

POLICY BRIEF

Outline for Systemic Treatment of Israel's Primary Socioeconomic Challenges

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Welfare and taxes provide a means for reducing poverty and income inequality at the symptomatic level, by dealing ex post with symptoms that already exist. While this social safety net is certainly a vital resource of last resort, the fundamental challenge is to reduce poverty and inequality at their source – that is, ex ante, in market incomes (before taxes and welfare payments) – by giving individuals the human capital and physical capital infrastructures that will enable them to find work and thrive in a modern economy.

The Israeli failure with regard to market income inequality is on two fronts. Domestic gaps in educational achievement in core subjects on international exams are consistently greater in Israel than they are in all of the world's developed countries (Ben-David, 2010 and 2011a). Economists often refer to the skill-biased technical change underlying the growth process as a primary factor driving up the demand for skilled and educated workers – and similarly, driving down the demand (in relative terms) for the relatively unskilled and uneducated. The resultant impact in Israel on employment and wages is clearly shown by Ben-David (2011b), Kimhi (2011, 2012), and others.

Alongside Israel's problematic human capital infrastructure is its long-neglected physical infrastructure. The country has two and a half times the road congestion of other Western countries – although the number of vehicles per capita in Israel is only about half the OECD average. One of the smallest countries in the developed world has managed to create what it refers to as “peripheries” at distances that would be considered “suburbs” in other countries.


These fundamental problems – and others – are manifested in Israel's high market income inequality. The country also provides a social safety net that is the second least effective – after the United States – in reducing the core inequality reflected in market incomes to a substantially smaller disposable income inequality (after taxes and welfare).


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Key policy points for changing Israel's problematic long-run socioeconomic trends in core areas: low productivity, high poverty rates and wide income gaps

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Low wage jobs due to low and poor levels of education – and an accompanying decline in opportunities for low-skilled workers (Ben-David 2011b) – are a key underlying source of Israel’s high rates of poverty and income inequality. Stier (2011) provides evidence of a substantial increase in the number of “working poor” households in Israel since the mid-1990s. Kimhi (2011) shows how differences in education have led to much larger wage gaps than are caused by differences in gender or in job experience/seniority – and these are growing more rapidly as well.

Also instrumental in heightening Israel’s income inequality are inadequate surrounding conditions such as affordable childcare as well as a lack of a quick, efficient, inexpensive and reliable transportation infrastructure that would increase access to jobs. The prevalence of large families with a relatively low percentage of two earners also contributes to a considerable extent to the high incidence of poverty and income inequality. Barriers to employment, particularly among Arab Israelis, are not always due to low levels of education and poor access. Discrimination, although hard to quantify, certainly plays a role as well.

Goldin and Katz (2008) write that the decay in America’s educational system underlies much of the increases in the country’s income inequality. They point out that this is a straightforward policy issue that can be addressed – and, if implemented well, could contribute to a substantial change in the magnitude of inequality in the United States. Acemoglu and Autor (2012) conjecture that a major barrier to “reversing America’s educational slide” that does not receive sufficient attention is politics. They write: “As it was politics that largely underpinned American schooling exceptionalism [in past decades], fundamental reforms and significantly expanded investments in the U.S. education system would only be possible if the political will is found to support them.” It is hard to overemphasize the importance of this conclusion with regard to Israel.

Israel is in urgent need of a fundamental shift in its national priorities focusing on three primary policy spheres that are briefly summarized here in outline form. The likelihood of such a shift actually occurring is primarily a question of political wherewithal.

First Policy Sphere: Creating Incentives and Providing Tools

- **Increasing incentives to work and to employ**

- **Replacing non-work incentives with incentives to work**

The share of employed prime working age Israeli men is low compared to other developed countries. Many families with prime working age parents receive sufficient governmental support to facilitate the choice of non-work as a lifestyle. One example of support that operates from the opposite direction, as a work incentive, is the negative income tax, which has begun to be enacted in Israel. It needs to be made more substantive and barriers to its receipt need to be brought to a minimum.

- **Substantially reducing the number of foreign workers**

On one side of the dichotomy are individuals able to choose non-work lifestyles. On the other side are the many employers who are allowed to avoid having to deal with the Israeli workforce by receiving permits to import large numbers of unskilled and uneducated workers, although these exist in abundance in Israel. The possibility to import foreign workers needs to be reduced considerably.

- **Providing tools and conditions – a comprehensive employment package**

A better employment incentive structure can only be successful in increasing employment if it is merged with a modular program that will improve the level of education and the skill set of the Israeli worker so that employment rates, productivity, and incomes will increase. This might include a “second chance” program for completion of high school and college, vocational training coordinated with the needs of the private sector, and job placements with incentives based on the workers’ success.

Second Policy Sphere: Creating a Supportive Environment

Elements that help create a supportive environment include:

- **Extended school days and subsidized afternoon youth enrichment programs**

For those at the bottom end of the skill and wage ladder, the provision of incentives and skills will be only partially effective, if there is little or no arrangement for their children. Longer school days – post-reform, to ensure quality improvements rather than babysitting – with enrichment programs in the afternoon will not only release parents to work, but will serve to better prepare these children for their futures.

- **Substantial upgrade of the transportation infrastructure**

Provision of fast, cheap and readily available transportation throughout the country is necessary for increasing access from the periphery to jobs in the cities. Some progress has been made in this regard in recent years, but it has proven to be much too little and much too slow given the huge gap in infrastructure between the developed world and Israel that was allowed to dramatically increase since the 1970s.

The combination of longer school days and better schools in the periphery with a transportation infrastructure that will bring nearly all of Israel’s population to within 30 minutes of one of its major cities will not only reduce the current housing crisis for young families by making larger apartments available for lower prices in areas that they would not consider living in today. It would also provide better schooling for those children already living in the periphery – with the potential of a better future for them – while providing their parents with greater access to jobs. This will not only reduce poverty and income inequality in market incomes today, it will also put the country on a path to their future reduction.

Third Policy Sphere: A Multi-Year Strategic Plan

While rear-guard actions like those outlined above are essential, it is no less important to realign Israel's national priorities to favor the good of the general public over the long run rather than current prioritization of sectoral interests and short-run gains. The government budget needs to be redone from top to bottom, in accordance with budgetary requirements derived from a new national agenda that should include:

- **Significant increase in budgetary transparency**

It is not possible today to know what Israel's national priorities actually are, how much money is being allocated to whom, and on the basis of what criteria. This is a process that the Ministry of Finance can implement within months – if it so desires.

- **Comprehensive and system-wide education reform**

Such a reform should concentrate on determining a much more focused and uniform core curriculum for all of the nation's children. It should substantially improve the way teachers are trained and compensated. Such a reform needs to greatly improve the efficiency of the cumbersome and byzantine bureaucracy of the Ministry of Education.

- **Heightened law enforcement by upgrading and increasing efficiency of the police and court system**

Roughly one half of Israeli's eligible for the minimum wage do not receive what they are entitled to by law. In addition, Israel's shadow economy is one of the largest in the developed world, accounting for about one-quarter of its GDP – over 200 billion shekels each year. A large number of transactions go unreported, court trials can last many years, and the resultant situation favors the dishonest at the expense of those who abide by the laws – at a tremendous national cost.

- **Health system ensuring quality medical care for all**

While coverage is universal and life expectancy among the highest in the world, the conditions for patients in Israel's hospitals are poor, with the lowest number of hospital beds per capita in the developed world. Physicians who are among the best in the world are compensated far below what they could earn abroad, or in other professions requiring similar skill sets in the private sector. While the stock of physicians per capita is still relatively high – due to the massive immigration from the former Soviet Union in the 1990s – the annual flow of both new physicians and new nurses is quite low, indicating potential supply problems in the future.

- **Welfare policy ensuring a quality social safety net that will enable adequate living standards for those who truly need it**

Among its current inequities, the same social welfare safety net that leaves the highest share – relative to the rest of the developed world – of retirement age Israelis in poverty (according to disposable incomes) also provides benefits at levels enabling working age individuals to choose non-work lifestyles at rates unparalleled in the developed world.

These policy spheres outline the three primary components of a systemic plan to deal with the fundamental causes of poverty and income inequality – as well as spurring productivity and economic growth – together with the symptoms after these problems have already manifested themselves. The primary idea is that policy makers need to see the big picture, understand the underlying problems and concentrate on reducing them over the long run, while utilizing the opportunities provided by short-term crises to deal with the deeper longer term problems. A specific example can highlight how this might work.

In the months following Israel's national elections in 2013, it became apparent that the new government faced a huge budget deficit reaching roughly NIS 40 billion. The common Israeli solution to such problems is to increase taxes while implementing across the board cuts in the budgets of the various ministries – with very little reprioritization. It is possible, however, to do things differently.

A case in point involves universal child benefits given to every family, regardless of the parents' income or work status. These benefits have a dual objective – to encourage childbirth and to reduce poverty in disposable incomes. Studies by Cohen, Dehejia, and Romanov (2007) and Toledano, Frish, Zussman, and Gottlieb (2009) show that the impact of the child benefits on fertility has not been evident anywhere except – in varying degrees – among Haredim (ultra-Orthodox Jews) and Bedouin Arab Israelis, two of the habitually poorest segments of Israeli society. In addition, there is a question regarding their effectiveness as a tool for reducing poverty – not to mention questions regarding their long-term impact.

Child benefits equaling NIS 175 or NIS 263 per child each month (the size of the benefit depends on the total number of children in the household) were provided universally to all families at the time. While these translated into about NIS 6 or NIS 9 (roughly \$1.60 and \$2.40) per day per child, the entire program cost the country NIS 7 billion each year. In light of the NIS 40 billion deficit that needed to be dealt with, this could have been a prime time to rethink the entire child benefit issue.

As suggested in Ben-David (2013), the government could take NIS 2 billion from the NIS 7 billion to help reduce its deficit while redirecting the remaining NIS 5 billion. Instead of continuing to provide benefits to each Israeli child, the entire amount could be directed exclusively toward the poorer Israeli neighborhoods and towns in the form of hot lunches in schools whose school days would be lengthened and lunchrooms built. This could have meant considerably more money directed toward each child in these areas than would otherwise have reached that child, but it will be in the form of ensuring at least one nutritious meal a day. There is one additional vital requirement in this policy: the schools must be a part of the systemic nationwide education reform outlined in the third policy sphere, and they must provide their pupils with a comprehensive core curriculum in the basic subjects. In this way, Israel would also have begun to deal with the long-run issue of inequality in opportunities and incomes. Parents would no longer be able to choose to deprive their children of a basic education – as is the case in most Haredi schools – while receiving child benefits that contribute to their ability to choose not to participate in the labor force.

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Summary Points

First Policy Sphere: Creating Incentives and Providing Tools

- Increasing incentives to work and to employ
 - Replacing non-work incentives with incentives to work
 - Substantial reduction in the number of foreign workers
- Providing tools and conditions – a comprehensive employment package
 - second chance program for completing high school and college
 - vocational training coordinated with the needs of the private sector
 - job placement with incentives based on the worker's success

Second Policy Sphere: Creating a Supportive Environment

including:

- Extended school days and subsidized afternoon youth enrichment programs
- Substantial upgrade of the transportation infrastructure, provision of fast and cheap public transportation throughout the country

Third Policy Sphere: A Multi-Year Strategic Plan

Government budget will be redone from top to bottom, in accordance with the budgetary requirements derived from a new national agenda

including:

- Significant increase in budgetary transparency
- Comprehensive and system-wide education reform
- Heightened law enforcement by upgrading and increasing efficiency of the police and court system
- Health system ensuring quality medical care for all
- Welfare policy ensuring a quality social safety net that will enable adequate living standards for those who truly need it

The Taub Center is an independent, nonpartisan, socioeconomic research institute based in Jerusalem. The Center conducts quality, impartial research on socioeconomic conditions in Israel, and develops innovative, equitable and practical options for macro public policies that advance the well-being of Israelis. The Center strives to influence public policy through direct communications with policy makers and by enriching the public debate that accompanies the decision making process.

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