

THE “THIRD WAY” AND THE ISRAELI ECONOMY

By Nick Gier

Jews all over the world just finished celebrating Yom Kippur—the Day of Atonement—and October 6 was the 43rd anniversary of the start of the 1973 Yom Kippur War. Israel is always in the news about uncertain peace talks or military operations, so I would like to take this occasion to write about the nation’s economy.

Israel is yet another example of the success of the Third Way between Communism and unfettered capitalism. According to libertarian, free-market theory, Israel should have failed economically long before the existential threats of the wars of 1967 and 1973.

Most of the Zionists who settled in Palestine were hard-core socialists. From 1948 onwards David Ben-Gurion’s socialist Mapai Party dominated the Knesset, Israel’s parliament. In 1968 Mapai merged with the Labor Party, and “Iron Lady” Golda Meir was Prime Minister during the tragedy the 1972 Munich Olympics. She was also Vice-President of the Socialist International at the time.

Israeli socialists established the most successful communes in human history. We know them as kibbutzim, which have been described as “both hypercollective and hyperdemocratic.” There was initially no private property, no money, no police, no courts, not even private mail. All the children were raised collectively.

Today there are 80,000 Israelis still living in 250 kibbutzim. They produce 12 percent of the nation’s exports, but they comprise only 2 percent of the population. About 15 percent of the members of the Knesset have been kibbutzniks and a large percentage of the army officers were raised communally.

The kibbutzim are famous for their agricultural products, but they have thriving industries as well. The concept of drip irrigation was invented on Kibbutz Hatzenm and its company Netafim now has offices in 110 countries. The Muslim countries Azerbaijan, Kazakhstan, and Uzbekistan have become friendlier to Israel now that they are benefitting from Jewish advances in irrigation. Primarily because of experiments on the kibbutzim, Israel is able to recycle 70 percent of its water, the most of any country in the world.

From 1950-55 Israel’s economy grew at a blistering 13 percent per year and then averaged 10 percent into the 1960s. From 1948-1970 the gross domestic product (GDP) quadrupled while the population tripled. Many countries have pulled themselves up by their bootstraps, but very few have leapfrogged into the industrial world as Israel has done.

In their book *Start-Up Nation: The Story of Israel’s Economic Miracle*, Dan Senor and Saul Singer state that Israel’s early success was “achieved through an entrepreneurial government that dominated a small primitive private sector.” Most free marketeers believe that governments that target certain industries for growth are bound to fail, but most of Israel’s “industrial policies” have been great successes.

At the time most Israelis thought his idea was absurd, but American Jew Al Schwimmer convinced Ben-Gurion and Shimon Peres to put up government funds for what is now Israel

Aerospace Industries. Starting with surplus World War II aircraft smuggled past the British, the company-- still government owned--now employs 16,000 people and produces jet planes, helicopters, and missiles.

In 1973 the economy stalled and remained in the doldrums until 1985. The 1967 war unleashed new economic growth, but the 1973 war did not garner the same results. The doctrinaire socialists, always unfriendly to private enterprise, had gone too far and were up against a wall. As Senor and Singer observe: "Once the government saturated the economy with big infrastructure spending, only the entrepreneurs could be counted on to drive growth."

In 1977 the conservative Likud Party broke 30 years of Labor Party rule, and except for 6 years of Labor governments, Likud has ruled Israel since then. Over time Likud brought the country back to the Middle Way between government control and free enterprise that has characterized the most successful mixed economies of the Third Way.

The economy actually got worse as inflation climbed to over 1000 percent by 1984. Likud Party was eventually able to reduce government expenditures from 77 percent of GDP to 46 percent, comparable to the U.S. at 45 percent, but much lower than France at 61 percent and Sweden and Denmark at 58 percent. Significant for the growth of private enterprise was a dramatic decrease in government-controlled credit from 65 percent to 5 percent.

Raising venture capital has always been a problem for a country perceived as averse to free markets and constantly at war with its neighbors. From 1990-2008 the Israeli Yozma (Hebrew for "initiative") industrial plan focused on technology and it issued grants totaling \$2 billion dollars to lure foreign investors to the country. (A comparable U.S. contribution would have been \$86 billion.) The return has been six fold on government investment. As Senor and Singer state: "Yozma provided the critical missing component that allowed the Israeli tech scene to join the tech boom of the 1990s." The U.S. and Israel (with only 7.6 million people) now lead the world in number of start-up companies. Israeli industries now make up 32 percent (22 percent in manufacturing) of the economy while agriculture stands at just 3 percent.

After the fall of the Soviet Union in 1989, about 800,000 Russian Jews immigrated to Israel over a 10 year period. Many of them were well trained engineers and computer scientists. By jump-starting its high tech sector, Israel was able to produce 500,000 skilled jobs far more quickly than a free labor market would have.

Most people are not aware of the fact that Intel's 8088 processor, which powered the first IBM PCs, and the 386 chip, which was seven times faster, were built by Israeli computer engineers. In 2003 Israeli engineers also invented the Centrino chip which made high speed laptop computing possible. Finally, dual core processors were developed in Intel's Development Center in Haifa.

Even with conservative leadership for last 27 of 33 years, Israel's income taxes are still 46 percent in the highest bracket. There are high budget deficits, even with \$3 billion in U.S. aid every year. Much government money goes to welfare and subsidized housing, mostly for the 22 percent who live below the poverty line. (The U.S. rate just went up to 14.6 percent.) There are, for example, 70,000 Ethiopian Jews (airlifted in 1984, 1991, and 1999) who arrived with very few skills and no knowledge of Hebrew. Unemployment runs as high as 50 percent among these

immigrants and the minority Arab population. Inequality is relatively high (39 on the Gini Scale) compared to the Nordic countries (24 average), but not as high as the U.S. at 45.

Even though Prime Minister Benjamin Netanyahu has pushed GOP-style policies and privatized most major companies, Israel still does not do very well by most international comparisons. With higher taxes and more government spending, Denmark ranks sixth in “ease of doing business” while Israel ranks 29th. On the Economic Freedom Index (www.heritage.org) Denmark sits in 9th place right after the U.S., but Israel is far behind at 44th.

Senor and Singer claim that government owned industries used to do well in Israel because there was very little corruption and everyone worked for the common good. But today, according to the corruption index at NationMaster.com, Israel ranks 28th, while all the Nordic countries and New Zealand, Singapore, Switzerland, Australia, and Austria are in the top ten.

At least health care costs are not a drag on the Israeli economy. By 1958 90 percent of Israelis were covered by government health care. In 1995 the conservative Likud government passed a major health reform law that required basic coverage for every citizen. Universal coverage always brings medical costs down, and Israel’s medical costs are 8.7 percent of GDP in stark contrast to the U.S.’s 17 percent. About 45 percent of hospitals are government owned, and Israel has one of the highest number of doctors per capita—4.6 per 1,000.

Aristotle, Confucius, and the Buddha all agreed that the moral virtues are relative means between extremes, and that the virtues must be fine tuned to adjust for different circumstances. I believe that the virtues of industry and commerce may very well come under the same principle. The Third Way between capitalism and Communism is a delicate balancing act between market forces and necessary government intervention. As opposed to the Nordic countries, Israel appears not yet to have found its proper mean.

Nick Gier taught philosophy at the University of Idaho for 31 years. Read his other columns on the “Third Way” at www.home.roadrunner.com/~nickgier/ThirdWay.htm.