



Israel Debates No. 12

12 November 2012

What has been achieved? On the political balance of Israel's social protest movement.

There is an election campaign going on in Israel. On 22 January 2013, early elections for the Knesset, the Israeli parliament, will take place. The main reason to bring the date forward – regular elections were scheduled in the fall of 2013 – was the fact that Prime Minister Netanyahu was neither able nor apparently willing to approve the State budget for 2013. It had foreseen necessary cuts in government spending and significant tax increases, which would inevitably have led to losses at the ballot box for both him and his coalition partners. So it was in his electoral interest to reschedule the elections and postpone the approval of the budget until afterwards.

It seems Netanyahu, who until recently dominated, almost unchallenged, the political scenery in Israel, meanwhile worries about securing re-election. One of the reasons for this is that, as an immediate consequence of the social protest movement last year, Israel experiences a new awareness of social and economic policy issues. The feeling of increasing social injustice, the dismantling of social state principles, a growing gap between rich and poor, housing rents that could no longer be paid and the rising costs of living brought hundreds of thousands of people onto the streets in the summer of 2011. Despite efforts by its leaders, the protests did not continue into the year 2012. Nonetheless, the movement and its demands for social justice and a functioning welfare state managed to significantly impact the country's political discourse. In the previous decades in Israel, it was security policy issues that were decisive in elections. This will not see any fundamental change in future. In view of the developments in the Arab world, the conflict with Iran and the still unresolved Middle East conflict, competence in matters of security policy will continue to play the key role. But there is a good deal to indicate that this alone may not suffice. The protests have raised greater public awareness of the importance of issues of economic and social policy in their country. As a result, people are expecting their political leadership to come up with concrete responses on these issues as well.

Another concern to Netanyahu is the resurgent Labor Party. It was that party's new vigor – apart from other possible tactical considerations – that led him and the Likud Party which he presides (27 Knesset seats) to form an electoral alliance with foreign minister Liebermann's nationalist right-wing party, Yisrael Beitenu

(15 Knesset seats). Netanyahu, clearly the front runner in all surveys, quite obviously wants to make sure that everything possible is done to win the election so that he is again entrusted with the formation of a government. For surveys also show that Labor, which only won 13 Knesset seats in the 2009 elections, meanwhile obtains 20 seats and more. The reason why this party, which only recently faced its most profound crisis ever, is currently enjoying a renaissance is the change of direction its chairwoman Shelly Yacimovich decided upon. When in September 2011 she was elected into office – largely supported by the spirit of the social protest movement – she initiated a radical personnel and program reform of the party. The core of that reform is the return to a social democratic agenda and the formulation of a clear alternative set of economic and social policies to the neo-liberal course of the Netanyahu government.

Labor obviously succeeded in productively incorporating the impulses generated by the social protest movement into its own renewal process. The renewal, which had begun as early as January 2011 when Ehud Barak established his new spin-off Atzmaut Party, constitutes both a reform of political content and a reform on the level of personnel. Many young people, who were involved in the protests, have joined the party since. Among them are some of the leaders of the protest, such as the chairman of the National Student Union, Itzik Shmuli, and the activist, Stav Shaffir. On the Labor Party list, both put themselves forward for a seat in the Knesset. They and other protesters were often criticized for having avoided a clear political stance out of consideration for the unity of the movement. From this, they drew the conclusion to join that party which they believe to best represent the goals and objectives of that movement. With their active contribution, they both want to ensure that the governing political Right does not again succeed in turning the issue of security into that one dominant theme of the electoral campaign and of Israel's domestic policy. They want to make sure that economic and social policy, social values such as solidarity and justice and the profound social inequalities and disparities play a key role both during the electoral campaign and in the future political dispute.

Ever since the protests came to an end in the late summer of 2011 and attempts to continue the protests this year failed, there is an ongoing debate, in Israel, on what the protest movement has achieved, whether the endeavour was a success or a failure. Below we present the analyses of two leading participants in the inner-Israeli debate over this issue:

Prof. Joseph Zeira of the Hebrew University of Jerusalem headed the economic team of the social protest movement commission of experts, which had established itself as an alternative to the Trajtenberg-Committee appointed by the government. In his analysis of the economic causes that led to the protest movement, he demonstrates that as a result of a neo-liberal economic policy that was pursued in Israel over the past two decades, real wages remained static despite strong economic growth, public services were drastically reduced and privatized and social inequality increased significantly. He believes the basis for the total dominance of neo-liberal concepts to be the fact that they hardly faced any political opposition over the past twenty years. The parties dominating that era – Likud, Labor, Kadima – adopted and implemented near identical socio-economic positions. Prof. Zeira believes another reason for the protests to be that, against the background of the Middle East conflict and the dominance of security issues, these economic and socio-political changes were introduced without hardly any public debate – behind the back of public awareness – and therefore in an undemocratic manner. As an alternative to a neo-liberal economic and social policy, Prof. Zeira demands a real change of course. In the areas of budget, labor market, com-

petition and the democratization of the socio economic discourse he presents specific proposals for the reconstruction of a welfare state in Israel. Based on comparative analyses with other OECD-countries, he demonstrates that such a change of course does not need to result in less productivity and economic growth, nor endanger economic stability – as critics of the protest movement like to claim. He concludes that another outbreak of the protests is only a matter of time, since the causes that led to them remain.

Haaretz' senior economics editor, **Nehemia Shtrasler**, is known in Israel as a vehement advocate of a liberal economic system. He believes the most successful achievement of the social protest movement was that, as a result, the secular middle class discovered its strength and found out that its socio-economic interests could no longer be ignored by policymakers. He does suppose that parts of the protest movement want to abolish the system of a free and social market economy that exists in Israel and, with the state as a principal player, roll out a neo-socialist economic order instead. Yet, the bankruptcy of socialism in Eastern Europe has shown that the state does not understand anything about economics and should therefore limit itself to guaranteeing compliance with the existing rules. He considers it inappropriate to speak of “predatory capitalism” in Israel and argues that the Israeli social system has a series of achievements to its credit. But he adds that changes are necessary to improve the social services. As a defender of the idea of a free market, he also criticizes infringements on the part of companies (monopolistic arrangements, the formation of cartels and company pyramids), since these are at the expense of the consumer. He says the astronomical revenues of business tycoons and company managers are unacceptable and considerably contributed to people's indignation. Shtrasler is convinced that when the rescheduled new elections to the Knesset are held in January 2013, not only security issues (Iran and the Middle East conflict) but also social and economic policy positions will determine the outcome of the elections.

Dr. Ralf Hexel, Head FES Office, Israel

Herzliya, 12 November 2012

The Israeli Social Protests and the Economy

by Joseph Zeira

1. Introduction

The summer of 2011 saw an eruption of a vast protest movement in Israel. It began with few small protests on price increases of dairy products. Then a young woman, by the name of Daphni Leef, started a facebook group around the issue of high rental rates in Tel-Aviv, which hurt mainly young people. On July 14th 2011 she built a tent in Rothshild Boulevard, in the center of the city and close to the country's financial center. From then on the protest spread fast. Within a few days there were hundreds of tents in the Boulevard, and thousands throughout the country, in almost every town. Within a week they staged a demonstration of close to fifty thousand people. The initial specific slogans on cost of living and housing were soon replaced by wider and much more general slogans like "The People Demand Social Justice," "Here Comes the Welfare State," "The Response to Privatization is Revolution," and "Ties between Capital with Government Are Criminal." There were daily demonstrations on various topics, like education, cost of child care, high prices, land reform and more. At the same time protestors also staged general demonstrations with growing numbers. By the end of July they were already 170 thousands, by August 300 thousands, mainly in Tel-Aviv, a week later almost 100 thousands in the periphery alone, and in September 3rd more than 400 thousand demonstrators throughout the country. What led to this outburst of protest and what made it so large? How did the government react to the protests? Will the protests return after their sharp collapse in 2012?

2. The Economic and Social Roots of the Protests

A brief look at the economic data can be quite revealing about the sources of the protests. In the twenty years that preceded it, from the early 1990s to the present, the Israeli economy and society went through huge changes. Inequality increased significantly, real wages were stagnant despite the high economic growth, and the public services supplied by the government have being reduced drastically. These developments made life for the lower and middle classes much harder, and especially for the young, who were the main to feel the brunt of these developments. We next turn to a detailed description of this process. Diagram 1 presents the inequality in Israel and in some countries (from the data set of Picketty and Saez) in 1970 and Diagram 2 presents the inequality measures for 2010. Inequality in these diagrams is measured by the share of income earned by the top 1% of the population. In 1970 Israel has been among the more equal countries and the share of income of its top percentile was 7%. In 2010 this top percent was earning 16% of total income and Israel is now at the top of the unequal countries, third only to the US and to Argentine. This reveals a sharp rise in inequality, both relative to the past and relative to other countries.

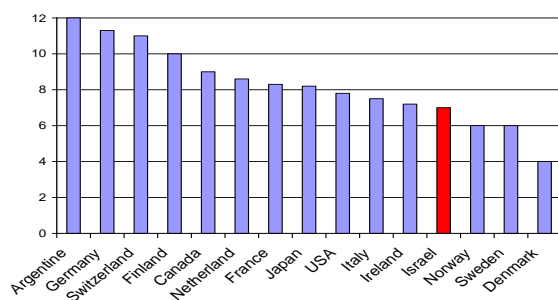


Diagram 1: Inequality in 1970

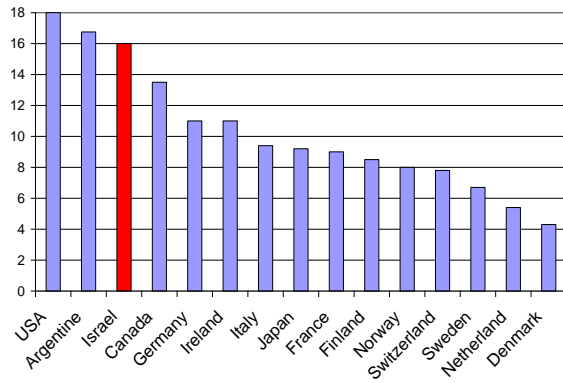


Diagram 2: Inequality in 2010

There are many reasons why inequality in Israel increased so much, and we will discuss some of these below, but one of the main reasons lies in the labor market, where wages did not fully catch up with the growing output. This has been especially true since the end of the 1990s. The economy grew since then at a high rate, more than 13% of real GDP per worker and even more in the private sector. Despite this high rate of growth the real wage has stagnated during this period. This is shown in Diagram 3, which describes the output per worker in the private sector by the blue line and the real wage in that sector by the red line. Clearly output per worker grew by more than 20% since 1999 while wages remained at approximately the same level.

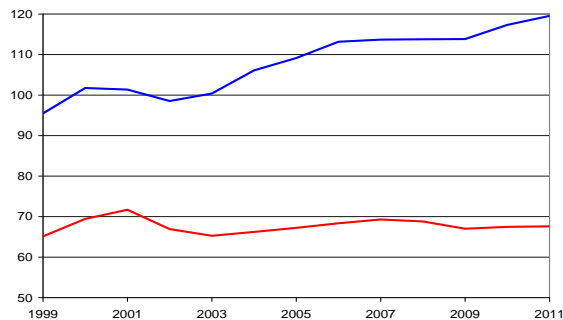


Diagram 3: Real Output per Worker and Real Wages in the Private Sector

This finding is very surprising. It shows that in the last decade economic growth did not benefit workers at all in Israel and it stayed mainly at the hands of the very rich. The stagnation of real wages also stands in sharp contrast with the prediction of economic theory. How can it be explained? There are a number of possible explanations. First the wide wave of privatization of public services (outsourcing) has shifted many jobs from the public sector to manpower companies, who pay much less. Second, the government allowed more foreigners to come and work, mainly in construction and agriculture. That also pushes wages down. Third, minimum wage is not seriously enforced and many workers get lower wages. Fourth, the government is restricting in many ways the ability of workers to unionize, which further reduces their ability to protect their wages.

But the middle and the lower classes suffered not only from stagnating income, but also from an erosion of the services they used to receive from the state, mainly education, health, housing and welfare. If we measure the expenditures on these services as percentages of GDP, as is common, we find that since the mid 1990s these expenditures declined significantly. Public expenditures on education went down from 8% of GDP to 7% of GDP in 2010, and that during a rise in the demand for education, implied by the introduction of colleges to Israel. The public contribution to health, in addition to what is paid by the health tax, went down from 3.8% of GDP to 2.6%. And the public support to housing, mostly of poor and young Israelis, went down most drastically, from 1.5% of GDP to 0.5% of GDP. No wonder the initial protest was on housing. The government has not built new public housing for a long time. The welfare expenditures were reduced drastically as well, especially after 2003. Child allowances, Old Age allowances, Pension Funds support, unemployment insurance and more, were all cut significantly. This also worried the young, fearing

the possibility that they might have to support their parents at old age by much more than they expected earlier.

What caused this erosion of public services? Diagram 4 shows that this trend was a pure ideological decision and was not a result of any economic need, as stated by many politicians. Diagram 4 describes the history of the Israeli fiscal policy since 1960. The blue line represents public expenditures (of all the public sector) as a share of GDP. The black line represents public income, mainly taxes, and the red line is the difference between the two, namely the surplus or the deficit (if negative). The diagram reveals an extraordinary fiscal history. Since 1967 expenditures increased immensely and reached a level of 75% of GDP. This rise was triggered by the rise in defense costs, due to the intensification of the Israeli-Arab conflict. Public income increased as well, but by less, and hence the deficit increased to an average of 15% of GDP during that period. The resulting high debt increased interest payments and that further increased public expenditures. In 1985 the economy was stabilized. Public expenditures went down during the late 1980s and the crucial reduction was that of defense costs. Hence, the major event that enabled the stabilization was the Peace Agreement with Egypt, finalized in the early 1980s, which eliminated the risk of large conventional wars.

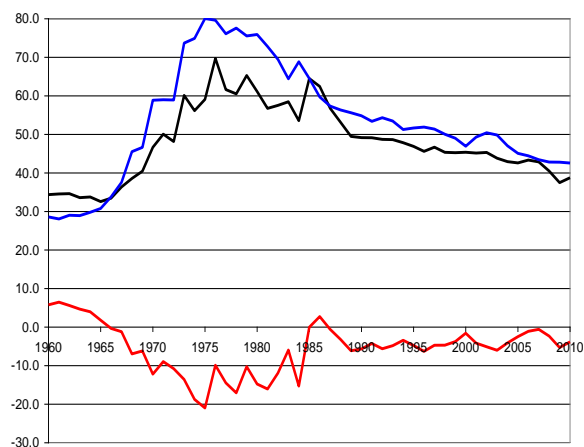


Diagram 4: Fiscal Policy in Israel: 1960-2010

After the stabilization, public expenditures reached a level of 52% of GDP in the early 1990s, which is common in Western Europe and the deficit became quite small. But the government kept reducing its expenditures, which reached 42% of GDP at 2010. Such a reduction was not required for fiscal consolidation, as the deficit was quite low since the early 1990s. Actually during this whole period public income was falling as well. This means that the reduction of expenditures was used not to reduce the deficit, but to reduce taxes. The taxes reduced were mainly direct taxes and they benefited mainly people with high incomes.¹ Hence, the erosion of public services was a result of a concerted effort by all the governments since the 1990s to privatize the economy and reduce the involvement of government.

The reason why this decline in public expenditures since the 1990s is so important becomes clear when we examine Diagram 5. This diagram presents an international comparison, which shows how public expenditures affect inequality. The diagram presents the OECD countries in the mid 2000s. On the horizontal axis I plot public expenditures as share of GDP. On the vertical axis I plot the GINI coefficient of the country, which is a measure of inequality, which goes from 0 in case of full equality, to 1 in case of full inequality (one person has all the income in the country). The diagram clearly shows that there is a strong and statistically significant negative relation between public expenditures and inequality. A reduction of 10% of public expenditures relative to GDP, as done in Israel since mid 1990s, raises the GINI coefficient by 5 points, which is very high and is actually most of the rise in inequality in Israel during these years.

¹ Half of wage earners in Israel are below the tax floor, so they don't pay income tax at all. Hence all reductions of income tax did not benefit them at all. Actually they benefited people with higher income, and also firm owners, as corporate tax was reduced as well.

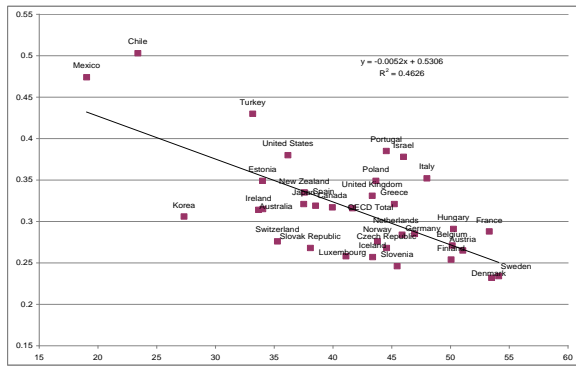


Diagram 5: Public Expenditures (% of GDP) and GINI in OECD Countries

It is important to add here that these economic and social changes created such an outcry in Israel not only because they hurt most of the population, and not only because most Israelis prefer a more equality and more solidarity, but also because people felt that the change was not publicly discussed and kind of sneaked in behind their backs. There are two main reasons for this feeling. One is that most of public attention in Israel during these years was given to Israeli-Palestinian issues and almost none to economic and social issues. The second reason is that the leading parties in Israel, Likud, Labor and Kadima, all shared the same socio-economic views and they led very similar policies when in power. Hence, the anger was not only at the change itself, but at the undemocratic way it was implemented, with almost no public debate.

3. The Reaction of the Government

The government was very surprised by the protests. The protesters called for a deep and radical change in the economic doctrine that was in power for a long time. And the increasing number of the protesters meant that they could no longer be ignored. Initially the government tried to divide and rule by appealing separately to the student unions, who joined the protest early on, or by talking about giving priorities once to the low income class and once to the middle class. Such maneuvers did not seem to stop the flood. Then

the government resorted to another solution, which is to appoint a committee of experts, which will recommend a set of policies to deal with the protesters' demands. As head the committee the Prime Minister nominated Professor Manuel Trajtenberg, the chair of the Planning and Budgeting Committee of the Council for Higher Education, which is a governmental public institution. Like Trajtenberg, most of the committee members were from the government, from the Finance Ministry, the Bank of Israel, the National Insurance Institute (Social Security), the Prime Minister Office and more. The committee deliberated for a month and then came with a set of recommendations.

It is important to understand that appointing a committee of experts, mainly from the public sector, limited the committee significantly from the very beginning. Experts cannot offer large changes in policy. They can suggest at most improvements within the current policy framework. It is important to understand that the government could have appointed a public committee, like the Katz committee in the mid 1970s, following the protests of the Israeli Black Panthers. That public committee indeed recommended significant changes in the Israeli welfare system. By appointing a committee of experts and not a public committee, the government indicated that it does not intend to change its policies significantly. This became especially clear when the committee declared that it will fully adhere to the fiscal "Expenditure Rule." This fiscal rule, which has operated since 2003, specifies by how much the public expenditure can increase every year. Although the rule went through some changes over time, it always implied that public expenditures should rise by less than GDP. In other words, this rule was a major tool in the ongoing reduction of public expenditures relative to GDP. By adhering to this rule the Trajtenberg committee basically agreed not to change economic policy significantly.

Indeed, the recommendations of the Trajtenberg committee follow the “Expenditure Rule” by the word. They call for some increase of public services, mainly extending public education from age 4 to age 3, but call for cuts in the defense budget in order to finance these additional costs. The report also calls for a change in the mix of taxation, namely some minor increases in income tax on high income, a one percent increase in corporate tax and some increase in capital income taxation. But the return from these increases in taxation should be directed to reduce tariffs on various imported goods, mainly food, in order to reduce the cost of living. The report therefore sharply separates between changes in public expenditures and changes in public income, due to the expenditure rule. As a result, the changes in public expenditures were quite small, being limited by the reduction of defense costs. Actually the most radical proposal of the committee was to stop the future plan of tax reduction by the government. This plan was issued by the Prime Minister, but for many years it raised objections by the Ministry of Finance and the Bank of Israel, who were worried that it might be fiscally unsustainable. The Trajtenberg committee seemed like a good opportunity to stop this tax reduction plan. The Trajtenberg committee also advocated various micro measures to spur investment in housing in various regions in the country, but did not offer a significant increase of housing budget.

At the end the government did not reduce defense costs and it even increased them. The only addition to public services was the extension of public education to age 3, which has not been fully implemented yet.² The income tax was raised but the tariffs were not reduced, because since then the economic situation worsened and the government needs these taxes to reduce its increasing deficit. After more than a year it

² This extension passed as a law already in 1983. Its implementation was delayed since then by the Ministry of Finance, in its annual “Law of Arrangements.”

seems that the impact of the Trajtenberg committee has been quite small.

4. The Proposals of the Protest Experts

A few days after the declaration of the government on the nomination of the Trajtenberg committee some of the leaders of the protest movement met with a large group of people, who were mainly university professors, from many areas of expertise, most of them known to be on the left side of the political spectrum. A few days after that meeting the expert teams started to work on their reports. The teams covered many areas: economic, education, housing, employment, welfare, law, and more. The teams worked in a very different way than the Trajtenberg committee. Their mandate was much wider. It was to suggest how to retreat from the ruling Neo-Liberal policies and how to begin to implement a welfare state in Israel. I headed the economic team and what follows reflects mostly its proposals.³ One of the main goals of the economic team was to show that a change in the economic and social policies is feasible, that it will not hurt the economy, will not jeopardize economic stability and not lower the rate of economic growth, as many critiques of the protest movement claimed.

Our economic proposals were in four main areas: budget or fiscal policy, the labor market, competition in product markets to lower cost of living, and democratization of the socio-economic debate. All proposals dealt mainly with the next three years and aimed at showing how the socio-economic policies can begin to change. We therefore called our report: “Change of Direction.” I list below our main recommendations.

³ The members of the economic team were both university professors and practicing economists: Lea Ahdut, Meir Amir, Arie Arnon, Petachia Bar-Shavit, Tamar Ben-Yoseph, Matan Gilat, Sharon Haddad, Roy Mimran, Arik Sherman, Boaz Sofer, Avia Spivak, Joseph Zeira and Anna Zapesochini.

1. We suggested that within three years public expenditures should increase by 2.5% of GDP. This amounts to 20 billion NIS in prices of 2010. This is clearly less than the total reduction of public expenditures in the recent decades, but we wanted to introduce the change moderately. The way these 20 billion NIS were divided between education, health, housing and welfare reflected the recommendations of the other teams. These additional expenditures should be financed by raising direct taxes, mainly on high incomes. The tax changes were raising the marginal income tax on income above 10 thousand dollars a month, raising the capital income tax from 20% to 30%, raising the corporate tax from 24% to 31%, and eliminating various loop-holes in this tax. According to our calculations these changes should raise public income by 20 billion NIS, so that all expenditures will be tax-financed. We also suggested a onetime investment in public housing that will be financed by debt. Such an investment, conducted within three years, could raise public debt by 2% only, which is not problematic being issued only once. The team insisted on tax finance not only due to commitment to fiscal stability, but also because we believe that additional public services can be sustainable in the long-run only if they are tax financed, which reflects a public commitment to finance them.

2. The team has viewed the labor market as a major source of the widening gaps in the Israeli society, especially the stagnation of wages in the recent decade, as explained above. Hence, we proposed a labor market reform, with the following main elements:

- a. Reverse the shift to manpower companies in the public sector and return to direct employment.
- b. Enforce minimum wage by recruiting more supervisors.
- c. Index minimum wages to the average labor productivity.
- d. Expand rights of labor unions.

e. Equate labor rights of foreign workers with those of domestic workers, and reduce imports of labor.

f. Remove labor market barriers faced by Israeli Arabs, mainly due to discrimination, and mainly in the public sector. g. Remove labor market barriers faced by Ultra-Orthodox Jews, mainly due to the need to stay many years in a Yeshiva in order to avoid military service.

3. Reducing the cost of living has been a major issue in the media discussion of the protest movement. Although we strongly believed that the level of wages was more important we proposed some measures that could reduce prices, especially in markets with monopoly power. We suggested to expand the use of price controls to more markets and to create public non-profit enterprises in some areas in order to increase competition and lower prices.

4. One of the main sources of public anger was that policies changed without a serious public debate, and this change was presented as an economic necessity, required by the experts, and not as a political choice. Hence, we strongly believe that the decision on economic policy should be returned to the public. We suggest two first moves in this direction. The first is to cancel the "Expenditure Rule." By dictating a-priori what the size of public expenditure will be it blocks any serious public discussion on this important socio-economic variable. The second move is to cancel the "Law of Arrangements." This law accompanies the annual budget and it involves hundred of various structural changes, mostly privatizations. It is not thoroughly discussed in the Knesset and all the package is voted as a single law. This has been one of the main tools in the privatization of public services in Israel over the last two decades.

In addition to these proposals the report of the economic team discussed thoroughly the effect of the public sector on the economy. Many critics of the protest movement claimed that a welfare state requires high taxation and that reduces

economic efficiency and might hurt economic growth. We presented an opposite economic view. Even if higher taxes reduce efficiency this is only part of what happens in the economy. When taxes are directed to increase public services they reduce some market failures in the areas of education, health, housing and welfare. As a result, the overall effect of the welfare state on output is not clear and seems to be insignificant. And indeed, our report shows that this is also the case empirically. The experience of the OECD countries shows that despite the various social policy and great diversity in size of public involvement across these countries, they are quite similar in the levels and rates of growth of output. Furthermore, the Israeli experience supplies another striking example that the size of public involvement does not have a significant effect on output. Since 1973 Israel GDP per capita has grown at a rather stable rate of 1.8% annually. During this period the share of public expenditures in GDP was close 80% in the first years and then went down all the way to 42%. This reduction did not affect the trend of economic growth at all. Hence, the decision on the size of public expenditures and on public services is not a technical economic issue but a political decision. It should reflect the public preferences on inequality, as demonstrated in Diagram 5.

5. What Lies Ahead?

In the last three decades the world experiences a retreat from the welfare state that was built during the 20th century and especially after WWII. This retreat has many reasons, among them the oil shocks of the 1970s, the collapse of the Soviet Union, the expansion of suburbs, and more. This process has not been uniform, and it was stronger in the US and UK and much weaker in the Scandinavian countries. The retreat from the welfare state has many social and economic outcomes, which are not yet fully understood today. But it becomes increasingly clear that this Neo-Liberal wave leads to greater dissatisfaction and

deep anger among growing numbers of people around the world. This anger led among many things to a global movement of protests. It first appeared in the Arab countries, and then spread to other areas. In Israel the protest movement was extremely wide, but also very short-lived. A full analysis of the Israeli protest movement, its dynamics and its leadership is clearly beyond the scope of this article, and is also not my area of expertise. But one thing can clearly be said. The background to the protests, the erosion of public services, the rise of inequality, the stagnation of wages, the lack of true public discussion of economic issues, all these have not changed yet. And the deep anger is still there. Hence, a new outbreak of protests is only a matter of time.

Prof. Joseph Zeira is Professor of Economics at the Hebrew University of Jerusalem. He held visiting positions at Harvard and other universities in the U.S. and is one of the most renowned economists in Israel. Joseph Zeira headed the working group on economy in the alternative expert team of the social protest movement.

Where is Che Guevara when you need him? The Social Protest Movement in Israel between Civil Awakening and Political Changes

Summary:

The social protest movement scored several notable achievements in the socio-economic sphere. It did not achieve all its goals, but it did raise public awareness. Suddenly, the secular middle class emerged as a new pressure group that can demand and even achieve its desires. Contrary to the statements of some of the protest leaders, the state has not abandoned its citizens. We do not live in Sodom and Gomorrah, but in a country with a free-market economy. Yet it is also a welfare state that does assist the weak members of society.

by Nehemia Shtrasler

What has the social protest achieved? Nothing. So they set up some tents on Rothschild Boulevard in the summer of 2011, they also had some large public gatherings, even the Trajtenberg Committee. So what? Nothing has moved an inch. Nothing has changed. What was in the past, is what will be in the future. There is no social justice, the state has abandoned its citizens, there is no decrease in the cost of living, even the heavy burden on the middle class has not changed.

We have heard these claims so many times from some of the protest leaders, also from commentators and ordinary citizens, that we have started to believe them — even though it is far from the truth, light years from the truth.

The social protest movement in Israel erupted on July 14, 2011 when Daphne Leef went to Rothschild Boulevard and set up a small tent to protest the outrageous prices of Tel Aviv rentals. From a small tent sprung a tremendous, unprecedented protest movement that shook up the government.

Prime Minister Benjamin Netanyahu was not indifferent to the protest. He feared it because it was directed against his economic policy. He understood that the more the protest would be allowed to grow, the greater effect it would have on the ballot-box. Therefore, Netanyahu tried to intercept it at the very beginning. He assembled the student leadership and made several promises to them regarding housing issues. When that didn't work he established the Trajtenberg Committee, already on August 10, in an attempt to take some wind out of the protest sails.

As opposed to most governmental committees that work slowly and over a protracted time period, the Trajtenberg Committee struggled with the problems while working quickly and efficiently. They submitted recommendations in record-breaking time — by September 26, 2011. These recommendations addressed four main issues: taxation, education, cost of living and housing.

The greatest changeover took place with regards to taxation. Netanyahu really changed his spots when he agreed to raise taxes — something he normally opposes. In fact, Netanyahu is known for his staunch belief in lowering taxes as a way to encourage growth and employment, and he even had a structured plan to continue to lower taxes on companies and individuals. Instead, we received an 180-degree-change: an increase in income tax on the top decile (ten percent) of the population; the imposition of a “rich person's tax” on incomes of over 800,000 a year; a raise of the corporate income tax as well as capital gain tax on the stock market. If people would have told me this would happen a minute before it happened, I would have thought they were pulling my leg.

In order to help young couples “make ends meet,” the government now gives working men with children under the age of 3, two tax credit points for each child. This improves the net income of young working couples — who were the heart of the protest.

In the field of education it was decided to provide free compulsory education from the age of 3, and study frameworks in the afternoon hours for children aged 3-9 who live in the periphery. Here, too, we see an improvement in the circumstances of families with young children who, as aforesaid, were the heart of the protest.

The committee's third issue was the cost of living, a painful, intractable problem. The problem of high prices exploded back in January 2011 when scores of demonstrators (in effect, drivers) demonstrated on the roads against the rise in the price of fuel. There, too, an achievement was scored, showing that the government does listen: a rise in the excise tax on fuel was cancelled, and afterwards the marketing profit-margin of the gas stations was lowered.

Later on, the cottage cheese protest erupted (in June 2011) over the exorbitant cost of cottage cheese and other food prices that are, indeed, relatively higher in Israel than in Europe and the United States. Here, too, some success was achieved when Tnuva, followed by Strauss and Tara, were forced to lower their prices on cottage cheese and other products. These were two "promos" that presaged the social protest storm that erupted on July 14 — symbolically, the anniversary of the French revolution.

The protest movement had some success regarding lowering the cost of living. The Trajtenberg Committee recommended the lowering of import duties in order to increase competition and reduce prices, and the Finance Ministry began the process. Import duties on industrial products and textiles are to be gradually lowered over 5 years, until there will be zero taxes on these products in January 2017.

However, the situation is much more complicated with regards to the food industry. The import duties on fresh food products such as beef, chicken and fish were only slightly lowered, so that even

after the reduction it was not worthwhile to import them to Israel.

The import duties on hard cheeses were reduced, but not the taxes on milk, soft cheeses, cream and butter. The duties on edible oil and cans of tuna were planned to be lowered somewhat, but governmental orders regarding them were not implemented because the government caved in to the pressures of the agricultural and food manufacturer lobbies.

There is a structured plan for the gradual lowering of duties on processed foods — such as juices, frankfurters, jams and spices — but the reduction is only partial and will extend over 3 years. Furthermore, trade barriers that prevent competition from imports have not yet been removed. Some examples of these barriers include trade levies, the control held by the Office of Standards and Regulations over the regulatory process, and the bureaucratic regulation of the Ministry of Health and the Ministry of Agriculture.

The bottom-line results are clear: protective tariffs on food products and trade barriers are still too high. Thus, there are almost no competitive imports of food products. Therefore, the prices of food products did not drop; instead, they remain too high. Yet it should be noted that without the social protest and without the Trajtenberg Committee, even the little that was accomplished, would have never come to pass.

The ultra-Orthodox won the housing jackpot

Regarding housing, the protesters have not scored any achievements. The ones who hit the jackpot were the ultra-Orthodox, who did not at all participate in the protest. Minister of Construction and Housing Ariel Attias (Shas) managed to distort the Trajtenberg Committee recommendations by invalidating the eligibility regulation of "utilizing one's full earning power." Instead, he replaced it with the strange criteria of "seniority in years of marriage," thus favoring ultra-Orthodox couples who marry at an early age. The result is

that the ultra-Orthodox continue to receive most of the subsidized apartments; this is now happening, for example, on the new community Harish.

It should also be noted that the Israel Land Administration (ILA) has not inundated the country with land for building, and the reform to expedite the process of licensing and construction has not been carried out. Thus the prices for apartments for members of the hard-working secular middle class that pay taxes and serve in the IDF — have not dropped at all. This subject continues to burn below the surface.

Change in the parallelogram of forces

But this is not the whole story. The most important gain of the protest was a shift in public awareness. Suddenly, the middle class realized that it could stop being the sacrificial lamb led to slaughter with its eyes closed, without even having the right to protest. Suddenly it became clear that the middle class has a great deal of power -- as soon as it unites, protests, and demonstrates. It is a fact that the country's alarmed leadership listened, even changed things. Suddenly, citizens are not content with their "day of the voter" every four years, but want, and can, wield their influence even during a term of office.

The protest attained more social justice for members of the secular-middle class, and even changed the deployment of political forces.

Until the social protest, the political agenda had been determined by the "usual" pressure groups: the ultra-Orthodox, the settlers, the agriculturists, the large employee committees, the Histadrut and the industrialists. They would make their appearances in the Knesset and the media to receive budgetary allocations. They were the privileged ones.

After the protest, a shift took place in the political parallelogram of forces. Suddenly, the middle class became a new pressure group that Knesset members must take into account when they

make legislative changes, so as not to get beaten up by the secular middle class on the voter's day of judgement. This is a revolutionary political change. While the essence of politics is a two-pronged struggle over the taxation system and the distribution of budgets, the protest movement led to greater power in the hands of the public at the expense of "Jerusalem." In other words: from now on, decisions are not only made in Jerusalem, the government and the Knesset. From now on there is a new player in the field, a player that must be taken into consideration: the secular middle class.

This significant change that affects all acts of the government is evident in the recommendations of the "centralization committee" to act against the great conglomerates and commercial pyramids. The change was also evident in the struggle for the rights of contractor workers, who succeeded in improving their wages and terms of employment. Finally, the large demonstrations for "sharing the burden equally" — in other words, drafting ultra-Orthodox men to the IDF, or at least to national service — are also offshoots of the social-protest movement. Now, the government can no longer afford to sweep this issue under the rug.

We are neither Switzerland nor Sweden

But if so many improvements were implemented, how is that so many people, including some of the protest leaders, continue to say "nothing was achieved"? Where does this great disappointment stem from?

It stems from the fact that some of the protestors did not just want to make a few improvements. Instead, they wanted to change our entire socio-economic system from the very foundation. They wanted Che Guevara to rise from his grave to carry out a neo-socialist revolution that would eliminate today's neo-liberal system, as they derisively call our current socio-economic system. But Netanyahu does not believe in neo-socialism and Manuel Trajtenberg is not interested in as-

suming the mantle of Che Guevara, even though he is of South American extraction.

Trajtenberg believes in the market economy, competition, unrestricted imports, and privatization. Simultaneously, however, he strongly feels that changes and adjustments must be introduced to the existing system in order to narrow the gaps between rich and poor, and to improve the circumstances of citizens who work hard to earn their livelihood — but still cannot make ends meet.

The revolutionary sector of the protest-movement wanted the current regime to fall and be replaced by a neo-socialist regime that would nationalize everything that had been privatized, would block imports, take action against the wealthy sector and transfer all the power to the government that knows better than its citizens what to do with the money (so they think). These protestors long for the economic system that has long since gone bankrupt in Eastern Europe. Today, only a few “happy” and “wealthy” socialist countries still exist, with amazing standards of living — such as Venezuela, Cuba and North Korea.

They believe that the state knows how to best manage the economy, therefore they oppose privatization. They do not understand that a state does not know how to run businesses and, therefore, it is best to leave management to the private sector. The state should content itself with drafting regulatory rules and effectively supervising their enforcement. Protest leaders want to increase the proportion of the state in the national product, and decrease the private sector’s percentage — even though this is a proven recipe for poverty and unemployment. They want the state budget to be much bigger than it is now, and impose more taxes on the public to finance it.

There are even those among the protest leaders who have no compunctions about pushing for an increase in spending without raising taxes, in

other words — increasing the deficit as much as they please. They are not moved by the collective plights of European countries that increased their expenses and deficits and are now in deep trouble, facing acute crises. These include Greece, Spain, France, Italy, Portugal and Ireland. Yes, they want to increase all the budgets, except for that of the defense budget. They want the state to spend more on education, housing, transportation, health, welfare and employment — without understanding that that would lead to collapse, as in Greece.

In order to exemplify a very small portion of the demands, I will cite here several clauses (out of dozens) of things that they feel the State ought to do: provide affordable public housing to all those who cannot afford to buy an apartment on the open market; subsidize mortgages; give them state guarantees; provide free education to each citizen from the moment of birth; lower the number of children in the classroom to 21 (the accepted number in Europe); increase the police and fire-fighting forces; lengthen maternity leave to half a year; increase the number of vacation days a year by law. In short, a true cornucopia of benefits, subsidies and allowances -- a la Greece. That is wonderful. I also want all those goodies, but I understand that it is an impossible dream for a country as small as ours, a country groaning under the burden of large problems.

Israel has major defense problems that no European country shares. We have old debts for which we pay a rate of interest twice as high as paid by OECD countries. We have very large populations that almost do not work: ultra-Orthodox men and Arab women. We provide tax benefits to those willing to invest in the periphery. Therefore it will take a very long time until we become like Switzerland or Sweden, and until we’ll be able to give our citizens what they have. Our standard of living ranks only 22nd place in the world, after most of the countries from Western

Europe. That may be disappointing, but it is the truth.

They continue to take us for a ride

The Israeli public doesn't like being swindled. They don't like being taken for suckers, therefore there is still much anger over several problems that the social protest did not solve and that continue to remain at the top of the socio-economic agenda list. Let's take, for example, the great tycoons who borrowed billions of shekels from the public via the pension funds, and used the money to acquire large companies. They built magnificent pyramids from these companies and, due to their great power, they managed to extract top prices from the public, and the profits flowed. But then circumstances changed: the world economic crisis appeared, and they were in trouble. In this situation, instead of paying back their debts to the last shekel, they "gave their debts a haircut" (a partial default on bond debt) so that the public and the banks received only a portion of their money.

A debt settlement such as this can happen because people can make mistakes in business and fail. But it is inconceivable, on the one hand, to take the large sums of money borrowed from the public and gamble it on dangerous investments, then milk the company for exorbitant dividends, conduct transactions with interested parties -- and continue to live an ostentatious lifestyle even after the concern can no longer return its debts. No-one should be allowed to build tremendous private homes, fly in private planes and celebrate at grandiose weddings — *before paying back their debts*. The two cannot go together. This reality turns us all into total suckers. It is also the exact opposite of a free market, in which a large number of companies compete for the pocket of the consumer. An open economy is opposed to pyramids, tycoons, cartels, monopolies. It fights all those who are connected to the governmental pipeline and enjoy excessive trade

protectionism that prevents free, fair competition. There is nothing more infuriating than the fantastic salaries withdrawn by controlling shareholders and high-level directors in those giant companies. In the "good" years they withdrew salaries of four, five and even six million shekel a year. But when it became clear that they failed, and the "bad" years come with their losses, they do not return even one shekel to the kitty. This is an infuriating ruse at the expense of the public stockholders. And it is also the opposite of a free market economy.

But it is not only the tycoons and high-level managers who have made a fool of us. The large employee committees that control the governmental monopolies, also milk us mercilessly. They, too, have turned us into complete suckers.

I am referring to the following entities: the Israel Electric Corporation; the Ashdod and Haifa ports; the air fields authority; the large banks; the defense industries; and the Israel Railway. These are all marked by inefficiency, surplus of manpower, inflated salaries, and total job tenure and job security. As a result, the public is forced to pay higher taxes and higher prices for all the products. They are no less problematic than the tycoons.

The protest failed on this point: it did not rise against the great employee committees or against the Histadrut that supports them. The protest people did not want to understand that these employee committees are part of the "privileged" group. They are part of those who receive too much, at the expense of the secular-middle class. Even the problem of contractor workers stems from the employee committees. As soon as it becomes impossible to fire a worker in the Ashdod port, in the Israel Electric Corporation or a governmental ministry, the employer has no choice but to import a contractor worker — because anyone else he brings into the company will never leave it, even if it become clear that he is totally unsuitable for the position.

The protest also failed with regards to the ultra-Orthodox population. It did not condemn the situation in which ultra-Orthodox males spend their time in Torah schools, and do not work. It did not raise a hue and cry against the billions they receive in the form of a strange assortment of government allowances and apartments for sharply discounted rates. Meanwhile, secular young couples cannot even afford to rent apartments.

The social protest movement wanted to include everyone in its bear-hug, including the ultra-Orthodox and settlers who receive giant budgets. It wanted to be loved by everyone, thus it kept its mouth shut regarding these two privileged groups. It also said nothing about the peace process that doesn't exist, something that necessitates ever-increasing additions to the defense budget. They did not understand that it is impossible to be nice to everyone. The sources of funding are limited and there is a fight over every shekel. If someone receives more, that means that the secular-middle class that carries the burden, receives less. Elementary, my dear Watson.

The protest also didn't say a word against the blatant tax discrimination in favor of the large export companies such as Teva, Yishkar, Israel Chemicals, Intel and Check Point. They enjoy ridiculously low corporate income tax rates of only 6%-12%, while the government raises taxes on the entire public.

Have we become like Sodom and Gomorrah?

One of the harshest criticisms of the social-protest people is that our economy is ruled by a cruel, dog-eat-dog capitalistic system that makes the rich richer, and the poor — poorer. It is not a welfare state, it lacks social justice, and the state has abandoned its citizens — so they say. Is our situation so severe? Do we really live in Sodom and Gomorrah?

In our search for an answer, let us examine the major instrument through which socio-economic

policy is conducted — the state budget. The budget in 2012 was 366 billion shekels.⁴ If we deduct from this sum the debt payments, we are left with 285 billion: this is the sum available to the government, to finance its expenses. This is a great deal of money; if we add the budgets of the local authorities and the health funds (that is the definition of the expenditures of the broad government) we reach 390 billion shekel, constituting 43% of the GNP (gross national product). This is a very respectable chunk of money. While there are countries that spend more than that — such as France, Sweden and Denmark — there are also countries that spend much less than that, such as Switzerland, Australia and South Korea.

Contrary to quotes from several protest leaders, the state budget has grown at a very rapid pace in recent years. In 2011 it rose by 2.7% in real terms, in 2012 it rose again by 2.7%, and in 2013 — by 3.0% in real terms. This constitutes nominal increases of 15, 13, and 20 billion shekels respectively — enormous sums. Thus our problem is not the magnitude of public spending, and not even its rate of growth. The problem is the inefficiency of the public sector that provides low-quality services to the public. In addition, the fact is that not the entire 43% of the GNP goes to social services, welfare, education and infrastructure budgets.

We have a giant defense budget (60.5 billion shekel) that constitutes about 6% of the Gross National Product, and we also have weighty past debts forcing us to pay high interest rates; this comes to about 4% of the GNP (38.6 billion shekel). In other words: only 33% of the GNP remains to fund social services, welfare, education and infrastructure expenses. And that is rather low. Therefore, when we compare our social welfare budget to those of European countries, we come out short. After all, they are richer than

⁴ One shekel is approximately equivalent to 0.25 dollars.

us with higher GNPs and they don't have a weighty defense millstone around their necks and no heavy interest payments to make. So why are we surprised that they are able to invest more than we are in: students, senior citizens, disabled and unemployed persons?

Nevertheless, it is not true that we lack a social welfare net. We do have one, and it is quite comprehensive. The state, despite its limitations and difficulties, spends huge sums on social services. It spends 36.3 billion shekel a year on education, transfers 7.5 billion to the universities, and provides free, state-sponsored education from age 3 through high school. We have few elitist private schools. The universities are public and tuition is low. Tuition is subsidized by about 80% of its real cost, so that anyone who wants [and qualifies] can acquire an academic education.

There have also been improvements in direct aid to society's weaker elements. The National Insurance Institute distributes allowances to senior citizens, widows, widowers and orphans, mothers and children. It also pays allowances toward nursing care, disability payments, work injuries, unemployment payments, and income support. There are few nations in the world that have such a developed social welfare system as Israel.

We also have one of the leading health systems in the world that provides good medical care to the entire population, whether or not you have paid your health tax and no matter how many children you have. Hundreds of thousands of citizens are privileged to receive advanced medical care, even though they pay only token fees. Numerous delegations from countries much richer than Israel come here to study our egalitarian health system. So perhaps the state has not abandoned its citizens, after all?

Progressive funding

Where does the money come from, to cover the budgetary expenses of 285 billion shekels? Mainly from taxes. Therefore it is important to

check whether Israel's tax system is progressive. It turns out that it is. Israel's income tax is the most progressive in the Western world. The five lowest deciles provide 3% of the total revenue, the three middle deciles provide 15%, and the two top deciles — that is, the richest families — provide 82% of the income-tax revenue. Even if we add to the pot the indirect taxes headed by VAT, the overall picture of revenue from taxes remains very progressive. To make it absolutely clear: The rich underwrite the poor, and that's the way it should be.

So perhaps, when all is said and done, we are not living in Sodom and Gomorrah, but in a country with a free market economy that is also a welfare state?

Election issues are no longer only political-military

At the beginning of October 2012, Prime Minister Benjamin Netanyahu announced that he was bringing the elections forward to January 2013. The social protest was one of the reasons for this. In fact, one can view elections as the "mother of all protests." The nation will have its say at the ballot box, where it will be decided which socio-economic policy is more appropriate for the present time. Netanyahu did not pass the 2013 budget in the Knesset (he couldn't have passed it, even if he had wanted to do so) — because the budget contains sharp, painful cutbacks in social welfare funding. Therefore Netanyahu preferred to conduct elections earlier, and then pass the painful budget with its unpopular cutbacks that run contrary to the spirit of the protest. In any event, the social protest will have great effect on the content of the election campaign. This is because the protest succeeded in moving the parallelogram of forces between the government and the public, to the benefit of the public.

The voice of the silent majority will be heard this time. The lethargic secular majority has awoken due to the protest and its voice will be heard in

the election campaign on all the socio-economic issues on the public agenda. The wide public now understands that there is a very strong and clear relationship between: the government's budget, taxes and subsidies vis-à-vis the citizens' quality of life and personal bank accounts.

Pioneer Daphne Leef has, meanwhile, established a company for the benefit of the public and sells stocks to the public. Youths and adults in their work-places are organizing themselves in the Histadrut and establishing employee committees. Itzik Shmuli, student leader who took an active part in the protest, is creating a "social settlement" in Lod. And Knesset members are much more sensitive these days to social-welfare demands coming from the public, both with regards to pricing as well as to workers' rights.

However, the change in the atmosphere has turned the country's wealthy people into scapegoats. Entrepreneurs who do well, have become negative figures and objects of criticism; hatred toward the rich is growing. A negative atmosphere has emerged against successful businessmen and against private ownership. "Privatization" has become a dirty word. All this is likely to dampen the desires of those who want to do business in Israel, thus harming growth and employment — and that is not only bad, it is also dangerous. Instead of hearing about business successes, we read more and more stories about exploitation and oppression of workers. The traditional economists avoid making public appearances and talking to the media; they have been replaced by academic sociologists, political scientists and educators.

Yet it is important to emphasize that the country's socio-economic framework has not changed following the protest. Israel, a country with a free market economy, is also a welfare state. We have not been transformed into a neo-socialistic regime, in which the state determines almost everything. But if the economic regime has not changed, the political map has moved. The Labor

party has strengthened; it gained the most from the social protest. We see this in the rise in the number of mandates given to the Labor party in public opinion polls.

A superficial look at the quantity of demonstrations and protests in 2012 may mislead us into thinking that the social protest movement has weakened, even disappeared. But that is inaccurate. Throughout the past year, Netanyahu succeeded in diverting public attention from internal issues to the Iranian nuclear conundrum. Clearly, when faced with a burning issue like Iran that involves real danger to life, social-justice demonstrations pale in importance. Later on, when it became clear that the elections would be moved up, it became uncomfortable to continue mass protests against the government. A young Likudnik will not demonstrate with a young Laborite against the government on the issue of the housing shortage (for example), when elections are already visible on the horizon. Therefore, the protest was exchanged for the "mother of all protests": elections. The upcoming elections are anticipated to be particularly stormy, with considerable participation of the public and high voter turnout. It has become clear that even politicians in their ivory towers are very sensitive to what the public has to say. The early elections will not only revolve around the political-military issue. The debate will not only deal with the relationship with the United States president, the (non-existent) negotiations with the Palestinians, and the Iranian nuclear issue. This time, socio-economic issues will take up the lion's share of the discourse.

In the upcoming elections, the candidates will not be able to wave only one flag. Each candidate will have to present their political-military roadmap, but also their socio-economic credo as well. These socio-economic issues include social justice, equal sharing of the load, the welfare state, poor versus rich, the size of the budget, level of the deficit, taxation level, duty-free imports, the

market economy, privatization, free competition, growth and unemployment. All these, will be the “hot” topics in the upcoming election campaign.

Nehemia Shtrasler is the senior economics editor at the daily newspaper Haaretz. He advocates a liberal free-market economy and is one of the most influential economic journalists in Israel. Furthermore he can prove successful activity as television commentator and lecturer. Nehemia Shtrasler is the recipient of the National Federation of Israeli Journalists’2012 lifetime achievement award.

Responsible:

*Dr. Ralf Hexel,
Head of the Friedrich-Ebert-Stiftung Israel*

Authors:

*Prof. Joseph Zeira
Nehemia Strassler*

Homepage: www.fes.org.il

Email: fes@fes.org.il