

The Challenge of Israeli Economic Growth in 2021

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The rapid vaccination process raises hope for the decline of the coronavirus pandemic in Israel and for an economic recovery. However, preparations for the recovery phase appear to be quite limited. Despite the tenuous political situation, the government, in cooperation with the relevant elements, must accelerate economic preparations for a recovery period in order to bring about rapid growth of GDP, and in particular, to reduce unemployment and its severe social consequences.

Israel is currently battling the coronavirus in two ways: vaccinating the population and managing a third lockdown, whose direct cost to the economy is estimated by the Bank of Israel to be NIS 3-3.5 billion per week. The vaccine process, which has been rapid so far, raises hopes for the eradication of the pandemic over the next few months.

However, it seems that the state's preparations for accelerating economic recovery are quite limited, and even at the outset of 2021, Israel does not have an approved budget and an overall economic plan. While Knesset elections are scheduled for March 2021, it is unclear whether long-term political stability, essential for the efficient management of the economy, will be achieved.

The 2021 budget, in the amount of NIS 419 billion, is a continuation budget (with additions) to the 2020 budget. The budget is subject to the rules of the continuation budget and is not based on an overall vision and planning by all government ministries. According to a report by the Knesset's Finance Committee (December 28, 2020), the budget available for 2021 as part of the "economic plan to deal with the coronavirus crisis" stands at NIS 72.7 billion (a 53.2 increase for 2021 and surplus of 20.4 from 2020). The chairman of the Finance Committee, MK Moshe Gafni, said in the summary of the committee's debate: "The country is in an unprecedented difficult situation economically: a situation in which people are losing their jobs and are hungry for bread, while we are headed to further elections without a [regular] budget – as if we were a third world country."

Despite the severity of the instability of the political system, the most important factor in emerging from the crisis is the vaccination of the population. In addition, the public

sector employs professionals, and the private sector has its own strong forces. Assuming that the pandemic in Israel subsides, a recovery is expected, which should be reflected in at least two main criteria measured by the Central Bureau of Statistics: GDP growth and unemployment rate in the labor force.

According to an estimate by the Bank of Israel from January 4, 2021, Israel's GDP shrank by 3.7 percent in 2020 compared to GDP in 2019. According to an estimate by the Ministry of Finance from January 17, 2021, GDP shrank by 3.3 percent in 2020. These estimates are lower than previous estimates presented by these bodies (the forecast presented by the Bank of Israel in October 2020 was for a drop of GDP in 2020 by 5 to 6.5 percent).

According to the Bank of Israel's forecast from January 4, 2021, in a scenario of rapid vaccination, which is indeed currently underway, GDP will grow by 6.3 percent in 2021 and 5.8 percent in 2022; whereas in the scenario of a slow vaccination, GDP will grow by 3.5 percent in 2021 and by 6 percent in 2022. According to the Ministry of Finance's forecast from January 17, 2021, in the primary scenario, GDP will grow by 4.6 percent in 2021. The alternative, less likely scenario of the Treasury forecast (continued morbidity for most of 2021) is that growth in 2021 will stand at only 1.9 percent.

Unemployment is one of the main parameters that reflect the relationship between the economic situation and the well-being of the population. In 2019, the number of employed persons was 3.967 million and the unemployment rate was 3.8 percent, a goal that Israel should strive to reach within a period of two to three years. At the peak of the first lockdown, the broad unemployment rate (including leave without pay) was 34.4 percent, and at the peak of the second lockdown was 23.5 percent. In the first half of December 2020, the broad unemployment rate was estimated by the CBS at 12.7 percent, with about 520,000 people (including the unemployed, the sick, and those not in the labor force after being fired or closing their businesses since March 2020). Now, with the third closure, there has been an increase in widespread unemployment. The most serious damage in this crisis is to employment in the tourism, trade, and leisure and entertainment industries and in small businesses, which suffer particularly due to lockdowns. During 2020, more than 70,000 small businesses were closed. Action must now be taken not to close good businesses just before the recovery phase.

Unemployment will remain high even after the pandemic subsides. According to the Bank of Israel's forecast, in a scenario of rapid vaccination, the broad unemployment rate will stand at 7.7 percent in the last quarter of 2021.

The expected problems in the labor market do not concern only the coronavirus crisis. In the rapidly growing ultra-Orthodox sector, a profound change is needed in the willingness of men to acquire education relevant to employment in industries where wages are higher than average and to participate in the labor force. According to the State Comptroller's report from May 2020, 84 percent of the ultra-Orthodox boys, high school students, chose "small yeshivas" and did not study core subjects such as mathematics, English, or science. According to the report, "among the ultra-Orthodox students, deep gaps in knowledge are created that will make it difficult for them, and will affect the productivity of the economy as a whole." Alongside this, the Arab sector is characterized by low labor productivity and low participation rates of women in the labor force.

Despite the difficulty of the current political situation, the intensity of the crisis and the need to emerge from it as quickly as possible require a comprehensive national economic plan of the government in collaboration with the business sector and local authorities, managed and implemented by a national operational headquarters. The program should include a variety of efforts, such as:

- a. Increasing employment: Efforts in this area exist, but they must be expanded, strengthened, and ensured they are implemented effectively. For example, the Ministry of Labor and Welfare intends to provide vocational training in 2021 to about 30,000 workers, three times more than in previous years. In addition, the ministry established an Employers' Administration in cooperation with the business sector and the socio-economic forum and the Histadrut (national trade union). The administration will collect information on the needs of the economy for employees, adapt professional training to the expected trends in the economy, and integrate employers in the training. During the crisis, the advantage of the technology sector was evident, as it was less affected, and some companies even grew as the demand for digital technology increased. Growth in this sector is expected to continue even after the crisis. Therefore, the first priority is to train employees for work in the technology sector and in other companies that require their employees to have high digital literacy.
- b. Reducing the current model, which guarantees the payment of unemployment benefits until June 2021: In December 2020, Finance Minister Yisrael Katz decided to work to extend the period of payment while on leave beyond June 2021, as long as the broad unemployment rate does not fall below 7.5 percent. However, the model does not encourage some people to return to work, so other models that reward returning to work should be implemented. For example, the National Insurance Institute will award a "return to work grant" to encourage a return to work by February 28, 2021, in case the new wage is lower than their previous wage.

- c. Supporting small businesses in the financial field and improving their capabilities in the digital field: In this context, on December 28, 2020, Facebook Israel CEO Adi Soffer Teeni said that there are about 540,000 small businesses in Israel that employ about 60 percent of the business sector, contributing 55 percent of the business sector's product, but only 14 percent show digital activity. The coronavirus crisis has illustrated the importance of the digital medium and accelerated its growth. Through this medium, businesses all over the country can grow and expand after the crisis. The government and authorities must provide digital infrastructure throughout the country.
- d. Reducing bureaucracy, directing businesses, and accelerating business processes.

In conclusion, economic-social recovery depends first of all on the decline of the coronavirus. Given rapid vaccination, forecasts indicate GDP growth in 2021 at a rate of 4.5-6.3 percent. This is of course presumes there will be no exceptional events, such as the spread of a mutation that is immune to the vaccine. Israel will also be affected by growth in the world economy. In the process of emerging from the crisis, reducing unemployment must be given first priority because it has broad social implications. A concentrated effort must be made to reach a broad unemployment rate of less than 7 percent before the end of 2021. In doing so, opportunities must be seized to work for the long-term development of the labor market, with the aim of raising the employment rate and labor productivity, especially in the ultra-Orthodox and Arab sectors (which together make up about 32 percent of the population), and in the periphery. This effort, necessary for stable long-term growth, requires cultural and budgetary changes, and many years.