

# The Economic Threat

by

Dan Ben-David

After three straight years in which Israeli income levels fell continuously, came 2004, with an increase of 2.4% in per capita GDP, the measure commonly used to indicate standards of living. This is a significant accomplishment that should not be taken lightly. While average United States incomes rose by 16% from 1996 until 2003, average Israeli incomes in 2003 returned to their 1996 level. Thus, it is good news when Israeli incomes have risen above where they were situated eight years ago.

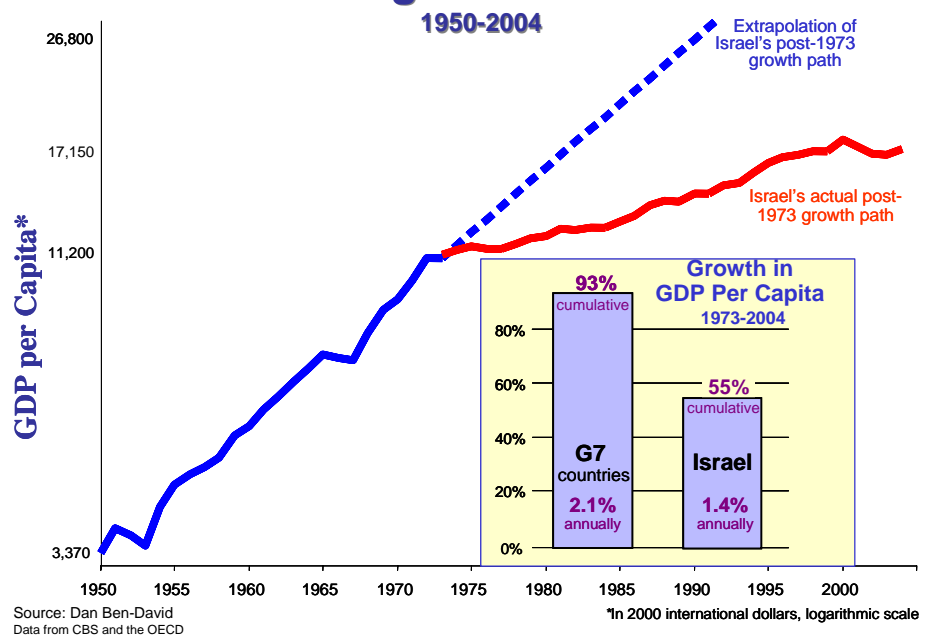
As the Israeli economy is apparently beginning to come out of the deep recession and returns to its normal growth path, the good news comes into a more accurate perspective, and the serious economic threat that we are facing begins to materialize. Since the seventies, the country is situated on a number of unsustainable long-run trajectories – low growth combined with high and steadily increasing rates of unemployment, poverty and income inequality – that put its future in jeopardy.

Israel veered toward a different socio-economic path in 1973. In the aftermath of the Yom Kippur war, which was the catalyst for what subsequently ensued, the country underwent a seismic transformation of its national agenda. A banana culture of governance took root, mediocrity and superficiality ascended to the top of the pecking order, budget priorities were significantly altered to reflect narrow, personal and messianic interests rather than to promote national interests – and the results are clearly evident in the graph.

The Israeli economy shifted in the seventies from one of the fastest growing in the west to one of the slowest. The country, which had been rapidly catching up with the world leaders has, since the seventies, been steadily falling farther and farther behind. While the average incomes in the leading western countries, the G7, have almost doubled since 1973, Israeli incomes rose by only 55%.

Despite everything that Israel has undergone since the seventies – wars, 3-digit inflation rates that the western world hasn't witnessed since WWII, and immigration that increased the country's population by a fifth within half a decade – these events were reflected only in fluctuations around the trend, while the long-run growth path itself appears to some as though it is etched in stone. There can be no greater misconception than this. The factors influencing the slope of a country's growth path are not preordained destiny but the result of its own national priorities.

## Israel's Long-Run Growth Path



A century has passed since Herzl died, but he already understood then what many of Israel's policy-makers still have not begun to comprehend. "It must be the country of choice" he said, as quoted in Nahum Gross's book. This does not just refer to Jews abroad who have options, but also to a growing number of Israelis who are able to choose where they prefer to live. The steady three decade decline of Israel – in relation to the leading western alternatives – represents an existential threat to the country.

In 1999, even before the onset of the severe recession that we are currently emerging from, I wrote in Haaretz (July 13 1999) about the deepening growth crisis and the form that the new national agenda will need to take in order for us to change the multi-decade trajectories. A year later, I repeated these proposals – together with fellow members in a team of leading Israeli academics headed by Haim Ben-Shahar – at a special cabinet meeting convened by Prime Minister Barak, and since then I have also shown them (in differing levels of detail) to Prime Minister Sharon, cabinet ministers, MKs, directors-general of cabinet ministries, and many other policy-makers.

Despite all this, it has become quite clear that our national agenda will not change until the Israeli public internalizes the critical implications of our current state of affairs – and begins to demand accountability from its elected officials. Hence, I will try to outline in upcoming articles the socio-economic picture of Israel and detail some of the main features of a new national agenda that has been formulated over the past few years together with colleagues from academia and other professions. There is an alternative to what you see in the graph.

## The Social Threat

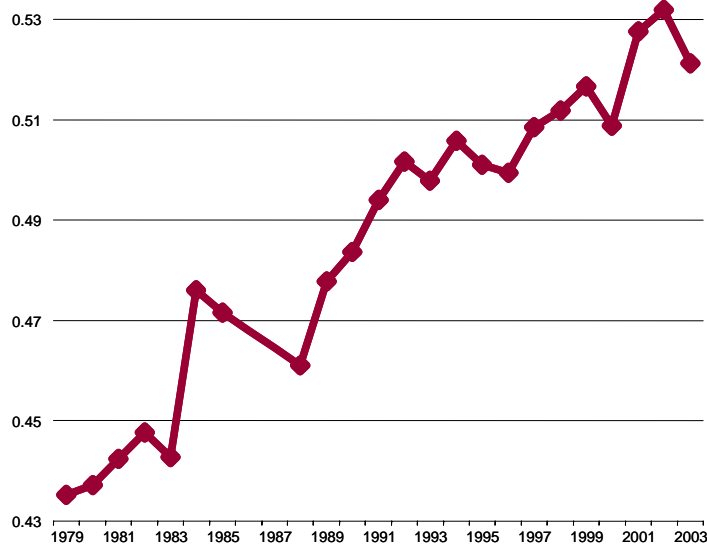
by

Dan Ben-David

Two of the primary socio-economic foundations in every democratic western country are high living standards and low income inequality. When one of these pillars weakens, the impact on society can be substantial. When cracks appear in both pillars, when the society in question receives the opportunity to live in a country of its own just once every two thousand years, and when this opportunity is provided only in a small oasis with few resources and many enemies, then this threat to the society's foundations becomes existential.

As I showed in Haaretz on February 4<sup>th</sup> ("The Economic Threat"), living standards in Israel have been falling farther and farther behind the leading western countries for three straight decades. At the same time, inequality in gross incomes (that is, before accounting for welfare payments and taxes) has become one of the highest in the west. As if this were not enough, income gaps within Israel have been steadily rising since the seventies, as can be clearly seen in the graph.

### Gross Income Inequality in Israel, 1979-2003\*



Source: Dan Ben-David, Tel-Aviv University  
Data from Israel Social Security Institute

\* Gini coefficient before welfare transfers and direct taxes. Old series until 1997 adjusted to new series that includes non-salary workers.

The poverty picture is similar. At the end of the seventies, just over one-quarter of the families in Israel lived under the poverty line according to their gross incomes. As a result of the steady, multi-decade, swell in the ranks of the impoverished, we have reached the point in which over a third of Israel's families now live below the poverty line according to their gross incomes. In lieu of dealing with the core issues that cause a large and growing portion of Israel's society to fall below the poverty line, we have to pay large and increasing amounts – that have long since surpassed our defense spending – in order to prevent this phenomenon from also manifesting itself in the net incomes that represent society's

last line of defense in the war on poverty and inequality.

The poverty and inequality trajectories that we are on are unsustainable in the long run. A considerable share of the population is not receiving either the tools or the conditions for coping in a modern, open and competitive economy – and it is growing at a faster pace than the remaining share of the population that must shoulder the burden of financing an increasingly expensive welfare safety net that only provides symptomatic treatment. Taking into account the fact that the combined impact of these trends is augmented by the steady retreat, in relative terms, of Israeli living standards from those of the leading industrialized nations, and in light of

expanding globalization that enables goods, capital – and people – to flow more and more freely to and from countries, then every possible alarm should be going off in the state of Israel. What we have undergone in recent decades is not the outcome of some preordained destiny but the direct result of our man-made national priorities since the seventies.

This is the anomaly and the promise called Israel. There is no other nation in the world with such dismal socio-economic features that is at the same time also the home to such bright points of light that are so essential for success. No other country outside the United States has better universities, more gifted doctors and researchers, higher quality technology, and greater potential – still.

We know what the problems are. We know where they can lead us. We also know how to solve them. What we need to know is that this anomaly cannot survive forever. Either the light will prevail and reach every corner of this small patch of land, or in the end it will flicker out – with all that this implies for the future of the third temple. It is all in our hands. I

## The Education Threat

by

**Dr. Dan Ben-David**

Department of Public Policy  
Tel-Aviv University  
member of the ELA commission

**Maj. Gen. (res.) Herzl Bodinger**

president of Rada Electronics  
former commander of the Israeli Air Force  
chairman of the ELA commission

---

In a country above which hovers an economic and social threat – a multi-decade decline in Israel's living standards relative to that of the leading western countries, and a steady increase, since the seventies, in levels of poverty and inequality to international peaks – not to mention the constant security threat, the time has come to provide core solutions. One of the primary causes, though clearly not the sole reason, for Israel's continuous socio-economic deterioration is the collapse of its educational system.

After having been one of the best in the world during the sixties, Israel's educational system has degenerated into the worst in the developed world and below a large number of developing countries. According to TIMSS exams given to eighth grade students during the nineties, Israel was ranked in 39th place out of 53 countries in core curriculum subjects such as mathematics and science – which gives a hint of the nation's future ability to absorb, utilize and develop new technologies that are the primary ingredients underlying the ability of an economy to grow, and of its future ability to operate and invent the advanced weapons and intelligence systems necessary for maintaining the existence of a country with our national security problems.

The educational gaps within Israel are larger than the gaps within 49 of the other 52 countries, which provides an indication of the magnitude of the income gaps that await our children when they grow up. As if this were not enough, those who will lead the country in another generation, our top students, came in 35th place when compared to the top 5 percentile of the other countries. The outcomes of other international exams such as PISA and PIRLS corroborate the TIMSS results as do the reading comprehension exams given by the IDF to native-born draftees which reflect a dramatic decline in the percentage of those meeting the minimum requirement – 60% in the eighties, 40% six years ago, and only 32% in 2003.

This is the cold, clear, piercing truth about our educational system and its dire implications, and this is the reason that we need to implement a wide-ranging and thorough structural reform in Israel's public education. This is the need that led to the creation of the independent ELA commission, to which we belonged, that conducted a two and a half year examination of the system in its entirety and drafted a first-of-its-kind (in Israel) proposal for wide-ranging systemic educational reform. Two months before we submitted our final report to the education minister and presented it before the Knesset's education committee, the official education task force headed by Shlomo Dovrat was commissioned by the government and given an directive identical to ELA stated objectives: do a comprehensive investigation of Israel's educational system and provide solutions.

In light of what appears to be an erosion process of the Dovrat recommendations to a point that may lead to its eventual abandonment, it is important to recall what this is all about. The Dovrat report provides serious core solutions to the system's ills. No longer will excellent teachers, and there are many of these, have to devote long hours of their own time in the afternoons, evenings and during vacations without receiving compensation. No longer will they and their less devoted colleagues receive equal compensation. The huge and wasteful

beaurocracy of the education ministry will be drastically cut, releasing many resources and budgets that will finally be able to make their way to the students. School principles will be given extended authority to run their schools, together with extended responsibility and accountability for the subsequent outcomes. Instead of the extremely low and sub-standard admissions requirements for teaching colleges, all future teachers will be required to master their subject matter at the university or general college level and graduate with at least a B.A. or B.Sc. (instead of a B.Ed) and a teaching certificate. The longer school day will allow children to receive assistance from their own teachers in the afternoon instead of having to pay for private tutors, and it will enable many more parents to participate in the labor force.

Even if there are a number of differences in the structure, there is nonetheless considerable similarity in the concept underlying the model proposed by the Dovrat task force and the solution suggested by the ELA commission, and it stands to reason that any serious commission that may be created in the future will also reach similar conclusions. Therefore, it is imperative that the Dovrat recommendations be implemented immediately and that an accelerated process begin to resolve the main problems posed by the report (there are quite a few of these). We have an extremely rare opportunity – the existence of a very important plan on the table together with a rare agreement between the three main persons responsible for its implementation and budgeting, the prime minister, the education minister, and the finance minister – for serious root canal treatment in one of the main areas determining the social, economic, and security viability of the state of Israel. The time has come to turn our increasingly barren hourglass around before it completely runneth empty.

## The Health Threat

by

Dan Ben-David

A nation with a future requires leadership with vision, caring, integrity and the ability to plan ahead. The decline – in relation to the western world – of Israel's economy, society and educational system since the seventies speaks for itself as to the caliber of our elected officials (though there were a few exceptions) over this period. A country's inner strength, upon which its defensive might is based, is determined by its living standards, the degree of its internal gaps, and the quality of life of its citizens.

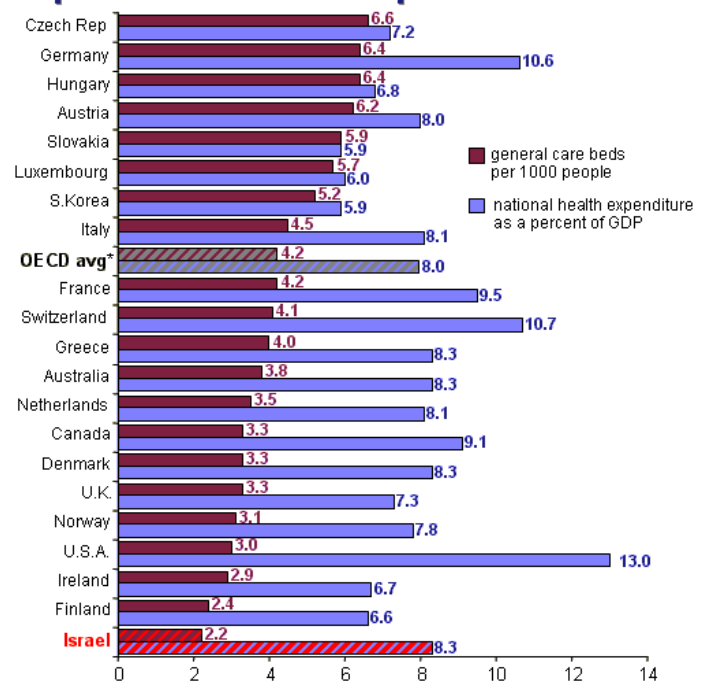
In this latter realm, the health threat to Israel is serious. This is a country that allows its first world doctors to be overshadowed by a third world managerial culture that abandons our loved ones to subsistence as vagabonds in hospital corridors during their weakest hours, that condemns them to premature death because of budgets that move intensive care and national medicine baskets downward on the budget prioritization ladder, that creates large gaps in the quality of medical equipment around the country. This is a country that, given the amount of money that it spends on health, should have looked substantially different at the dawn of the 21<sup>st</sup> century.

Israel's national health expenditure as a percentage of its GDP puts it in 8<sup>th</sup> place among 29 OECD countries. On the other hand, the number of general care hospital beds per 1000 persons is just 2.2 – below all of the western nations. While bed occupancy in internal medicine units abroad is 65-75%, the annual Israeli average was 106% in 2003, and during winter the occupancy rates reach 150-200%! As if this were not enough, investment's share of the national health expenditure fell from 6% in 1980 to 3.7% in 1990, reaching 3.9% in 2000, so don't hold your breath for any improvements any time soon.

Since the national health law was enacted in the mid-nineties, private spending rose from a quarter to a third of the national health expenditure. We pay more, but the waiting periods for medical specialists just get longer and longer. The wait to see a cardiologist can reach 4 months – but this only regards an evidently minor organ such as the heart, so there is no rush to get a diagnosis.

About 5% of the general care beds in Europe are in intensive care units (ICU's). In the United States the proportion is 10%. There are

### Relationship between health expenditure and hospital beds



\* The average is for all 28 OECD countries with expenditure data and all 22 countries with data on beds.

Source: Dan Ben-David, Tel-Aviv University  
Data from health ministry, originally from CBS and OECD.



1,600 beds in the Sheba medical center at Tel-Hashomer, one of Israel's premier hospitals – but just 10 of these are in the intensive care unit. In Ichilov, another first tier hospital, there are 1,000 beds, and (according to the Bulldozer TV program) only 9 in the ICU. Even when the equipment is donated and reaches the hospital at no expense to Israeli taxpayers, someone still prevents budgeting for the medical team that could operate it.

Beds in intensive care units are three times more expensive than regular hospital beds. Therefore, our managerial wizards prefer giving us less beds in the ICU's (with fatality rates of 15%) and transfer our nearest and dearest to intensive care rooms located in the internal medicine units (with fatality rates of 65-85%). Even though the actual differences are not quite that large since the lack of space in the ICU's forces them to transfer to the intensive care rooms patients with lower chances of survival, the inferior equipment and the substantially more diluted staffing with less intensive care experience seals the fate of the majority of those who are transferred.

The problem of the health system is not a lack of money, though my personal preference would be to increase the health budget at the expense of the nationalistic preferences of the current health minister. But first, there is a need to know where the money that we spend on health is actually going. As is common in these parts, no one is accountable, there is no transparency – and there is no one that can be relied on in our national leadership. It is time for the prime minister to appoint a national task force, as he did with education, comprising blue ribbon professionals specializing in health, social work, management, economics and law in order to rejuvenate a sick health system that literally affects our quality of life.



## The Budget Threat

by

Dan Ben-David

The story of the “health basket”, that bundle of medicines and medical technologies included in the annual national health bill, symbolizes how this country formulates its national priorities. The public commission in charge of determining the annual additions to the basket has concluded that the required new drugs and technologies will cost 470 million NIS. But the government is not willing to approve more than a 200 million NIS addition to the basket. “No money” is the commonly heard claim.

How many other budget items influence our quality of life more than health care in an hour of need? In a country that tosses around sums like 290 million NIS (and up) as if they were candy as part of coalition agreements, isn't it possible to find another 270 million NIS that will benefit patients from all of the parties, races and religions? The intention is not to increase the budget but to ask a simple question: where is all of our money really going?

The time has come to puncture the public illusion that the State of Israel does not have sufficient funds to adequately take care of business. Not everything here is going to defense – though it is true that too much is being wasted on defense in the absence of adequate transparency and public oversight. However, there is more than enough left over for civilian purposes.

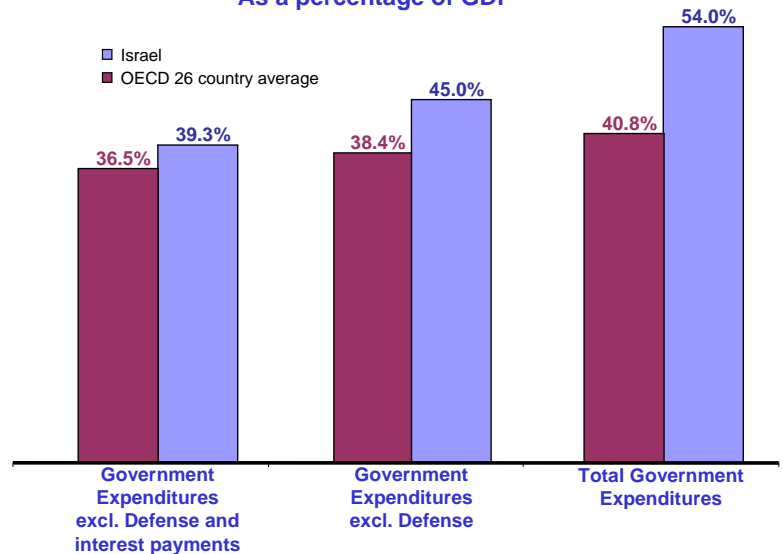
According to the Bank of Israel, public expenditure in 2003 reached 268 billion NIS, or 54% of GDP. That same year, average public expenditure among OECD countries amounted to just 40.8% of GDP. However, contrary to public mythology, the difference in expenditure is not just because of Israel's large defense outlays. Even after excluding defense spending, civilian public expenditure in Israel is 45% of GDP, compared with an average of 38.4% in the OECD.

In other words, there is no lack of money – and for a long time now there hasn't been a lack of money – in terms of non-defense, civilian, expenditures in comparison with the OECD. Hence, there is no justification for the relative decline in livings standards or the steady increase in poverty and income inequality over the past 30 years. It is all a question of national priorities.

The oft-cited “mahapach” (loosely translated as “revolution”) that we underwent in the 1970s was much more far-reaching and extensive than most people imagine. It changed our fundamentals at their very core and it actually moved an entire country to new long-term trajectories. Disastrous ones, as it turns out.

### Government Expenditures 2003

As a percentage of GDP



source: Dan Ben-David, Tel-Aviv University  
Data from the Bank of Israel, the OECD and the CIA.

As a result of such high levels of spending, the exceedingly heavy tax burden in Israel is insufficient and we need to borrow. Interest payments on these loans in 2003 surpassed 29 billion NIS. For comparison purposes, Israel summarily chucks into the sea – i.e., pays its lenders rather than investing in infrastructure and providing services – each year an amount much larger than its entire public expenditure on primary and secondary education. This is an amount similar to, not the health basket, but the entire public health expenditure. This is what Israel’s national agenda looks like since the 1970s.

The time has come for the Israeli public to replace its hard drive and change its operating system – to internalize the fact that it is our money that is in the hands of those whom we elected to decide on its allocation. The MK’s and cabinet ministers did not win the Lotto and receive from us billions of shekels – our hard-earned money that we pay as taxes – for purposes of self-glorification or for providing jobs to party hacks. It is long past time for national, as opposed to nationalistic, considerations to finally prevail over narrow personal and sectoral interests. After thirty years, the time has come for a new “mahapach” – one that returns the country to the trajectory of sanity.

---

## Toward a True Socio-Economic Turnaround

by

Dan Ben-David

---

Perhaps a little more modesty would have been in order before the finance minister convened a press conference to inform the nation of our expected entry into the club of the ten leading countries within the next ten years. This is the same person who gave a nearly identical address in his first year as prime minister in 1996. Average living standards in the G7 countries that year were 38% higher than in Israel. Since then, their standards of living rose by 17% while ours rose by just 3% (in fact, our living standards would have fallen by 2% had it not been for the outlier year, 2000). Thus, the finance minister should understand if we wish to abstain from a repeat screening of the horror movie that he and his party imposed on us over the past eight years.

Living standards in Israel have steadily been falling farther and farther behind the leading western countries for the past 30 years. Poverty and income inequality have been steadily rising throughout this period, reaching western peaks in recent years. Can such a country actually change direction? In the Wild East in which we live, the existential question is not whether such a change is possible – it is – but what needs to be done in order to ensure a successful turnaround.

Real treatment at the source of the problems requires adequate provision of the tools and working conditions necessary for the Israeli worker to succeed in an open and competitive economy. In “A Blueprint for Improving the Employment Outlook in Israel,” an academic interdisciplinary team that I headed (team members included two sociologists, Noah Lewin-Epstein and Haya Stier, and two economists, Avner Ahituv and I, from Tel-Aviv and Haifa Universities) emphasizes the importance of a systemic approach integrating short and long term solutions. The main points of our comprehensive plan include:

1. Work incentives and reduction of the tax burden:
  - (a) replacement of work disincentives with work incentives;
  - (b) combining all sources of aid and subsidies, with transparent criteria for allocation;
  - (c) combining family incomes from all sources and widening the tax base;
  - (d) reduction of government expenditures to enable reduction of the tax burden.
2. Significant reduction in the number of foreign workers.
3. An integrated system for adults including:
  - (a) supplementary education (the “Second Chance” program);
  - (b) vocational training;
  - (c) job placement.
4. Substantial improvement of Israel's educational system and:
  - (a) truly free compulsory education;
  - (b) longer school days;
  - (c) subsidized enrichment programs for children and youth during after-school hours.
5. Significant upgrading of Israel's transportation infrastructure.
6. Investment in research and development

7. A change in the political culture that includes:
  - (a) serious law enforcement;
  - (b) credible public policies,
  - (c) provision of a national security horizon.

If press releases and public claims are to be believed, the government is already implementing the recommendations. But there is more here than meets the eye.

The government purportedly wants more people to work, so what is the wisdom of cutting the formal welfare aid channels without touching the huge backdoor financing channels well hidden from public scrutiny in non-transparent and unfathomable budget items? Where is the voice of the finance minister with regard to non-enforcement of basic labor laws like minimum wage? Is it serious to concentrate on the expulsion of illegal foreign workers with one hand, while the other hand continuing to issue entry permits to new workers,, and while there is no move to substantially increase the hiring cost of foreigners relative to Israelis? Job placement ala the Wisconsin Plan is not a substitute for upgrading education among working age products of Israel's abysmal educational system, nor for providing skills compatible with a modern economy – and the intent is not more failing vocational training programs of the kind currently available.

The requirement to report incomes annually – combined with serious enforcement and penalties that act as strong deterrents – will facilitate discernment of the truly needy while introduction of a negative income tax will increase the motivation to work, supplement low incomes, and act as an incentive for more complete reporting of business activity.

In a country not blessed with unlimited funds, the recommendation for a substantial improvement in the transportation infrastructure is not intended to condone the waste of billions on unnecessary trains to Eilat or slow trains (slower than buses) through Beit Shemesh to an out-of-the-way Jerusalem station. The recommendation for significant improvement in the educational system does not correspond with the deafening silence of the education and finance ministers when their government signed a recent coalition agreement completely releasing ultra-orthodox schools from implementing any reforms.

Any hope of successfully turning around Israel's long run trajectories is heavily dependent on a shift from incomplete, ineffective and superficial policies slickly packaged with glossy slogans and excessive marketing, to long overdue serious, professional management of the country.