

Chapter 8

Welfare Policy Issues

- ◆ The level of poverty remained unchanged during 2009–10: the incidence of poverty among individuals, according to the accepted relative definition, stood at 24.7 percent of the population, which represents about 1.77 million poor people. At the same time, there was an increase in the incidence of poverty among families and in absolute terms, in the income gap (which measures the average distance of the poor's income from the poverty line) and in the Sen index (which is a weighted combination of the incidence of poverty, the income gap and inequality among the poor).
- ◆ The incidence of poverty among the working population has been characterized by an upward trend over the last decade and is substantially higher than in other OECD countries. The growth in the working poor reflects on the one hand the entry of weaker segments of the population into the labor force and on the other hand the lack of an effective policy to improve human capital and the labor income of populations with low earning ability. The lax enforcement of labor laws is an additional factor explaining the low wages of workers at the bottom of the wage scale, which also has an effect on the incidence of poverty among this population.
- ◆ The incidence of poverty and its intensity are particularly high among the ultra-Orthodox and the Arabs, two groups that are characterized by low employment rates and high birth rates. These are also populations in which the extent of poverty has grown significantly over the last decade, while the incidence of poverty among non-ultra-Orthodox Jews has remained stable.
- ◆ The incidence of poverty among the elderly has declined in recent years, after a significant increase at the beginning of the decade. This is primarily due to the fact that the old age pension has eroded to a lesser extent than other allowances.
- ◆ In 2009–10, income inequality continued to worsen, with the Gini index reaching about 39 percent. The indexes of inequality are high in Israel relative to the OECD countries and in historic terms. The increase in the inequality of net income reflects stability and even a reduction in the inequality of economic income, in parallel to a decline in the contribution of transfer payments and taxes to reducing inequality.
- ◆ The direct contribution of transfer payments and direct taxes is very low relative to other OECD countries and it has declined almost continuously during the last decade. In 2009–10, their contribution was stable and even rose somewhat.
- ◆ The earned income tax credit (EITC), which is in its first year of implementation, raised 4.5 percent of its poor recipients to above the poverty line. The EITC is one of the only policy measures that makes it possible to increase the income and welfare of low-income households without reducing the incentive to work and without adversely affecting the demand for labor. It is focused on weak populations and therefore is an effective policy tool for assisting the working poor. It is recommended to increase the size of the grant and applying it nationwide.
- ◆ Affirmative action in the allocation of core teaching hours in primary education for students from weak backgrounds has been reduced in scope since the 2007–8 school year. It is worthwhile to increase resources to those students.

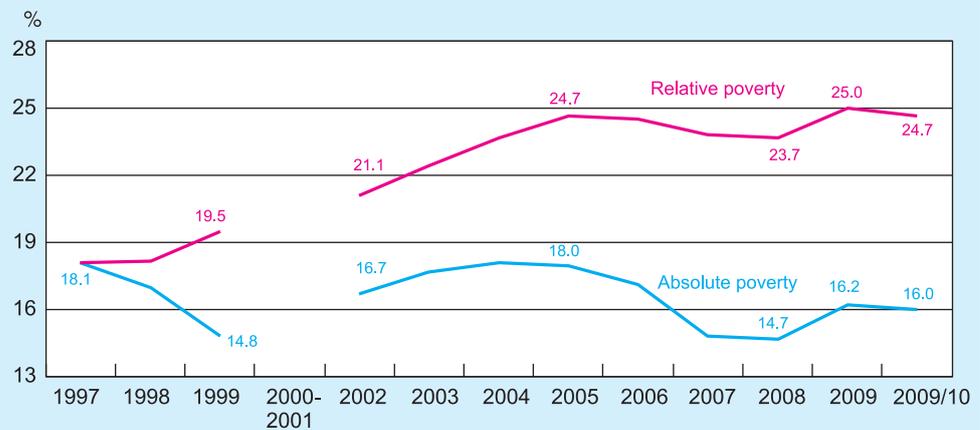
1. POVERTY AND INCOME INEQUALITY AND THE POLICY TO REDUCE THEM¹

a. The trends in the incidence of poverty

The scope of poverty increased in 2009 while it stabilized in 2009–10.

The incidence of poverty among individuals (according to the accepted relative index) reached 24.7 percent in 2009–10,² which represents some 1.77 million individuals. The incidence of poverty measured according to the absolute approach (a fixed poverty index) was 16 percent. These rates reflect a lack of change in the scope of poverty (relative to all of 2009) following their decline in 2006 and 2007 (Table 8.1 and Figure 8.1) and an increase in 2009. A similar trend can be seen in the measures of

Figure 8.1
Incidence of Poverty among Individuals by Different Approaches,^a 1997–2009/10^b



^a The relative poverty line is calculated according to half the median equivalized income.

^b The data are based on a survey conducted between July 2009 and June 2010.

^c In 2000 and 2001, Arabs of Jerusalem were not included in income surveys and expenditure surveys. Those years were excluded from the figure so that the indices would be comparable.

SOURCE: Based on Central Bureau of Statistics' Income and Expenditure surveys.

¹ This part of the chapter relates to welfare policy that directly or indirectly affects poverty and inequality. It will not discuss welfare policy in other important areas, such as education, health, individual security, housing, personal and community services, culture, entertainment, sport, quality of the environment and religious services. For a discussion of these areas, see later in the chapter and Chapter 6.

² Most of analysis in this chapter is based on the data of the Income Survey and the Expenditure Survey. The last Income Survey covered the period from July 2009 until June 2010. Figures from this survey will be referred to as applying to 2009-10. The last Expenditure Survey covered the year 2009 and therefore data based on the Expenditure Survey is updated only to 2009.

For an explanation of the various indicators of poverty and inequality, and other terms appearing in this chapter, see Chapter 8 in the Bank of Israel Annual Report for previous years and the Annual Review of the National Insurance Institute for 2009, from page 337 onward.

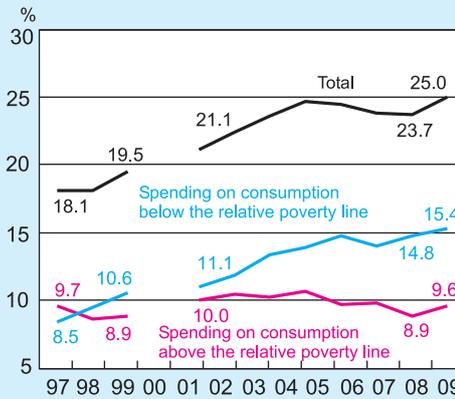
the intensity of poverty, with the income gap and Sen index rising in 2009 and remaining unchanged in 2009–10.

The proportion of the poor consuming under the poverty line declined relative to 2008, though it remained high at 61.5 percent (Table 8.1). The number of the poor consuming above the poverty line has remained relatively stable during the last decade and rose somewhat in 2009 (Figure 8.2), while the proportion of the poor consuming under the poverty line has been characterized by an uptrend during the last decade, in parallel to the increased incidence of poverty.

In the absence of consecutive panel surveys of the same individuals over time, consumption under the poverty line is commonly used as an indicator of persistent poverty.³ Therefore, the trends over the last decade are apparently an indication of growth in the “hardcore” poor, who are characterized by deep and persistent poverty. In contrast, the small increase in the number of poor consuming above the poverty line may indicate an increase in the number of individuals whose income has fallen to under the poverty line temporarily, as a result of the crisis, though they still possess economic resources that allow them to smooth consumption and maintain their standard of living. However, since the poor who are consuming above the poverty line have increased their housing expenditure to a large extent due to the increase in housing prices, it may be that part of the increase in the rate of the poor consuming above the poverty line is only the result of the increase in housing prices and does not reflect an improvement in their standard of living or an increase in the proportion of the temporarily poor.

The increase in the scope of poverty from the second half of 2008 until June 2009 was a reflection of the crisis’ effect on the labor market. The crisis had a widespread effect on employment during this period but particularly so among the weaker segments of the population, i.e. those with low levels of education, residents of the Periphery and Arabs (there is overlap between these groups). The average income for salaried workers also eroded in real terms. During the second half of 2009, there were signs of a recovery in the economy as a whole and particularly in the labor market and this

Figure 8.2
Incidence of Poverty among Individuals,^a by Spending on Consumption, 1997–2009



^a In 2000 and 2001, Arabs of Jerusalem were not included in income surveys and expenditure surveys. Those years were excluded from the figure so that the indices would be comparable.
SOURCE: Based on Central Bureau of Statistics' Income and Expenditure Surveys.

The increase in poverty from the second half of 2008 until June 2009 reflected the effects of the economic crisis on the labor market.

³ The basic assumption made here is that individuals tend to smooth their consumption. Therefore, to the extent that the change in income is temporary, individuals will not drastically cut their expenditures but rather will use their savings and/or take out loans in order to maintain their consumption. When the reduction in income persists, they will reduce consumption at a rate similar to that of the decrease in income.

Table 8.1
Main Poverty Indicators, 2002 to 2009/10^a

	2002	2004	2006	2008	2008/9	2009	2009/10
	(percent)						
A. Poverty indices							
A1. Relative index ^b							
Equivalized poverty line (NIS)	1,395	1,449	1,629	1,742	1,768	1,815	1,842
Number of poor ('000)	1,317	1,529	1,644	1,646	1,702	1,769	1,761
Incidence of poverty (individuals)	21.1	23.6	24.5	23.7	24.3	25.0	24.7
Incidence of poverty (families)	18.1	20.3	20.0	19.9	20.2	20.5	20.1
Income gap ^c	29.7	33.3	33.8	34.2	34.3	35.5	35.6
SEN index ^d	0.090	0.111	0.115	0.113	0.116	0.123	0.121
Proportion of poor whose consumption is below the poverty line	52.5	56.6	60.4	62.4		61.5	
A2. Incidence of poverty according to fixed index ^b —individuals	16.7	18.1	17.1	14.7	15.5	16.2	16.0
Incidence of poverty according to fixed index measured according to the CPI of the lowest quintile—individuals	16.8	18.0	17.2	15.1	15.9	16.8	16.4
A3. Change in real income of family in lowest quintile ^e		-1.9	5.4	-1.4	0.4	1.2	1.1
Change in per capita GDP	-2.6	2.8	3.8	2.5	-0.5	-1.6	0.5
Change in median per capita real income ^f		2.8	4.4	-0.6	-1.3	0.8	0.8
B. Incidence of poverty in selected groups							
Children	29.6	33.2	35.8	34.0	35.0	36.3	36.0
Aged 65+	20.3	25.4	22.7	22.7	22.1	21.8	20.3
Arabs	49.5	51.6	57.6	53.1	53.3	57.4	56.9
Ultra-orthodox ^f	50.5	57.4	57.2	60.4	59.0	58.5	60.7
Members of households with one earner	25.1	31.3	35.9	35.6	36.4	38.7	40.0
Members of households with two or more earners	3.0	3.8	4.2	4.3	4.8	5.2	4.6

^a The data in the column 2009/10 are based on a survey carried out between July 2009 and June 2010, and those in the column 2008/9 are based on a survey carried out between July 2008 and June 2009. The comparison of the year ended June 2010 is against the corresponding year which ended June 2009.

^b The relative poverty line is calculated as half the median monetary income. The absolute poverty line is calculated relative to its real level in 1997.

^c Average gap between the poverty line and the income of poor families.

^d The Sen index combines the incidence of poverty, the income gap, and inequality among the poor.

^e The quintiles are determined according to the disposable income per standard capita, and every quintile contains 20 percent of the families, in accordance with the definition of the government's target. The rate of change in 2009/10 is calculated compared with the equivalent period a year earlier—July 2008 to June 2009.

^f There is a difficulty in identifying the ultra-orthodox in the Income Survey. They are identified here based on one household member learning in a post secondary religious institution (yeshiva).

^g People belonging to a household with one earner.

^h People belonging to a household with two or more earners.

SOURCE: Based on Central Bureau of Statistics Income Surveys and Expenditure Surveys.

was reflected in an increase in the rate of employment and a moderate increase in the average wage (see Chapter 5 in this report). However, the recovery in the labor market was manifested primarily in the improved situation of higher-educated workers, while the rate of employment did not rise among less-educated workers and their real labor income did not improve.

According to typical cyclical trends, the benefits of growth reach the weak segments of the population with a delay and only in part, since in general the status of these individuals in the labor market is unstable and their earning ability is low. In contrast, a crisis affects them immediately and with greater intensity than stronger segments of the population. This is because in general they are characterized by low levels of human capital and therefore the cost of laying them off, from the employer's point of view, is relatively low.

The trends described above are also reflected in the decomposition of the change in the incidence of poverty into two components: that due to the change in the income distribution and that due to the shift in the poverty line.⁴ When the standard of living and the median income increase, the poverty line rises accordingly. In this situation, even if there is no change in the distribution of income among the lower strata, the incidence of poverty is likely to increase as a result of the shift in the poverty line. In other words, even if the income of those in the lower quantile remains unchanged, they become relatively poorer. Similarly, one can calculate the absolute effect that is a result of the change in the distribution of income. In 2009 and later in 2009–10, the two effects worked to increase the incidence of poverty (Figure 8.3). Thus, for example, in 2009–10, the medium income per standard individual, and therefore the poverty line according to the relative approach, grew moderately by 0.8 percent in real terms (relative to the parallel period, i.e. July 2008 to June 2009). If it were not for this upward shift in the poverty line, the incidence of poverty would have grown by only 0.2 percentage points due to the decrease in the income of the weaker populations. Thus, we can conclude that the shift up in the poverty line contributed an additional 0.2 percentage points to the increase in the incidence of poverty. The composition of the change in the incidence of poverty in 2009 as a whole was similar. These trends, which differ from previous years, are additional evidence of the particularly adverse effect of the last crisis on the weaker segments of the population. Although this effect was more limited in 2009–10 than in 2009, the trend remained unchanged.

The incidence of poverty and its intensity were particularly high among Arabs and the ultra-Orthodox (Figure 8.4; Table 8.3). These are also groups in which the scope of poverty increased by the greatest extent in recent decades, while among non-Ultra-Orthodox Jews, the rate of poverty remained almost unchanged during the last decade. The high level of poverty among these populations reflects the combination of a small number of income earners and large families together with low earning

The economic crisis had a greater effect on the weak segments of the population while the recovery was not fully felt among them.

The incidence of poverty and its intensity are particularly high among Arabs and the ultra-Orthodox.

⁴ The change in the incidence of poverty from year to year has three components: the effect of a change in the poverty line, the effect of the distribution of income and a component that reflects a combination of these two effects. The size of the combined component is negligible and therefore was included within the effect of the change in the poverty line.

Table 8.2
Rate of Employment and Average Wage Income, by Segments of the Population ,
Ages 25-64, in selected years

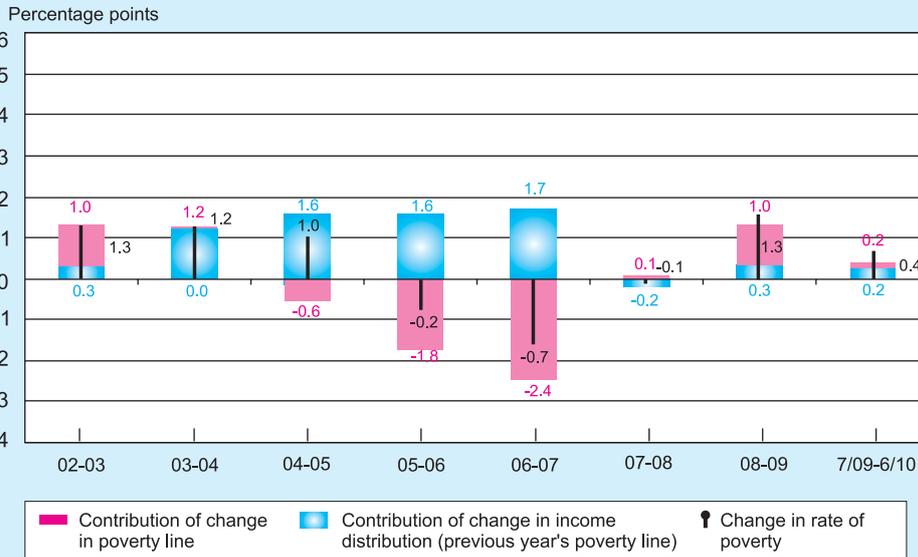
	Rate of employment			Average wage income (at 2009 prices)					
	1997	2003	2008	2009	1997	2003	2008	2009	2009/10 ^a
	Men								
Total population	77.3	73.4	77.6	75.7	9,829	10,091	10,655	10,198	10,120
Arabs	74.8	66.3	72.1	70.7	6,161	6,406	6,351	6,099	6,128
Ultra-orthodox Jews ^b	42.2	36.2	39.3	38.5	7,336	7,470	7,931	6,822	6,332
Population excluding Arabs and ultra-orthodox Jews	79.6	77.3	81.6	79.6	10,535	10,754	11,544	11,076	10,995
0-10 years of education	67.4	58.3	62.8	61.7	6,064	6,027	6,163	5,802	5,759
11-12 years of education	82.7	76.6	80.7	78.3	8,557	8,111	8,151	7,670	7,627
	Women								
Total population	55.8	59.3	64.6	64.2	5,963	6,311	6,816	6,793	6,702
Arabs	19.3	20	24.1	24.7	4,528	5,032	4,501	4,654	4,809
Ultra-orthodox Jews ^b	47.1	50.3	56.7	58	4,585	5,391	5,112	4,966	4,889
Population excluding Arabs and ultra-orthodox Jews	63.1	67.3	73.5	73	6,065	6,410	7,029	7,025	6,915
0-10 years of education	25.5	24.1	27.5	27	3,363	3,672	3,521	3,634	3,533
11-12 years of education	58	58.1	61	59.6	4,990	5,043	5,319	5,007	4,989

^a The data in this column are based on a survey carried out between July 2009 and June 2010.

^b There is a difficulty in identifying the ultra-orthodox in the Income Survey. Here they are identified as families in which the last educational institute attended by a member of the family was a talmudic college.

SOURCE: Based on Central Bureau of Statistics' Labor Force and Income Surveys.

Figure 8.3
Contribution to Changes in Rate of Poverty among Individuals,^a
2003–June 2010



^a The contribution of a change in the poverty line to the rate of poverty is calculated here as the difference between the total change in the rate of poverty and the change that stems from a shift in the distribution of income relative to the previous year's real poverty line.
 SOURCE: Based on data from Central Bureau of Statistics' Income Surveys.

ability. The increase in the incidence of poverty among the ultra-Orthodox and Arabs is also reflected in the increased incidence of poverty among children, of whom an increasing proportion live in ultra-Orthodox or Arab households. In addition, the incidence and intensity of poverty is to a large extent influenced by level of education, which is consistent with education's influence on earning ability. The incidence of poverty among the elderly has declined in recent years (after a significant increase at the beginning of the decade as a result of the cut in allowances) and is lower than the average incidence of poverty in the population as a whole. This is explained by the fact that the old age pension has eroded less than other allowances.

Table 8.3
Indices of Relative Poverty among Individuals by Various Characteristics and by Selected Sectors of the Population, 2009-10^a
Head of household aged 25-64

	Poverty indices		Distribution	
	Rate of poverty	Income gap ^b	Percentage of the poor	Percentage of the population
Total	24.3	36.4		
Years of education				
Up to 8	57.2	39.9	18.4	7.8
9-10	46.8	38.1	16.2	8.4
11-12	26.4	35.4	34.7	32.0
13-15	18.7	32.8	17.2	22.4
16+	11.1	37.0	13.4	29.3
Family size				
1	19.8	34.7	2.7	3.3
2-4	13.2	34.9	25.2	46.4
5-6	25.4	35.7	36.6	35.0
7-8	52.4	38.9	22.0	10.2
9+	64.1	37.5	13.5	5.1
Number of wage earners				
0	77.2	52.0	33.9	10.7
1	40.3	29.6	56.3	33.9
2+	4.3	20.1	9.8	55.4
Population group				
Ultra-orthodox ^c	60.9	38.5	17.4	6.9
Arabs	57.8	38.1	48.6	20.4
Population excl. ultra-orthodox and Arabs	11.4	32.8	34.0	72.6
Single-parent families	39.8	37.3	7.9	4.8
Immigrants (since 1990)	16.4	28.5	10.8	16.0

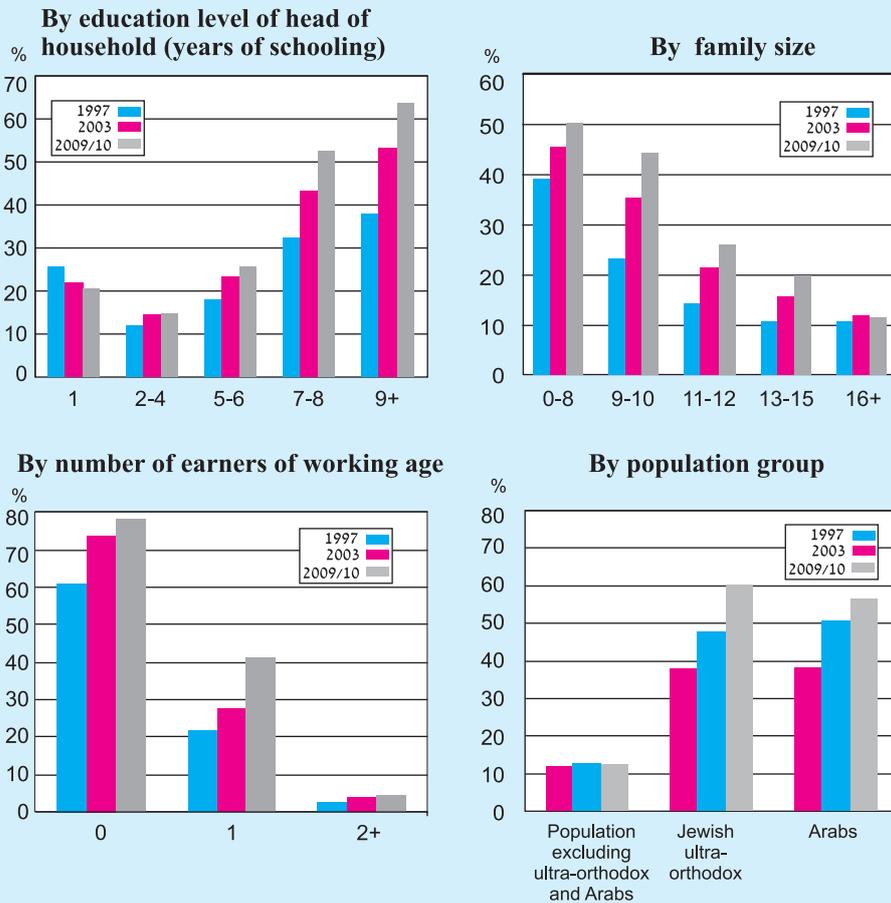
^a Based on a survey carried out between July 2009 and June 2010.

^b Average gap between the poverty line and the income of poor families.

^c There is a difficulty in identifying the ultra-orthodox in the Income Survey. Here they are identified as families in which the last educational institute attended by a member of the family was a talmudic college.

SOURCE: Based on Central Bureau of Statistics Income Surveys.

Figure 8.4
Rate of Relative Poverty (Individuals) by group, 1997, 2003 and 2009/10^a



^a The data are based on a survey conducted between July 2009 and June 2010.
 SOURCE: Based on data from Central Bureau of Statistics' Income Surveys.

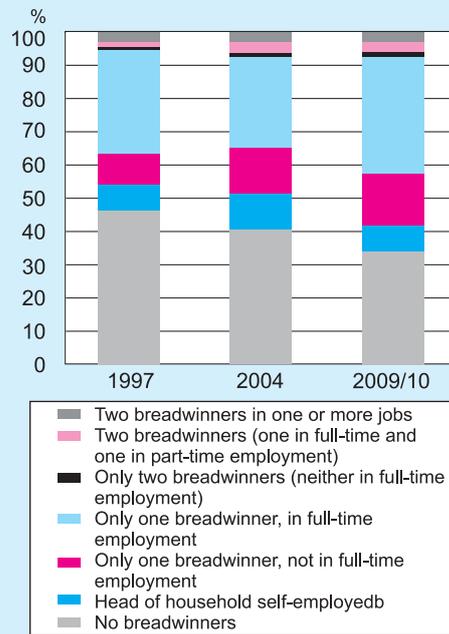
The working poor

About two-thirds of the poor live in households with at least one income earner (Table 8.4; Figure 8.5).⁵ The incidence of poverty among individuals living in households with at least one income earner reached 18 percent in 2009–10, which is very high in historical terms and in comparison to other OECD countries. Although in the OECD, 60 percent of the poor live in households with at least one income earner (in the mid-2000s), the average incidence of poverty among the employed was only 7.7 percent since the overall rates of poverty in these countries is much lower.

The incidence of poverty among individuals in households with at least one income earner is particularly high in Israel.

⁵ Out of all households in which the head of the household is aged 25 to 64.

Figure 8.5
Features of the Employment of the Poor,^a 1997, 2004 and October 2009



^a Poor who live in a household the head of which is aged 25-64.

^b All the poor who live in a household the head of which is self-employed. These households are likely to have additional workers working either full or part time. The other categories include only wage earners. SOURCE: Based on Central Bureau of Statistics Income and Expenditure Surveys.

About two-thirds of the poor living in households with at least one income earner (hereafter: the working poor) are Arabs. Their proportion of the working poor was more than three times their proportion in the population (i.e. about one-fifth). Among Jews (both ultra-Orthodox and non-ultra-Orthodox) the phenomenon of working poor is less prevalent. The problem of the working poor among the Arab population is particularly prevalent among households with only one fulltime income earner, which accounts for about half of the Arab poor. The incidence of poverty among this group has grown significantly during the last decade and reached 70 percent in 2009–10. During the last decade, there has been an increase in the proportion of Arabs living in households with more than one income earner within the total Arab population, in parallel to a decline in the proportion of Arabs living in households without any. It is possible therefore that there has been a change in the composition of the Arab population living in households with one income

earner, which has worked to increase their incidence of poverty. In other words, a relatively weak group consisting of households who previously did not have any income earners was added while a relatively strong group consisting of households that previously had a single income earner left this category when an additional income earner was added.

The increase in the number of working poor, in view of the policy measures taken to encourage weaker segments of the population to join the workforce, raises the question of whether the situation of the working poor has indeed deteriorated. In other words, have they become poorer or has there been a change in the composition of employment, whereby individuals who were previously poor and relied on allowances were forced to join the workforce when allowances were cut, thus increasing the number of working poor even though their situations had remained unchanged. In the absence of panel data that follow individuals over time, this question cannot be addressed directly. However, an examination of the composition of employment over the last decade may provide an indication of the importance of changes in the composition

The problem of the working poor is more severe among the Arab population and within that population among households with only one fulltime income earner.

Table 8.4
Characteristics of Employment, Wages and Poverty,^{a,b} 2009/10, in Households whose Head is Aged 25–64^c

	Total	Arabs	Ultra-orthodox ^d	Population excl. Arabs and the ultra-orthodox
Total	6,138,557	1,253,648	426,085	4,458,824
Proportion of population	100.0	20.4	6.9	72.6
Number of poor	1,491,287	724,249	259,297	507,741
Proportion of all poor	100.0	48.6	17.4	34.0
Total number in households with at least one wage earner	5,484,437	1,023,015	297,710	4,163,712
Proportion of population	89.3	81.6	69.9	93.4
Incidence of poverty	18.0	49.4	48.9	8.1
Proportion of the poor in this group	66.1	69.8	56.1	66.1
Head of household self-employed	719,458	160,744	31,244	527,470
Proportion of population	11.8	13.0	7.1	12.0
Incidence of poverty	17.2	37.3	43.2	9.5
Proportion of the poor in this group	8.3	8.4	5.3	9.7
Head of household employee				
One wage earner (not employed full-time)	452,723	70,648	104,739	277,336
Incidence of poverty	51.5	69.9	75.5	37.7
Proportion of the poor in this group	15.6	6.8	30.5	20.6
Proportion earning less than minimum wage ^f	20.4	27.3	18.0	19.9
Average hourly wage among the poor	28.5	29.1	33.1	26.5
One wage earner (in full-time employment)	1,571,425	486,158	78,560	1,006,707
Incidence of poverty	33.2	72.1	49.9	13.1
Proportion of the poor in this group	35.0	48.4	15.1	26.0
Proportion earning less than minimum wage ^f	13.7	20.0	11.0	12.0
Average hourly wage among the poor	22.6	23.5	25.6	20.4
Two wage earners (at least one in full-time employment)	108,429	14,301	17,729	76,399
Incidence of poverty	21.2	17.6	32.9	19.1
Proportion of the poor in this group	1.5	0.3	2.3	2.9
Proportion earning less than minimum wage ^f	14.8	0.0	5.0	17.8
Average hourly wage among the poor ^e	26.7	29.8	37.4	24.1

(Cont.)

Table 8.4 (Cont.)**Characteristics of Employment, Wages and Poverty,^{a,b} 2009/10, in Households whose Head is Aged 25–64^c**

	Total	Arabs	Ultra-orthodox ^d	Population excl. Arabs and the ultra-orthodox
Two wage earners (at least one in full-time employment)	663,204	83,737	26,815	552,652
Incidence of poverty	7.1	17.6	20.4	4.8
Proportion of the poor in this group	3.2	2.0	2.1	5.3
Proportion earning less than minimum wage ^f	5.9	10.5	11.4	5.1
Average hourly wage among the poor ^e	21.5	20.7	19.2	22.3
Two wage earners (two in full-time employment)	1,302,463	128,012	24,350	1,150,101
Incidence of poverty	2.9	19.2	4.1	1.1
Proportion of the poor in this group	2.5	3.4	0.4	2.4
Proportion earning less than minimum wage ^f	6.4	19.5	9.5	5.3
Average hourly wage among the poor ^e	20.9	20.0	25.1	22.2

^a The average wage, and classification as self-employed or employee, Arab or ultra-orthodox, are determined based on the head of the household. The table does not show data relating to households whose head is both self-employed and an employee, as their number is small.

^b Percent, unless stated otherwise.

^c The head of the household is the main wage earner in the household, i.e., the one working the most hours per week (including members of the professional army). If a household has more than one member that satisfies this criterion, or if the household has no wage earner, the interviewee determines who is the head of the household.

^d There is a difficulty in identifying the ultra-orthodox in the Income Survey. They are identified here as families in which the last educational institute attended by a member of the family was a talmudic college. This definition may create a bias with regard to people with a lower tendency to participate in the labor force.

^e Due to the small number of observations, these data are not statistically significant.

^f People whose average hourly wage is less than 95 percent of minimum hourly wage.

SOURCE: Based on the Central Bureau of Statistics Income Survey.

There are two main causes for the existence of the working poor: large households and low earning ability.

of employment. Among people living in households with one fulltime income earner, the proportion of Arabs increased while at the same time the proportion of non-ultra-Orthodox Jews decreased. This change in the breakdown worked to increase the incidence of poverty among this group since the incidence of poverty is higher among Arabs. In contrast, there has been a continuous increase in the proportions of individuals with higher levels of education (both among non-ultra-Orthodox Jews and among Arabs) and demographic groups in which the incidence of poverty is relatively low, which would act to reduce the incidence of poverty.

There are various factors accounting for the existence of the working poor; however, the two most prominent are large households and low earning ability. These factors

are common to ultra-Orthodox and Arab households, as well as to non-ultra-Orthodox households. Low earning ability is manifested in a low level of education or education that does not match the demands of the labor market, in low-wage professions and in employment in industries with a relatively low average wage. This results in low wages for the working poor, which are about one-half or even less than the wages of other workers with similar characteristics. Apart from this, the low wages of the working poor are also the result of lax enforcement of labor laws. Thus, the working poor, whose status in the labor market is precarious and easily exploited, find it difficult to exercise their rights. This is manifested in, among other things, the high proportion of the working poor who earn less than the minimum wage, which illustrates the crucial role played by the enforcement of labor laws.

b. Inequality of income

In parallel to the increased scope of poverty, we have been witness to increasing inequality in income during the last decade. Table 8.5 presents a number of accepted indicators of inequality while Table 8.6 presents the trend in income shares of the various quantiles and the lowest and highest deciles. The various indicators point to an increase in inequality that is reflected in an improvement of the situation of better-off populations and a deterioration in the situation of worse-off populations. The comparison of indexes calculated according to economic income (after tax earned income and pension, minus National Insurance benefits) to those calculated according to disposable income indicate stability and even a moderate decline in the inequality of economic income, even though there has been a significant reduction in the progressivity of government policy. These two trends together were reflected in an increase in the inequality of disposable income.

The increase in inequality characterized most of the developed countries during the last two decades,⁶ though its level in Israel, as measured by the Gini index and other indicators, is one of the highest among the developed countries. Moreover, the main increase in inequality in the OECD countries occurred during the decade between the 1980s and the mid-1990s while during the subsequent decade the uptrend moderated in many of the countries and inequality even declined in some. Furthermore, in most of the countries, policy has become more progressive, which means that inequality in disposable income grew more slowly than inequality in economic income.

According to the economic literature, the main factors in the expansion of inequality include those that operate in the labor market, whether directly or indirectly, and demographic factors, which operate through the composition of the population. In

During the last decade, inequality in economic income has been relatively stable and has even declined somewhat, while the inequality in disposable income has increased.

The level of inequality in Israel is one of the highest among the developed countries.

Direct taxes and allowances are making less of a contribution to reducing inequality.

⁶ OECD (2008), "Growing unequal? Income distribution and poverty in OECD countries". It should be mentioned that during the last decade the upward trend in inequality has leveled off in the OECD countries (according to the average Gini index for 30 OECD countries from the beginning of the 2000s until the mid-2000s). However, in Israel, as in the US, inequality is continuing to grow. See OECD (2010): OECD Review of Labor Market and Social Policies, Israel.

Table 8.5
Indices of Inequality, 1997-2009/10^{a,b}

	Gini, net income	Gini, economic income	The contribution of direct taxes and transfer payments to the reduction of the Gini index ^c	The ratio of 90th percentile to the 10th percentile	The ratio of the median to the tenth percentile	The ratio of the median to the mean
1987				4.4	2.3	0.9
1995				4.8	2.2	0.85
1997	0.346	0.504	31.3	5.0	2.3	0.82
1998	0.344	0.506	32.0	5.0	2.3	0.84
1999	0.348	0.501	30.6	4.9	2.3	0.83
2000	0.338	0.492	31.2	4.9	2.3	0.85
2001	0.345	0.512	32.5	5.0	2.3	0.84
2002	0.355	0.520	31.8	5.2	2.4	0.84
2003	0.355	0.508	30.2	5.5	2.5	0.84
2004	0.367	0.504	27.2	6.0	2.7	0.83
2005	0.374	0.504	25.7	6.1	2.7	0.82
2006	0.379	0.503	24.6	6.1	2.7	0.82
2007	0.369	0.492	25.0	6.0	2.7	0.83
2008	0.372	0.491	24.3	6.2	2.7	0.83
2009	0.375	0.490	23.4	6.2	2.8	0.83
2009/10	0.379	0.495	23.5	6.3	2.8	0.83
OECD average (mid-2000s)	0.31	0.45	31.1	4.2	2.1	
OECD average (mid-1990s)	0.30			4.1		

^a The data in this row are based on a survey carried out between July 2009 and June 2010.

^b The indices were calculated based on the equivalence scale used by the OECD, according to which the standard number of persons in a household is equal to the square root of family size.

^c The direct contribution of direct taxes and transfer payments to the reduction of the Gini index is calculated as the percentage difference between the Gini index calculated for the economic income and the Gini index calculated for disposable income.

SOURCE: Based on Central Bureau of Statistics' Income Surveys, "Growing unequal? Income distribution and poverty in OECD countries", OECD (2008).

Table 8.6
Shares of Income Quintiles,^{a,b} 1997-2009/10

	Calculated according to net income					Calculated according to economic income					Difference between net income and economic income				
	Lowest		Quintiles		Top	Lowest		Quintiles		Top	Lowest		Quintiles		Top
	decile	quintile (1)	2, 3 and 4	quintile (5)	decile	decile	quintile (1)	2, 3 and 4	quintile (5)	decile	decile	quintile (1)	2, 3 and 4	quintile (5)	quintile (5)
1997	2.6	6.9	51.8	41.3	25.2	0.0	1.4	46.5	52.1	33.8	5.5	5.4	5.4	-10.8	
1998	2.7	6.9	51.9	41.2	25.3	0.0	1.4	46.2	52.4	34.2	5.5	5.7	5.7	-11.2	
1999	2.7	6.9	51.7	41.4	25.7	0.0	1.7	46.2	52.1	34.1	5.2	5.4	5.4	-10.6	
2000	2.8	7.0	52.3	40.7	24.9	0.0	1.7	47.0	51.2	33.1	5.3	5.3	5.3	-10.5	
2001	2.5	6.7	52.1	41.3	25.5	0.0	1.1	46.3	52.6	34.4	5.6	5.7	5.7	-11.3	
2002	2.2	6.2	52.0	41.8	25.9	0.0	1.0	45.7	53.3	35.2	5.2	6.3	6.3	-11.5	
2003	2.2	6.1	52.3	41.6	25.5	0.0	1.2	46.8	52.1	34.1	5.0	5.5	5.5	-10.5	
2004	1.9	5.6	52.0	42.3	25.9	0.0	1.3	47.0	51.8	33.5	4.4	5.1	5.1	-9.4	
2005	2.0	5.7	51.3	43.0	26.6	0.0	1.4	46.6	52.0	33.8	4.2	4.7	4.7	-9.0	
2006	2.0	5.6	50.9	43.5	27.3	0.0	1.6	46.2	52.2	34.2	4.0	4.7	4.7	-8.7	
2007	2.0	5.7	51.6	42.7	26.5	0.1	1.8	46.9	51.3	33.4	3.8	4.8	4.8	-8.6	
2008	2.0	5.6	51.4	43.0	26.6	0.1	1.9	46.7	51.4	33.5	3.7	4.8	4.8	-8.4	
2009	1.7	5.2	51.7	43.1	26.7	0.1	1.9	47.2	50.9	33.0	3.4	4.4	4.4	-7.8	
2009/10	1.8	5.3	51.4	43.2	26.9	0.0	1.8	46.9	51.3	33.6	3.5	4.6	4.6	-8.1	

^a Income quintiles are based on the weights used in the OECD scale.

^b Net income quintiles are calculated from net income, and economic income quintiles from economic income. Each quintile contains 20 percent of individuals/observations.

^c Data for 2009/10 are based on a survey carried out between July 2009 and June 2010.

SOURCE: Based on Central Bureau of Statistics' Income Surveys.

addition to these factors are of course government involvement and its degree of progressivity, as well as factors that affect the inequality of non-labor income.

The trends in the labor market are known to have a dominant effect on inequality. These work through the following channels: first, through changes in wage inequality between segments of the population and within them; in the effect of structural and business cycle changes in the labor market which change the relative demand for labor and as a result employment and relative wages; as well as changes in taxation, globalization, etc.; and second through changes in the composition of labor input, whereby an increase in rates of employment works in general to reduce inequality while an increase in the proportion of part-time jobs (or fulltime workers who only work for part of the year) works to increase inequality. In addition, factors that affect employment, whether directly or indirectly, are of critical importance, including government policy to increase employment rates. In Israel, it is important to mention the effect of the employment of non-Israeli workers, which works to worsen inequality by reducing the wages and chances of finding employment for Israelis with low levels of skills and education. Another factor worth mentioning in this context is the relatively lax enforcement of labor laws in Israel, which primarily affects low-wage workers.

In order to analyze the effect of these factors on the distribution of income, results are presented below for the decomposition of the Gini index according to income source (which describes, for each year, the contribution of each source of income to the inequality of net income) and according to segment of the population (which describes, for each year, the contribution of inequality within each group and between groups to total inequality in the population).

Table 8.7 presents the decomposition of the Gini index according to source of income. The results show a decline in the proportion of labor income in net income, in parallel to a similar decline in the (negative) proportion of direct taxes and in the Gini index for labor income. These trends reflect a similar picture to that obtained from other indicators of inequality. Thus, there was a decline in the inequality of economic income alongside the reduced contribution of transfer payments and taxes, which are reflected in the significant increase in inequality of net income. The contribution of allowances to reducing inequality declined significantly, as a result of their lower proportion of income and in parallel to the lower negative correlation between allowances and total income. In other words, not only did allowances account for a smaller proportion of total disposable income (which may reflect a positive change) they also became less concentrated among low-income earners. The negative correlation of direct taxes with total income in fact grew (despite the statutory changes that worked to reduce tax rates for high-income earners) and therefore the fall in their contribution to reducing inequality was entirely the result of their lower proportion in income.

Among the various types of labor income, the contribution of self-employed income grew as a result of an increase in all the factors: inequality (the Gini index), its proportion in total net income and its correlation with total income. The opposite trends characterized salaried income: a decrease in the Gini index and in the correlation

Table 8.7

Components of the Gini Index, by Source of Income, 2004 and 2009/10

Type of income (equivalized)	2004				2009/10					
	Share in total income ^a	Gini correlation ^b	Gini index	Absolute contribution to inequality	Relative contribution to inequality	Share in total income ^a	Gini correlation ^b	Gini index	Absolute contribution to inequality	Relative contribution to inequality
As self-employed	0.134	0.550	0.947	0.070	0.188	0.149	0.604	0.930	0.084	0.218
Head of household wage income	0.567	0.720	0.596	0.242	0.651	0.514	0.707	0.587	0.213	0.557
Spouse's/partner's wage income	0.208	0.750	0.808	0.126	0.339	0.202	0.708	0.789	0.113	0.294
Other earners' wage income	0.088	0.599	0.906	0.048	0.128	0.088	0.562	0.893	0.044	0.115
Capital	0.028	0.721	0.964	0.020	0.053	0.040	0.736	0.960	0.028	0.073
Pension and further education funds	0.072	0.557	0.930	0.037	0.100	0.070	0.547	0.930	0.036	0.093
National insurance	0.127	-0.195	0.625	-0.015	-0.042	0.112	-0.102	0.644	-0.007	-0.019
Government institutions and from abroad	0.033	0.067	0.922	0.002	0.006	0.028	0.033	0.923	0.001	0.002
Direct taxes	-0.258	-0.922	-0.663	-0.158	-0.423	-0.202	-0.934	-0.677	-0.128	-0.334
Total	1.000			0.372	1.000	1.000			0.383	1.000

^aThe share of this type of income in total net equivalized income, calculated using the scale of OECD weights.

^bThe correlation between the type of income and the net equivalized income.

SOURCE: Based on Central Bureau of Statistics' Income Surveys, using the DASP program.

The effect of the aging population and small households in increasing inequality has been of a smaller magnitude than the effect of large households.

with total income, as well as in the proportion of the head of the household's salaried income within total income.

The main demographic factors affecting inequality are the age distribution and the composition of households (by size, number of working-age members and number of children). These two factors of course overlap to a large extent, though they are not identical. Common living arrangements, such as small versus large households, single income earners, people living alone, etc., are to a large extent determined by the age distribution of the population, though also by many other social and cultural factors. Inequality in the OECD countries during the last two decades has been most affected by the aging of the population. This phenomenon has led both to an increase in the ratio of dependency and a major increase in the number of single households (which reduces the household's economies of scale and increases the disposable income needed to preserve a minimal standard of living). At the same time, the proportion of single parent families also increased. These two phenomena also exist in Israel but are not as dominant with respect to their influence on inequality. In Israel, the effect of large families is greater and is in fact particularly common among relatively low-income segments of the population. Changes in birthrates have second-order effects: in most developed countries, birthrates are in fact higher among weaker segments of the population, which increases the proportion of low-income earners in the population and thus worsens inequality. However, in most OECD countries, the decline in birthrates during the last two decades has been more dominant in the weaker segments of the population, which has tended to offset the increase in inequality. In Israel, as well, birthrates have fallen to a greater extent among Moslem women, a group that is characterized by high birthrates and widespread poverty.

Figure 8.6 presents the decomposition of the Gini index according to segments of the population.⁷ In other words, it describes the contribution of inequality within each group and between the groups to total inequality in the population. The dominant group with respect to its effect on inequality is working-age individuals, due to its large proportion of the population and its relative heterogeneity. The contribution of inequality within this group to total inequality was significant during the last decade, due to the increase in its proportion of the population and of income, and primarily due to the increase in its heterogeneity. Although inequality among the elderly is high, its contribution to overall inequality is small due to the relatively small size of this group.

The decomposition of inequality among the working age population shows that inequality is primarily the result of inequality among non-ultra-Orthodox Jews in view of the relative size of this group and its relatively large share in income. Nonetheless, the increase in inequality since 1997 was primarily due to the increase in inequality between groups. Although there was an increase in inequality within each group, the

⁷ The Gini index is calculated using disposable income (after direct taxes and transfer payments) per standard individual. Inequality is measured between individuals and characteristics are determined by those of the head of the household.

contribution of the Arabs and the ultra-Orthodox to inequality is small due to their low proportions of income and among non-ultra-Orthodox Jews the increase in the Gini index was offset by the significant decline in their proportion of the population.

An additional disaggregation of inequality among non-ultra-Orthodox Jews aged 25–64 according to level of education shows that the contribution of inequality among the groups has declined somewhat while the contribution of inequality within each group has grown. The largest increase in the contribution to total inequality was in the group with post-secondary education, whose heterogeneity grew, in parallel to the significant increase in its proportion of the population and of income. In contrast, the proportion of mid- and lower-income earners in the population is shrinking, in parallel to an even greater decline in their proportion of income. Thus, their contribution to inequality is relatively small despite the large degree of heterogeneity within this group.

In conclusion, during the last decade, inequality has been primarily affected by the increase in inequality within the working-age population, which was primarily the result of increased inequality between non-ultra-Orthodox Jews on the one hand and Arabs and ultra-Orthodox Jews on the other. Among non-ultra-Orthodox Jews, the increase in inequality within the higher-educated group and the increase in its proportion in the population and in income had a dominant effect.

c. Policy measures to reduce poverty and inequality

Government policy to deal with poverty and inequality include direct policies, through the distribution of allowances and other transfer payments, and indirect policies, such as measures designed to decrease poverty by expanding employment or increasing the wages of the working poor. During the last decade, the question of how to reduce poverty and inequality has been discussed by numerous committees and in various government and public forums. In addition to the recommendation of the various committees, position papers and statistical studies have been published by various bodies in Israel and abroad, among them the detailed report by the OECD, which Israel has recently become a member of.

Of the many recommendations made by the various committees, a few stand out as having a broad consensus behind them. First, it is agreed that it is worthwhile reducing poverty and inequality in Israel which are at high levels both in historical terms and in comparison to other OECD countries. Second, the relatively low rates of employment in Israel are one of the main causes of poverty and inequality and therefore the government should focus on reducing poverty by increasing employment and formulating a policy for allowances and taxes that does not affect the incentive to work. In addition, the various allowances and transfer payments should be available only to those who cannot earn a living on their own. Nonetheless, since being employed does not guarantee being above the poverty line, efforts should also be made to increase the incomes and earning power of low-paid workers (through an

During the last decade, inequality has mainly been affected by the increase in inequality within the working-age population, which was primarily the result of increased inequality between non-ultra-Orthodox Jews on the one hand and Arabs and ultra-Orthodox Jews on the other.

A reduction in poverty through an increase in employment must be accompanied by policy measures that improve the situation of workers with low earning ability.

Figure 8.6
The Gini Index by Groups—
The Contribution of Inter- and Intra-Group Inequality to Inequality within
the Whole Population^a
Selected Years

Gini index for the whole population		
Year	Gini index	Contribution of inter-group inequality to the general Gini index
1997	0.346	0.0872
2005	0.3769	0.0687
2009/10	0.3829	0.0618

Gini index for those aged 15–24		
Year	Gini index	Contribution to the general Gini index
1997	0.2991	0.0000
2005	0.2513	0.0000
2009/10	0.1915	0.0000

Gini index for those aged 25–64		
Year	Gini index	Contribution to the general Gini index
1997	0.3388	0.2466
2005	0.3726	0.2793
2009/10	0.3738	0.2868

Gini index for those aged 65+		
Year	Gini index	Contribution to the general Gini index
1997	0.3934	0.0026
2005	0.3938	0.0027
2009/10	0.4037	0.0027

Year	Contribution of inter-group inequality to the Gini index in the main working age groups:
1997	0.0912
2005	0.1234
2009/10	0.1328

Gini index among Arabs		
Year	Gini index	Contribution to the Gini index for those aged 25–64
1997	0.286	0.0053
2005	0.3425	0.0073
2009/10	0.3603	0.0079

Gini index among non-ultra-Orthodox Jews		
Year	Gini index	Contribution to the Gini index for those aged 25–64
1997	0.3169	0.2115
2005	0.3306	0.2113
2009/10	0.3312	0.2066

Gini index among ultra-Orthodox Jews		
Year	Gini index	Contribution to the Gini index for those aged 25–64
1997	0.2741	0.0004
2005	0.3327	0.0006
2009/10	0.3251	0.0008

Year	Contribution of inter-group inequality to the Gini index among non-ultra-Orthodox Jews in the main working age groups:
1997	0.1137
2005	0.1017
2009/10	0.1011

0–10 years of education		
Year	Gini index	Contribution to the Gini index among non-ultra-Orthodox Jews aged 25–64
1997	0.2945	0.0085
2005	0.3269	0.0035
2009/10	0.3205	0.0021

11–12 years of education		
Year	Gini index	Contribution to the Gini index among non-ultra-Orthodox Jews aged 25–64
1997	0.2853	0.0329
2005	0.3096	0.0268
2009/10	0.2982	0.0258

13+ years of education		
Year	Gini index	Contribution to the Gini index among non-ultra-Orthodox Jews aged 25–64
1997	0.2987	0.0701
2005	0.3088	0.1099
2009/10	0.3189	0.1227

^a The calculated Gini index is the Gini index of standard per capita disposable income (after direct taxes and transfer payments). Inequality is measured between individuals, and the characteristics are determined by those of the head of the household.
SOURCE: Based on Central Bureau of Statistics Income and Expenditure Surveys.

Table 8.8
Selected Years Main Policy Indices
(percent)

	2002	2004	2006	2008	2008/9 ^a	2009	2009/10 ^a
Contribution of transfer payments and direct taxes to the reduction of the incidence of poverty among individuals ^b	34.3	26.8	23.3	24.9	24.5	23.2	23.4
Share of welfare expenditure in GDP ^c	28.6	26.2	24.9	25.1	25.6	25.6	25.7
Welfare expenditure per capita ^c (NIS '000, at 2009 prices)	25.4	23.8	24.2	24.9	25.4	25.4	25.7
Share of transfer payments to households in GDP ^{c,d}	8.9	7.9	7.3	7.3	7.9	7.9	7.4
Transfer payments per capita ^{c,d}	7.9	7.1	7.0	7.2	7.8	7.8	7.4

^a Data for 2008/9 are based on a survey carried out between July 2008 and June 2009. Data for 2009/10 are based on a survey carried out between July 2009 and June 2010.

^b The contribution is calculated as the percentage difference between the incidence of poverty after deducting direct taxes and transfer payments and the incidence of poverty including them.

^c The figure for 2008/9 is for the whole of 2009, and the figure for 2009/10 is for the whole of 2010.

^d Transfer payments minus actual pension payments to public service pensioners.

SOURCE: Based on Central Bureau of Statistics Income and Expenditure Surveys.

earned income tax credit (EITC), more efficient enforcement of labor laws, assistance in training and placement, etc.). In addition, since the incidence of poverty and its intensity are particularly high among Arabs, the ultra-Orthodox and those with a low level of education, a policy should be adopted that can eliminate the disadvantages that characterize these populations.

The active policy measures for encouraging participation in the workforce are described at length in Chapter 5 of this report (The Labor Market). In general, it can be said that despite the increased scope of programs like these, the budget invested in them is small in comparison to other countries and their effect on employment remains limited.

Government policy regarding taxes and transfer payments has undergone radical change during the last two decades, which reduced its level of progressivity and its contribution to reducing poverty and inequality. Transfer payments, and in particular guaranteed income supplements and child allowances which are aimed primarily at the weak segments of the population, have been cut and at the same time statutory tax

Changes have been made in direct taxation and transfer payments which significantly reduce their progressivity.

rates have been reduced, which mainly benefited high-income earners.⁸ As a result of these policy measures, the level of government intervention, i.e. total transfer payments minus direct taxes relative to disposable income, is significantly lower than at the beginning of the decade (see Table 8.9).

The results of the changes in tax and transfer payments policy are also reflected in the large decline in the contribution of this policy to reducing poverty and inequality, which is measured by the difference between an index of poverty or inequality (the incidence of poverty or the Gini index, for example) calculated using economic income (total income not including transfer payments and taxes) and the same index calculated using net income (after the addition of transfer payments and the deduction of taxes).⁹

In 2010, the Government modified the socioeconomic targets it had adopted in 2007. The overall long-term goal for employment is to reach an employment rate among the 20–64 age group equal to the average of the 15 developed countries (defined according to GDP per capita), while reducing employment gaps between various segments of the population. The employment target for 2010–20 includes the minimal desired employment rates for various segments of the population, according to age and sector (for a full description of the employment target, see Government Decision 1994

Taxes and transfer payments are having less of an effect in reducing poverty and inequality.

In 2010, the Government changed the employment targets it adopted in 2007.

Table 8.9
Share of Government Intervention^a in Disposable Income, 2002-2009/10^a

Quintile	2002	2003	2004	2005	2006	2007	2008	2008/9	2009	2009/10
Lowest	56.5	53.5	49.1	47.2	45.6	42.6	42.5	42.4	42.4	42.9
2	29.5	29.7	27.4	27.5	25.9	23.7	24.1	24.6	25.3	26.6
3	4.5	5.7	5.5	3.9	5.0	3.5	4.4	5.7	6.6	5.9
4	-10.6	-9.4	-10.1	-8.8	-7.6	-9.0	-7.2	-5.8	-4.8	-4.7
Highest	-38.6	-33.0	-31.3	-28.9	-27.8	-29.9	-27.4	-24.7	-23.1	-24.0

^a Data based on a survey carried out between July 2009 and June 2010.

SOURCE: Based on Central Bureau of Statistics Income Surveys.

approved on July 15, 2010 and Chapter 5 in this report). The Government's decision did not relate to the income target that had been included in the Socioeconomic Agenda adopted in 2007 and in the State Budget for 2009–10. (According to this target, the

⁸ For a comprehensive survey of the changes in policy and their effect on income inequality, see Leah Ahdut, "The State Budget and inequality of income: Israel in the last two decades", draft for discussion, Seminar on the State Budget for 2010-11, Van Leer Institute, Program for the Economy and Society, May 2010.

⁹ This indicator does not take into account the effect of the tax and allowances system on the labor market and, through it, the indirect effect on poverty and inequality according to economic income. Therefore, if changes in the tax and allowances system have a positive effect on participation rates and employment, this indicator will underestimate the contribution of economic policy to the reduction in poverty and inequality and vice versa.

Figure 8.7a
Incidence of Relative Poverty among
Individuals and the Effect of Transfer
Payments and Direct Taxes,^{a,b}
1997 to 2009/10^c
(percent)

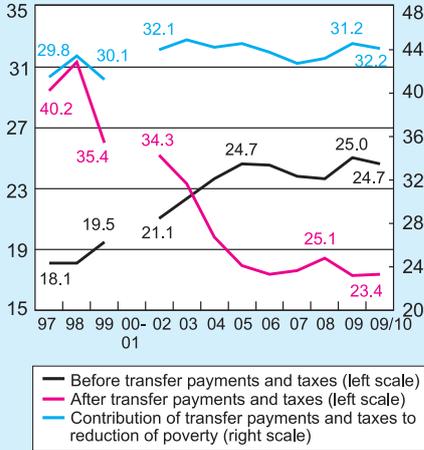
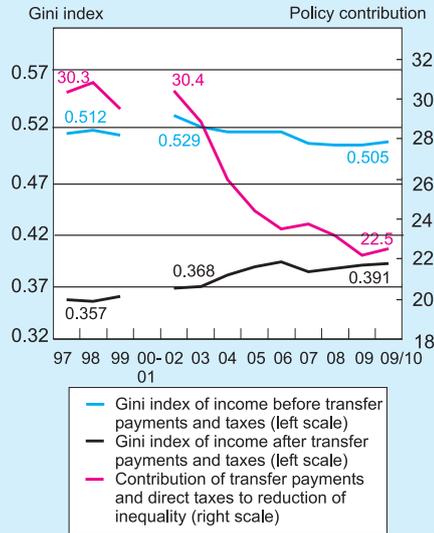


Figure 8.7b
Inequality and the Effect of
Transfer Payments and Direct
Taxes^a, 1997 to 2009/10^b



^A In 2000 and 2001, Arabs of Jerusalem were not included in income surveys and expenditure surveys. Those years were excluded from the figure so that the indices would be comparable.
^B Transfer payments from individuals and from abroad have not been deducted from disposable income; this causes a difference between data in the figure above and those of the National Insurance Institute.
^C The data are based on a survey conducted between July 2009 and June 2010.
 SOURCE: Based on Central Bureau of Statistics Income Surveys.

income of the lower quantile needs to grow by 10 percent more than GDP per capita.) In any case, the target was achieved in 2009, despite the increase in poverty, since gross income per family in the lower quantile rose, while GDP per capita fell. The increase in gross income per family was not the result of the change in the composition of the population in the lower quantile, which worked to lower gross income per standard individual, nor the changes in direct taxation that worked to lower disposable income per standard individual. Therefore, an absurd situation was created in which the target was achieved only because of the deterioration in the economic situation and despite the increase in poverty and the worsened situation of the weak segments of the population. An alternative target was suggested in June 2010 by the Committee to Examine Employment Policy, according to which the increase in the income of the lower quantile of households between 2010 and 2020 would exceed by 10 percent the increase in median income during those years. A proposed secondary target calls for an increase in the proportion of labor income in the total average income of the lower quantile from 47 percent (in 2008) to 60 percent in 2020. The employment targets proposed by the Committee were adopted in Government Decision 1994; however, as already mentioned, it did not include the income target.

An additional channel for government policy, apart from the direct policy of taxation and transfer payments and the active policy to encourage employment, is the adoption of measures to increase the earning ability of workers, particularly those at the bottom of the wage scale and on the margins of the labor market. These mainly include the EITC, the setting of an effective minimum wage, the enforcement of labor laws, reducing the number of foreign workers, reducing the scope of temporary work arrangements and other employment arrangements that are aimed at minimizing the responsibility of employers for their workers, etc. In the long run, there is a realization of the crucial importance of improving the public education system and increasing its efficiency, as a tool for increasing social mobility and narrowing gaps.

One of the most important and most efficient policy measures for dealing with the issue of the working poor has been the EITC, which has a positive effect on the welfare of working individuals. This policy improves the economic situation of households in which there are low-income earners and raises them above the poverty line. This is done by raising wages and therefore the incentive to work rather than relying on allowances. There is also added value in reducing poverty and increasing employment, as a result of the effect on the children of workers receiving the credit. Essentially, the EITC is one of very few policy measures that make it possible to increase the incomes and welfare of low-earning households without reducing the incentive to work or the demand for labor. Since it is focused on the weak segments of the population it can be used effectively to assist the working poor.

The EITC was introduced in a number of geographic areas in Israel in October 2008. The findings from its first year of operation indicate that it achieved impressive success. In those areas where it was introduced, the EITC raised about 4.5 percent of the credit recipients to above the poverty line, reduced the intensity of poverty and increased the labor income of the lowest quantile of credit recipients by 12 percent. On average, 45 percent of those eligible for the credit actually applied, which is relatively high in international terms and taking into consideration the early stage of the program and its relatively limited scope in Israel. The research team that monitored the program recommended that it be introduced nationwide and that the amount of the credit be increased.¹⁰

The nationwide implementation of the EITC is planned in 2012 for income earned in 2011. The EITC law specified that until its nationwide introduction the credit would be paid only in areas in which the Lights to Employment program is implemented (and nationwide for single-parent fathers with children up to two years old and mothers). As a result of the cancellation of the Lights to Employment program, in May 2010, it was decided that the credit would be paid only for the months January to April 2010 and not for the rest of 2010. This decision went against the declared goal of the Government to encourage participation in the labor market and it lowers the welfare of low-wage earners. It is also liable to disrupt the process to increase the percentage

¹⁰ “The Earned Income Tax Credit – results of the first year of implementation” (June 2010). Report of the research team monitoring the implementation of the EITC law.

The earned income tax credit is a focused and efficient way of dealing with poverty and inequality.

It is recommended that the earned income tax credit program be introduced nationwide and that the amount of the credit be increased.

of potential recipients that participate in the program, which according to the research team's findings is dependent on the size of the credit.

The setting of the minimum wage above the equilibrium level is another step aimed at raising the wages of workers at the bottom of the wage scale. These workers are characterized by a lack of experience, a low level of schooling and low learning ability. The Histadrut and the employers have recently agreed to raise the minimum wage to NIS 4300 and the Ministry of Finance and the Prime Minister have announced that they intend to apply this increase to workers in the public sector as well. However, in the public sector this will apply only to workers whose "true" wage is below the relevant level and the Histadrut has been invited to negotiations in order to consider the possibilities for implementation. According to simulations we carried out, the raising of the minimum wage will reduce the rate of poverty among the working poor by about one percentage point, which represents about 4.5 percent of the poor on average, assuming that compliance with the law and the rate of employment remain at their current levels. According to the same simulation, the raising of the minimum wage will have a larger effect on reducing poverty among individuals living in households with two income earners (since in most such poor households both of the income earners earn around the minimum wage). The effect of raising the minimum wage on the working poor is likely to be much larger if there is an improvement in enforcement; however, it is also liable to be much smaller, to the extent that it adversely affects employment. It should be mentioned that given the existing level of enforcement, raising the minimum wage is less efficient than the EITC in reducing the number of working poor, since it does not focus on the weaker segments of the population (due to the fact that a not insignificant proportion of those earning the minimum wage belong to the top quantiles according to disposable income per capita)¹¹ or on parents with children. Nonetheless, improved enforcement of the minimum wage is likely to significantly reduce poverty (to the extent that it does not have a negative effect on employment).

The Branch for the Enforcement of Labor Laws in the Ministry of Industry, Commerce and Employment was reinforced in 2007 following the State Comptroller's Report and the recommendation of the Steering Committee for the Enforcement of Labor Laws. The number of posts for inspectors was increased from 16 to 45 and in addition 57 students were hired as part-time employees. In total, the Branch has about 70 inspectors, which is equivalent to one inspector per 40 thousand workers, which compares to the international standard of one inspector per 10 thousand workers.¹² The Branch for Enforcement is making efforts to improve enforcement through initiated activities, cooperation with governmental and non-government bodies (such as the

The effect of the increase in the minimum wage on poverty is dependent on the level of enforcement and the extent of its effect on employment.

The enforcement of labor laws in Israel is relatively lax.

¹¹ In the breakdown of the population into quantiles according to disposable income per standard individual (total household income from all income earners and all sources of income divided by number of standard individuals in the household, according to the accepted scale of equivalence in Israel). About 10 percent of those earning the minimum wage belong to the upper quantile, about another 20 percent to the fourth quantile and about 30 percent to the middle quantile.

¹² OECD (2010): OECD Review of the Labor Market and Social Policies, Israel.

amendment to the Law of Tenders that requires those competing for tenders to present their record of compliance with the labor laws), etc.; however, its limited manpower is a significant constraint. The Branch for the Enforcement of Labor Laws estimates that the scope of violations is substantially higher than in other countries, which have not only more inspectors but also have a more deeply rooted culture of compliance with the law. In the absence of relevant data, it is difficult to estimate the scope of non-compliance with the labor laws; however, studies of the minimum wage laws indicate a very low rate of compliance.¹³

2. GAPS IN SCHOLASTIC ACHIEVEMENT AND AFFIRMATIVE ACTION POLICY IN PRIMARY EDUCATION

The allocation of resources to education has the potential to improve scholastic achievement and other educational outcomes and in the final analysis will contribute to strengthening the economic status of the individual and integrating him within modern society. Many studies have found a positive, though sometimes weak, link between inputs and outputs in education.¹⁴ The findings show that the inputs are more effective in improving output for pupils at a young age and from a relatively weak background.

Understanding the link between the allocation of resources and educational outcomes is particularly important in the case of Israel due to the large gaps in scholastic achievement according to school system (and in particular between the Jewish and Arab education systems) and socioeconomic background of the pupils, as can be seen in the results of both national and international examinations. These gaps emphasize the need for considering an affirmative action policy in the allocation of resources. Furthermore, one of the declared goals of the educational system is to bridge gaps in scholastic achievement while providing equal opportunity to individuals who are from a weak socioeconomic background and as a result are educationally disadvantaged.

In this section, we will focus on a short description of the gaps in educational achievement in Israel and the policy of affirmative action in the allocation of teachers' working hours in the primary schools, which are the main input in the education system.¹⁵

¹³ Tami Eliav, Miri Andveld, Daniel Gottlieb and Yisrael Vakchenovski (2009) "Trends of non-compliance with the minimum wage law: the case of Israel", The National Insurance Institute, the Department for Research and Planning, Study 99, June 2009.

¹⁴ This is partly due to the complexity of the teaching and learning processes and the difficulty in measuring the output of the education system. For surveys of the effects of inputs on outputs in education see:

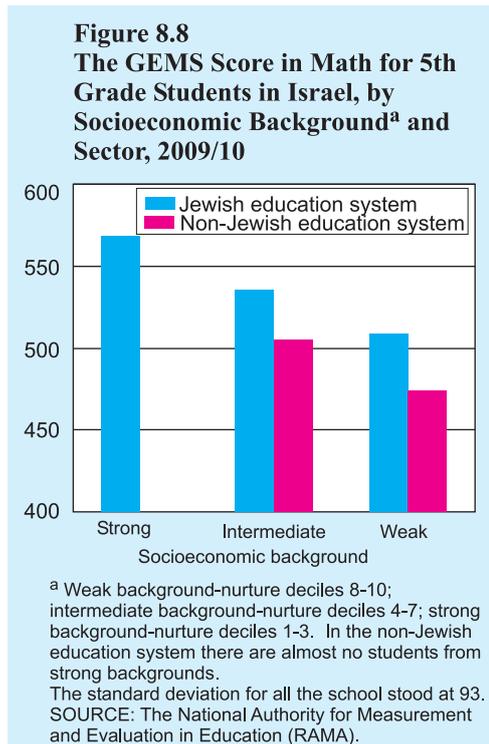
E.A. Hanushek (2006). "School Resources", in: E. Hanushek and F. Welch, *Handbook of the Economics of Education*, Vol. 2, Ch. 14, Elsevier B.V.

H. Holmlund, S. McNally and M. Viarengo (2010). "Does Money Matter for Schools?", *Economics of Education Review*, 29(6), 1154-1164.

¹⁵ A more detailed and comprehensive discussion of these issues can be found in the Bank of Israel Annual Report for 2004 and 2008.

There are significant differences in scholastic achievement according to pupils' socioeconomic background.

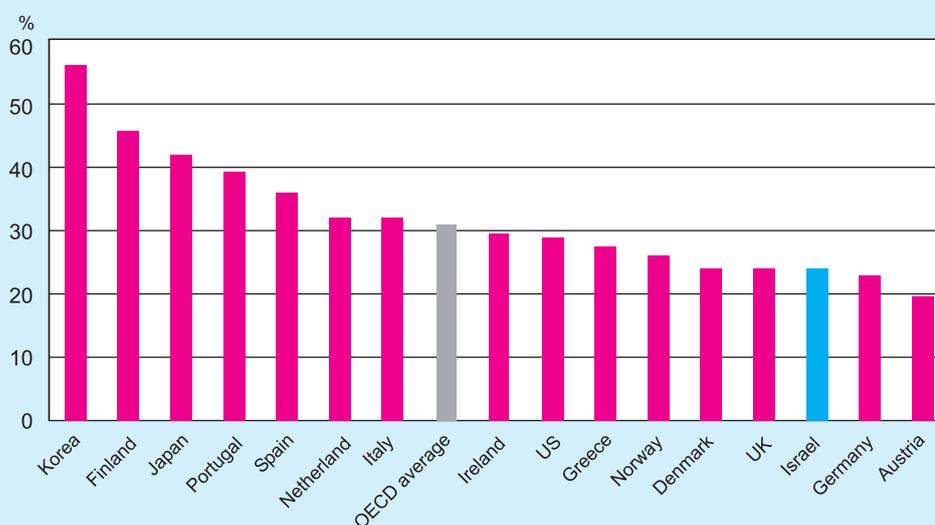
The rates of learning among children from weak backgrounds and Arab children in preschool education are much lower than those of other children. The gaps in educational achievements are already significant in primary school, which can be seen, for example, in the GEMS exam (abbreviation for Growth and Effectiveness Measures for Schools, Meitzav in Hebrew), which tests the pupils' knowledge and understanding in subjects that are viewed as the necessary toolbox for a graduate of the education system (Figure 8.8). The gaps in GEMS scores in the various subjects remain unchanged, and sometimes even widen, as a pupil moves from one grade to the next. The drop-out rates from school are higher among students from weak backgrounds and their matriculation scores are lower, both in terms of eligibility for a matriculation certificate and its quality. As a result, their possibilities are limited for being admitted to institutions of higher learning in general and into high-earning fields in particular.



The results on international exams in which Israeli pupils have participated (such as PISA and TIMSS) indicate that average scores in Israel (particularly in the Arab education system) are low relative to most OECD countries and that there is a high proportion of students with low levels of knowledge (and the achievements of these students also fall short in comparison to their counterparts in other countries). Furthermore, there are huge differences in achievement within a school and primarily between schools. These findings are not surprising considering the socioeconomic polarization in Israel and they reflect wide gaps in the ability of parents to provide their children with the assistance they need. In Israel, the correlation between socioeconomic background and achievement is stronger than in most OECD countries, which explains much of the variation between schools. Furthermore, a relatively small proportion of students from a weak background in Israel attain a level of achievement that exceeds to a large degree the level that would be expected according to their background (Figure 8.9). These findings may imply that the Israeli education system is less successful than those in other Western countries in eliminating the educational disadvantages of pupils from a weak socioeconomic background and in achieving equality of opportunity in education.

The correlation between socioeconomic background and educational achievement in Israel is stronger than in most OECD countries.

Figure 8.9
Share of Resilient Student in PISA 2009 Reading Test among Disadvantaged Students,^a Israel and OECD countries



^a Student (aged 15) in the bottom quarter of the PISA index of economics, social and cultural status (ESCS) in the country of assessment who perform in the top quarter across student from all countries after accounting for ESCS. SOURCE: OECD (2010). *PISA 2009 Results: Overcoming Social-Background - Equity in Learning Opportunities and Outcomes* (Volume II).

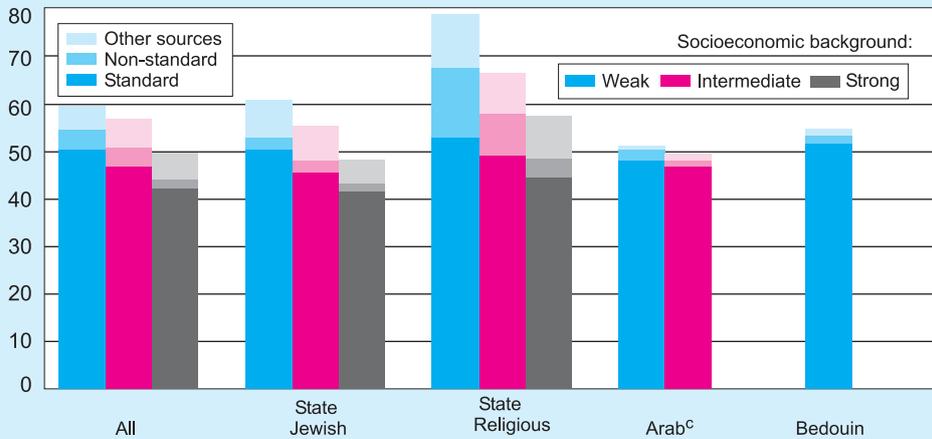
The education system has several channels for intervention in order to reduce inequality in education, one of which is affirmative action in the allocation of teachers' working hours to benefit students from weak backgrounds.¹⁶ We will focus on the allocation of hours to primary schools, through the analysis of data gathered by the Ministry of Education in a sample of schools (the "standard audit") which does not include the ultra-Orthodox education system and special education. The analysis examines standard hours which are the core hours allocated by the Ministry of Education according to clear and uniform rules; non-standard hours that are allocated by the Ministry of Education and other government ministries (such as hours provided by National Service girls/soldier teachers, tertiary education students tutoring pupils and a five-year program in the Arab sector); and hours from other sources (non-profit organizations, parents and local authorities).¹⁷

In 2007–8, the weaker a student's socioeconomic background, the more teachers' working hours per class (and per pupil) he received, within each education system

¹⁶ Only some of these hours are provided to home rooms; the rest are channeled to split classes and individual instruction and some to other uses such as duty hours. The analysis of working hours did not include support staff, such as secretaries, maintenance workers, etc.

¹⁷ This section is based on N. Balas, et al. (2010). *Budgeting of the Elementary School System 2001-9*, Bank of Israel, Research Division, Discussion Paper 18. It does not analyze in details the allocation of other sources, which is presented here for the first time.

Figure 8.10
Number of Weekly Hours per Class in Primary Education System^a according to Sector, Socioeconomic Background^b and Source of Funding, 2007/8



^a Regular official primary schools with Grades 1-6 only.
^b A weak background - Nurture deciles 8-10; intermediate background - Nurture deciles 4-7; strong background - Nurture deciles 1-3.
^c Including Druze (and Circassian). Does not include East Jerusalem.
 SOURCE: Idea - Economic Management & Consulting Ltd. and BOI calculations.

(Figure 8.10). However, given socioeconomic background, classes in the State Religious Jewish system benefited from many more hours than those in the State Jewish system and this was even more the case in comparison to the non-Jewish education system. This was due partly to the gender-separated classes in the State Religious system.¹⁸ In the allocation of standard hours, which account for more than four-fifths of total hours, a policy of affirmative action was adopted to some extent within each school system and there were no major differences in the allocation between school systems given socioeconomic background. In contrast, non-standard hours and hours from other sources went primarily to pupils in the Jewish education system, and the State Religious system in particular, while the number of these hours reaching the non-Jewish education system was negligible. As a result, these hours contributed to the gap in the allocation of hours between the various school systems, to the detriment in particular of pupils from weak socioeconomic backgrounds in the non-Jewish education system, who constitute the majority of pupils from weak backgrounds.

Teachers' working hours financed from other sources, i.e. non-profit organizations, parents and local authorities, constituted about one-tenth of total hours and the proportion provided by non-profit organizations stood at about two-thirds. The activity of non-profit organizations focused mainly on pupils in the Jewish education system, while their activity in the non-Jewish education system was negligible, and

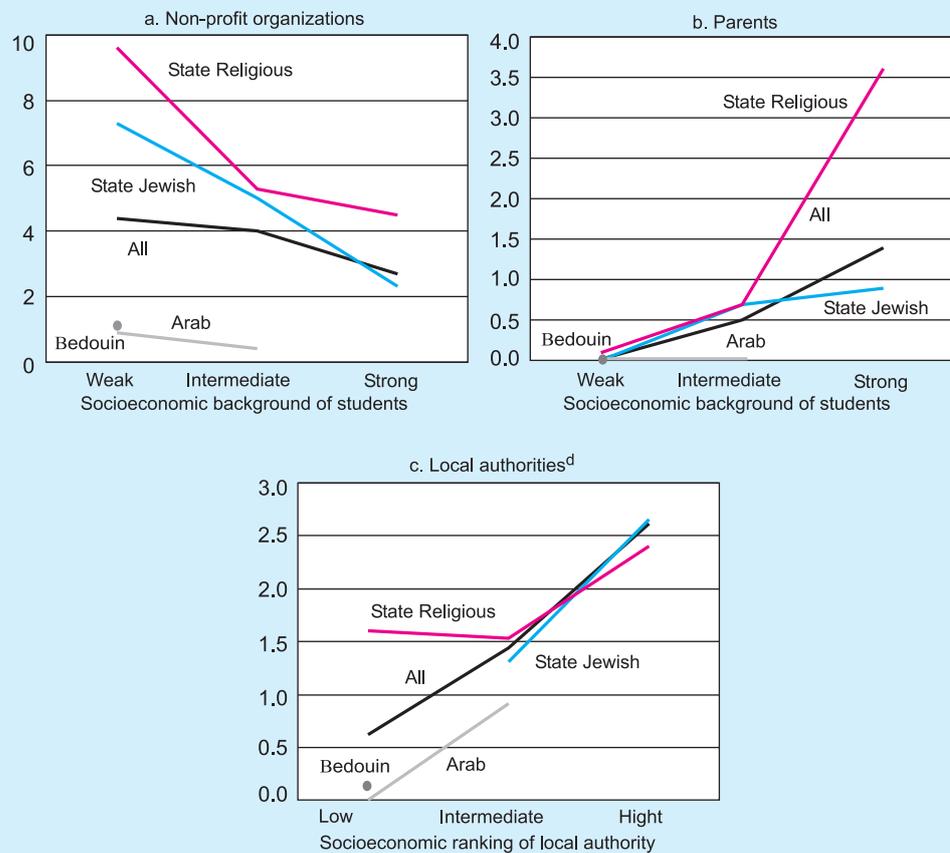
¹⁸ A student in the State Religious system also receives an addition 0.2 standard weekly hours for prayer (about 5 hours per class).

As part of the Ministry of Education's allocation of core teachers' working hours in primary education, preference is given to pupils from weak backgrounds in all the sectors.

The distribution of additional hours by the Ministry of Education and other sources (local authorities, non-profit organizations and parents) benefit mainly pupils in the Jewish education system.

they adopted a clear policy of affirmative action (Figure 8.11a). The participation of parents in the funding of teachers' working hours in the additional curriculum program (Talan in Hebrew) was particularly focused on the State Religious school system (perhaps due to the desire to meet religious needs) and was almost completely absent from the non-Jewish education system (Figure 8.11b). Parents' participation in funding was positively correlated with the parents' socioeconomic background, as

Figure 8.11
Number of Weekly Hours per Class in Primary Education System^a, Financed by Other Sources, According to Source of Funding, Sector^b and Socioeconomic Background,^c 2007/08

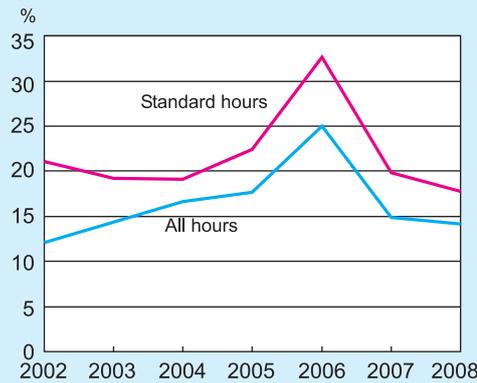


^a Regular official primary schools with Grades 1-6 only.
^b Arabs - Including Druze (and Circassian). Does not include East Jerusalem.
^c A weak background - Nurture deciles 8-10; intermediate background - Nurture deciles 4-7; strong background - Nurture deciles 1-3.
^d Socioeconomic ranking of local authorities in 2006, according to Central Bureau of statistics. Low - clusters 1-3; intermediate - clusters 4-7; high - clusters 8-10.
 SOURCE: Idea - Economic Management & Consulting Ltd. and BOI calculations.

expected.¹⁹ The local authorities funded many more teachers' working hours in the Jewish education system than in the non-Jewish education system (Figure 8.11c). The higher the socioeconomic ranking of a local authority, the more support it provides. This is primarily because weak local authorities (which include most of the non-Jewish local authorities), in which the residents are for the most part families with a weak socioeconomic status, find it difficult to support the local school system.

A significant step towards strengthening affirmative action in primary education was taken during the 2003–4 school year, with the start of the gradual transition to allocation of standard hours per student rather than per class, together with an updating of the allocation formula in the spirit of the Shoshani Report (August 2002). This involved the definition of an educational disadvantage index on the level of the student (the Nurture Index) for the purpose of calculating the differential allocation per pupil, which took into account socioeconomic background. Following the implementation of the report, the number of standard hours provided per class (and per student) grew significantly in the non-Jewish education system, where classes are more crowded and pupils are from relatively weaker backgrounds; however, the gap remained significant. Affirmative action to benefit pupils from a weak socioeconomic background was expanded to a large extent with the implementation of the report (Figure 8.12); however with the transition to budgeting using a combined standard, with the start of the implementation of the Strauss Report in the 2007–08 school year, affirmative action policy was reduced in scope. This as due to the guarantee of a minimum number of hours per class (36) in order to, among other things, ensure the implementation of the required curriculum, which left only a few hours (about 5 percent)

Figure 8.12
The Gap in Number of Weekly Standard Hours per Class in the Primary Education System^a between Students from a Weak vs. a Strong Socioeconomic Background,^b 2001/2 to 2008/9^c



^a Regular official primary schools with Grades 1-6 only.
^b A weak background - Nurture deciles 9-10 (higher quintile); A strong background - Nurture deciles 1-2 (lowest quintile).
^c 2000/1 was omitted from the graphs due to the small number of observations in each quintile.
 SOURCE: Idea - Economic Management & Consulting Ltd. and BOI calculations.

Affirmative action in the allocation of core hours has been reduced in scope since the 2007–8 school year with the transition to the new budgeting method.

¹⁹ Payments by parents in the upper quantile of family income per capita for a child in primary school in 2003 were more than twice the size of payments by parents in the lower quantile. In total, the expenditure on education per child in primary school in the upper quantile was five times higher than in the lower quantile. (H. Heller et al. [2007]. Public and Private Expenditure on Education for Pupils in Primary Education in Israel, 2003, Central Bureau of Statistics, special publication 1303).

for distribution according to the new Nurture Index, which had been recommended by the Strauss Report.²⁰

It would be worthwhile increasing the number of teachers' working hours allocated to affirmative action in primary education.

Therefore, it would be worthwhile increasing the number of teaching hours allocated to affirmative action in the primary education system by allocating hours beyond the minimum to a class according the new Nurture Index, in which the connection between a student's educational disadvantages and the quota of hours he is provided with is stronger than in the Shoshani index. On the assumption that there is a desire to reach the level of affirmative action that prevailed prior to the implementation of the Strauss Report, additional sources are needed in an amount estimated at hundreds of millions of shekels per year. This funding can come from an increase in the Ministry of Education budget and/or from internal shifts in the budget (see the Bank of Israel Annual Report for 2008, Chapter 8). In any case, consideration should also be given to the allocation of teachers' working hours in the junior high schools and high schools according to the new Nurture Index since the current scope of affirmative action in these systems is negligible.

²⁰ An additional step to reinforce affirmative action was taken as part of the implementation of the New Horizon program in the primary schools, starting in the 2007-8 school year. Thus, teachers were added five individual working hours, which could be used for tutoring of weak students. Nonetheless, in the primary education system most of the heterogeneity due to socioeconomic background is, as mentioned, between schools rather within schools. Thus the contribution of individual hours to reducing gaps in educational achievement throughout the country is limited.