

Overview

This document is submitted to the Government of Israel by the National Economic Council as a suggestion for the framework of the comprehensive socio-economic policy for the years 2008-2010 (heretofore “Agenda”).¹ We will open with a description of the central trends characterizing the current economy and society in Israel, while examining their primary weak points. On this basis, a range of policy tools is presented, and is intended to deal with those central problems, both in the short/medium and long-terms. Furthermore, the document sets out the principles meant to guide the outlined policy and its operation, as well as the specific quantitative goals by which the policy will be examined over a long period of time.

The Agenda presented herein includes two primary tracks: the prime goal of the first track is **to reduce poverty while encouraging growth**, while the key is to be found in encouraging employment with suitable wages and an economic horizon. The goal of the second operational track is **to create leverages for balanced, long-term growth**, primarily through improving education at all levels and strengthening and leveraging science, technology and research & development. The vast majority of the current document will be dedicated to the first track, since staff work on this track advanced more rapidly. We are at the height of the preparatory work for the second track (the principles of which will be presented later in the document) and we hope to publish a second, parallel policy paper soon.

The majority of policy tools included in the Agenda are not new at all, not in Israel and certainly not in the world. The “innovation”, if there is one, stems, first and foremost, from those tools being used as one, as decreed by a consistent professional outlook, in the framework of the comprehensive, multi-year plan, which is guided by clear goals. Therefore, we make substantial use of the experience gained in operating similar policy tools in other countries in the world (specifically in the field of active labor market policies), and furthermore, we draw from, rely on and proceed with previous plans in these fields which were outlined in Israel. A clear example of this is the plan recently presented by the Minister of Finance and adopted by the Government (which includes “steps to reduce socio-economic gaps and increase the rate of participation in the labor market”), parts of which are closely

¹ This document is constructed in the format of a “white paper”, that is to say a policy paper which professionally but not too technically details the background, policy tools and the expected results, as is accepted in other countries in the world, specifically England.

incorporated in the Agenda. We are not occupied with originality, but rather in adapting the various policy tools to the special and changing circumstances of Israeli society, while focusing on the public and governmental attention paid to such a plan, by creating cooperation between Government factors central to its implementation, and in ensuring the necessary budgetary and institutional sources for the long-term, as these are the conditions critical to its success.

Background

Over the last few years, the Israeli economy has shown strength and stability, which are expressed in the impressive macro-economic data: high growth rates during the last three years, price stability, a sharp decrease in the debt-gross domestic product(GDP) ratio and an unprecedented surplus in the balance of payments. In addition, according to the record level of foreign investments, the ongoing up-swing in the stock exchange and the strengthening of the shekel, we can learn that domestic and international expectations are for a long-term continuation of these impressive accomplishments. In addition, the positive data become even clearer in light of the fact that they were achieved despite the Second Lebanon War.

However, a thorough examination beyond the macro shows a picture which is much more complex, with current, acute problems, as well as question marks regarding the future ability of the economy and of the strength of the social fabric. The primary issues which arise in this context are:

- ***Domestic issues:*** a high and ongoing incidence of **poverty**, specifically among children (approximately 35% of Israeli children live under the poverty line), when poverty is focused in the Haredi and minority sectors; widening **inequality** – a record high among OECD countries.
- ***In the global environment:*** a widening gap in **product per capita** between Israel and the United States; massive entry of new players in advanced **research & development**, and therefore an undermining of Israeli superiority in this field; a worsening of the geo-political environment, which wouldn't lead to a decrease in the **security burden** in the coming years.

The deep and wide-spread poverty constitutes not only a mark of disgrace for the State of Israel today, but also constitutes a threat to the continued prosperity of the economy in the near future, for several reasons: first, the increasing budgetary burden resulting from supporting the needy, which is, for the most part, in the scope of providing relief without providing a solution for the root of the problem. Second, and more importantly, poverty in such dimensions means that a significant portion (about one third) of young workers who will join to the labor market in 5 to 10 years will arrive with clear disadvantages in education, health and other skills needed to utilize their production potential. In addition, the widening of gaps threatens social unity, and therefore a series of depended parameters therein, beginning with crime and including not willing to participate in the security burden. The widening gap in product per capita between Israel and the United States threatens to draw away the highest level of young talent– what is referred to as the “brain drain”. It is clear that “economy” and “society” are intertwined, and that one cannot be dealt with without the other. It is also clear that economic growth in and of itself, the crown of economic performance in general, cannot necessarily by itself provide an appropriate answer to poverty and increasing polarity, certainly not in the period of time we would like. This is why we view reducing poverty while encouraging growth as our primary goal, which must guide the fundamentals of the socio-economic policy in Israel in the coming years.

The Principles for Formulating the Agenda

In order to formulate the policy tools to deal with the central problems presented in the foregoing, the background factors for their creation must be examined, as the specific intention here is to deal with the roots of the problems and not only the symptoms (as is known, treating the symptoms sometimes perpetuates and exacerbates the fundamental problem). From the analysis of the poverty figures, it is quite clear that **the lack of suitable employment** is one of the immediate central factors which stand behind it: while the incidence of poverty among families without wages reaches 68%, among families with two wages, the poverty rate drops to only 3%. Lack of employment has two primary aspects: high unemployment rates, and a low rate of participation in the labor force, both of which are in accordance with international standards. An important factor in lack of suitable employment relating to *demand* for labor force is an ongoing eroding of productivity in traditional industries and in the service sector, which are large-scale employers in the economy.

Among the long-term factors, there are obvious, ongoing failures at all levels of the education system, which constitutes the basis for the creation and preservation of quality human capital. These failures find expression in the steep, long-term decrease in achievement in the State education system, in the inadequate, systemic treatment of toddlers and in children and teens at risk, in the diminishing of professional-technological education and in the regression of higher education and scientific research. Some of these fundamental problems result from global processes over which we have no direct control (such as accelerated globalization), but the phenomena grow stronger in light of the unique characteristics of the State of Israel.

From an analysis of these background factors, the two tracks of action mentioned earlier are derived: the first is **reducing poverty while encouraging growth**, and at its core is encouraging employment with suitable wages and an economic horizon; the second is the creation of **leverages for balanced, long-term growth**, and at its core is fixing education at all its levels, in science, technology and research & development.

These are the principles on which the Agenda is based, and of which the strict preservation of their existences is no less important than the content of the policy themselves:

1. Implementing the Agenda **as one unified whole**, with a **comprehensive and systemic** approach, while remaining committed to the **long-term**.
2. Determining defined, quantitative **goals**, which will be added to the existing economic goals.
3. The **Prime Minister** himself taking an active role in leading the Agenda.
4. The cooperation of a **broad range** of professional factors in formulating the specifics of the plan and its implementation, first and foremost the leading economic offices, the Bank of Israel, the National Insurance Institute, the Central Bureau for Statistics, etc.
5. The establishment of a **professional oversight mechanism**, which can draw conclusions in real time and offer the appropriate changes.
6. Allocating **multi-year budgets** for the years 2008-2010, while maintaining fiscal discipline.

The First Track: Reducing Poverty While Encouraging Growth

A. Goals²

In the framework of implementing the Agenda, it is proposed that two quantitative multi-year goals be determined, which will be added to the existing macro-economic goals, namely with regard to inflation and deficit:

1. The goal is to reduce the **incidence of poverty** among Israeli families to a rate of **17.2%** by the end of 2010, compared to 20.2% today. In other words, an average annual reduction of 1% in the rate of poverty for the years 2008-2010. Upholding this goal will raise approximately 60,000 families above the poverty line, which comprises 242,000 individuals, including approximately 115,000 children. Upholding this goal will return the poverty rate to its level of a decade ago.
2. The goal of increasing the rate of employment between the ages of 25 and 64 to 71% by the end of 2010, when compared to a rate of 68% today. In other words, an average annual increase of 1% in the employment rate for the years 2008-2010. Upholding this goal will lead to the entry of over 92,000 people between the ages of 25 and 64 to the labor force, and will increase the employment rate in Israel to the average rate in OECD countries.

Achieving these goals has not only immense social importance, but also far-reaching economic influence: according to the estimations, achieving the employment goal is expected to add 1.3% to 2% to the gross domestic product (which is NIS 8-12 billion), and will also bring a significant addition to the State's income and a savings in allocation payments.

B. Policy Tools

To achieve the goals presented in the framework of the first track, seven policy tools are proposed and detailed below. Each of them stands by itself, but it would be a mistake to refer to each of them separately, since the strength of the program is both in its being one totality, and because of the synergistic influence between the tools, which strengthens the separate effects. For example, the introduction of negative income tax requires the decisive

² It must be emphasized that the preliminary goals which appear herein were formulated in accordance with simulations conducted by the National Economic Council. When specific goals in these fields are determined by the Agenda Implementation Committee, headed by the Director General of the Ministry of Finance, they will be brought to the Government for approval.

enforcement of labor laws, specifically the minimum wage; the Mehalev program requires negative income tax, etc.

The tools are as follows:

1. **Encouraging Productivity and Renewal of the Traditional Industries and Services**

The branch of traditional industry and the services sector are the largest employers in the economy, however they suffer from low levels of work productivity, a lack of innovation and low levels of competitiveness. These factors are slowing growth in these fields, decelerating the growth of demand for work and perpetuate low wages for the workers in these fields. Therefore, it is proposed to encourage technological, marketing and organizational innovation in these sectors by supporting designated research & development with a broad and customized definition, promoting **industrial design**, and encouraging the adoption of information and communication technologies (ICT). In addition, processes of exporting a broad range of services must be adopted, and we must act to remove the obstacles to competition and competitiveness between those with a strong local character.

2. **Treatment of Concentrations of Poverty – Haredis and Minorities**

Poverty in Israel is divided very non-uniformly by populations: Haredis and Minorities together constitute nearly one-fourth of the population in Israel, but represent more than half of poor families. The primary factors behind such high poverty rates are amplified by high unemployment, an extremely low rate of participation among Haredi men and Arab women, labor discrimination, a barrier to military service, cultural gaps, high birth rates, etc. These factors demand focused treatment in these sectors, when a significant portion of the tools are common to both sectors, and some are distinct. Therefore, the “Tal Law” must be reinstated, civilian-community service must be expanded and modified to serve as a tool which trains for employment, encourage the establishment of outsourcing centers in Haredi and Arab towns, particularly in exporting services, acting systemically against employment discrimination, etc.

3. **Procuring Individual Tools for Integration into Employment**

Israeli society is characterized by high heterogeneity in its population as a whole, and in the unemployed populations in particular, which finds expression in a wide variety of employment obstacles. Therefore, there exists a need for individual

treatment and procuring a wide range of skills for the unemployed, which will provide an answer to the range of obstacles, and for ongoing and continuing assistance until they are fully integrated in the labor market. This is the goal of the “*Mehalev*” program, which has been operating on a trial basis for about three years. However, during the implementation of the program, numerous problems were discovered both in the economic model on which it was based, and the method of its implementation (again, in light of the high heterogeneity of the target population). Therefore, there is a need to incorporate far-reaching changes, some of which have already been formulated in the framework of the team headed by the Director General of the Prime Minister’s Office, Raanan Dinur, in which members of the National Economic Council took part. These changes will constitute the basis for expanding the program until it is fully national. Therefore, it is proposed to expand the “Tevet” (“Increasing Employment”) program operated in conjunction with the Joint Distribution Committee, the goal of which is to deal with the employment problems of specific, weaker populations, such as Haredis and those with disabilities. As complementary tools supporting employment, it is proposed to improve the accessibility of transportation to workplaces, expand the assistance and subsidies for day care³, focus the campaign for professional training primarily on on-the-job training and act to integrate the disabled into the labor market by implementing the conclusions of the “Laron Committee”, and by the “Adjusted Minimum Wage” program operated by the Ministry of Industry, Trade and Labor.

4. **Negative Income Tax**

This tool has been in use for years in the United States and other western countries, and its goal is to reduce poverty among working families as well as increase the incentive to integrate those with low wage-earning potential into the labor market. Since its establishment, the National Economic Council has stood for establishing negative income tax as part of the Agenda which was being formulated, and therefore we viewed with great satisfaction the Minister of Finance’s initiative to introduce it, within the framework of the plan adopted by the Government on February 4, 2007. However, there are a number of aspects in the manner of the operating of negative income tax which demand further, intensive examination (which will be detailed below), specifically prior to national implementation.

³ See Government Resolution No. 1134 of 4.2.07 which deals with this topic.

5. **Enforcing Labor Laws**

Israel currently suffers a laxity in the enforcement of labor laws (minimum wage, overtime, foreign workers, etc.), a fact which contributes to the perpetuation of the working poor. In order to treat this phenomenon, we should act to allocate additional resources for oversight (expanding oversight and outsourcing) in accordance with the relevant Government Resolutions. In addition, adoption of the treaty on this subject between the Manufacturer's Union and the Worker's Union should be examined as a basis for action, we should develop computerized methods for locating those who violate labor laws, increase cooperation between law enforcement authorities and other sources of information and regulate legal aspects in order to relieve the pressure on enforcement (such as applying civil law to some offences and making the policy of punishment more severe).

6. **Further Reduction in the Number of Foreign Workers**

According to estimates, there are approximately 180,000 foreign workers in Israel, when the majority of legal workers are employed in construction, agriculture and frail care. These workers are competing over jobs with Israelis on the lower wage levels, and even cause external negative, social and economic influences. Therefore, there is no choice but to continue severely reducing their number, as the private profit from employing foreign workers does not justify the cost **to the economy** of shunning Israeli workers. Therefore, the permitted employment of foreign workers must be severely restricted, while creating an outline for reducing quotas, increasing enforcement in the matter while emphasizing enforcement actions against **the employers** and the equalizing of the cost of employing them to that of Israeli workers (including National Insurance, minimum wage, etc.) and even collecting a surcharge which will reflect the negative "external influences".

7. **Streamlining the Allocation System**

The majority of allocations currently given by National Insurance are universal, that is to say, they are given to anyone who fits the demographic criteria (primarily age), without any consideration of socio-economic status. As a result, the allocations include high budgetary costs (approximately NIS 22 billion per annum) when their effectiveness are doubtful, in the sense that their contribution to the welfare of the neediest is relatively low. Accordingly, it is proposed to examine the establishment of an outline for targeted allocations, at least in addition, which will be given from

here on out, when the case which seems the most appropriate for this is old age allocations.

In almost all the proposed tools, the need for current and accessible information infrastructures containing the economic characteristics of each individual, including real-time data regarding income from various sources, runs through as a parallel thread. This is true with regard to establishing a policy of targeted allocations, operating an efficient system of negative income tax, computerized enforcement of labor laws, the “Mehalev” program model, which encourages quality job placement, etc. Therefore, as a parallel, overarching process, the procedure for reporting and collecting economic data by the authorities (primarily the tax authorities and the National Insurance Institute) should be significantly improved, the computerized system which is at their disposal and their ability to process and maintain existing databases should be upgraded and linking them should be ensured. This process will increase the effectiveness of the variety of proposed tools and will even greatly expand the operative possibilities of socio-economic policies. It is worth mentioning in this context Israel’s advantages in establishing the appropriate information infrastructure for these needs: the existence of a universal identity card, the relatively small size of the population and proven abilities among the most advanced in the world in the field of information technology.

The Second Track: Leverages for Balanced, Long-Term Growth

As aforesaid, the core of the Agenda presented herein is the first track, when the policy tools relating to the second track are still in the preparatory stages. Therefore, we will make do here with just mentioning the central actions in this context:

- **Upgrading education at all its levels:** this channel includes systemic treatment of children and teens at risk, in accordance with the Schmidt Report; rejuvenating treatment of toddlers (the “Good Start” program); re-starting the comprehensive reform of the education system reforming teacher training; resuscitating professional education through a variety of tracks in high school while ensuring mobility.
- **Nurturing higher education, science, technology and research & development:** this channel includes reforms in higher education (in the framework of the Shochat Committee); encouraging designated research & development, specifically in biotechnology and nanotechnology, in traditional industries, in Home Land Security, etc.; strengthening the relative advantages of Israel in selected technological fields;

structural reform in governmental treatment in the fields of higher education, science, technology and research & development (such as examining the ministerial responsibility for each of these subjects, including reviving the National Council for Civil Research & Development, etc.)

Conclusion

As a sort of summary, Diagram 1 presents the variety of tools intended to treat various populations during their life cycles, starting with infancy until retirement. The Agenda presented here relates only to some of these tools – additional tools will be detailed in the framework of the second track, and others demand separate consideration. The basic point of view which guides us is not that the State must take care of every need of an individual throughout his life, but rather that it should place at his disposal each of the basic tools necessary for the individual to take care of himself. Of course, the great challenge is to shape practical content for this statement which is suitable to the characteristics of the economy, in a rapidly changing world. We have our work cut out for us...

Diagram 1

<p>Infancy</p>	<ul style="list-style-type: none"> *Improving the standard of care in daycares and nurseries *The “Good Start” Program 	
<p>Children and Teens</p>	<ul style="list-style-type: none"> *Re-starting education reforms *Implementing the Schmidt Report 	
<p>Pre-Employment</p>	<ul style="list-style-type: none"> *Civil service; procuring skills and removing obstacles *Reforms in higher education 	
<p>Working</p>	<ul style="list-style-type: none"> *Individual tools – “Mehalev”, “Tevet”, professional training *Negative income tax *Enforcement of labor laws, the matter of foreign workers *Encouraging innovation in traditional industries and services *Dealing with of centers of poverty and unemployment 	
<p>Retirement</p>	<ul style="list-style-type: none"> *The streamlining and concentration of the system of old age allocations *Mandatory pensions *Reverse mortgage plans, encouragement of community volunteering 	