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Should the United States Create a West Bank/Gaza Enterprise Fund (WGEF)?

Daniel F. Runde

Introduction

It is in the interest of the United States to explore the creation of an enterprise fund for the West Bank and Gaza as part of its continuing efforts to foster peace and prosperity in the Middle East. With the growth of joint Israeli-Palestinian ventures and people-to-people exchanges facilitated by an enterprise fund, the United States can create common entrepreneurial ground on which a more robust peace process can stand. The spread of Covid-19 has shuttered schools and businesses and limited public gatherings in places such as markets, increasing the financial stress felt by many in the region. The pandemic has also exacerbated youth unemployment, which now stands at 42 percent, illustrating there is acute need for social and economic opportunities. Post-Covid-19, employment prospects may more easily improve if, alongside a lightening of the political climate, there is greater access to capital. The deployment of innovative financial instruments to spur private sector growth can prompt dramatic socioeconomic changes in the West Bank and Gaza.

What Are Enterprise Funds? The First and Second Wave of Enterprise Funds

Enterprise funds are established by the U.S. government to provide equity financing and loans to companies in developing countries, with the aim of promoting private sector development abroad. Enterprise funds can be compared to impact investing, having a dual purpose: enterprise funds not only generate financial returns for the United States when properly managed, but also seek to support economic development efforts in recipient countries. These institutions function like private equity funds; they are independently managed by outside investment professionals that take significant risks and use creative investment strategies to advance private sector development abroad. They are unique in their management and development approach and embody the core U.S. private sector values of freedom, risk-taking, and creativity. They are strong complements of other U.S. development efforts and few countries outside the United States have pursued similar endeavors.

Enterprise funds may provide equity financing and debt and/or technical assistance to inexperienced locals who have entrepreneurial aspirations, thereby supporting the growth of markets and the establishment of economic diplomacy in geostrategic locations. Funds may invest in and make loans to small and medium-sized enterprises (SMEs); provide technical assistance; introduce new financial products (mortgage lending, mortgage securitization, credit cards, and others); and support sectors such as telecoms, finance, and construction.

There have been two waves of enterprise funds to date: the first wave was during President George H.W. Bush's administration in the early 1990s and the second wave was during the presidency of Barack Obama in early 2011. The enterprise funds of the 1990s were aimed at bolstering the private sector in former communist states in Central and Eastern Europe and the former Soviet Union. The second wave of enterprise funds was partly a response to the Arab Spring, meant to provide essential capital and private-sector expertise in two fragile yet strategically important countries to the United States: Egypt and Tunisia (Box 1). The development impacts of enterprise funds included the introduction of modern technologies in developing countries, the development of capital markets and private equity funds, management support and training for entrepreneurs in SMEs, and improved corporate social responsibility. Further, the funds also worked to facilitate the development of an infrastructure for private enterprise and establish a proper framework for corporate governance to foster privatization and encourage foreign investment.

The U.S. Agency for International Development (USAID) was, and continues to be, the primary implementor of enterprise funds. But enterprise funds are typically controlled and administered by a board of directors that is composed of relevant professionals, while the day-to-day operations are carried out by management teams. The board is responsible for guiding the direction of the fund and establishing a reporting structure between the fund and USAID through semiannual reviews, site visits, and independent audits to verify financial reporting. Under this framework, flexibility is encouraged in enterprise funds' investments and programmatic decisions. For example, some funds may be designed to have a limited life span (i.e., a 10- to 15-year period) and end once their mission is accomplished. The initial 10 funds initiated under President H.W. Bush generated over $200 million in returns for the U.S. Treasury and helped stabilize the economies of their recipient countries.

Table 1: U.S. Foreign Enterprise Funds

Country	Fund	Capital ($ in millions)	Population (in millions)
Tunisia	Tunisian-American Enterprise Fund (TAEF)	100	11.8
Baltic States	Baltic-American Enterprise Fund (BalAEF)	50	5.9
IFI	Internsational Fund for Ireland (IFI)	543	4.9
Albania	Albanian-American Enterprise Fund (AAEF)	30	2.8
Egypt	Egyptian-American Enterprise Fund (EAEF)	300	102
USG Authorization of Funds	Total	1,023	

Source: Egyptian-American Enterprise Fund (EAEF), Egyptian-American Enterprise Fund Inaugural Impact Report (New York: EAEF, 2020); Tunisian American Enterprise Fund (TAEF) Impulsion au Developpement, Annual Report 2018 (Tunis, Tunisia: TAEF)

BOX 1: CASE STUDY - ENTERPRISE FUNDS OF THE SECOND WAVE: EGYPT AND TUNISIA

The Tunisian-American Enterprise Fund (TAEF) and Egyptian-American Enterprise Fund (EAEF) were authorized by Congress in 2011 to encourage private-sector growth and greater stability in the North Africa region in the wake of the "Arab Spring." The funds' primary focus is the development of Egyptian and Tunisian SMEs through instruments such as loans, equity investments, and technical assistance. Since 2011, USAID has obligated $100 million to TAEF and $300 million to EAEF. Both funds' boards include Tunisians, Tunisian-Americans, Egyptians, and Egyptian-Americans, respectively, along with U.S. financial experts. TAEF and EAEF work closely with local partners who are attuned to the strengths and weaknesses of the local economies.

In the case of EAEF, $200 million has been invested in seven companies and three funds, producing a return rate of 20 percent (the fund's current portfolio is valued at $450 million). Money from EAEF has been used to seed Egyptian-run private equity and venture capital firms, which has extended the fund's reach through indirect investment to over 50 SMEs. The fund has also attracted $311 million in Foreign Direct Investment (FDI), and EAEF's portfolio now includes education, healthcare, and agricultural endeavors that affect the lives of more than 20 million Egyptians. Civic and economic improvements resulting from EAEF have included increased access to financial and payment services, increased employment opportunities and improved gender balance, and increased access to social services, along with a healthier private sector and stronger equity and capital investment landscape.

In the case of TAEF, $52 million has been mobilized for investment in 54 companies across a variety of sectors, including chemistry and plastics, education, IT, building materials, handicrafts, and food and agribusiness (as of 2018). The average amount allotted to these (predominantly) SMEs was $1 million. The fund has also provided $6.2 million to two microfinance institutions that support entrepreneurship throughout the country. In addition, TAEF has created TASF, Tunisia's first Search Fund, to identify and connect promising business ventures.

Objections to the creation of EAEF and TAEF were raised in 2011, citing the lack of certainty around economic and political stability within the two countries. In this way, the cases of Egypt and Tunisia are similar to that of Gaza and the West Bank. Both funds were authorized during crises of governance and political turmoil—in Egypt's case, the crisis reoccurred for two years. Despite the political climate into which they were introduced, the economic and civic benefits of the funds—in terms of job and wealth creation as well as their commercial successes—are evident. Their successes can be attributed to the care of their management teams and their flexibility in working with their partners on the ground.

A WGEF Would Inspire a Third Wave of Enterprise Funds

Despite the success of two waves of enterprise funds, they remain an underutilized U.S. development tool. In 2018, CSIS made the case that there is an opportunity for the United States to update the enterprise fund model and authorize a third wave of enterprise funds to help spur private sector growth and create jobs in select regions of the world. The first group of candidates would include countries with geostrategic importance to the United States. In the short run, given security and demographic challenges, enterprise funds should be established in the Middle East region. In particular, a West Bank/Gaza Enterprise Fund would be of strategic importance to the United States and help boost the private sector in this volatile part of the world (Box 2).

BOX 2: HONORING CONGRESSWOMAN NITA LOWEY

A Palestinian enterprise fund should be established to carry on the work begun by retiring Congresswoman Nita Lowey (NY-17), whose concern for the wellbeing of both Israelis and Palestinians and search for solutions to longstanding conflict in the region serve as an inspiration to all who strive for a more peaceful world. Congresswoman Lowey has been a champion of foreign aid throughout her career, perpetually prioritizing development and diplomacy as crucial aspects of U.S. foreign policy. As her cosponsor on the Partnership Fund for Peace Act of 2019, which would create a new fund that pairs economic development capacity-building efforts with reconciliation and strengthening of civil society in Israel and Palestine, Congressman Jeff Fortenberry stated, "we often hear about the road map for peace in the Middle East; the challenge is laying the proper foundation for the road."

As the chairwoman of the House Appropriations Committee and chairwoman of the Subcommittee on State and Foreign Operations, Congresswoman Lowey promoted efforts to reduce global poverty, increased access to education and economic development, encouraged good governance and rule of law in developing societies, and saw to the provision of life-saving humanitarian assistance around the globe in times of need. Her interest in the Middle East peace process was firmly rooted in ensuring Israel's safety and long-term survival, as well as the well-being of Palestinians, especially girls and women.

A West Bank/Gaza enterprise fund would provide capital and support to residents of the Palestinian territories. The support would come in the form of equity, loans, and technical assistance that would enable market connections and create fertile ground for the growth of organic financial infrastructure. The fund would also work with trusted, preestablished financial institutions, such as the Palestinian Monetary Authority, to further guarantee loans and make use of local networks that are known quantities to prospective fund patrons. There is also the possibility of joint Palestinian-Israeli firms working as partners to reduce costs, as many are quietly open to the prospect of expanding their reach if offered the reassurances provided by the fund.

The World Bank has been engaged in the Palestinian territories since 1992, providing grants in cooperation with trust funds to finance the Palestinian Authority's (PA) projects in sanitation, municipal services, education, and social protection. In addition to further developing these projects, U.S. enterprise support could foster development in the region's solar energy, agriculture, tourism, hospitality, and microfinancing sectors. The fund would legitimize Palestinian enterprises from every economic sector: agriculture (palm and date farmers), manufacturing (leather, shoes, furniture, stone, and marble craftsmen), and services (tourism). It would also seek partnerships and exterior sources of funding, including from foreign governments, who would provide ready appeal for Palestinian business partners. Aid from Norway or Germany, for example, may come with a higher trust quotient than the United States, which is seen as a staunch ally of Israel.

It is critical that an enterprise fund for the West Bank and Gaza be tailored to the needs of local communities, just as the International Fund for Ireland (IFI) was (Box 3). The earliest stage of community development is "money on the table," which can be quickly allotted to projects dictated by the community according to their most pressing needs. This initial investment serves to garner community support and attract further investment. It is also important that a West Bank/Gaza fund strongly emphasizes employment and training opportunities for youth—especially considering the high youth unemployment rate in the Palestinian territories. Furthermore, women need to be supported to achieve economic empowerment and full participation and integration into the labor market.

BOX 3: CASE STUDY - THE INTERNATIONAL FUND FOR IRELAND (IFI)

The IFI provides a strong model for how development funds, when supported by foreign governments and paired with strengthening civil society and peacebuilding efforts, can foster stability in areas of heightened conflict and poverty. Jonathan Powell, the chief British negotiator during the Northern Ireland Peace Process, has called the IFI the great unsung hero of the peace process, supporting intercommunal civil society engagement and economic/community development. The IFI was established in 1986 by the governments of the United States, Canada, Australia, New Zealand, and the European Union.

The initial agreement was that the fund should target projects in Northern Ireland and the border counties of the Republic of Ireland with a desired funding ration of 75 percent to the North and 25 percent to the Southern border counties, in line with the population sizes of those areas. One of the key elements that made the IFI so successful was the creation of an independent board, comprising of a chairman and six board members appointed jointly by the Irish and British governments. Of the six board members, three had to be from Northern Ireland and three from the Republic of Ireland. The international donors appointed observers to the board to assist in its work as well as offer the Fund international diplomatic support. Since its inception, the IFI has slowly tilted its activity away from economic development to center more on dialogue and reconciliation programming. This shift in priority mirrors the progress towards a stronger economic condition, more robust political governance, and greatly reduced violence.

Since 1986—12 years before the peace agreement it helped to create foundations for—the IFI created 55,000 jobs, engaged more than 15,000 young people in training programs, and leveraged €899 million of funding into total investments of €2 billion at a 1:2.2 ratio. The fund's success was thanks to its flexible approach, its relative lack of bureaucracy, its freedom to innovate and take risks, and the meaningful support given to projects by the fund's managing agents and secretariat. In these ways, the fund was responsive and adaptable to the needs of the communities which it served, fostering a sense of partnership and trust. The fund's success grew parallel to the peace process in Ireland and proved that similar programs can be useful in laying the secular economic groundwork for lasting stability. As Senator George Mitchell stated in 2016, "The International Fund for Ireland has been of great importance in helping reconciliation to take hold among the people of Northern Ireland. It is contributing so much to the bringing forward of full, genuine, meaningful, and permanent reconciliation."

The concept behind the IFI was to create an international fund that could be used to support community-centered economic projects and initiatives that involved youth in skills training and civic affairs. The centering of person-to-person development was the distinguishing feature of the IFI's work in Ireland, and the success of the program was based on creating a sense of community ownership and encouraging collaboration between different groups, whether those groups were across town or across the border. Though it was set up in partnership between the British and Irish governments, the fund's operation was independent of both, and it was emphasized to partners and participants that it was not a government intervention (an important distinction to make, and one which a West Bank and Gaza fund, paired with a peacebuilding program, should similarly strive for). The Wider Horizons Programme, Knowledge through Enterprise for Youth (KEY), and Learning and Education Together

(LET) are a few examples of initiatives designed to provide non-politicized space for youth to come together, be exposed to new ideas, and make connections. There was an aggressive focus on diverting these youth away from antisocial behaviors, crime, and drug use. These deliverables were intentionally small and required the extensive involvement of community groups on the ground.

Distinct Features of a WGEF

CSIS recommends that the West Bank/Gaza enterprise fund budget be at least $50-$200 million. This figure is enough to ensure that a workable number of SMEs are equipped to get off the ground. It is crucial to long-term success that a critical mass of these smaller enterprises is established and enough money circulates that the entrepreneurial ecosystem can self-replicate; therefore, the minimum amount for investment in one enterprise should be around $100,000-$200,000. For example, perhaps an investment would go towards a company that rented agricultural supplies to farmers or a microlending institution that could provide more access to capital and generate a return in a relatively short period of time.

Ideally, the fund would be managed by Israelis or Palestinians—locals who know the market—but perhaps the Middle East Investment Initiative (MEII) could serve as the fund manager. The success of similar funds (in Tunisia, for example) was predicated upon the management teams' knowledge of and preexisting involvement in the communities they served. Many Palestinians are unwilling to take on long-term debt and may need additional technical assistance to develop or scale their operations. One advantage that the fund offers is its ability to provide equity for loans taken out with local banks, which, along with its ability to provide technical support, creates assurance and effectively de-risks their investments. Another advantage would be the fund's ability to connect Palestinian SMEs with Israeli exporters and the broader market as most Palestinian businesses do not have connections to Israeli or even other Arab-world businesses.

The World Bank evaluates that private investment in the main productive sectors of the Palestinian economy is key to achieving sustainable growth because it increases the export base and opens the door for Palestinian goods and services to compete in global markets, generate jobs, and promote entrepreneurial activity. The majority of economic enterprises in the Palestinian territories are SMEs, with 88.1 percent classified as very small enterprises with 1 to 4 employees and only 1.1 percent classified as large enterprises with more than 20 employees. In 2014, 13.4 percent of the Palestinian population was formally employed in the agricultural sector, but informal agricultural sector employment was estimated at 90 percent. In the Palestinian territories, olives are one of the major crops, along with palm and dates. Other products include stone and tile known as "Jerusalem stone," pottery, glass, soap, weaving, embroidery, and wood or mother-of-pearl carvings. These products represent the majority of commercial exports from the Palestinian territories and they would all be reliable areas for investment. Potential growth sectors, including solar energy and microfinancing, are worthy of further investigation.

However, the Palestinian territories lack an SME strategy, an SME agency, and overall statistics to track their performance. Following the experience of enterprise funds in Central and Eastern Europe during the 1990s, where funds pushed for changes in regulations and legislation to enable the development of effective investment programs, a West Bank/Gaza enterprise fund should take advantage of opportunities to affect policy reforms and push for regulatory changes. The MEII has attempted to make significant societal reforms in the Palestinian territories, providing $129 million through its Loan Guarantee Program, which seeks to transition the Palestinian economy from a collateral-based system to a cash-based one. For resilient change such as that prompted by MEII, the West Bank/Gaza enterprise fund should seek a budget that is between $50-$200 million.

Yet a WGEF Is No Silver Bullet to Peace and Economic Stability

Development aid and economic stimulus are not necessarily predictors of increased peace in the West Bank and Gaza. The period of greatest growth for the Palestinian territories in the late 1990s also saw some of the most bloodshed (see Annex). The United States must be prepared for reality to play out differently than planned and for fortunes to shift with the political winds. This is not to say that the United States should not try, however, nor is it to suggest that the United States should regard peace as a lost cause.

There are also certain cultural and political barriers to be overcome when working in the Palestinian territories, specifically around development finance—the inclusion of Israeli settlements is a non-starter, for one. In addition, given that Hamas has maintained a plurality in the Palestinian parliament since 2006, the United States has imposed conditions, limitations, and restrictions on the issuance of aid in the West Bank and the Gaza Strip. However, an exception to these restrictions would be made if Hamas recognizes Israel's right to exist and commits to nonviolence. Furthermore, an enterprise fund would likely have difficulties in Gaza because the PA is not present there, which makes it difficult for businesses to operate outside of Hamas's influence. The United States must be careful to observe the particulars of the situation from both the Palestinian and Israeli perspectives and only seek common ground. Due to the situation on the ground, the Palestinian territories may necessitate a higher degree of flexibility and commitment, including longer review periods as well as a willingness to accept modest returns as evidence of success.

It is important that these risks be understood and accepted in order to encourage the kind of economic activities that will establish an essential foundation for future enterprise funds or other like ventures in the West Bank and Gaza. Creating breathing room in which the peace process can grow builds valuable political capital for the United States.

Conclusion

Ultimately, a West Bank/Gaza enterprise fund is not meant to create lasting peace in the region—a task beyond the fund's scope—but to create greater economic viability and stability within Palestinian territories in anticipation of the eventual fruition of the peace process. An enterprise fund for the West Bank and Gaza, paired with people-to-people economic activities, would be another mechanism for the United States to build relationships in one of the most conflicted regions of the world. Drawing on several past development finance experiences in similar regions, this fund could be highly targeted and customized to fit the specific needs of Palestinian businesses, allowing for the flexibility needed to fill niche sectors and doing so under the guidance of competent, experienced minds. Similar projects have demonstrated that there are willing partners on the ground and in the international community who could work with the fund to deliver services and assistance as well as external sources of funding. The United States must look at the long-term benefits for itself and for its allies in investing in these territories now, when the international community is needed more than ever.

Daniel F. Runde is senior vice president, director of the Project on Prosperity and Development, and holds the William A. Schreyer Chair in Global Analysis at the Center for Strategic and International Studies in Washington, D.C.

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Annex 1: A Brief Summary of Israeli-Palestinian Relations since 1993

In 1993, the government of Israel and the Palestinian Liberation Organization (PLO) signed the Oslo I Accord in Washington, D.C., agreeing to a framework for relations between the two parties which would gradually facilitate lasting peace. The crux of the agreement was that the Israelis would gradually cede control of the occupied territories of the West Bank and Gaza over to the Palestinians. The assassination of Israeli Prime Minister Yitzhak Rabin in November 1995, however, derailed the process, which finally unraveled in 2000 when Prime Minister Ehud Barak and PLO chairman Yasser Arafat failed to reach further agreement during a meeting at Camp David.

Peace talks centered around a two-state solution have resumed and halted several times over the last 20 years, and hostility between Israelis and Palestinians has simmered, with occasional spikes in violence. Since 2011, Israeli settlement in the West Bank has accelerated, and tensions have steadily risen in the region since 2014. The expansion of settlements (including the demolition of Palestinian homes) and talks of annexation, which are largely supported by the Israeli government and seen by Palestinians as encroachment and an affront, remain the most contentious point. The Israeli blockade of Palestinian exports and imports and Palestinians' exclusion from Israeli ports further complicates the situation. It is understood by most experts that Israeli annexation of Gaza or the West Bank, in particular, would come with a very high cost: politically, the move would isolate Israel from the international community, and by excluding the possibility of a two-state solution, the move could precipitate the dissolution of the PA and foment a disaster scenario. Talk of annexation has grown in the past weeks and the international community is watching the situation closely.

The signing of the Oslo I Accord in 1993 brought a round of significant U.S. investments in the Palestinian territories aimed at creating economic opportunity and growth. More than $5 billion in USAID foreign aid has been committed over the last 30 years towards developing and sustaining the PA. It has been used for debt relief, sanitation, public and private economic development, infrastructure development, education, governance, health, and essential humanitarian assistance to the Gaza Strip, as well as serving as a lifeline to dozens of NGOs devoted to conflict mitigation and peacebuilding measures. From 1990 to 2018, the United States also paid for roughly one-third of the $1 billion United Nations Relief and Works Agency's (UNRWA) annual budget, which provides food, shelter, education, medical care, microfinance, and other humanitarian and social services to 5 million Palestinians, including refugees living in Jordan, Lebanon, and Syria.

In 2018, under President Trump, the budget for foreign aid to the West Bank and Gaza was reduced from $250 million to $50 million and an additional $65 million in UN assistance was withheld. The U.S. allotment of $360 million towards the UNRWA budget was also halted. In February 2019, USAID aid payments ceased entirely, but the USAID mission in the Palestinian territories continues operations, according to USAID officials. Because the UNRWA primarily serves at-risk and refugee communities, its provision has been deemed essential to preventing violence and radicalization within those already marginalized populations. Some UN member countries have raised their contribution to the UNRWA in order to fill the gap left by the United States, but there is still an acute need for support inside and outside of the territories. An enterprise fund for the West Bank and Gaza could make up for some of this need.