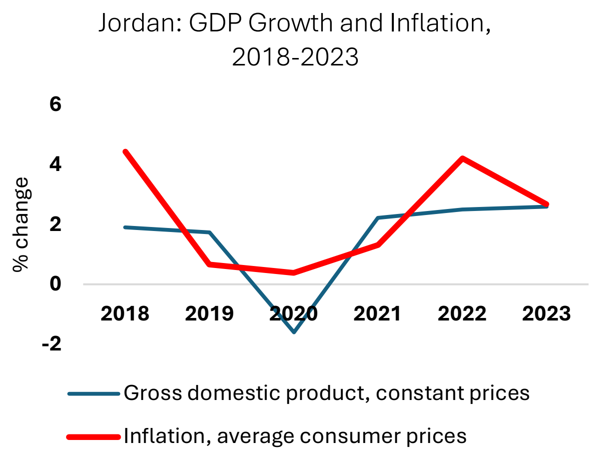
44. International Monetary Fund, *Lebanon: 2023 Article IV Consultation*, June 29, 2023, *https://www.imf.org/en/Publications/CR/Issues/2023/06/28/Lebanon-2023-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-the-535372*.

45. UN High Commissioner for Refugees, *UNHCR Mid-Year Trends*, October 25, 2023, https://www.unhcr.org/mid-year-trends-report-2023.

in extreme poverty.[46] A recent World Bank study estimates that poverty has tripled in Lebanon, from 12 percent in 2012 to 44 percent in 2022, and income inequality has significantly increased.[47] This presents a worrying trend, especially in light of Lebanon's protracted financial and economic crisis. Despite a long history of providing refuge to populations seeking a safe haven, the global shortfall of funding to the UNHCR, the UN Refugee Agency, has also affected Lebanon.

Jordan

Jordan's strong commitment to an ambitious reform program, supported by the IMF, helped mitigate the socioeconomic impacts of the COVID-19 pandemic, the cost-of-living crisis brought on by the war in Ukraine, and the overall tightening in global financial conditions. At the start of the pandemic, the Jordanian economy had already been buffeted by a multitude of regional and global shocks, including the closing of its borders with Iraq, disruption of its gas supply, and hosting refugees fleeing the Syrian crisis. Growth was not strong, and exports and FDI were not robust. Unemployment and public debt had increased to 19 and 78 percent, respectively, by 2019. Furthermore, public service utilities were under pressure as a result of hosting Syrian refugees who at the time made up 15 percent of the population.[48] The cost-of-living crisis brought on by the war in Ukraine incurred significant fiscal costs when the authorities introduced untargeted fuel subsidies as a way to help ease the impact of high commodity prices. With the support of an IMF Extended Fund Facility, the authorities were able to leverage 334 percent of its quota at the IMF to achieve and preserve macroeconomic stability, reduce government debt to sustainable levels, and proceed with a broad range of macroeconomic and structural reforms, while working to mitigate the impacts of these overlapping crises on the most vulnerable. Nonetheless, persistent challenges remain: high unemployment, which rose to 22.3 percent in 2023, and disproportionately affects Jordan's youth, and a high debt-to-GDP ratio.



Source: *IMF October 2023*

Figure 9

Jordan hosts the world's second highest number of refugees per capita; however, critical global funding for refugees has been falling. As of October 2023, Jordan was host to 730,000 refugees (registered with the UNHCR). Of these, 89 percent were Syrian, 8 percent Iraqi, and the rest were a mix of Yemeni, Sudanese, Somali, and other nationalities. It is worth noting that there are also 2.3 million Palestinian refugees in Jordan, according to the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA), the earliest of whom started arriving in 1948.[49] Despite Jordan's long record of welcoming refugees, the most recent data shows that as of November 2023, only one-fifth of the total requested funding has been received. Such a dramatic shortfall in funding has adversely impacted the basic needs and food security status of the country's refugee population. Recent data shows that poverty rates among Jordan's refugee population increased by 10 percentage points, to 67 percent in 2023, over just a two-year period.[50]

3. Fragile and conflict-affected states

The MENA region is home to six fragile and conflict-affected states, four of which are in conflict (Iraq, Syria, Palestinian territories, and Yemen) and two suffer from institutional and social fragility (Lebanon and Libya). Persistent conflicts and fragility erode institutional capacity, hinder effective policy implementation, reduce economic opportunities, and exacerbate social inequalities.[51] Institutions in conflict and fragile settings lack the capacity and resources to provide necessary public services.

46. UN High Commissioner for Refugees, *UNHCR Global Appeal 2024*, January 31, 2024, https://reporting.unhcr.org/global-appeal-2024-6383.

47. World Bank, Lebanon: Poverty and Equity Assessment 2024—Weathering a Protracted Crisis, May 23, 2024, https://documents1.worldbank.org/curated/en/099052224104516741/pdf/P1766511325da10a71ab6b1ae97816dd20c.pdf.

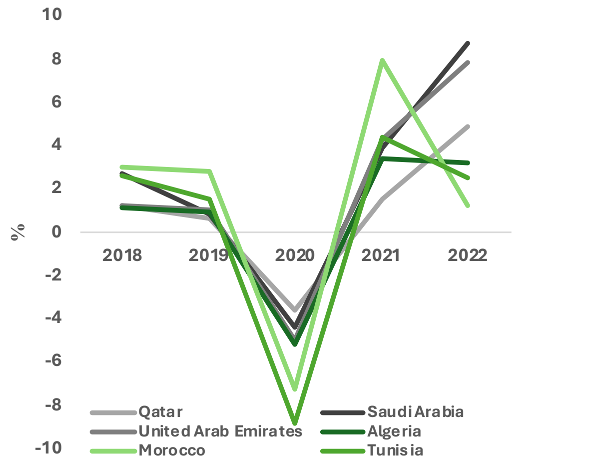
48. International Monetary Fund, Jordan: 2022 *Article IV Consultation and Fourth Review Under the Extended Arrangement Under the Extended Fund Facility, Request for Augmentation and Rephasing of Access, and Modification of Performance Criteria*, July 18, 2022, https://www.imf.org/en/Publications/CR/Issues/2022/07/13/Jordan-2022-Article-IV-Consultation-and-Fourth-Review-Under-the-Extended-Arrangement-Under-520668.

49. International Monetary Fund, Jordan: Request for an Extended Arrangement Under the Extended Fund Facility and Cancellation of the Current Arrangement Under the Extended Fund Facility, January 11, 2024, https://www.imf.org/-/media/Files/Publications/CR/2024/English/1JOREA2024001.ashx.

50. UNHCR, *Jordan: Vulnerability Assessment Framework: Socio-Economic Survey on Refugees in Host Communities*, June 3, 2024, 12, https://data.unhcr.org/en/documents/details/109075.

51. UNECSWA, *Addressing Climate, Peace, and Security in the Arab Region*.

Growth in the Gulf and Maghreb Countries, 2018-2022



Source: *IMF WEO October 2023 Database,* October 2023 WEO *Figure 10*

Even before the pandemic, fragile and conflict-affected states (FCS) had been confronting the greatest challenges in the region. Not only did the pandemic exacerbate the income divergence between these economies, the region, and the rest of world, but the confluence of crises since then and the ever-tightening global financial conditions are sure to have heightened other socioeconomic challenges. In 2022, the IMF projected that per capita incomes in fragile states would not regain their 2019 levels until 2024.[52]

The protracted conflict in Yemen has resulted in an acute, and still unresolved, humanitarian crisis in the country that has severely weakened its institutions, increased poverty, and worsened food insecurity. Even before the conflict, which began in 2014, Yemen had the lowest GDP per capita in the region. A decade later, the UN estimates that 80 percent of the population require humanitarian aid: 14 million are in dire need of immediate assistance and 4.5 million are displaced. Between 2015 and 2023, GDP per capita contracted by 54 percent, pushing more and more of the population into extreme poverty.[53] The Houthi blockade on oil exports by the Internationally Recognized Government (IRG) had severe impacts on 2023 growth and the country's fiscal and monetary sectors. In addition, long-standing vulnerabilities to climate change and the significant financing gap have further weakened the Yemeni economy.[54] Tightening global financial conditions have resulted in falling donor support to development partners. Institutional capacity is constrained—and further complicated and threatened by the presence of a rival government formed by the Houthi-run North. What's more, differing exchange rates are a challenge to policy, and the Houthis' control over the ports closes off access to imports, most important of which are food supplies.

4. Gulf Cooperation Council and the Maghreb Countries (Algeria, Morocco and Tunisia)

From 2017 to 2022, the three largest Gulf economies—Qatar, Saudi Arabia, and the United Arab Emirates (UAE)—were impacted by the global economic landscape and the COVID-19 pandemic, as were the economies of Algeria, Morocco, and Tunisia. The Gulf countries, through their medium- to long-term vision, had started to prioritize diversifying their economies to reduce dependence on hydrocarbon revenues. Advancing that vision helped their post-pandemic recovery, especially when global demand for oil plummeted at the start of the pandemic. Qatar maintained a strong fiscal position through its sovereign wealth fund and supported economic activity by injecting liquidity into the financial sector. Fiscal and liquidity support measures helped mitigate the impacts of the pandemic while the Gulf state moved forward with preparations for hosting the 2022 World Cup. The UAE, by diversifying its economy— including substantial investments in technology, renewable energy, and tourism—and implementing fiscal and regulatory easing measures to mitigate the pandemic's impacts, maintained a resilient external position. Saudi Arabia, through its Vision 2030, laid the foundations for a more diversified economy with less dependence on the oil sector. The Saudi authorities also implemented fiscal support measures to help mitigate the impacts of the pandemic. The oil price collapse and slow recovery during the pandemic significantly affected Algeria's hydrocarbon dependent economy. To address the resulting fiscal shortfall, the Algerian authorities initiated structural reforms and advanced fiscal consolidation to reduce the deficit. In Morocco and Tunisia, both significantly dependent on tourism and manufacturing, faced acute economic disruptions but were able to secure international financial assistance and implemented targeted fiscal policies to stabilize their economies.

52. Franck Bousquet, "Fragile and Conflict-Affected Economies Are Falling Further Behind," International Monetary Fund (blog), January 21, 2022, https://www.imf.org/en/Blogs/Articles/2022/01/21/fragile-and-conflict-affected-economies-are-falling-further-behind.

53. World Bank, *Yemen Economic Monitor*, June 26, 2024, ix, https://documents1.worldbank.org/curated/en/099926206242412700/pdf/IDU1dc601b321062b148fc1b59414e6cd5c70a66.pdf.

54. World Bank, *Yemen Economic Monitor*.

II. Regional Impacts

Matrix of the Macroeconomic and Social Costs of Conflict in the Middle East and North Africa

	Macroeconomic Cost									Social Cost			
Country	Infrastructure Destruction	Extended Conflict	Sectoral	Labor Market	Inflation	Fiscal	Financial Sector Vulnerability	Current Account Vulnerability	Growth Impacts	Food Insecurity	Displacement	Loss of Education Capital	Poverty
Epicenter Countries													
Israel	Check	X	X (Tourism, Construction)	X		X			X		X	X	
Palestinian Terr.	X	X	X	X	X	X	X	X	X	X	X	X	X
Neighboring Countries													
Egypt			X (Tourism)	X		X		X		X	X		X
Jordan			X (Tourism, Restaurant)	X		X					X		X
Lebanon	X	X	X (Tourism, Agriculture)	X	X	X		X		X	X	X	X
Fragile and Conflict Affected Countries													
Yemen		X			X	X		X	X	X	X	X	X
Gulf Countries & other MICs													

Source: Author's Categorization

Figure 11

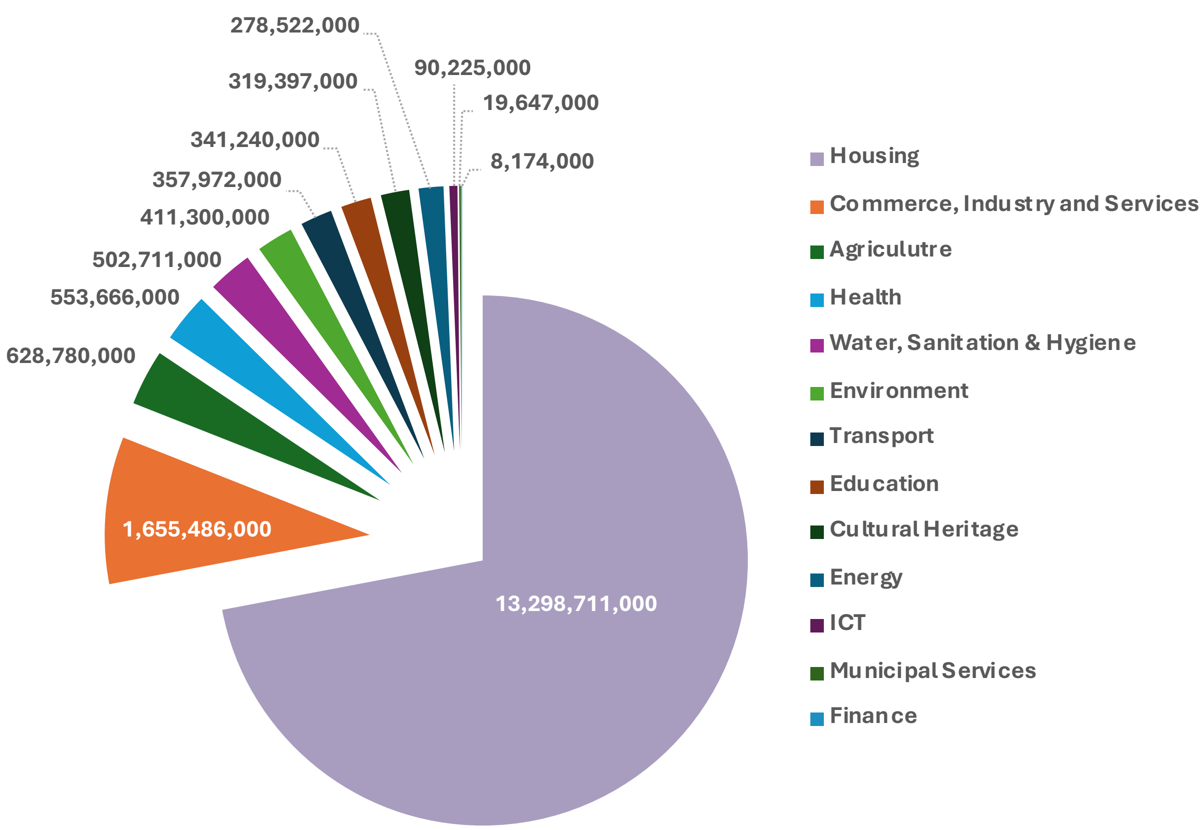
A. THE ECONOMIC COST OF THE CONFLICT

1. Damage to infrastructure

The full extent of the destruction in Gaza cannot yet be tallied, but the World Bank, UN, and the EU conducted an interim assessment of the damage to physical infrastructure in January 2024. The assessment puts the cost of the damage at nearly $18.5 billion, equal to 100 percent of the combined GDPs of Gaza and the West Bank in 2022.[55] Figures below shed light on the extent of the damage and highlight the dire humanitarian conditions that surviving Gazans face without shelter or access to health care, safe drinking water, sanitation, and transportation. Public service delivery of basic utilities has collapsed completely. Reconstruction will be a daunting task. It may take up to 14 years to clear the 37.4 million tons of debris[56] the war has left in Gaza.

It will be critical to think beyond the war and to plan for the future. This not only means planning for the physical reconstruction, but simultaneously leading with humanitarian assistance until there is a degree of stability for people to return and revive economic activity. The responsibility will be borne by the international community to provide the funds required to rebuild. Furthermore, the politics of control over Gaza and whether the government of Israel will end its blockade over the Strip will remain key to the reconstruction effort. Under one scenario, if the government of Israel ends the blockade over the Gaza Strip, reconstruction begins immediately after the end of the war, and the economy of Gaza grows at a sustained rate of 10 percent, it can recoup its pre-blockade (2006) economic activity by 2035. Under a more conservative scenario, if the blockade continues after the war, reconstruction starts, and the Gazan economy grows at 0.4 percent per year, it will take the economy seven decades to reach its 2022 level of economic activity.[57]

Estimated Cost of Damages In Gaza, USD, as of January 2024



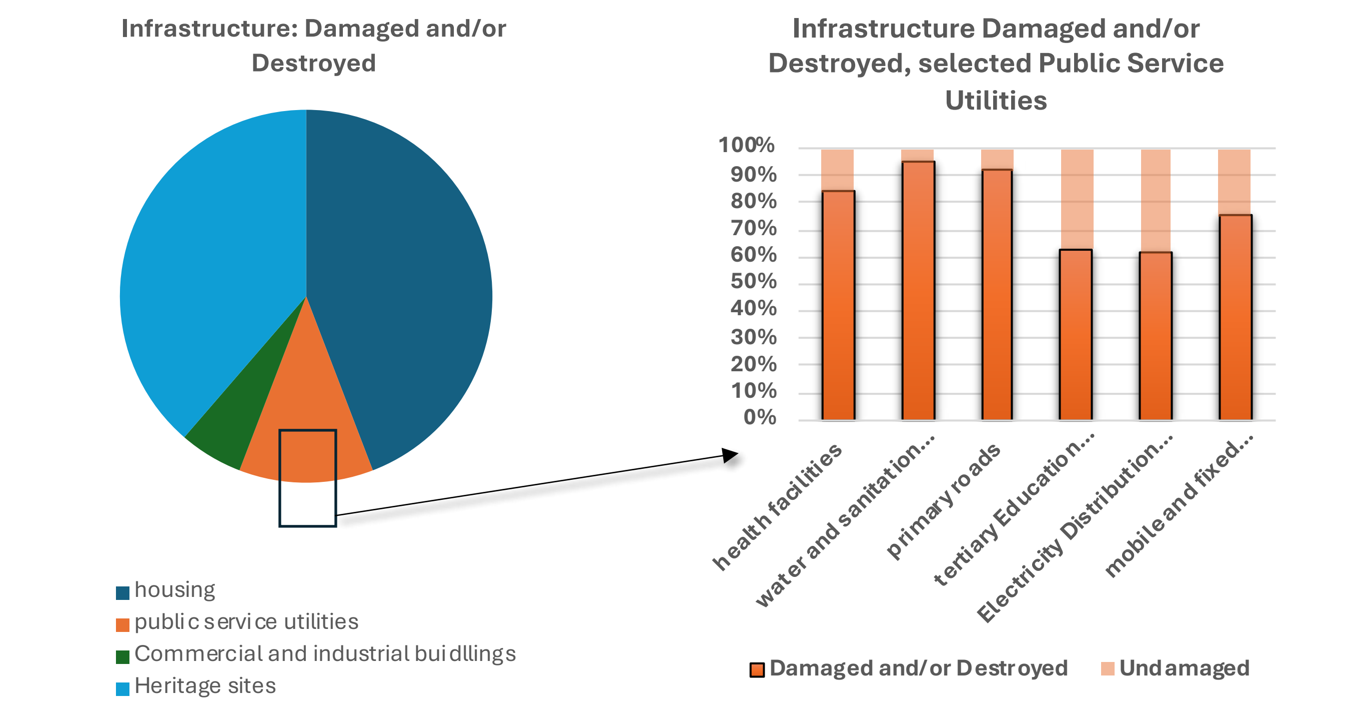
Source: WB 2024. Accessed 05-16-24

Figure 12

55. World Bank, *Joint World Bank, UN Report Assesses Damage to Gaza's Infrastructure*, April 2, 2024, https://www.worldbank.org/en/news/press-release/2024/04/02/joint-world-bank-un-report-assesses-damage-to-gaza-s-infrastructure.

56. Famine Early Warning Systems Network, *Gaza Strip Targeted Analysis*, May 31, 2024, https://fews.net/sites/default/files/2024-06/Gaza-Targeted-Analysis-Update-042024-Final_3.pdf; Conor Lennon, "Clearing Munitions from Gaza 'Years and Years of Work,'" *UN News*, March 19, 2024, https://news.un.org/en/audio/2024/03/1147686. According to the UN Mine Action Service, the debris is laced with unexploded ordnances that pose significant safety threats not only to the reconstruction process but also to the delivery of humanitarian aid now and in the future.

57. United Nations, "Planning the Post-War Reconstruction and Recovery of Gaza," *UN News*, April 6, 2024, https://news.un.org/en/story/2024/04/1148296.



Source: WB 2024. Accessed 05-16-24

Figure 13

However, the politics and funding plans of the "day after" remain unclear. Decisions around the control and form of governance within the Gaza Strip are still in flux. There are calls ranging from ousting all Palestinians from the Gaza Strip and building Israeli settlements to calls for an independent PA-controlled Gaza. Funding of the postwar reconstruction remains unclear as well. Some Gulf countries have been mentioned as possible donors. Following a meeting in Oslo, Norway, among donors and countries in December 2023, some states set an initial budget of $3 billion over a ten-year period, with the UAE, Saudi Arabia, and Qatar as the largest donors.[58] Other possible donors could include the EU and Germany since they have been major humanitarian aid donors to the Palestinian territories in the past. Another is the United States, which may be called upon to help fund the reconstruction efforts. There are also calls for Israel to shoulder a large part of the reconstruction costs, given it is responsible for the damage and it has been recognized as an occupying state by the UN, the EU, and other international organizations. Still, the absence of political consensus around a "day after" plan obscures how the funds will be furnished, which is a crucial step in light of the massive amount of damage inflicted on Gaza's infrastructure.[59] As a result, some officials from the EU and the United States may balk at using taxpayer money to fund the reconstruction of infrastructure without a complete resolution to the conflict for fear the reconstruction effort returns to square one as a result of future conflicts.[60]

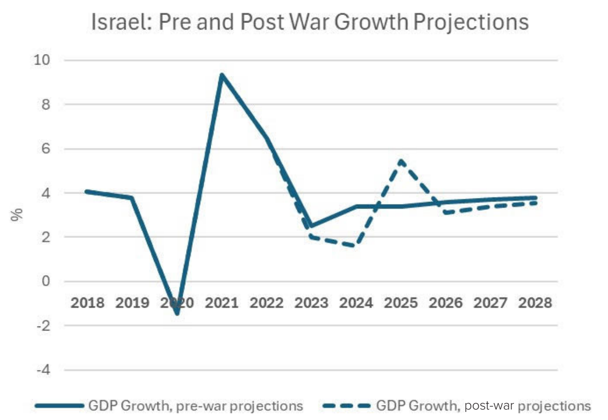
2. Impact on Economic Growth

The onset of the war caused supply and demand shocks that led to a decline in Israeli economic activity by 21 percent in the fourth quarter, year on year. Investment demand and private consumption fell during the fourth quarter of 2023, by 26 and 8 percent, respectively. Seven months past the start of the war, the Israeli authorities stated that the direct impact of the war had reached its peak at the end of 2023 and was starting to wind down. On the demand side, data showed that private consumption was recovering and Israelis who lived in the northern part of the country were returning to their homes, but it also indicated that the supply shock impacts would linger. In its April 2024 staff forecast, the Bank of Israel (BOI) assumed that the war would continue through 2024, with increasing intensity, and that by 2025, the direct impact on

58. Taylor Luck and Fatima AbdulKarim, "A Plan for Gaza's Future Is Taking Shape. Obstacles Loom," *Christian Science Monitor*, December 22, 2023, https://www.csmonitor.com/World/Middle-East/2023/1222/A-plan-for-Gaza-s-future-is-taking-shape.-Obstacles-loom#:~:text=Under%20the%20plan%2C%20Gulf%20states%20have%20set%20an,according%20to%20a%20Gulf%20official%20who%20requested%20anonymity.

59. Reconstruction costs are expected to exceed the $18.5 billion, according to the EU-UN-World Bank's interim assessment in January 2024. World Bank. Gaza Strip Interim Damage Assessment, 2024.

60. Cathrin Schaer, "Israel Conflict: Who Will Pay for Gaza Reconstruction?" *DW*, December 13, 2023, https://www.dw.com/en/israel-conflict-who-will-pay-for-gaza-reconstruction/a-67714098.



Source: *[IMF, WEO Database, October 2023, & April 2024](#)* *Figure 14*

Israel: Forecast Adjustments, 2024, Q1 – Q2

	2023	2024	2025		
	Actual	Forecast for 2024	Change from Q12024 forecast	Forecast for 2025	Change from Q12024 forecast
GDP	2	1.5	-0.5	4.2	-0.8
Private Consumption	-0.7	2	-2.5	5	-0.5
Investment in fixed assets (excluding ships and aircraft)	-2.9	-9	-5.5	8	-2.5
Public consumption (excluding defense imports)	7.2	8	3.5	-5.5	-3.5
Exports (excluding dia-monds and startups)	0.1	-1.5	-0.5	4.5	0.5
Civilian imports (ex-cluding diamonds, ships and aircraft)	-7.2	-5	-1	3.5	-4.5
Broad unemploy-ment rate – annual average (ages 25–64)	4.4	4	0.3	3.8	0.5
Government deficit (percent of GDP)	4.1	6.6	0	4	-0.6
Debt to GDP ratio	62	67.5	0.5	68.5	1.5
Inflation	3.3	3	0.3	2.8	0.5

Source: *[Bank of Israel](#)* *Figure 15*

the economy would start to wane.[61] This view was broadly in line with IMF projections reflected in their latest projections in which GDP was expected to grow by 2 percent in 2024 and by 5 percent in 2025. However, in its July 2024 forecast, the BOI revised down their growth forecasts by 0.5 percent in 2024 and by 0.8 percent in 2025. Inflation forecasts have also been revised— from 2.7 percent to 3 percent in 2024, and to 2.3 percent in 2025—and interest rates are forecasted to increase. Expectations that the war will be longer and more intense imply that supply and demand shocks will continue to weigh heavily on the economy. On the demand side, public and private consumption are expected to fall due to lower government spending and higher taxes, while tourism will continue to suffer, especially as conflict along the northern border intensifies. On the supply side, supply shocks will linger due to ongoing labor shortages and the below-capacity level of production in combat zones.[62]

In the first quarter of 2024, real GDP in the Palestinian territories fell by 35 percent, driven by an 86 percent contraction in Gaza's economy during the same period.[63] Prior to that, the end of the fourth quarter in 2023 saw a decline in growth in the Palestinian territories of just under 30 percentage points year-on-year, driven by a contraction of between 81 and 86 percentage points in Gaza compared to the same period one year earlier. [64] The significant decline in first-quarter growth in 2024, as recently reported by the World Bank, is much larger than previously expected. In an earlier report, the World Bank had projected that Gaza's GDP may contract by more than 50 percent in 2024, while the Palestinian territories as a whole could see a decline of 6.5 to 9.4 percent during the same year. [65]

As the full extent of the war's impact on Gaza continues to unfold, the outlook for 2024 and beyond remains highly uncertain. GDP per capita in the Palestinian territories was 12 percentage points lower in 2023 than in 2022 and is expected to decline further in 2024. In Gaza, GDP per capita fell by 28 percentage points in 2023, reaching $1,084, which is one-fifth of the GDP per capita in the West Bank. Furthermore, the substantial amount of tax revenues, or "clearance revenues," held by Israel is exacerbating an already weakened economy

61. Bank of Israel, *Research Department Staff Forecast, April 2024*, April 8, 2024, https://www.boi.org.il/en/communication-and-publications/press-releases/research-department-staff-forecast-april-2024/.
62. Bank of Israel, *The Macroeconomic Forecast of the Research Division, July 2024*, July 8, 2024, https://www.boi.org.il/publications/pressreleases/07-7-24/.
63. World Bank, *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*, September 2024, https://thedocs.worldbank.org/en/doc/c25061ab26d14d7acc0330d5a7b4d496-0280012024/original/PalestinianEconomicUpdate-Sept2024-FINAL.pdf.
64. Data from the Palestinian Center of Bureau Statistics points to an 81 percent fall in Q4 GDP in 2023, while the World Bank (2024) puts the estimate closer to an 86 percent contraction.
65. World Bank, *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*, May 2024, https://thedocs.worldbank.org/en/doc/ce9fed0d3bb295f0363d690224d1cd39-0280012024/original/Palestinian-Econ-Upd-May2024-FINAL-ENGLISH-Only.pdf.

GDP: USD Million, 2022-2023

			2023				
GDP, USD Million*	**2022**	**2023**	Q1*	Q2*	Q3*	Q4**	Q423 Growth y-o-y
Palestinian Territories	15,635.0	14,773.7	3,941.3	3,974.3	4,017.7	2,840.4	-29.49
Gaza	2,713.3	2,100.4	655.9	643.6	671.9	129.0	-81.26
% of total	17.4	14.2	16.6	16.2	16.7	4.5	
West Bank	12,921.7	12,673.3	3,285.4	3,330.7	3,345.8	2,711.4	-18.82
% of total	82.6	85.8	83.4	83.8	83.3	95.5	

Notes: USD Million in 2015 prices *Source: Palestinian Monetary Authority* *Figure 16*

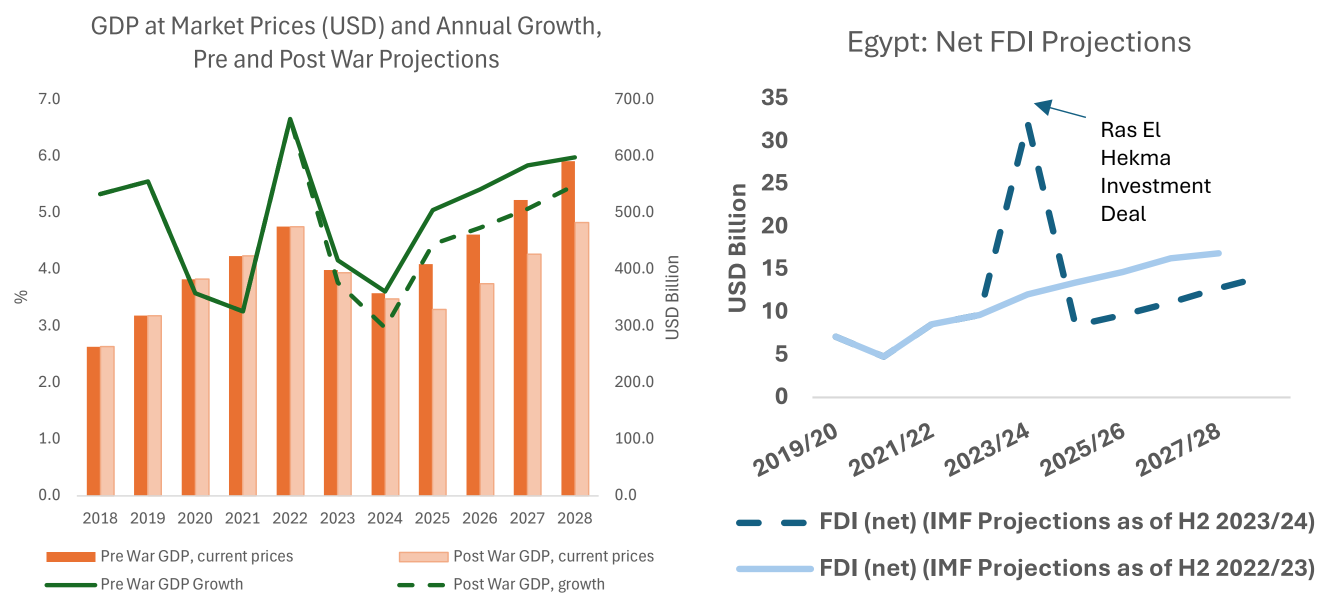
in the territories.

In neighboring countries like Egypt, growth prospects have already been affected by the war, but a prolonged and more intensive war in Gaza—set against significant geopolitical uncertainty—could have more severe and lasting macroeconomic implications. On the assumption that the war would be over by the end of 2024, growth prospects in Egypt have dampened. A comparison of pre- and postwar growth projections reveals that annual growth may fall between 0.5 and 0.6 percentage points per year by 2025. Suez Canal receipts fell by 47 percent in January 2024, year on year, and continued Red Sea attacks may work to permanently re-route maritime trade away from the Suez Canal, costing Egypt a dependable inflow of foreign currency and fiscal revenue. Should the war be prolonged and/or intensified, investor interest may shift away from Egypt and the region, making it a less favorable investment destination. It is therefore imperative for Egypt to be able to weather this unfavorable scenario by pursuing policies that reestablish and preserve macroeconomic stability and reform legacy structural imbalances.

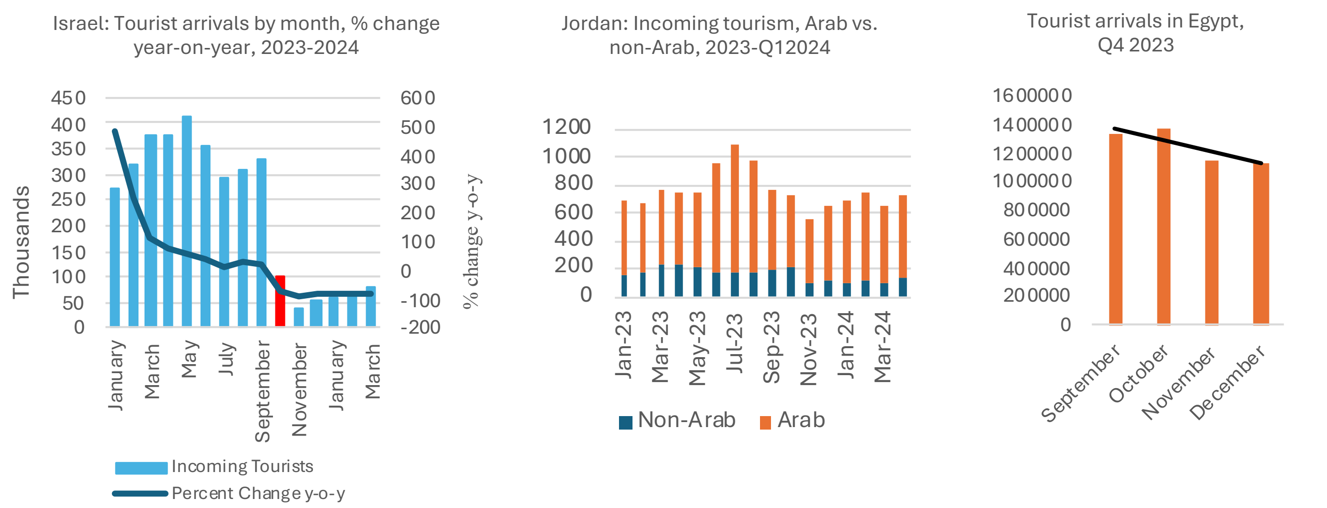
3. Economic Impact: Sectoral Breakdown

To date, the war in Gaza has predominantly impacted countries' tourism, agriculture, construction, and trade sectors, with negative spillovers to labor markets.

Tourism, especially from Western countries, fell from the start of the war in Gaza. In Israel, incoming tourism fell by 73 percent in October 2023 and even further in November, by 89 percent, year to year. Further escalation along Israel's



Source: IMF, Arab Republic of Egypt: First and Second Reviews Under the Extended Arrangement Under the Extended Fund Facility, Monetary Policy Consultation, and Requests for Waiver of Nonobservance of a Performance Criterion, and Augmentation and Rephasing of Access *Figure 17*



Source: [Israel CBS](#) and Author's Calculations

Source: [Central Bank of Jordan](#) and Author's Calculations

Source: CAPMAS and Author's Calculations

Figure 18

northern border with Lebanon will likely delay prospects of recovery. Neighboring countries have also been affected. Egypt's incoming tourism sector fell in the fourth quarter of 2023, ending the boost in tourism that returned numbers to their pre-COVID levels. In Jordan, "lost" tourism revenue is estimated to have reached JD 205 million between November 2023 and March 2024 as a result of travelers from non-Arab countries cancelling trips.[66] Another adversely affected sector was restaurants, partly due to reduced tourism since the onset of the Gaza war, but it also was the result of a national boycott of "branded" fast food chains that reported an 85 percent drop in revenues.[67] Similar boycotts have been spreading across the region; when McDonald's international's licensed division missed analyst expectations in the last quarter of 2023, the company cited the sharp fall in demand in the Middle East, Indonesia, and Malaysia.[68] Calls to boycott various brands continue to ripple throughout the region, and while some may be short-lived, consumers are apt to shift to buying substitute products on a more permanent basis. In Lebanon, where the tourism sector was one of the few that was somewhat resilient during the financial crisis of 2018, the war in Gaza adversely affected the sector and related businesses. Tourism fell 13.5 percent, year on year, during the first quarter of 2024, further impacting the livelihoods of those dependent on the sector.[69] Business in the restaurant sector fell by 80 percent during the last quarter of 2023, and hotel occupancy, after an initial moderate rise before October 7, fell to between 0-7 percent by the end of 2023.[70] Even countries farther from the conflict were impacted: Hotel reservations for Israeli tourists in Morocco at the end of 2023 were canceled, and New Year's holiday bookings came in at below pre-pandemic levels.[71] At the end of 2023, in its medium-term outlook, Banque du Maroc projected that travel receipts on average would remain stable in 2024 before picking up in 2025.

The construction sector in Israel was significantly affected once Palestinian workers from West Bank and Gaza were prevented from crossing into the country. On average, from 2018 to 2022, a quarter of the construction sector's employment consisted of Palestinians, most of whom live in the West Bank and rely on the work as their main source of income. Though 65 percent of the jobs in the sector are held by Israelis, construction is not a prominent source of employment for Israelis as it absorbs on average just 5 percent of Israel's workforce. As a result, the sector's economic activity has fallen

66. Jordan Ministry of Tourism and Antiquities, *Tourism Quarterly Review, Q1 2024*, 2024, https://mota.gov.jo/ebv4.0/root_storage/en/eb_list_page/quarterly_review_-_q1_2024_en.pdf.

67. Jordan Ministry of Tourism and Antiquities, T*ourism Quarterly Review, Q1 2024*.

68. Daria Mosolova, "Customer Boycotts Leave Bitter Taste for Starbucks and McDonald's," *Financial Times*, February 9, 2024, https://www.ft.com/content/d3995b6e-3b63-4f7b-958e-17f990975b20.

69. Famine Early Warning Systems Network, "Lebanon," accessed June 18, 2024, https://fews.net/middle-east-and-asia/lebanon; UN Office for the Coordination of Humanitarian Affairs, *Lebanon: At a Glance—Escalation of Hostilities in South Lebanon, as of 29 May 2024*, May 30, 2024, https://reliefweb.int/report/lebanon/lebanon-glance-escalation-hostilities-south-lebanon-29-may-2024-enar.

70. Sami Moubayed, "How Gaza War Fallout Impacted Regional Tourism," *Gulf News*, November 24, 2023, https://gulfnews.com/opinion/op-eds/how-gaza-war-fallout-impacted-regional-tourism-1.99561717.

71. Ahmed Eljechtimi, "Morocco Hit Record Tourism Arrivals Despite Quake and Gaza War," *Reuters*, December 18, 2023, https://www.reuters.com/world/africa/morocco-hit-record-tourism-arrivals-despite-headwinds-2023-12-18/.

by more than 50 percent since the start of the war.[72] Meanwhile, through government-to-government agreements and MOUs with India and Sri Lanka, the Israeli authorities are working to replace Palestinian workers with other foreign workers across key sectors, including construction.[73] These efforts include bringing close to 100,000 workers from India to fill positions left by Palestinians for a three-year period through 2026 and some 20,000 Sri Lankans brought in to work in the agriculture and construction sectors.[74] However, replacing Palestinian workers will present numerous challenges: It takes time to move workers, there are economic costs including lowered productivity, the costs of housing and healthcare, and education and welfare services. What's more, some Israelis fear that such a huge inflow of foreign workers may ultimately change the country's social fabric.[75] As a result, both the construction and agriculture sectors may continue to face significant labor shortages in the short to medium term.

Change in Economic Activity: Y-o-Y Q4-2023, %

Sector	Gaza	West Bank
Agriculture, Forestry, and Fishing	–93.4	–13.3
Mining, Manufacturing, Electricity, and Water	–92.1	–26.7
Construction	–96.2	–26.8
Wholesale and Retail Trade	–90.8	–17.7
Transportation and Storage	–90.3	–20.7
Finance and Insurance	–95.1	–7.2
Information and Communication	–90.0	–10.4
Services	–62.8	–12.7
Others (including Public Sector)	–83.4	–22.3
Total	–81.3	–18.8

Source: IMF, Arab Republic of Egypt: First and Second Reviews Under the Extended Arrangement Under the Extended Fund Facility, Monetary Policy Consultation, and Requests for Waiver of Nonobservance of a Performance Criterion, and Augmentation and Rephasing of Access[76]

Figure 19

In the Palestinian territories, economic activity has collapsed in Gaza and significantly contracted in the West Bank, with dire impacts on food security, poverty, and employment. The agro-processing sector in the Palestinian territories not only contributed 15 percent to GDP, it also was a notable source of employment and contributed to food security. Since the onset of the war, the damage to the wider agricultural sector is estimated at $629 million—most of it concentrated in the north—and 81-86 percent of all agricultural land was damaged.

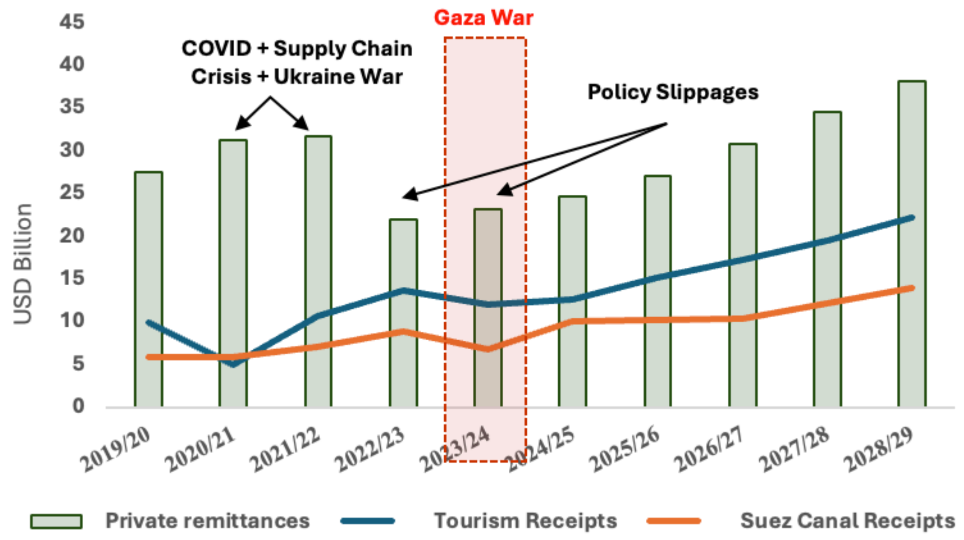
In Lebanon, where the conflict reached the country's southern border, almost three-quarters of farmers reported a loss of income. 1,240 hectares of land have been destroyed, 340,000 farm animals lost, 10 water facilities damaged, and 72 schools partially or fully closed.[77] In 2023, the agriculture and industry sectors in Lebanon saw negative growth of 3 and 8 percent, respectively, and the forecast for 2024 is a contraction in the agriculture sector of 10 percentage points.[78] If the conflict between Hezbollah and Israel escalates, the impact on the agriculture sector and the livelihoods of those who work in it will likely deepen and take longer to resolve.

4. Current Account Vulnerabilities

Depressed tourism revenue as a result of the war in Gaza, as well as any escalation of the conflict along Lebanon's southern border, will exert pressure on Banque du Liban's reserves and the country's ability to finance critical imports. Tourism is one of the few resilient sources of foreign currency inflow for Lebanon, and the government has relied on it to contribute to growth; conflict escalation, however, will deprive the Lebanese economy of the benefits from this inflow.

Against a backdrop of a mounting foreign currency crisis, the war in Gaza helped exacerbate Egypt's escalating macroeconomic challenges. Historically, and in the midst of the most severe macroeconomic shocks, Egypt could always depend on two relatively stable sources of foreign currency inflows: private remittances and Suez Canal receipts. However, and in the midst of rising inflation brought on by the Ukraine war, anemic foreign currency earnings due to unrealized export earning potential, and excessive spending on mega infrastructure projects, the macroeconomic stability gains achieved under Egypt's 2017 reform program slowly but assuredly declined. Ad hoc policies aimed at curtailing the demand for the dwindling source of foreign reserves pushed private remittances away from the financial system toward informal channels into the country, further stoking foreign currency pressures. Remittances continued to decline, by 21.2

72. Jeremy Sharon, "Despite Ostensible Ban, Tens of Thousands of Palestinians Working in Israel—report," *The Times of Israel*, March 24, 2024, https://www.timesofisrael.com/amid-ostensible-ban-tens-of-thousands-of-palestinians-working-in-israel-report/.
73. Middle East North Africa Financial Network, "Officials Announce Thousands of Indians Employees to Arrive in Israel," April 30, 2024, https://menafn.com/1108156205/Officials-announce-thousands-of-Indians-employees-to-arrive-in-Israel.
74. Uditha Jayasinghe, "Thousands of Sri Lankan Workers Set to Depart for Israel Despite War," *Reuters*, November 23, 2023, https://www.reuters.com/world/thousands-sri-lankan-workers-set-depart-israel-despite-war-2023-11-23/#:~:text=Dias%20is%20among%2020%2C000%20workers,minister%20told%20Reuters%20on%20Thursday.
75. Esteban Klor, "Is There a Connection Between Palestinian Workers in Israel and Terrorist Attacks Within the Green Line?," International Institute for Strategic Studies, June 17, 2024, https://www.inss.org.il/publication/palestinian-workers-data/.
76. World Bank, *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*.
77. UN Office for the Coordination of Humanitarian Affairs, *Lebanon: At a Glance*.
78. Economist Intelligence Unit. *Country Report: Lebanon*. June 2024.

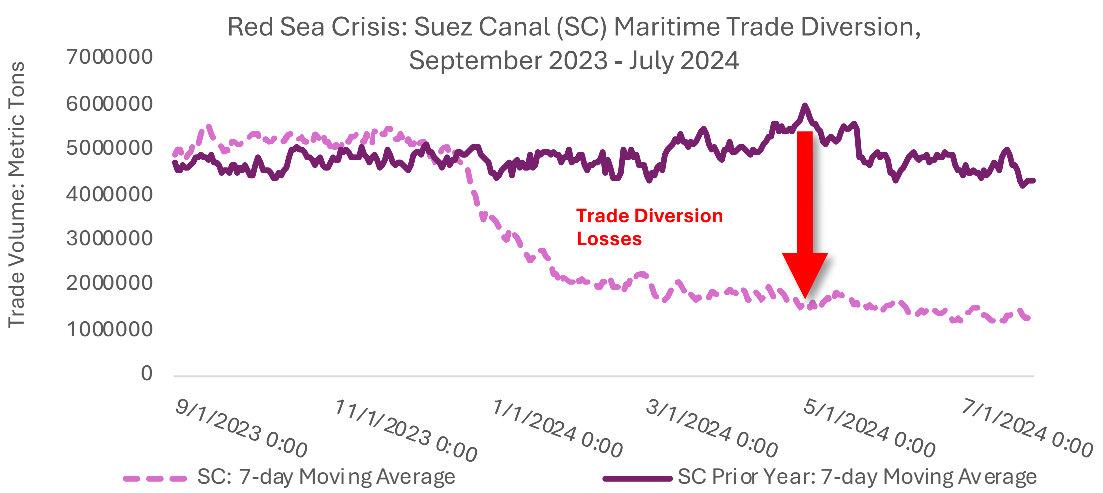


Source: IMF, Arab Republic of Egypt: First and Second Reviews Under the Extended Arrangement Under the Extended Fund Facility, Monetary Policy Consultation, and Requests for Waiver of Nonobservance of a Performance Criterion, and Augmentation and Rephasing of Access

Figure 20

percent, reaching only $9.4 billion in the first half of 2023-24.[79] The current account deficit narrowed in fiscal year 2022-23 to 1.2 percent of GDP, compared to 3.5 percent the prior fiscal year, due to lower non-oil imports brought on by foreign currency shortages, flourishing tourism activity which exceeded pre-COVID levels, and higher transport receipts from the Suez Canal. But the onset of the war in Gaza predictably depressed tourism revenue in the last quarter of 2023, and the attacks in the Red Sea by the Houthis on Israel-linked vessels reduced the historically consistent Suez Canal earnings by nearly half.

Rising energy costs, lower tourism receipts, and foreign currency pressures have adversely affected external positions of some Maghreb countries and Yemen. Morocco and Tunisia, as net importers of energy, felt the pressure of deteriorating trade balances and increased fiscal pressures due to rising energy import costs, which have strained public finances and external positions. Though the price of oil has shown moderate increases overall, its volatility has given rise to some uncertainty, thereby complicating fiscal planning and investment strategies. As for Yemen, the current account deficit increased by 1.5 percent in 2023 over 2022 to reach 19.3 percent due to the cessation of oil exports resulting from the Houthi-imposed blockade.[80] As a result, pressure on the Yemeni rial rose, and it depreciated in Aden , which is home to Yemen's official government, by end 2023. However, the decrease in



Sources: UN Global Platform; IMF PortWatch (portwatch.imf.org)

Figure 21

79. Central Bank of Egypt, *Balance of Payments (BOP) Performance During the First Half of FY 2023/2024*, 2024, https://www.cbe.org.eg/-/media/project/cbe/page-content/rich-text/bop/april-2024/press-release-balance-of-payments-performance-in-the-first-half-of-fy-2023-2024.pdf.

80. World Bank, *Yemen Economic Monitor: Navigating Increased Hardship and Growing Fragmentation*, Spring 2024, https://documents1.worldbank.org/curated/en/099926206242412700/pdf/IDU1dc601b321062b148fc1b59414e6cd5c70a66.pdf?_gl=1*mjdgmf*_gcl_au*MTExNDQyNDkwMy4xNzIzMjE3MTM3.

global commodity prices and lower domestic demand helped to markedly reduce inflation.

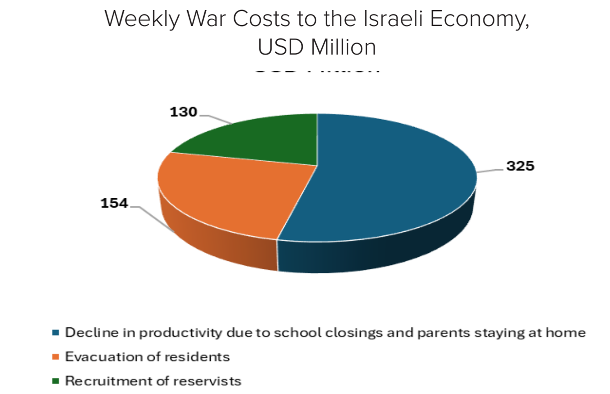
5. Fiscal impact

The fiscal costs from the war in Gaza differ depending on each country's profile. The fiscal burdens are greater for countries directly involved in the conflict.

During the fourth quarter of 2023, immediate militarization reportedly cost the Israeli economy close to $600 million per week, which equals roughly 6 percent of weekly GDP, due to reservist mobilization and school closures.[81] An estimated 360,000 reservists were mobilized, the second largest reservist mobilization in Israel's history, which made up almost 4 percent of the population and 8 percent of the labor force.[82] Furthermore, the evacuation of Israeli residents near the Gazan and the West Bank borders, as well as the closing of schools, led to significant absences from work.

Some estimates put the associated personnel costs at $41 million per day in the early days of the fighting; seven months into the war, those costs had begun to decline.

Israel's high militarization budget may crowd out other growth-enhancing revenue and expenditure allocations, undermining the government's efforts to firmly place debt on a downward trajectory. Prior to the war, the deficit was expected to reach around 2 percent of GDP, and debt was decreasing. Just over five months into the war, the Knesset approved an amended budget law that increased the budget deficit to 6.6 percent of GDP for 2024.[83] During the first quarter of 2024, cumulative expenditure growth came in at just under 36 percent more than the same period in 2023 and cumulative revenue growth fell by just over 2 percent over the same period.[84] To contain and cover some of the increased spending,



Note: Costs above do not include costs to the Israeli economy of labor shortages due to frozen work permits for Palestinian workers.

Source: Wrobel, The Times of Israel, accessed on May 13, 2024

Figure 22

the government decided to marginally increase the health tax, implement a 1 percentage point increase in the VAT, reduce the development expenditure outlays for Arab communities by 15 percentage points, and reduce budgets across all the ministries by 5 percentage points.[85] However, and despite attempts to rationalize expenditures and mobilize domestic resources, this amended wartime budget pushed the debt-to-GDP ratio along an upward trajectory over the medium term.[86] The latest data from the Ministry of Finance shows that as of August 2024, the budget deficit stood at 8.3 percent of GDP, vis a vis the 6.6 percent previously approved under the amended budget law in February 2024.[87] Other than military spending, the increase in expenditure outlays include funding for evacuated civilians and reserve soldiers amid the ongoing war until end of 2024.[88]

The Palestinian Authority has been grappling with an escalating fiscal crisis since the outbreak of the war. Sanctions imposed on the PA by the Israeli government in

81. Sharon Wrobel, "War Is Costing Economy Some $600M—Bank of Israel," *Times of Israel*, November 9, 2023, https://www.timesofisrael.com/war-is-costing-economy-some-600m-a-week-due-to-work-absence-bank-of-israel/.
82. Jennifer Hassan and Adam Taylor, "Israel's Massive Mobilization of 360,000 Reservists Upends Lives," *Washington Post*, October 10, 2023, https://www.washingtonpost.com/world/2023/10/10/israel-military-draft-reservists/; Matthias Dietrich, "Economic Fallout of Israel's Gaza Strip Operation Threatens Growth Prospects," International Institute for Strategic Studies, February 16, 2024, https://www.iiss.org/online-analysis/military-balance/2024/02/economic-fallout-of-israels-gaza-strip-operation-threatens-growth-prospects/.
83. Israeli Ministry of Finance, "The Knesset Approved Today (Wednesday) in the Second and Third Reading an Update to the State Budget 2024 Following the Expenses of the 'Swords of Iron,'" March 13, 2024, https://www.gov.il/en/pages/press_13032024.
84. Israeli Ministry of Finance, Estimated Budget Prediction: Data for 2024, August 8, 2024, https://www.gov.il/BlobFolder/news/press_09092024/en/PressReleases_eng_press_09092024-file1-eng.pdf.
85. *Haaretz*, editorial, "Israel's 2024 Budget Is All About Survival and Special Interests," January 16, 2024, https://www.haaretz.com/opinion/editorial/2024-01-16/ty-article-opinion/israels-2024-budget-is-all-about-survival-and-special-interests/0000018d-0ef4-d71c-ad9f-4ff68df00000.
86. International Monetary Fund, World Economic Outlook Database, April 2024, https://www.imf.org/en/Publications/WEO/weo-database/2024/April/download-entire-database.
87. Bank of Israel, *The Macroeconomic Forecast of the Research Division, July 2024*, July 8, 2024, https://www.boi.org.il/publications/pressreleases/07-7-24/.
88. Sharon Wrobel, "Israel Budget Chief Warns about Dangers of Spending Limit Breaches to Economy," *Times of Israel*, September 11, 2024, https://www.timesofisrael.com/israel-budget-chief-warns-about-dangers-of-spending-limit-breaches-to-economy/.

the form of larger withholdings from clearance revenues[89] related to Gaza payments have reduced revenue receipts by more than 50 percent.[90] Furthermore, the severe economic contraction and the persistently low levels of foreign aid have weighed heavily on the budget and pushed the financing gap for 2023 to $682 million, equivalent to 3.9 percent of GDP.[91] The financing gap was filled by borrowing from domestic banks and higher arrears to the private sector, public employees, and the pension fund.[92] Estimates potentially indicate that, ceteris paribus, the financing gap is more recently projected to reach $1.86 billion in 2024, vis a vis $1.2 billion in May of 2024.[93][94] Such a persistently high and growing financing gap, coupled with the constrained resource mobilization landscape and potential, means the Palestinian Authority's fiscal position is on the verge of calamity.

Though debt servicing is currently out of the budget's expenditure, and the deficit may be contained to 1.8 percent in 2024, the spillovers from the war in Gaza, including the escalating conflict along the southern border, could exacerbate Lebanon's weakened fiscal position.[95] The drop in tourism since the start of the war in Gaza reduced foreign currency inflows which play a critical role in helping to finance imports. That, along with a continuation or escalation of the conflict along Lebanon's southern border, will adversely affect the agriculture sector and food supply in the country. Food shortages may raise prices and fuel inflation and food insecurity, placing additional pressure on the government to increase its support of the most vulnerable individuals in the population, further straining the government's fiscal position.

6. Impact on Banking and Financial Stability

To mitigate the impact of the war, the BOI took steps to preserve macroeconomic and financial stability and to support households and small businesses. To maintain financial stability, the BOI intervened through a series of measures, including foreign currency sales, swap transactions, a repo program, and other credit easing programs designed to calm the markets and reduce uncertainty. In January 2024, the BOI lowered rates by 25 basis points to help stabilize the economy, noting that reduced economic activity had lowered inflation to below the uppermost band.[96] The GOI also introduced a series of measures aimed at supporting workers and businesses affected by the conflict, including the impact of the mass call on reservists to military duty. These measures included cash transfers, postponement of social security payments, deferral of value-added tax payments, and flexible loan terms, among others.[97]

The Palestinian Monetary Authority maintains strong oversight of the banking sector, but even though the banking system is liquid, well capitalized, and in line with the Basel III requirements, political, institutional, and economic challenges from the war have put extreme pressure on the banking system. The government of Israel extended a waiver, set to expire at the end of June, that allows Israeli banks to cooperate with Palestinian banks without fear of legal reprisals, thereby sustaining correspondent banking relationships and avoiding a banking and economic crisis in the Palestinian territories.[98] After the onset of the war, the Israeli government threatened to cut off ties between Israeli and Palestinian banks, a move that would have severely affected the economies of Gaza and the West Bank. It is imperative to maintain correspondent banking relationships with Israeli banks so as to process shekels earned by the West Bank economy for services and salaries. These banking relationships are critical for processing almost $8 billion a year in imports from Israel, which include electricity, water, fuel, and food. They also facilitate around $2 billion a year in exports from the Palestinian territories.[99]

89. Clearance revenues are revenues collected by the government of Israel on behalf of the Palestinian Authority and transferred after deductions have been made. The majority of said revenues are VAT and import duties and need to be remitted monthly according to the Paris Protocol signed in 1994 by the Palestine Liberation Organization and the government of Israel. See World Bank, *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy, and UN Trade and Development, Palestinian Fiscal Revenue Leakage to Israel Under the Paris Protocol on Economic Relations*, accessed July 2, 2024, https://unctad.org/publication/palestinian-fiscal-revenue-leakage-israel-under-paris-protocol-economic-relations.

90. World Bank *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*.

91. World Bank *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*; Palestine Economic Policy Research Institute, *Palestine Economic Update: May 2024*, https://mas.ps/en/publications/10299.html.

92. World Bank, *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*.

93. World Bank, World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy, September 2024.

94. Palestine Economic Policy Research Institute, Palestine Economic Update: May 2024.

95. Economist Intelligence Unit. *Country Report: Lebanon*. June 2024.

96. Bank of Israel, "The Economy and Economic Policy During Social Crisis and War," in *Bank of Israel Annual Report 2023*, March 28, 2024, https://www.boi.org.il/media/2euk2zws/chapter-1-2023.pdf.

97. Economist Intelligence Unit. *Country Report: Israel*. April 2024.

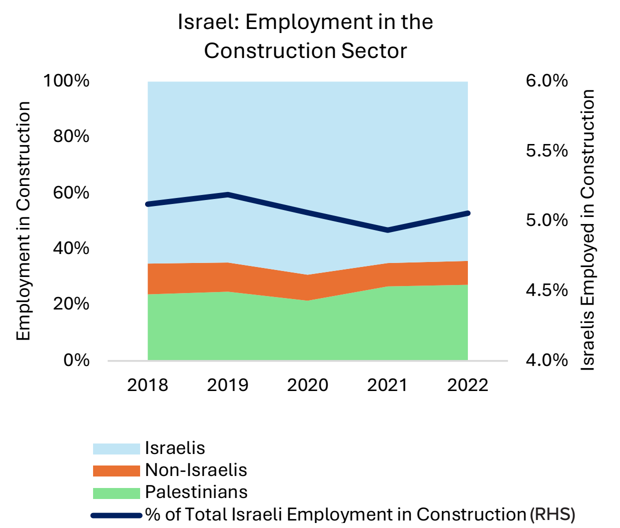
98. *Reuters*, "Israel Extends Cooperation Between Israeli and Palestinian Banks, Official Says," June 30, 2024, https://www.reuters.com/world/middle-east/israel-extends-cooperation-between-israeli-palestinian-banks-official-says-2024-06-30/.

99. David Lauder, "Yellen Concerned about Israel's Threats to Cut Off Palestinian Banks," *Reuters*, May 23, 2024, https://www.reuters.com/world/middle-east/yellen-concerned-about-israels-threats-cut-off-palestinian-banks-2024-05-23/.

7. Impact on the Labor Market

Labor market shocks in the epicenter of the conflict and in neighboring countries may have longer lasting effects if the war continues and/or the conflict along the southern border of Lebanon escalates. In Israel, the labor supply shocks have had a significant impact. At the start of the war, an estimated 360,000 reservists were mobilized. At almost 4 percent of the population and almost 8 percent of the labor force, this was estimated to be the second largest reservist mobilization in Israel's history.[100] Furthermore, the government suspending work permits for Palestinians to cross into Israel, citing unnecessary security risk, further exacerbated Israel's labor supply shortage in certain sectors of the economy.[101] Right before October 7, close to 170,000 Palestinian workers (150,000 from the West Bank and 20,000 from the Gaza Strip) were entering Israel for employment.[102] After October 7, the Ministry of Defense froze work permits of Palestinians entering Israel, severely impacting the construction and agriculture sectors. The agricultural sector, though a relatively small sector in the economy (it contributes an average of 2 percent to GDP), is heavily dependent on foreign workers, including Palestinians and Thai nationals. During harvest time, it relied on volunteers to help, but the construction sector, relying on labor of various skills, may continue to grapple with significant labor shortages despite the Israeli authorities' plan to replace Palestinian workers with workers from South Asia.

Unresolved labor shortages and legacy structural imbalances will continue to impede the Palestinian's economy's full recovery through the medium term. The continued ban on Palestinian labor, coupled with the inability to replace these workers with similarly skilled foreign labor in a timely manner, will particularly impact the construction and agriculture sectors. Furthermore, addressing the Israel Defense Forces' (IDF) increased manpower needs may necessitate extending military service for individuals and reduce their contribution to civilian economic activity. In that regard, domestic policy discussions around including the Haredi population in military service is expected to continue. It will be necessary to address the legacy structural challenges that existed in the economy prior to the Gaza war—including low labor productivity, low employment



Sources: Central Bank of Israel Central Bureau of Statistics

Figure 23

rates among the Arab and Haredi populations, and raising the standard of living in Israel—for the economy to fully optimize resources for growth and development. A recent study by the BOI found that for a cost of 3 percent of GDP per annum, the economy's potential for growth could increase by more than 20 percent of GDP in the medium to long run.[103]

In the Palestinian territories, the extent of the labor market shock may be difficult to evaluate due to the ongoing war. Already weakened by high levels of unemployment prior to October 7, preliminary estimates show that unemployment in Gaza increased to 75 percent in the fourth quarter of 2023, and more than 201,000 jobs were lost by the end of January 2024.[104] In the West Bank, where the labor market relies on the private sector and Israel, unemployment increased in Q4 2023 to 32 percent, compared to 13 percent the previous quarter, as a result of suspending Palestinian work permits to Israel, restricting movement and disrupting communication across the West Bank, and the faltering economic activity these caused.[105] Simply put: The labor market in Gaza has collapsed. Recent estimates by the International Labour Organization (ILO) reveal that unemployment in Gaza and the West Bank has now reached 79.1 and 32 percent,

100. Hassan and Taylor, "Israel's Massive Mobilization of 360,000 Reservists Upends Lives"; Dietrich, "Economic Fallout of Israel's Gaza Strip Operation threatens growth prospects."

101. A recent study examined the claim that Palestinians entering Israel with work permits pose a security rise to Israel. It concluded that violence from Palestinians with work permits was very rare. In its policy recommendation, the study highlighted that not allowing Palestinians to work in Israel damages the Palestinian economy (Israeli-sourced employment contributes one-fifth of Palestinian GDP) and, as a result, may actually raise desperation and lower the opportunity cost of conflict, thereby increasing the security risk to Israel. See Klor, "Is There a Connection Between Palestinian Workers in Israel and Terrorist Attacks Within the Green Line?"

102. Sharon, "Despite Ostensible Ban, Tens of Thousands of Palestinians Working in Israel."

103. Bank of Israel, "The Economy and Economic Policy During Social Crisis and War."

104. World Bank, *World Bank Economic Monitoring Group: Impacts of the Conflict in the Middle East on the Palestinian Economy*.

105. Palestinian Central Bureau of Statistics, "On the Occasion of the International Workers' Day, H.E. Dr. Ola Awad, President of Palestinian Central Bureau of Statistics (PCBS), Presents the Current Status of the Palestinian Labour Force in 2023, https://www.pcbs.gov.ps/portals/_pcbs/PressRelease/Press_En_InterWorkDay2024E.pdf.

respectively.[106] In Q4 2023, 88 percent of Palestinians in the West Bank working in Israel became unemployed as a result of the suspension of their work permits, and 72 percent who had worked in the Israeli settlements prior to October 7 lost their jobs.[107] Across the Palestinian territories, unemployment has surpassed 50 percent.[108]

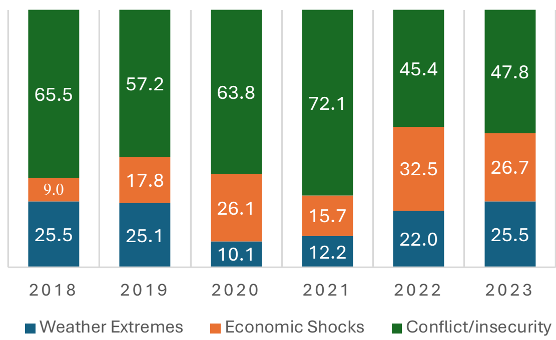
B. SOCIAL COST OF CONFLICT: FOOD INSECURITY AND SOCIAL VULNERABILITY

There are three main drivers of acute food insecurity: extreme weather, economic shocks, and conflict/insecurity.[109] While data on food insecurity is often difficult to obtain, insights from the World Food Program suggest the number of people suffering from acute food insecurity in 2023 more than doubled over pre-pandemic levels to 333 million.[110] In the Middle East and North Africa, conflict and economic shocks are the prevalent drivers of acute food insecurity. These two drivers are often intertwined, with conflict resulting from or contributing to food insecurity.[111] The pathways from conflict to food insecurity are born of several failures. In the extreme case when conflict destroys physical capital and institutions, it disrupts food systems and production processes, thereby impeding public service delivery. Even if physical capital is not destroyed, socioeconomic activity is still adversely impacted and food insecurity is an outcome. The extent of the impact depends on the level of growth and development of the affected country or countries, and this is where the double incidence of economic shocks and conflict, as is the case in some countries in the MENA region, produces the worst outcome. In 2023, nearly a quarter of the global population needing humanitarian assistance resided in the region.[112]

Using the 1996 World Food Summit's definition of food security, it is a multifaceted state with four crucial dimensions: Food is available, all people have physical access to it, they are able to afford it, and they can utilize it according to their preferences. Implicit in this definition is a country's macroeconomic stability, or lack thereof, and its external position—more specifically, its ability to generate foreign currency to finance food imports. Needless to say, the level of overall growth and development will determine the extent of a country's food insecurity. An indicator that measures the state of food security at the macro level was developed by Breisinger et al.[113] This macro food security indicator takes into account two of the region's exceptional characteristics: Most of the countries are net food importers, and they are either net labor exporters or importers. Therefore, each country's ability to generate the foreign currency required to import food depends in part on workers' remittances as a vital source of net foreign currency inflows. The higher the ratio of food imports to total foreign currency inflows (exports and net worker remittances), the more a country's food security is vulnerable to their foreign currency earning potential and related shocks.

By late 2023, the status of the Gaza Strip was elevated to being the most severe food crisis in IPC and GRFC history. By the fourth quarter of 2023, food prices in Gaza had increased by 39 percent, quarter on quarter, and the cessation of fuel and gas supplies through the crossings led to a 143 percent increase in transportation costs in Gaza in Q4 2023, quarter on quarter.[114]

Drivers Of Acute Food Insecurity, 2018-2023, % Of Acute Food Insecure Globally



Source: [*2024 Global Report on Food Crises*](), *accessed 05-31-24.*

Figure 24

106. United Nations, "Amid Gaza War, Children Now Work So Families Can Survive: ILO," *UN News*, June 7, 2024, https://news.un.org/en/story/2024/06/1150776; Gabrielle Tétrault-Farber, "Unemployment Nears 80% in Gaza, UN Agency Says," *Reuters*, June 7, 2024, https://www.reuters.com/world/middle-east/unemployment-nears-80-gaza-un-agency-says-2024-06-07/.

108. Palestinian Central Bureau of Statistics, "On the Occasion of the International Workers' Day."

109. Tétrault-Farber, "Unemployment Nears 80% in Gaza."

110. Food Security Information Network, *2024 Global Report on Food Crises*, accessed May 31, 2024, https://www.fsinplatform.org/report/global-report-food-crises-2024/.

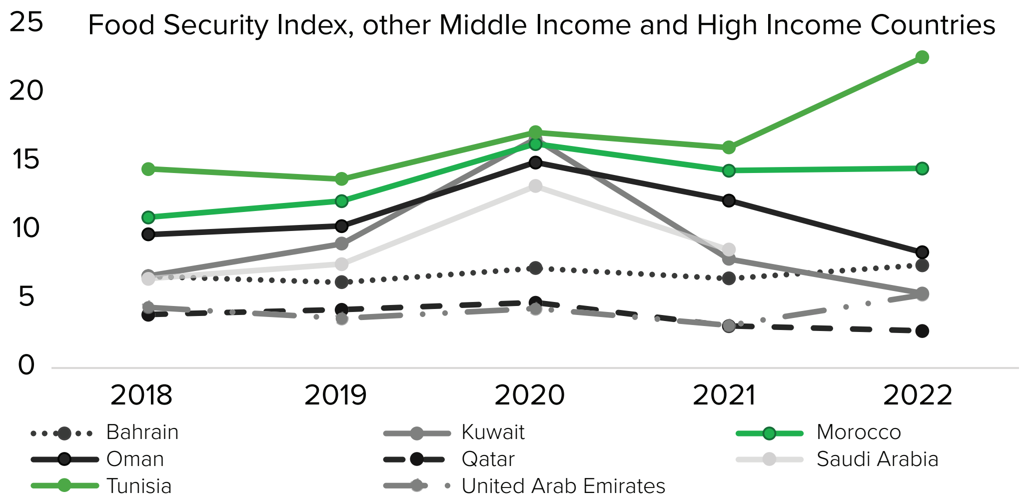
111. World Food Programme, "A Global Food Crisis," accessed May 31, 2024, https://www.wfp.org/global-hunger-crisis#:~:text=WFP%20estimates%20%E2%80%93%20from%2078%20of%20the%20countries,know%20where%20their%20next%20meal%20is%20coming%20from.

112. Clemens Breisinger et al., *Building Resilience to Conflict Through Food Security Policies and Programs: Evidence from Four Case Studies*, International Food Policy Research Institute, May 2014, https://ebrary.ifpri.org/utils/getfile/collection/p15738coll2/id/128136/filename/128347.pdf.

113. United Nations Economic and Social Commission for Western Asia, *Inequality in the Arab Region: Crisis upon Crisis*, 2024, https://www.unescwa.org/sites/default/files/inline-files/inequality-arab-region-crisis-key-messages-english.pdf.

114. Clemens Breisinger et al., *Beyond the Arab Awakening: Policies and Investments for Poverty Reduction and Food Security* (Washington, DC: International Food Policy Research Institute Food Policy Report, 2012), http://ebrary.ifpri.org/cdm/ref/collection/p15738coll2/id/126781.

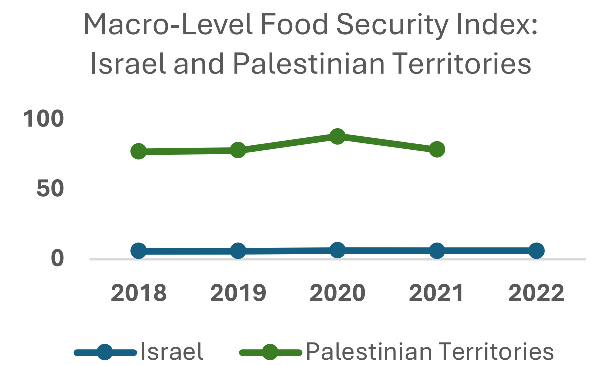
115. Food Security Information Network, *2024 Global Report on Food Crises*.



Sources: Online IMF Database. Balance of Payments and International Investment Position - Search - IMF Data. Accessed 04-29-24
World Bank WDI Indicators taken from WB Data Bank online
Breisinger et al, 2014

Figure 25

The Gaza war has compromised food security in the three neighboring countries in a landscape already hampered by preexisting economic challenges. The area's most vulnerable populations have been affected, including refugees living in these three countries (Figure 27 below). In Lebanon, the severe currency devaluation triggered by the financial crisis in October 2019 set the stage for a rapidly deteriorating food security situation in a country that relies on imports for most of its food and non-food needs. Furthermore, the damage to the country's main grain silos during the Beirut port explosion in August 2020 undermined both the supply and access to food.[115] The record fall in the value of the local currency led to soaring food inflation, which reached 352 percent in March 2023 and impacted the most vulnerable members of the Lebanese and refugee populations.[116] Food insecurity in Lebanon deteriorated further when the attacks in Gaza escalated into cross-border fighting between the IDF and Hezbollah between October 2023 and March 2024. Fighting on the southern border of Lebanon resulted in over 90,000 people fleeing to the north of the country toward safety, compromising their livelihoods and their access to food.[117].



Sources: same as figure 25

Figure 26

Displacement to Host Countries in MENA, 2023

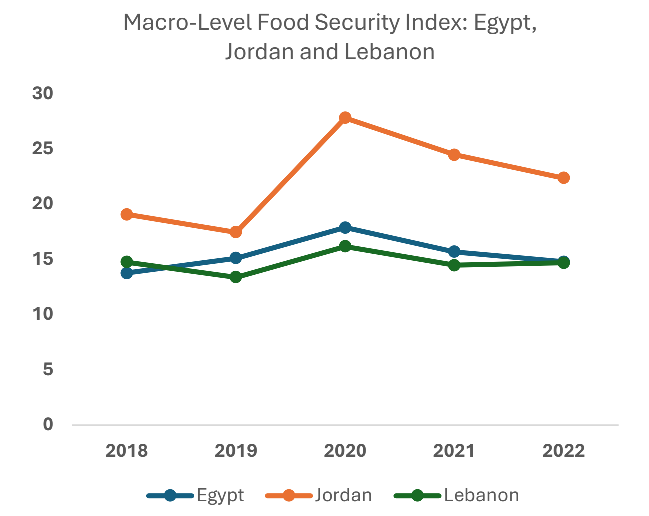
Country	Total Number of Forcibly Displaced People (Million)	IDPs (Million)	Refugees and Asylum-Seekers (Million)	Country of Origin
Algeria	0.1	0	0.1	Western Sahara, Syria, Mali
Egypt	0.8	0	0.8	Sudan, Syria, Palestine
Iraq	1.4	1.1	0.3	Syria, Iran, Turkey
Jordan	3.1	0	3.1	Palestine, Syria, Iraq
Lebanon	1.4	0.07	1.3	Palestine, Syria, Iraq
Palestinian territories	1.7	1.7		
Syria	7.3	6.6	0.6	Palestine, Iraq, Afghanistan
Yemen	2.9	2.8	0.07	Somalia, Ethiopia, Syria

Source: FSIN and Global Network Against Food Crises, 2024. accessed 05-31-24)

Figure 27

116. Food Security Information Network, *2024 Global Report on Food Crises*.
117. Food Security Information Network, *2024 Global Report on Food Crises*.
118. Famine Early Warning Systems Network, Reduced Assistance in Lebanon Leads to Widening Consumption Gaps, March 2024, https://fews.net/node/31915/print/download.

Whether fragility results from conflict, weak macroeconomic conditions, and/or institutional weaknesses, the war in Gaza is impacting the region's vulnerable and fragile economies. Taking the case of Yemen, even before the war in Gaza, close to a decade of protracted civil conflict and severe socioeconomic conditions had already destroyed economic opportunity and livelihoods in the country. Internal flare-ups have increased recently, resulting in some displacement, though well below pre-truce (2022) levels. The Sanaa-based authorities' (SBA) sanctioned attacks on maritime shipping in the Red Sea and the Gulf of Aden have exacerbated the already dire food security conditions in Yemen. Fishing and related supply chain livelihoods have been disrupted, and further UN-brokered peace negotiations between the Internationally Recognized Government (IRG) and SBA are on hold due to the conflict in the Middle East.[118] Livestock have been sold off because of the herders' inability to afford the necessary fodder to rear the animals to maturity. Climate-change-related weather shocks, which have become more frequent and more intense, caused crop failures that further affected agricultural livelihoods. And in response to the Houthi maritime attacks, humanitarian food assistance has been paused. Finally, Yemen imports around 90 percent of its staple cereals and all of its staple rice and sugar supply, most of which enters through the SBA-controlled Red Sea ports. In the face of a depreciating currency in the IRG-controlled areas, millions of people will continue to suffer from acute food insecurity. For other FCS and their displaced populations, the socioeconomic impact of the war in Gaza on the hosting economies will land most heavily on the vulnerable segments of the population.



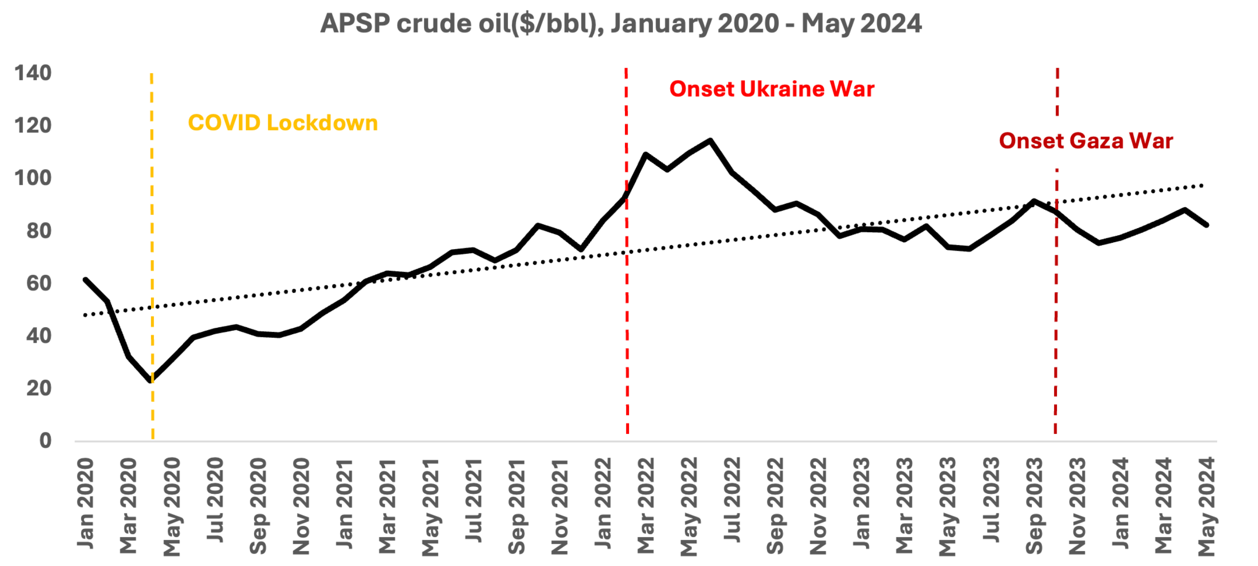
Sources: same as figure 25, 26 *Figure 28*

Humanitarian aid flows to Gaza, clean water availability, and fuel supply deliveries have declined by 80 to 90 percent below normal levels since the start of the war. The dire humanitarian conditions worsened even further after Israeli forces closed key crossings (including Rafah and Erez) to aid entering Gaza. When compared to previous conflict episodes between Gaza and the IDF, there can be no doubt that the current one has wrought by far the most significant damage. The ongoing war is projected to raise the poverty rate to 60.7 percent across the Palestinian territories, and Gaza's economy and development has been set back 40 years, according to some estimates.[119]

119. Famine Early Warning Systems Network, *Despite Seasonal Improvement with Ramadan, Food Consumption Gaps to Widen*, accessed June 6, 2024, https://fews.net/middle-east-and-asia/yemen/food-security-outlook/february-2024.

120. Palestine Economic Policy Research Institute, *Palestine Economic Update: May 2024*.

III. Global impacts



Sources: IMF, accessed June 8, 2024

Figure 29

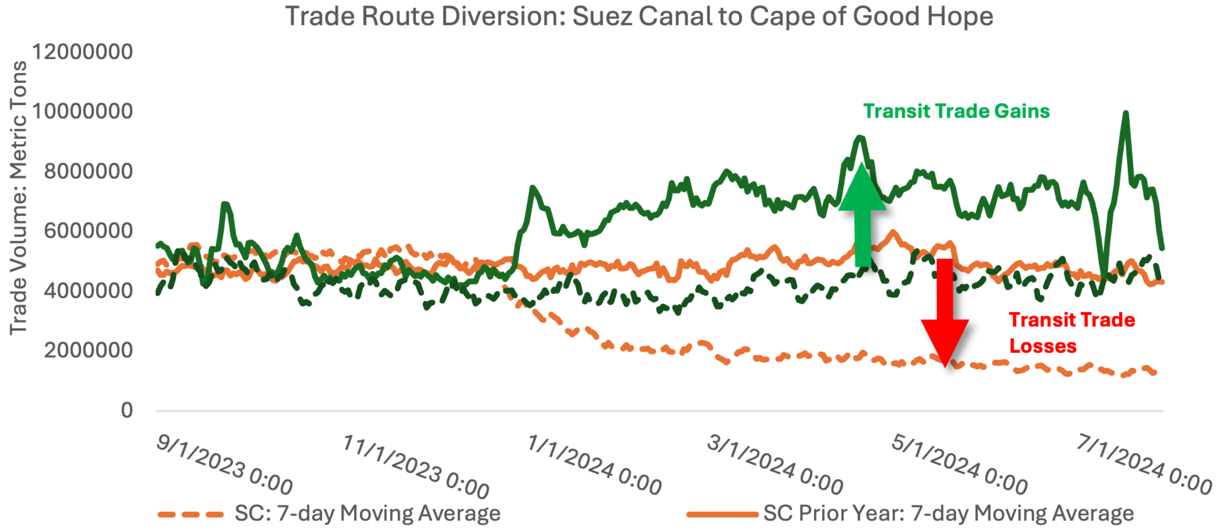
A. GEOPOLITICAL RISKS AND COMMODITY MARKETS

Since the start of the war in Gaza, the conflict along the southern border of Lebanon, and the Red Sea attacks, oil supplies have managed to stay resilient, and the price of crude has remained below levels recorded during previous geopolitical flareups in the Middle East. Initially, though, oil prices rose as markets reacted to potential supply disruptions, with prices ticking up from around $85 per barrel to over $95 within a few weeks. Natural gas prices in Europe also rose by around 10 to 15 percent due to a fear of wider regional instability. Both the supply-side and demand-side dynamics led to a mostly moderate movement in oil prices, even after OPEC+ began voluntary production cuts[120] in late 2022. On the supply side, higher output by non-OPEC+ countries, including the United States, Brazil, and Guyana, has outpaced global demand for oil. More specifically, technological advancements and improved well productivity in the US shale oil market has helped boost US shale oil production to three-quarters of US oil on the global market.[121] The steadily increasing non-OPEC+ supply and weaker global demand for oil, especially from China, has helped curb price pressures despite the increase in global freight rates of oil tankers by around 50 percent.

Lower interest rates in advanced economies may help revive global demand for oil and exert upward pressure on oil prices, especially if maritime rerouting away from the Red Sea continues due to recurring attacks there. The European Central Bank projected that the inflation rate across the block will reach 2 percent by the end of 2024 and in early June lowered its rate by 25 basis points—its first rate cut in five years. With global inflation steadily converging to central banks targets, rate cuts may start to take place across advanced economies, easing financing conditions and spurring global demand. Under this scenario, if the maritime disruptions continue in the Red Sea, however, the longer and more expensive routes may finally start impacting the price of oil, especially since one of the main routes that has been most affected is the Middle East to Europe route, where shipping costs increased by 200 percent from mid-November 2023 to mid-March 2024. In general, geopolitical tensions and conflict

121. OPEC+ announced in early June that it would extend most output reductions into 2025, but it may begin phasing out some voluntary cuts at the end of the third quarter of 2024, subject to market conditions. See Camilla Palladino, "Opec+ Is Running Out of Road," *Financial Times*, June 4, 2024, https://www.ft.com/content/862a4d03-0428-4034-96ee-ab0d4fbf87fe.

122. Palladino, "Opec+ Is Running Out of Road"; *Reuters*, "US Oil Output in Top Shale Regions to Hit Six-Month High in June, EIA Says," May 13, 2024, https://www.reuters.com/business/energy/us-oil-output-top-shale-regions-hit-six-month-high-june-eia-2024-05-13/#:~:text=Shale%20production%2C%20which%20represents%20about%20three-quarters%20of%20total,highest%20monthly%20output%20per%20rig%20since%20November%202021.



Sources: UN Global Platform; IMF PortWatch (portwatch.imf.org)
Acessed September 24, 2024

Figure 30

escalations may further constrain cross-border flows of food, fuel, and fertilizer, potentially compromising global inflation dynamics, food security, and global growth prospects.[122]

B. GLOBAL FINANCIAL RISKS

Inflation globally has been converging toward target levels and rate hikes have hated and even reversed; as a result, investor risk appetite has been steadily growing. Though inflation has declined worldwide, central banks across the world remain vigilant to ensure that inflation safely converges to target levels.[123] Global financial conditions have loosened, generally speaking, and several low-income, developing economies have been able to re-access international markets.[124]

Additional interest rate cuts in advanced economies may help ease fiscal pressures in debt-burdened economies elsewhere and work to improve debt dynamics. However, the still high interest rates, elevated deficits, and softer than anticipated growth in debt-ridden countries may pose risks to their outlook if refinancing costs rise.

C. MARITIME DISRUPTIONS AMID SECURITY CONCERNS

The Red Sea attacks that started in November 2023 disrupted 12 to 15 percent of that year's global maritime trade. Ongoing attacks have since disrupted supply chains by diverting maritime trade routes away from the Suez Canal toward the Cape of Good Hope. The Suez Canal is the shortest maritime route between Asia and Europe.[125] Prior to the Houthi attacks in the Red Sea, the Suez Canal handled 25 to 30 percent of all container shipping, 12 percent of seaborne oil, and 8 percent of seaborne LNG and of the grain trade.[126] However, after the Houthi attacks, 9 out of 10 large container ships have been diverted en route from Asia to Europe, presenting a myriad of challenges for the global community and the countries directly involved.[127] While the rerouting has not yet led to inflationary pressures globally, trade between Asia and Europe has been hit hardest, since 40 percent and 95 percent of trade and ships traveling back and forth between the two regions, respectively, would normally cross through the Red Sea. Moreover, the Red Sea

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123. International Monetary Fund, *Steady But Slow: Resilience Amid Divergence*, World Economic Outlook, April 2024, https://www.imf.org/en/Publications/WEO/Issues/2024/04/16/world-economic-outlook-april-2024.

124. In June, 2024, the ECB lowered rates by 25 basis points, pointing to an eventual rate reduction by the US as well.

125. International Monetary Fund, "The Last Mile: Financial Vulnerabilities and Risks," April 2024, https://www.imf.org/en/Publications/GFSR/Issues/2024/04/16/global-financial-stability-report-april-2024.

126. Parisa Kamali et al., "Red Sea Attacks Disrupt Global Trade," International Monetary Fund (blog), March 7, 2024, https://www.imf.org/en/Blogs/Articles/2024/03/07/Red-Sea-Attacks-Disrupt-Global-Trade; Congressional Research Service, Red Sea Shipping Disruptions: Estimating Economic Effects, May 8, 2024, https://crsreports.congress.gov/product/pdf/IF/IF12657#:~:text=Some%20analysts%20estimate%20that%20the%20temporary%20blockage%20of,growth%20by%200.2%20to%200.4%20percentage%20points%20%28p.p.%29.

127. Congressional Research Service, *Red Sea Shipping Disruptions: Estimating Economic Effects*.

128. Costas Paris, "Ship Freight Rates Soar as Red Sea Diversions Become a Norm," *Wall Street Journal*, May 20, 2024, https://www.wsj.com/business/logistics/ship-freight-rates-soar-as-red-sea-diversions-become-a-norm-79f33b7c.

disruptions have impacted Israeli ports as shipping hubs,[128] with Bay Port's operations dropping by 40 percent since the outbreak of the war, mainly as a result of lower trans-shipment activities.[129] Indeed both Haifa's Bay Port and Ashdod Port fell in the overall ranking according to the World Bank's Container Port Performance Index 2022 and 2023 when globally comparing operational performance across ports.[130] Not only do the trade disruptions undermine the movement of critical food and humanitarian supplies headed for Africa, but a prolonged diversion in maritime trade routes will also impact all the affected regions in both the short and medium term.

The maritime trade route diversion yields both economic and climate-related consequences. Shipping capacity overexpanded after 2021 when e-commerce increased to satisfy lockdown constrains and the spike in global demand. The resultant overcapacity then caused freight prices to drop to a third of their 2021-22 levels. By contrast, the current maritime route diversion is raising container freight charges by nearly 30 percent. Despite these increases, weak global consumer demand and a sizable slack in firm profit margins kept prices stable despite the higher freight costs. If the status quo continues, longer-term freight rates will most likely be determined by EU environmental regulations and their relevant additional costs.[131] Maritime emissions, however, are expected to rise in 2024 due to the longer routes and higher speeds needed to cross those distances in time. Maritime trade on average contributes around 3 percent to global emissions; in an attempt to achieve climate neutrality in the EU by 2050, including an intermediate target of (at least) a 55 percent net reduction in greenhouse gas emissions by 2030, the European Commission recently implemented a series of maritime legislative proposals aimed at meeting these objectives.[132] If access through the Red Sea remains blocked, the longer shipping routes, faster speeds, and increased use of smaller and less fuel-efficient vessels[133] will likely be an obstacle to achieving these goals.[134] Current compliance costs for the sector will have to increase to align with the regulations underpinning maritime emissions under the EU's Emission Trading System, which began in January 2024.[135] If the higher shipping costs stick, and global consumer demand picks up—which it may if the US also lowers interest rates following the ECB's rate reduction in early June—those higher costs may cause global inflationary pressures, especially since the Houthi attacks in the Red Sea are ongoing.

129. Julia Frankel, "Israel's Economy Is Struggling. Economists Say Ending the War Would Help," Associated Press, August 26, 2024, https://www.msn.com/en-us/money/companies/israels-economy-is-struggling-economists-say-ending-the-war-would-help/ar-AA1pqu4E?ocid=BingNewsVerp.

130. Galia Lavi, "Three Years of the Bay Port: A Status Report," The Institute for National Security Studies, INSS Insight No. 1895, September 10, 2024, https://www.gov.il/en/pages/glcier10092024.

131. World Bank, The Container Port Performance Index 2022: A Comparable Assessment of Performance Based on Vessel Time in Port (English), Washington, DC: World Bank Group, http://documents.worldbank.org/curated/en/099051723134019182/P1758330d05f3607f09690076fedcf4e71a

132. Economist Intelligence Unit, "Red Sea Risks and EU ETS Will Hurt Maritime Sector," March 12, 2024, Global trade update: Red Sea disruptions - Economist Intelligence Unit (eiu.com).

133. European Commission, "Monitoring, Reporting and Verification of EU ETS Emissions," accessed May 29, 2024, https://climate.ec.europa.eu/eu-action/eu-emissions-trading-system-eu-ets/monitoring-reporting-and-verification-eu-ets-emissions_en.

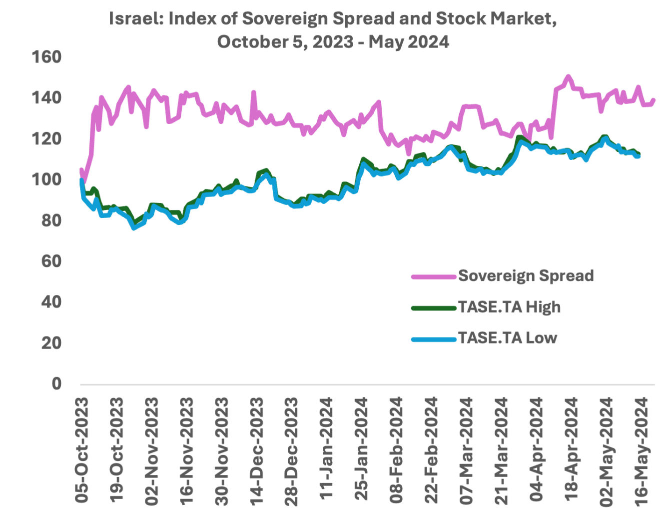
134. Security concerns as a result of the Red Sea attacks and capacity constraints led to the increased use of smaller and less fuel efficient sea vessels in maritime shipping routes.

135. World Economic Forum, "What Is 'Slow Steaming' and Why Is the Red Sea Crisis Affecting Shipping Emissions?," March 19, 2024, https://www.weforum.org/agenda/2024/03/slow-steaming-emissions-red-sea-trade/.

136. Economist Intelligence Unit, "Red Sea Risks."

IV. Conclusion

Adverse geopolitical developments in the Middle East and North Africa, including an escalation of the conflict, would bring



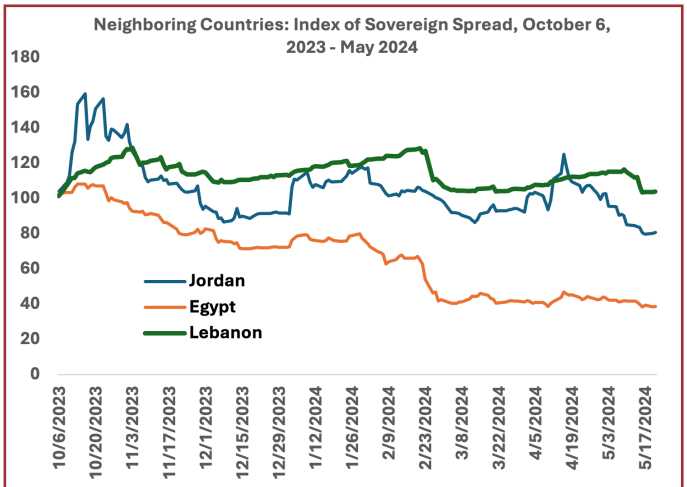
Sources: UN Global Platform; IMF PortWatch (portwatch.imf.org) Accessed 05-21-24

Figure 31

about significant vulnerabilities and greater uncertainty. An escalation, heightened intensity, or longer duration of the conflict in Gaza may re-price sovereign risk for countries in the region and widen spreads. Sovereign spreads widened after the October 7 attacks and have not returned to their pre-October 7 levels. In Israel, stock market prices plunged following the attacks but have been recovering since. In their Q2 2024 forecast, the BOI predicts that the economy's sovereign risk premium will decline at a lower rate than its estimates the previous quarter; as a result, higher interest rates will be required to control inflation. However, the prolonged duration of the war and its escalation into other countries are expected to negatively impact Israel's ratings with credit agencies. More recently, Moody's downgraded Israel's credit rating by "two notches" on September 27, 2024. [136] The month prior, Fitch downgraded Israel's credit rating by one grade. These downgrades are likely to place upward pressure on Israel's cost of borrowing abroad.

Neighboring countries Jordan and Lebanon also witnessed the same repricing of their sovereign risk and spreads, which have yet to return to their pre-war levels. Egypt's sovereign spreads were already high due to preexisting macroeconomic challenges and therefore were less impacted by the war in Gaza.

An escalation of the conflict may adversely impact commodity markets, especially given the oil production cuts announced by the OPEC+ countries, which could raise inflationary pressures and possibly tighten global financial conditions.[137,138] Under such a scenario, debt-burdened economies, including those in the region, would find it challenging to achieve, and preserve, macroeconomic stability and debt sustainability in the medium term. If geopolitical tensions in the region continue to escalate, shipping and insurance rates along the Red Sea route may continue to rise, and fiscal revenue for countries that benefit from the Red Sea route would not recover. Furthermore, fuel and food imports via Red Sea ports and humanitarian aid to the African continent would be disrupted. As a result, any rise in the price of basic goods, including food and medicine, will exacerbate the plight of consumers already struggling with high poverty levels and depleted capacities to cope.[139]



Sources: UN Global Platform; IMF PortWatch (portwatch.imf.org) Accessed 05-21-24

Figure 32

137. *Reuters*, "Moody's cuts Israel's rating, warns of drop to 'junk'," September 28, 2024, https://www.reuters.com/world/middle-east/moodys-cuts-israels-rating-warns-drop-junk-2024-09-27/.

138. International Monetary Fund, "Steady but Slow: Resilience amid Divergence."

139. Wayne Duggan, "August 2024 Stock Market Forecast," *Forbes*, June 3, 2024, https://www.forbes.com/advisor/investing/stock-market-outlook-and-forecast/.

140. Food Security Information Network, *2024 Global Report on Food Crises.*

Escalating Risks as a Result of the Israel-Gaza War

Course of action	Resulting risks
Longer duration of the conflict	• Greater uncertainty in the region • Re-pricing of sovereign risk • Negative investor risk sentiment towards the region • Negative macroeconomic and growth impacts
Escalation of the conflict	• Higher commodity prices with inflationary pressures • Greater disruptions in supply chains leading to inflationary pass through • Further tightening global financial conditions • More severe humanitarian aid disruptions and greater food insecurity
Failure of global efforts to bring about a permanent ceasefire	• Greater loss of lives and livelihoods and exacerbated social costs • Entrenched macroeconomic vulnerabilities in the region and spillovers to the rest of the world • Higher risk of political instability in the region
Lack of postwar reconstruction plans	• Lack of political consensus around "day after" plan reduces clarity on how the funds will be furnished, a crucial step to address the unprecedented extent of social vulnerabilities and damage.
Exacerbated socioeconomic impacts due to geoeconomic fragmentation	• Rising trade restrictions will exacerbate the negative spillovers from a longer duration and escalation of the conflict.

Figure 33

Israel-Gaza Conflict, Geoeconomic Fragmentation, and Impacts on Global Growth

Global integration may not have delivered the promised benefits to all economies, but the increasing geoeconomic fragmentation resulting from escalating trade tensions between the world's two largest economies, the United States and China, is expected to negatively impact growth prospects for many countries. Mounting trade restrictions and the resurgence of protectionism and industrial policies that began in 2019 will adversely affect global medium-term growth prospects due to shifting trade linkages and losses in efficiency. [140]

A recent study estimates that the longer-term costs of trade fragmentation may be anywhere from a modest 0.2 percent of global output to almost 7 percent; if technological decoupling were included in the analysis, loss in output could reach as high as 8 to 12 percent in some countries.[141] Though the precise magnitude of the impact may vary, geoeconomic fragmentation is sure to adversely affect trade, financial, investment, and technological flows along geopolitical lines.[142] Global geoeconomic fragmentation may worsen still by the end of 2024, when voters in 64 countries participate in elections that promise to have consequential outcomes for many years to come.[143] Growth and development gaps among advanced, developing, and low-income economies will widen, with the latter countries standing to lose the most—an average of 4 times the simulated global economic output loss if commodity markets fragment along US-China political lines.[144]

Moving Beyond the War

The Gaza war has intensified since October 7, and a more concerted global effort is needed to stop it from triggering a regional war and causing more fatalities and far-ranging disruption. The ongoing conflict highlights the important role international organizations play in addressing humanitarian crises, but the scale of the devastation underscores the urgency for a more proactive and comprehensive global effort to fully assess the impact of the crisis and develop effective strategies to finance and proceed with reconstruction efforts as soon as a permanent cease-fire is reached. In the meantime, collaborative international initiatives are crucial to attend to immediate humanitarian needs. Regional and local stakeholders in the reconstruction process will need to embed sustainable development at the core of the reconstruction plan, ensuring that peace and resilience are key outcomes. It is also imperative to identify who will finance the reconstruction plans based on fair burden-sharing.

The Gaza war has led to significant disruptions in trade, with key supply chains interrupted. Countries in the region with structural imbalances need to advance necessary reforms to address these macroeconomic and social challenges and build economic resilience. Resilience is even more critical for countries facing economic and/or financial difficulties, such as Egypt, Jordan, and Lebanon, which are also grappling with large refugee populations.

141. International Monetary Fund, "Steady but Slow: Resilience and Divergence."

142. Shekhar Aiyar et al., *Geoeconomic Fragmentation and the Future of Multilateralism*, International Monetary Fund, January 2023, https://www.imf.org/-/media/Files/Publications/SDN/2023/English/SDNEA2023001.ashx; Kristalina Georgieva, "Confronting Fragmentation Where It Matters Most: Trade, Debt, and Climate Action," International Monetary Fund (blog), January 16, 2023, https://www.imf.org/en/Blogs/Articles/2023/01/16/Confronting-fragmentation-where-it-matters-most-trade-debt-and-climate-action.

143. Chikako Baba et al., "Geoeconomic Fragmentation: What's at Stake for the EU," International Monetary Fund Working Papers, November 2023, https://www.imf.org/-/media/Files/Publications/WP/2023/English/wpiea2023245-print-pdf.ashx; Gita Gopinath, "Cold War II? Preserving Economic Cooperation Amid Geoeconomic Fragmentation" (plenary speech, International Monetary Fund, December 11, 2023), https://www.imf.org/en/News/Articles/2023/12/11/sp121123-cold-war-ii-preserving-economic-cooperation-amid-geoeconomic-fragmentation.

144. Koh Ewe, "The Ultimate Election Year: All the Elections Around the World in 2024," *Time*, December 28, 2023, https://time.com/6550920/world-elections-2024/.

145. Gopinath, "Cold War II? Preserving Economic Cooperation Amid Geoeconomic Fragmentation."

The conflict has exacerbated political instability in the region and beyond, prompting greater economic uncertainty that deters foreign investment. Investors are likely to demand higher risk premiums, increasing the cost of capital for businesses across the region. Additionally, the destruction of infrastructure and the diversion of public funds to military and humanitarian needs will likely slow economic growth. The war has strained government budgets across the region, with countries boosting defense spending, often at the expense of social and development programs. This reallocation of resources could have long-term implications for poverty reduction, education, and healthcare. It is crucial for regional governments to collaborate in addressing these challenges, fostering resilience in their economies, and working toward a peaceful resolution that facilitates sustainable development and growth.

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