

Israel:

Economics, Politics, and Peace

Oct 11, 1996



Brief Analysis

The promise of Oslo evoked high expectations of reconciliation between Palestinians and Israelis. Its danger, however, lies in the mechanisms Oslo outlined to reach that reconciliation and the exaggerated expectations Oslo produced.

A unique dynamic of the Oslo process is that the further one proceeds, the more difficult are the problems one faces. As the negotiations approach final status issues, the process is far from over; rather, by then the parties have only reached the end of the relatively uncomplicated beginning. It is useful to view the entire process through its three main components:

- Political -- Final status negotiations are a search for middle ground. Both parties need to be flexible, while each is expected to remain tough on certain issues; finding a balance is what constitutes statesmanship.
- Security -- Demonstrated by last week's events, each step must be taken with extreme caution. Not only on the humane level no one wants any more loss of life but also on the practical level. Nothing will derail the peace process more than the lack of security.
- Economic -- This is not a zero-sum game. All sides need to be more forthcoming due to the genuine interest we and the Palestinians share in the improvement of their standard of living. Strengthening the economy would be a win-win situation for all parties involved.

Israel's strategy is two-pronged: continuing negotiations and, though less glamorous but most essential, maintaining stability. The relationship between the two is interdependent: governments of the region must create stability in order to conduct successful negotiations, while at the same time negotiations will create stability.

In this regard, the economic component is the easiest of the three to address. A range of activities that could improve the living conditions of Palestinians are underway. For example, Israel has already increased the number of Palestinians allowed to work in Israel to 39,000 and set a target of 50,000. Israel has also eased restrictions on the movement of Palestinian businessmen travelling between the West Bank and Gaza. But the economic component of peace depends on Palestinian cooperation as well as on the need for international donors to honor their financial promises. While the donor conferences, facilitated by the United States, have been productive in generating financial pledges, more countries must be brought into the process and those that have made pledges must fulfill their commitments.

The government's long-term policy is to create more prosperity, or at least less poverty, which would build incentives for the Palestinians to continue with the peace process even when there are difficulties.

Israel-Jordan Relations

Currently, Israel has an opportunity to build the sort of warm, cooperative relationship with Jordan it unfortunately

never had with Egypt. Since the Camp David Accords in 1979, Israeli-Egyptian relations have remained cool, regardless of whether Likud or Labor was in power. Nevertheless, Israel paid a high price for peace with Egypt, and it was worth it.

The situation with Jordan is different. Israel and Jordan can be a model for peace throughout the entire region, specifically for the Palestinians. There is a ripe opportunity for the citizens of both Israel and Jordan to realize the benefits of peace, because Jordanian society has made itself more open to peace. Though the peace treaty was signed between Israel and Jordan in 1994, the Israeli government and King Hussein have had "very good" relations since 1970 when the king expelled the PLO from the East Bank.

Much more must be done to nurture the relationship between Israel and Jordan, especially economically. If a prosperous economic relationship is cultivated between Israel and Jordan, that prosperity will spill over into Palestinian society and ultimately help create an environment more conducive for positive movement on the Israeli-Palestinian track.

Israeli Economy

Israel is committed to a more liberal, less government-regulated and more competitive economy. An invigorating force in the economy is the surge of skilled labor among Russian immigrants. Since their absorption into Israel beginning in 1989, the GDP has grown 6 percent annually and unemployment has decreased from 11 percent in 1992 to the current rate of 6 percent. Export rates grow by about 9 percent a year and this year's GDP is expected at about \$94 billion, about twice what it was not long ago.

The Likud government inherited a budget deficit of about 11-12 billion shekels (about \$4 billion). To remedy the excessive government expenditure, the cabinet made major cuts about 4.5 percent from next year's budget that will be implemented in December. The government hopes to avoid a shut down similar to the U.S. Congress last fiscal year, but since the nature of Israeli democracy has significantly changed due to the adoption of an American-style electoral system, Knesset members are having an awkward time adjusting and hope not to face the kind of gridlock the U.S. Congress encountered, especially since Likud holds only twenty-two seats of the sixty-six seat coalition. It is a tough path, but Israelis are resolved to follow it.

The Ministry of Finance's two main priorities are: cutting the budget and liberalizing the economy. There is unprecedented interest in Israel from within the international banking and investment communities, especially in the fields of high-tech and sophisticated industries and infrastructure. Absorption of the skilled Russian labor force has recreated the Israeli economy into a producer of high-tech and sophisticated goods; and Israel is in the midst of major infrastructural projects, including the construction of roads, electricity networks, and a subway system in Tel Aviv.

While there is much work to be done in terms of liberalization, it is important to underscore the real difference between Israel and post-Soviet states like Poland or the Czech Republic: the Israeli government does not own that much of Israeli industry. Of what it owns, however, it is in the country's best interest to sell as many government-owned companies as possible. Currently, 23 percent of Bezek, Israel's telecommunication company, has been made public and the government intends to sell the remainder. The purpose of making such a move, however, must be to encourage competition—not simply to pass a nationalized company off into the hands of a private monopoly.

Furthermore, it is very encouraging that in 1995 Israeli companies earned about \$500 million in the American stock market; in the first nine months of 1996, \$750 million; and by the end of the year, \$1 billion. This is proof that the international financial community has confidence in Israeli business and the Israeli economy.

> The Israeli government is pleased with President Mubarak's decision to go ahead with November's economic summit in Cairo and hopes to build deeper economic relationships with the participating countries.

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