

Economic Impact of the Gaza War

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The Gaza war has had a devastating impact on the Palestinian economy. Elsewhere in the region, however, the adverse effects have been relatively limited. In Israel, growth has slowed and the fiscal deficit has increased, but the economy was performing well before the conflict, and Israel has strong financial buffers. Egypt and Jordan have been affected by the disruption to maritime traffic in the Red Sea owing to attacks by Yemeni Houthi forces on international shipping, but they have also received substantial financial support from international institutions and Gulf Arab states. The Lebanese and Syrian economies were already in deep trouble, and the Gaza war has made little difference.

The main reason for the relatively limited economic impact is that the conflict has, by and large, been contained. There has been some spillover into Lebanon, and there was a brief surge in tensions between Iran and Israel, with the first direct exchange of fire between the two states in April. However, this stopped short of triggering a regional escalation that could have affected global energy supplies.

One way of quantifying the economic effects of the Gaza war is to compare International Monetary Fund (IMF) forecasts of some core indicators in the October 2023 and April 2024 publications of its World Economic Outlook. Of the countries directly affected, the biggest variations in performance and outlook are the West Bank & Gaza and Israel. Egypt and Jordan show marginal deterioration. (The IMF does not provide forecasts for Lebanon and Syria in this data series owing to the lack of reliable statistics).

Prior to the 7 October attack on Israel by Hamas from Gaza, the economic outlook for the Palestinian territories was reasonable, albeit clouded by the growing turbulence in the West Bank. The Gaza economy stood to benefit from an increase in Israeli work visas and some potentially helpful infrastructure developments, notably Israel's approval of plans to develop the Gaza Marine offshore gas field and a project to expand El-Arish port in Egypt with a view to expanding its role as a hub for Gaza trade. The Gazan economy also benefited from cash transfers of \$15 million – \$30 million per month from Qatar to pay civil servant salaries, in a long-standing arrangement approved by Israel.

The IMF's October report estimated that there would be a modest slowdown in growth in the West Bank & Gaza to 3% in 2023 from 3.9% in 2022, easing to about 2.5% on average in 2024-25. The average fiscal deficit over the four-year period was put at just below 2% of GDP. In the April report, the IMF estimated that the West Bank & Gaza economy contracted by 6.1% in 2023, and it did not offer any forecasts for 2024-25. It is clear from the massive destruction in Gaza that the economy of that territory is heading for a large contraction in 2024, possibly in the order of 80%. There is a chance of some recovery in 2025 if reconstruction starts, but it will be many years before the economy returns to pre-7 October levels. The West Bank economy is also heading for a significant contraction, amid escalating violence – in particular from Israeli settlers – and the choking off of tax revenue from Israel. The West Bank and Gaza economies will further suffer from the exclusion of Palestinian workers from Israel.

The absence of Palestinian workers has also had an effect on the Israeli economy, particularly in the construction sector, although the government is looking to address this issue by encouraging migration from

elsewhere, for example India. Labour shortages were at their most acute in the first period of the war, owing to the full mobilization of reserves for the armed forces. Economic activity has revived since the start of 2024 as reservists have returned to work. According to the IMF, the Israeli economy is set to grow by 1.6% in 2024, compared with 2% growth in 2023. Earlier forecasts envisaged growth of about 3% on average in this period. The main change in the IMF forecasts is a big increase in the fiscal deficit to about 6% on average in 2023-25 from just over 2% in the previous report. Israel's public debt is about 67% of GDP, just below the average level for OECD member states, and so there should be little difficulty in financing the higher deficits. Moreover, Israel has a large cushion of more than \$200bn in foreign exchange reserves. At the start of the war, the Bank of Israel released \$30bn of its reserves to support the currency, which has been stable since then.

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Based on these bare statistics, the damage to the Israel economy does not appear to be too severe. However, Israel is likely to be on a war footing for a long time to come, and its international reputation has suffered amid the outraged reaction around the world to the scale of the destruction and civilian casualties inflicted by the Israeli war machine. Israel could end up being subject to sanctions and consumer boycotts, which would affect its exports while impairing investor sentiment. Israel's plans to develop its economic relations with Gulf Arab states have been dealt a heavy blow.

Israel's economic links with Jordan and Egypt have not been seriously affected, despite the strong pro-Palestinian feelings of the populations of these countries. Both Egypt and Jordan have come to depend on the supply of natural gas by pipeline from Israel's offshore Mediterranean fields, Tamar and Leviathan. Jordan is also working on a project to secure desalinated water from Israel using solar power generated in Jordan. Apart from a brief interruption at the start of the war, these gas flows have continued, and Egypt

has even signed a deal to increase imports from mid-2025. Work on the joint project with Jordan is likely to slow down, however.

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For Egypt, the main adverse economic effect of the Gaza war has been the 60% reduction in traffic through the Suez Canal. The consequent loss of about \$350 million per month in Suez Canal tolls has hit Egypt's foreign exchange earnings and squeezed its budget revenue. The loss has also had an impact on real GDP growth. However, tourism has not been seriously affected, and Egypt has benefited from more than \$50 billion in financial support from the UAE, the IMF, the World Bank and the EU. The biggest contribution has come from the UAE, with the conclusion of a \$35 billion deal with ADQ, an Abu Dhabi-owned investment company, to develop the Ras el-Hikma region on the Mediterranean coast, west of Alexandria. This deal paved the way for the IMF to revive its suspended loan programme, while increasing its size by \$5 billion to \$8 billion. One of the conditions was for Egypt to float its currency. This entailed making a hefty devaluation, but the inflow of foreign exchange from the UAE meant that the adjustment was smaller than it would have been without the Ras el-Hikma deal.

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At the start of the Gaza war, Egypt's economy was in deep trouble. By mid-2024, the outlook was more positive, thanks to the inflow of funds. This can be attributed to some extent to the concern of the inter-

national community to prevent a full-blown economic crisis that could affect Egypt's political stability at a time of heightened regional tensions, owing to both the Gaza war and the conflict in Sudan.

TABLE 3 Variations in IMF Outlook for Economies Most Affected by the Gaza Conflict

% change year-on-year	2022	2023	2024	2025
Egypt (October 2023 outlook)*				
Real GDP	6.6	4.2	3.6	5.0
Fiscal balance	-5.8	-4.6	-10.7	-11.1
Egypt (April 2024 outlook)				
Real GDP	6.6	3.8	3.0	4.4
Fiscal balance	-5.8	-5.8	-10.9	-9.3
Jordan (October 2023 outlook)				
Real GDP	2.5	2.6	2.7	3.0
Fiscal balance	-7.2	-7.0	-6.6	-4.7
Jordan (April 2024 outlook)				
Real GDP	2.4	2.6	2.6	3.0
Fiscal balance	-7.0	-7.3	-7.7	-5.3
Israel (October 2023 outlook)				
Real GDP	6.5	3.1	3.0	3.3
Fiscal balance	0.6	-1.6	-2.1	-2.8
Israel (April 2024 outlook)				
Real GDP	6.5	2.0	1.6	5.4
Fiscal balance	0.6	-5.0	-8.2	-5.4
West Bank & Gaza (October 2023 outlook)				
Real GDP	3.9	3.0	2.7	2.4
Fiscal balance	-0.9	-1.3	-2.2	-2.4
West Bank & Gaza (April 2024 outlook)				
Real GDP	4.1	-6.1	n/a	n/a
Fiscal balance	-0.9	-1.1	n/a	n/a

* Egypt's accounts are for June-July fiscal years.
Source: IMF World Economic Outlook.

Jordan has also benefited from international support, with the IMF approving a \$1.2 billion loan in January. This will help the government to cope with the impact of the Red Sea blockage on operations at Aqaba Port, and the downturn in tourism. However, Jordan's economy could be hit hard if the conflict in the West Bank escalates.

The Gaza war has had a negligible impact on oil and gas prices, despite the critical importance of the Middle East to the global energy market. The effective closure of the Suez Canal to oil and liquefied natural gas (LNG) traffic from the Gulf to Europe has not caused serious supply disruptions. Most of Qatar's LNG exports go to Asia, and its Europe-bound cargoes have been diverted around the Cape of Good Hope. With European gas demand weak, the delays in the Qatari shipments have not been an issue, and in any case, most of Europe's LNG imports come from the US, Russia, Algeria and Nigeria, and therefore do not require a Suez Canal transit. Likewise, most oil exports from the Gulf go to Asia. Saudi Arabia has also been able to boost Europe-bound exports from its Red Sea terminal at Yanbu thanks to its internal pipeline system.

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The situation nevertheless remains precarious. It is hard to envisage any relief for the Palestinian economy without a robust post-conflict political process. The war has deepened political divisions within Israel, which could end up affecting economic activity, while the damage to Israel's international standing will have negative economic repercussions. If Israel carries out a major offensive in Lebanon, this will once more raise the risk of an escalation involving Iran, which would prompt renewed anxiety about the security of energy flows from the Gulf.