Reichman University

Aaron Institute for Economic Policy

In the name of Aaron Dovrat z"l

The Pyramid of Growth in Israel's Arab society

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This is a short summary, for the full paper (in Hebrew) see
https://www.runi.ac.il/research-institutes/economics/aiep/policy-papers

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Aaron Institute for Economic Policy

Dedicated to the memory of Aaron Dovrat

The vision of the Aaron Institute for Economic Policy in the Tiomkin School of Economics is to support sustainable economic growth and social resilience, along with poverty reduction. To achieve these goals, the institution strives to design a strategy based on measurable goals, which can be subjected to international comparison, and propose detailed plans for economic policies based on the most updated international knowledge. We focus primarily on reforms towards economic growth stemming from increasing employment and raising the GDP per hour worked (labor productivity) in Israel.

The key measure of sustainable economic growth – GDP per capita – is still low in Israel compared to leading developed countries, and so is labor productivity. Through its economic studies, the Aaron Institute presents goals, innovative policy tools, and reforms to promote growth, high-quality employment, and labor productivity.

The Institute's mission is to help shaping the socioeconomic policy in Israel through the development of long-term plans that address the full range of economic and social issues facing the Israeli economy. Our main focus is families with less than median income, who comprise significant parts of the Arab and Haredi (ultra-Orthodox) populations. In these groups specifically, increasing employment and productivity would greatly contribute to achieving the goals of growth, social resilience, and poverty reduction. In addition, our studies aim to influence the professional discourse, and to stimulate discussion based on reliable information and socioeconomic research that offers practical tools to achieve these goals.

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The Center for Economic Policy of the Israeli Arab Population

The Aaron Institute has established The Center for Economic Policy of the Israeli Arab Population with a vision of advancing the manufacturing and business economy in Israeli-Arab population, and enhancing its integration in the Israeli economy. The activity of this center is part of Aaron Institute's comprehensive economic strategy for the Israeli economy, which aims to achieve sustained growth in GDP and labor productivity, along with reduced poverty and inequality. The center’s activity focuses on presenting government decision-makers with recommendations for implementation of long-term economic policies for Israel’s Arab population, and promoting their enactment in practice.

In accordance with the center’s vision, activity revolves around designing strategies and devising policies in the fields of education, employment, and infrastructure, through collaboration with various government offices, and particularly the Ministry of Finance and the Authority for Economic Development of the Minority Sectors. Policy recommendations include proposals for detailed programs which are based on up-to-date data regarding the Arab population in Israel, as well as economic knowledge acquired nationally and internationally, while taking into consideration existing customs and cultural norms in Israel, including political limitations. Research findings and recommendations are presented at public roundtable discussions held in Arab localities, with participants including Arab and Jewish professionals such as researchers, decision-makers, and senior figures from the business and public sectors. Our collaboration with government offices, especially the Ministry of Finance, enables us to enhance the center’s impact and to translate its proposals into government decisions with allocated funds, which engender the implementation of long-term policies in various fields.

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The Pyramid of Growth in Israel's Arab society

The labor income per individual in Israel's Arab society has shown an impressive increase over the last decade (2012-2022), yet it still represents only 44% of the corresponding figure in the non-Haredi Jewish population.[1] This disparity in labor income per individual is an indication of the socio-economic inequality between these two population groups, while also pointing to the currently untapped economic potential of the Arab society within the Israeli economy.

In order to establish a measurement and reference framework which would help identifying the strengths and weaknesses underlying the gaps in labor income per individual, The Center for Economic Policy of The Israeli Arab Society at Aaron Institute developed the Pyramid of Growth in the Arab Society. This pyramid provides a tiered overview of the social and economic components which are necessary for reducing the gaps in the average individual income between Israel's Arab and non-Haredi Jewish societies. Thus, the pyramid incorporates the various dimensions of the gap into an integrative presentation, forming the basis for discussing economic strategy and for prioritizing the areas of intervention and reforms required to promote growth and accelerate the integration of the Arab society in the Israeli economy, bringing it in line with the non-Haredi Jewish society.

Examining the 2022 pyramid reveals gaps between the Arab and non-Haredi Jewish societies across all components. Ongoing gaps are evident in economic metrics such as human capital level, public investment level, employment rate and quality, while the most severe disparities are evident in the social metrics – primarily crime, resilience of local authorities, and social cohesion. Examination of trends over time and comparison of the 2022 growth pyramid to that of 2012 shows significant advancement in components such as investment in human capital, digitization, and public capital, as well as reduction of the gaps in these areas. At the same time, there has been a marked downturn in the social metrics, particularly in regard to crime and social cohesion. This finding underscores the need for ongoing investment, not just in the economic aspects but also in strengthening social components as a precondition for realization of the growth potential.

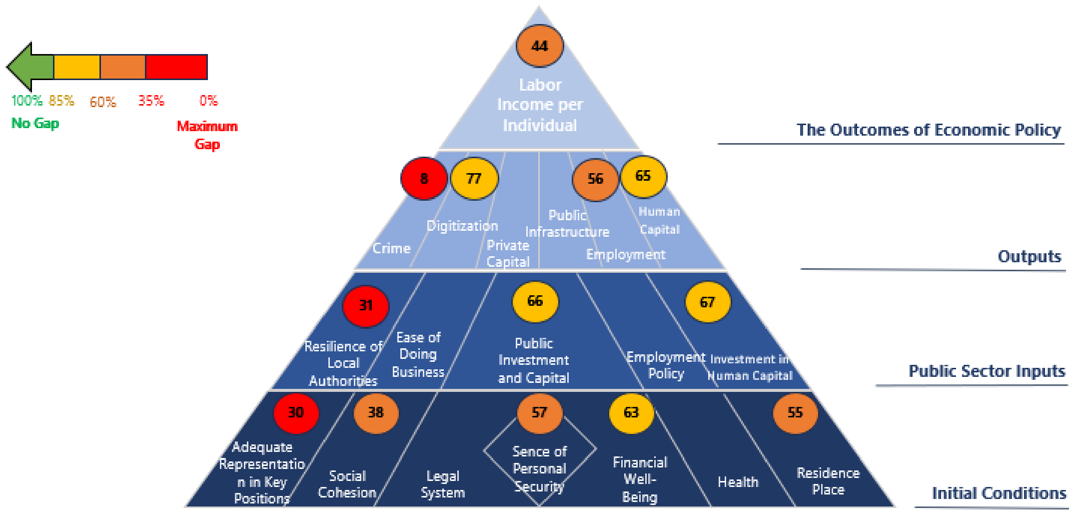
[1] Labor income per individual is the income from work of all men and women of the relevant ages, including zero income for individuals who are not employed or have no labor income.

1. Summary and Conclusions

Over the last decade (2012-2022), Israel's Arab society has been a growth engine of the Israeli economy. During this period, the Arab society has gained an impressive increase in real labor income per individual in the primary working age group (25-64), at a higher rate than that of Israel's Jewish society (Haredi as well as non-Haredi), leading to a narrowing of the gap in labor income per individual between the two population groups. As a result of this narrowing of the gap in labor income per individual, alongside the growing size of the Arab society as a share of the overall Israeli population, the share of the Arab society out of the total labor income at ages 25-64, which serves as an indication of the Arab society's contribution to the GDP, has increased from 8.2% in 2012 to 10.5% in 2022. Along with the contribution to the Israeli economy, to the GDP and to the growth of the economy, an increase in the Arab society's labor income also means an improvement in its standard of living and reduced poverty rates, as well as an increase in government tax revenue and reduced dependence of the Arab population on government subsidies and welfare services. These positive trends in the Arab society have taken place against the backdrop of a government policy that boosted incentives for work and encouraged education, combined with the implementation of the 5-Year Plan for Economic Development of the Arab Society.

However, despite this impressive progress in the last decade, the gap in labor income per individual is still substantial. In 2022, labor income per individual in the Arab society was only around 44% of that of the non-Haredi Jewish society. This gap is an indication of the socio-economic inequality between these two population groups, while also pointing to the currently untapped economic potential of the Arab society within the Israeli economy. In order to accelerate the growth in labor income and reduce gaps, is it necessary not only to assess the scope of the gap but also to establish a systemic framework which would facilitate identification of its underlying causes, an in-depth discussion of the economic strategy of the state of Israel, and pinpointing the areas of intervention and reforms required to promote growth and to reduce the gaps in labor income per individual between the Arab and non-Haredi Jewish societies. For this purpose, The Center for Economic Policy of the Arab Society at Aaron Institute developed the Pyramid of Growth in Arab Society model. This model provides a measurement and reference framework for identifying the strengths and weaknesses underlying the gaps in labor income per individual between the Arab and non-Haredi Jewish societies. The pyramid is presented in figure 1.

Figure 1: The Pyramid of Growth - Arab Society Compared to Non-Haredi Jewish Society, 2022



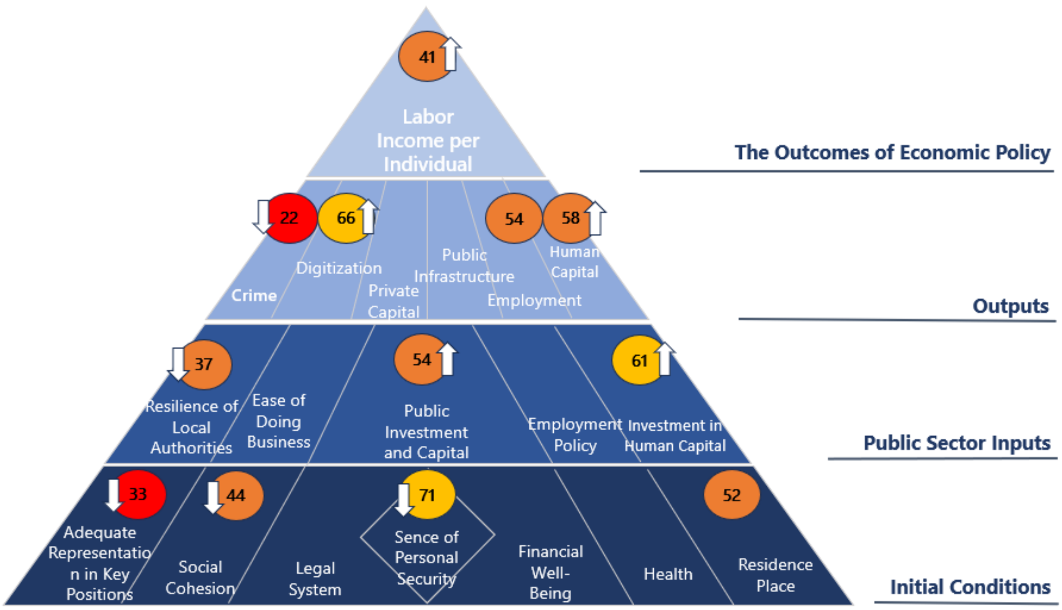
The pyramid comprises four tiers, from its top to the base tier. The top of the pyramid represents labor income per individual, which serves as a primary metric for standard of living and as a basis for comparing the economic condition of the Arab society to that of the non-Haredi Jewish society. The next tier down is that of outputs, reflecting metrics which represent the Arab society's accomplishments in areas such as employment, education, and skills. These components are means to achieving the main goal at the top of the pyramid, which is increasing labor income per individual. The success of the products tier depends on the two tiers below it – the public inputs tier and the initial conditions tier. The public inputs tier represents public sector activity which is imperative to the functioning of the economy, and it rests as previously mentioned on the initial conditions tier which encompasses the basic preconditions essential to the existence of a functioning society and a thriving economy, such as health, security, financial stability, etc.

The pyramid is meant to serve as a conceptual tool for strategic thinking and identification of the sources of the gaps. The uniqueness of this approach lies in its ability to provide an integrative overview of the scale and dimensions of the gap, thus offering a basis for discussing economic strategy and prioritizing the necessary areas of intervention and reforms.

Examining the 2022 pyramid reveals gaps between the Arab and non-Haredi Jewish societies across all metrics. Ongoing gaps are evident in economic metrics such as human capital level, public investment level, and the rate and quality of employment. However, the most severe disparities revolve around the social metrics – primarily crime, resilience of local authorities, and social cohesion. In these metrics, the Arab society is particularly worse off in comparison to the non-Haredi Jewish society.

Comparing the 2012 growth pyramid to that of 2022 (Figure 2) shows significant advancement in components such as investment in human capital, digitization, and public capital, as well as reduction of the gaps in these areas. On the other hand, there has been a marked downturn in the social metrics, particularly in regard to crime and social cohesion. This finding underscores the need for ongoing investment, not just in the economic aspects but also in strengthening social components as a precondition for realization of the growth potential.

Figure 2: The Pyramid of Growth – Arab Society Compared to Non-Haredi Jewish Society, 2012-2022



Based on the economic disparities revealed by the pyramid, we recommend advancing a comprehensive, integrative policy for reducing the gaps between the Arab and non-Haredi Jewish societies, which would focus on three main courses of action: enhancing human capital, improving employment quality, and expanding access to economic opportunities. More specifically, we propose increasing the rate of tertiary and academic education; investing in language proficiency and soft skills; expanding the labor market participation of Arab individuals with low education attainment, particularly women; upgrading employment centers; removing transportation and regional barriers; developing employment hubs in the vicinity of Arab municipalities; and encouraging business entrepreneurship and innovation.

Beyond the economic aspects, the situation calls for a systemic, coordinated response to the severe social challenges, primarily the high crime rates in the Arab society. For this purpose, it is necessary to formulate a dedicated policy for crime prevention which would include strengthening the enforcement apparatus, establishing public trust in the legal authorities, investing in preventative communities and informal education infrastructures, and strengthening the sense of personal safety and social cohesion. Concurrently, existing governmental development plans should continue to be consistently implemented, including investment in infrastructures, housing, transportation, and complementary inputs for human capital.

In conclusion, the last decade has been characterized by a marked improvement in the economic integration of Israel’s Arab society and an increase in its contribution to the national economy. Nevertheless, gaps in labor income per individual have remained substantial, particularly in regard to the basic social metrics. The Pyramid of Growth model provides a systemic framework for identifying strengths and weaknesses, and for formulating a gap reduction strategy, bearing in mind that strengthening both the social and the economic components is an essential condition for realizing the full growth potential of this population group.