11

Economic Relations Between Israel and the United States

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Introduction

The Israeli economy has been outperforming the expectations of its skeptics over the last few years (see Table 11.1). Economic growth has been at record levels, relative to both the recent past and the performance of other advanced economies. Inflation is on a downward path and the government budget is moving into balance. Unemployment, while still quite high, has been stable, given the large increase in working-age former Soviet Jews. And in spite of criticism over delays in privatizing large public enterprises, the government has moved forward in liberalizing the capital market and removing trade barriers.

Since its establishment in 1948, Israel has benefited greatly from economic relations with the United States, which have been dominated by financial assistance. In recent years economic exchanges between the United States and Israel have intensified, matured, and become more balanced, growing from less than $1 billion in 1970 to almost $11 billion in 1990 (see Table 11.2).[1] There has been an increase in financial assistance, trade in goods, investment flows, and technology exchanges, independent of political developments. In addition to these four areas, there is now evidence that Israel might also be importing U.S. economic policies.

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TABLE 11.1 Indicators of the Israeli Economy (percentage annual change, unless otherwise specified)

	1990	1991	1992	1993 Estimate	1994 Forecast	Amount in 1992
Gross domestic product (GDP)	5.8	6.2	6.6	3.5	5.5	$58.9 billion
GDP per capita	0.6	0.8	3.0	8.0	2.8	$11,277
Exports of goods and services	2.5	−1.5	14.4	10.3	9.0	$18.3 billion
Imports of goods and services (civilian)	8.3	15.4	13.0	10.0	6.4	$24.7 billion
Investment in fixed assets	22.4	48.1	4.9	−5.0	10.9	$13.7 billion
Immigration (in thousands)	200	176	77	80	80	
Population	3.1	6.1	3.5	2.7	2.6	5.2 million
Unemployment rate	9.6	10.6	11.2	10.2	9.4	208,000
Consumer price index	17.6	18.0	9.4	10.5	9.0	
Budget deficit, excluding credit (percent of GDP)	5.0	6.4	4.9	3.2	3.0	$2.9 billion

Source: "Bank Hapoalim Economic Report," Bank Hapoalim, Issue 49, November 1, 1993.

Financial Assistance

U.S. economic assistance to Israel began with small grants between 1952 and 1955 and expanded over the next ten years to include Export-Import, Food for Peace, and general economic loans. It was not until after the Six Day War in 1967 that the United States began providing Israel with military loans on an annual basis. These loans totaled $250 million through the 1960s. The 1973 Yom Kippur War served as another watershed for military assistance to Israel, beginning with $1.5 billion in military grants and almost $1 billion in military loans in 1974. Over the next ten years the United States provided $6.4 billion in military grants and $8.8 billion in military loans. In 1981 grants replaced loans for economic assistance, and in 1984, with the prospect of Israel having to begin repaying past military loans, the United States restructured its military assistance to Israel also from loans to grants. Aid throughout the rest of the decade leveled off at $1.8 billion in military grants and $1.2 billion in economic grants annually.

Israel has been receiving the largest share of annual U.S. financial assistance since 1976.[2] There are several other unique aspects of assistance to Israel. Economic assistance, which until 1979 was focused on agricultural and food programs, can be used with few conditions for general budgetary support. In 1987, the U.S. Congress passed a provision allowing countries such as Israel to refinance outstanding military debts, carrying interest rates over 10 percent, in the commercial market, guaranteed by the U.S. government. Israel currently owes the United States approximately $4.3 billion in direct economic and military loans and another $5 billion in guaranteed commercial loans. The United States has never canceled any of Israel's official debts, but it has waived repayment of some loans, as it has recently chosen to do for Egypt and Jordan. Another unique aspect of U.S. aid to Israel is that a significant amount of it is used to purchase military items produced in the United States. This is a clear case in which foreign aid cre-

TABLE 11.2 U.S.-Israel Economic Relations: U.S. Financial Assistance and Bilateral Trade and Investment (in millions of U.S. $)

	1960	1965	1970	1975	1980	1985	1990
U.S. grants to Israel	13	5	13	507	1,025	3,350	2,987
U.S. loans to Israel	43	60	81	271	760	0	0
U.S. exports to Israel			430	999	1,549	1,679	2,726
U.S. imports from Israel			186	308	954	2,138	3,489
U.S. investment in Israel	NA	64	84	211	379	717	756
Israeli investment in U.S.	NA	NA	NA	NA	324	494	626
TOTAL			794	2,296	4,991	8,378	10,584

Sources: U.S. Department of State, U.S. Department of Commerce (various publications).

ates jobs in the donor country. Given this feature, the total amount of aid actually overstates its contribution to the Israeli economy. In fact, only a small percentage of the military grants are spent in Israel and the vast majority of the economic grant aid is devoted to servicing loans used to finance past weapon sales.

Since 1974 U.S. aid to Israel has been directly and indirectly linked to Israel's national security needs. Military grants have financed the vast majority of the increase in Israeli military spending over the period. Economic assistance has basically been tied to repaying the United States for military loans prior to 1984. The Cranston Amendment, appended to foreign aid legislation since 1984, states that it is U.S. "policy and intention" to provide Israel with economic assistance "not less than" the amount it owes the United States in annual debt service payments (principal and interest). This provision does not bind the government, but aid levels have conformed to this intention since 1984.

Although the United States has been the largest donor of financial aid to Israel, it was not until 1986, when in conjunction with providing $1.5 billion in supplemental assistance in support of the Emergency Stabilization Program in 1986, that the United States began providing Israel with economic advice through the Joint Economic Development Group (JEDG). Secretary of State George Shultz, an internationally renowned economist in his own right, personally supervised this effort to encourage Israel to introduce market-oriented reforms and begin the process of reducing its dependence on U.S. aid. It is true that the United States encourages economic reforms in many countries, but the extent of its involvement in promoting and monitoring economic reform in Israel is unique.

Given the economic and political realities of the day and despite the favorable treatment through the 1980s, by the end of the decade, Israeli officials realized that it was unrealistic to depend on the United States to meet all of Israel's economic needs. However, conditions in Ethiopia and reforms in the Soviet Union suggested that Israel had to be prepared to face huge financial burdens in absorbing new refugees. In addition, the government realized that it would need large amounts of foreign capital to help finance economic reforms that had been under way, albeit at a slow pace, since 1986. Based on these considerations, the Israeli government decided in 1990 to request U.S. government guarantees of $10 billion in commercial loans over a five-year period. It was clear that Israel needed access to more capital, and the fact that these would be commercial loans would mollify those concerned about Israel's dependence on U.S. aid.

Israel's interest in pursuing the idea of the loan guarantees was delayed by the Gulf War, and the official request was not made until September 1991. President Bush asked Congress to delay consideration of Israel's request until January 1992, arguing that it would jeopardize his administration's efforts to convene a Middle East peace conference. The administration changed its position and conditioned its support for the loan guarantees on Israel's freezing of all settlement activity in the West Bank and the Gaza Strip. After the June 1992 Israeli election, when Yitzhak Rabin and the Labor party assumed control of the Knesset and the government and introduced a limited freeze on settlements in the territories, President Bush announced that he would support loan guarantees for Israel. Title VI P.L. 102–391 was signed on October 6, 1992.

In sum, the United States has played several different roles in providing financial assistance to Israel. At the beginning, it provided Israel primarily humanitarian aid. Following the 1967 war, the United States began treating Israel as a strategic ally and aid grew in size and nature, moving from humanitarian and economic assistance to military assistance as well. During the 1980s the U.S. role took on another dimension, and the United States became Israel's "lender of last resort," providing emergency economic and humanitarian assistance and guaranteeing private loans. There is growing concern that this aid distorts market incentives in the Israeli economy, and the United States has taken an interest in promoting market-oriented reforms. Budgetary pressures have heightened interest in weaning Israel from U.S. aid, as it is apparent that large aid flows to Israel are not in the long-term interests of either country.

Trade

Israel has been cut off from commercial relations with its neighbors as a result of the Arab boycott. As part of the boycott, Arab countries refuse to buy any products made in Israel or produced with any inputs produced in Israel. Given its need for trade because of a lack of natural resources, Israel has followed a policy of securing access to European and U.S. markets. In addition to economic certainty, these markets provided commercial demands that permitted Israel to move up the "industrial ladder," from agricultural goods to technology-intensive manufactured goods.

The most important factor contributing to the increase in U.S.-Israeli economic ties since 1984 is merchandise trade. Total bilateral trade between the two countries doubled from $3.4 billion in 1984 to $7.8 billion in 1992, accounting for more than half of all economic flows between Israel and the United States. Given the relative sizes of the two economies, this trade in aggregate is certainly more important to Israel than to the United States.

U.S. products have consistently amounted to approximately 20 percent of all Israeli imports. U.S. exports to Israel in 1992 were valued at $4 billion, of which half were concentrated in machinery and transport equipment, including aircraft and equipment, telecommunications equipment, automatic data processing machinery, and measuring and controlling instruments. On the Israeli export side, the United States has become an important market for Israeli goods. During the 1970s the U.S. market accounted for less than 10 percent of Israeli exports. U.S. purchases of Israeli products have grown over the past two decades, and the U.S. market now accounts for almost a third of all Israeli exports.

The United States imported $3.8 billion in Israeli goods in 1992, almost all of which was manufactured goods. The top U.S. imports of Israeli goods include cut diamonds and jewelry, aircraft and equipment, telecommunications equipment, optical and medical equipment, parts for office machinery and automatic data processing machinery, and scientific and measuring instruments. Relative to its other markets, the United States currently purchases 40 percent of Israel's machinery and mechanical appliance exports and over a third of Israel's optical, photographic, medical, and measuring devices exports.

Several political developments explain the expansion in U.S.-Israeli trade in recent years. Most important, in 1985 the United States and Israel signed the Free Trade Area Agreement (FTA). Israel saw it as a means of locking in and expanding preferential access to the U.S. market, which it had been afforded under the Generalized System of Preferences (GSP). In addition to other political reasons, the United States wanted to ensure its own access to the Israeli market, as Israel had already signed a similar bilateral free trade agreement with the European Community (EC) in 1975. The FTA brought tariffs down in both countries and promoted more trade, but there is still no guarantee that both countries will reach the ultimate goal of totally duty-free bilateral trade by 1995.

U.S.-Israeli trade promises to continue to be important, but significant future growth in Israeli trade is most likely to be associated with the emerging markets in Eastern Europe and the Far East. Israeli trade policy has already shifted attention, focusing on unilaterally removing import barriers to goods from countries other than the United States or EU members. Excitement over the U.S.-Israeli FTA has dissipated, and both countries have shown very little enthusiasm for negotiating the removal of tariffs on the most highly import sensitive products. These negotiations were to begin in 1990, and tariff reductions were to be phased in by 1995. Both the United States and Israel have yet to agree on the list of products to be discussed, let alone any timetable for phasing out tariffs. Initial interest in extending the original FTA to include trade in services is also now history, given U.S. attention to the North American Free Trade Agreement (NAFTA) and the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) talks.

Trade is a primary example of how Israeli economic relations grow out of political relations but then take on an independent status. The FTA was clearly motivated by political factors, and the agreement has now opened the Israeli market to American products, enabling U.S. exports to almost double between 1985 and

1991. Even though Israeli products already received preferential access to the U.S. market through the GSP, prior to the FTA, Israeli exports to the United States still grew by $1.5 billion between 1985 and 1991. Political attention may have turned elsewhere, but business interests will continue to follow markets, especially the newly opened markets in the United States and Israel.

Foreign Investment

Foreign investment is one area that has not fully developed in the bilateral relationship. The value of U.S. investment in Israel averaged about $600 million during the 1980s and has risen to more than $700 million over the past few years. In spite of Israel's policy of encouraging foreign investment, there are numerous barriers to such investment in Israel, the most significant being the secondary Arab boycott. In addition to the direct boycott of Israeli products, the secondary boycott is aimed against any country that has commercial relations with or invests in Israel, including foreign investment. In addition to the boycott, national security concerns and restrictive bureaucratic business regulations have also deterred investment. There is growing awareness in Israel that the country needs foreign private capital in order to return to pre-1967 economic growth rates. Various governments have attempted to reduce the bureaucratic barriers since 1986. The greatest achievement has been reform of the capital market, including the removal of foreign capital controls. Economic stability since 1986 has also improved the investment environment in Israel.

Bilateral foreign direct investment flows are small in both absolute terms and relative to other U.S.-Israeli economic flows; thus they do not warrant too much attention here. One important explanation for the fact that Israeli investment in the United States is larger than its reciprocal is that U.S. barriers to foreign investment are much lower than those in Israel. In addition, the United States is seen as a much "safer" place to invest, although commercial investment in Israel may in fact have a higher economic return. Overall, Israel is not an important player in foreign investment in the United States.

Technology Partnerships

Both the U.S. and Israeli economies support technologically advanced industries. In the case of the United States, this is primarily the result of large investments in research and development. Israel's highly skilled labor force has promoted the country's membership among the world's advanced-technology countries. Bilateral technological exchange is a natural outgrowth of these factors. This is one area in which economic relations between the United States and Israel can be characterized as "cooperative" and balanced, which is unique given the differences in the two countries' size and available resources.

The Israel-U.S. Binational Industrial Research and Development Foundation (BIRD), founded in 1977, is at the center of technological cooperation between the two countries. With an original endowment of $110 million, cofinanced equally by the United States and Israel, BIRD was established "to promote and support joint, nondefense, industrial research and development activities of mutual benefit to the private sectors of the two countries." Using the interest on the initial endowment, the foundation provides matching funds to projects bringing together U.S. and Israeli companies for the purpose of developing and commercializing innovative, nondefense, high-technology products and processes. Since its inception, BIRD has invested close to $100 million in over 300 projects, 175 of which have already led to more than $3 billion in sales. These projects have produced five U.S. jobs for every one Israeli job created. About half of all projects initiated within the past few years have been between companies brought together by BIRD. The foundation is viewed by both the United States and Israel as a prime example of the benefits for both countries when they enter into cooperative arrangements.

The Binational Science Foundation (BSF) and the Binational Agricultural Research and Development Fund (BARD) are two other examples of U.S.-Israeli cooperation. BSF, founded in 1972, grants funds to support research in the natural and applied sciences, including agriculture, health sciences, and technologies of broad interest to both countries, such as mass transportation, energy, and environmental research. BARD, like BIRD, founded in 1977 as an endowment fund of $110 million, awards grants for cooperative research projects that include active collaboration between Israeli and American scientists.

Building on these successes, President Clinton and Prime Minister Rabin announced on March 15, 1993, the establishment of a U.S.-Israel Science and Technology Commission aimed at increasing cooperation in science, technology, and defense conversion programs. This new commission is expected to encourage joint ventures in areas in which Israeli scientists, especially those from the former Soviet Union, have demonstrated expertise.

"Rabinomics"—Putting Clintonomics into Practice

U.S.-Israeli economic relations have recently broadened beyond the traditional aid, trade, investment, and technology flows. It seems that Yitzhak Rabin has been benefiting from U.S. economic policies by borrowing a page from Bill Clinton's economic strategy book.

Two notions characterize economic policymaking in Israel. The first is that although Israeli public debate is dominated by national security issues, economic concerns have played a significant role in the outcomes of four of the last five elections.[3] Second, all but one of Israel's prime ministers have seemed to observe an unstated tradition of lack of interest in economic matters, in spite of the fact that recent developments have forced Israel's leaders to become more sensitive to economic issues.[4]

Yitzhak Rabin's administration has not proven to be much different than preceding administrations with respect to these two notions. To begin with, even though the 1992 election focused on addressing the Israeli-Palestinian conflict, in the end, both Prime Minister Shamir and candidate Yitzhak Rabin were also judged on their ability to address Israel's pressing economic problems. Many people felt that the Shamir government was not moving aggressively enough in absorbing the flood of immigrants from the former Soviet Union, thereby causing severe pressure on the economy. Interestingly enough, Yitzhak Rabin, like most of his predecessors, did not have any particular expertise in economic issues, but he was viewed by the electorate as being more capable of helping the economy. Rabin was successful in "taking" the economic issue away from Shamir, which helped him win the election.

The economic themes of Rabin's campaign in early 1992 were very similar to those espoused by Bill Clinton in the United States later that year. Both candidates focused on the importance of increasing public investment in human and physical capital, including education, training, technology, and infrastructure. This strategy proved as successful for Yitzhak Rabin as it did for Bill Clinton.

In actuality, Rabin inherited an economy very much on the mend. Long-term structural improvements in the economy resulting from the 1985 stabilization program were firmly in place. The number of new immigrants had fallen and the initial public resource–intensive stage of the absorption of the half million Jews from the former Soviet Union had already taken place. The immigrants were also beginning to make their own contributions, starting the process of reversing their net drag on the economy.

The Israeli economy grew by 6.6 percent in 1992, the highest growth rate of any industrialized country that year, and close to 4 percent in 1993. Inflation fell below 10 percent in 1992, for the first time since the 1970s, and was expected to rise less than one percentage point in 1993. Unemployment has been falling steadily, from close to 12 percent in the beginning of 1992 to approximately 10 percent by the end of 1993. Israel managed to create a quarter of a million jobs in 1993, quite an achievement, but still not enough jobs to absorb all the talent of the recent immigrants and the young new entrants into the labor force.

There are numerous similarities and differences between the U.S. and Israeli economies. Notwithstanding these differences, it is interesting to note that both Governor Bill Clinton and Yitzhak Rabin shared a similar economic strategy during their respective campaigns. Given this similarity in strategy, it is interesting to compare the actual records of both leaders.[5]

Focusing on the domestic economy and the need to create jobs and raise incomes proved to be a successful election strategy for both Rabin and Clinton. However, Prime Minister Rabin seems to be more successful than his colleague President Clinton in translating these campaign themes into actual policies.[6] Probably the best exposition of the Clinton campaign's economic strategy was put forward in *Putting People First,* written by Bill Clinton and Al Gore when they were governor and senator respectively. This strategy had five components: (1) putting the American people to work, (2) rewarding work, (3) supporting lifelong learning, (4) providing affordable quality health care, and (5) revolutionizing government. The plan called for investing $50 billion per year (approximately 1 percent of GDP) while cutting the federal budget deficit in half (from 5 percent to 2.5 percent of GDP) by 1996.

In the absence of any similar document by Yitzhak Rabin, the following is a review of economic achievements of the first year of the Rabin government. It is based on the goals set out by President Clinton during his campaign.

Putting People First: The Israeli Version

The Clinton plan called for several approaches to "reward people who work hard creating new jobs, starting new businesses, and investing in our people and our plants here at home." Rabin has also concentrated on "investing in people," focusing on education reform and investment in public infrastructure and technology.

Favorable economic conditions enabled the Rabin government to enact some tax-policy changes aimed at reducing the cost of creating jobs. The payroll tax on businesses was removed and there was a two-percentage-point reduction in the employers' national insurance contribution (similar to U.S. Social Security). There has also been some discussion of reducing the corporate tax rate.

Under the rubric "Rebuild America," Governor Clinton's plan envisioned the renovation of transportation systems, the establishment of an information network, the development of environmental technologies—all accomplished with economic resources that had been freed up by defense conversion. Like the United States, Israel is also in the process of converting defense resources to civilian purposes. Defense purchases constituted between 12 and 14 percent of GDP from 1981 to 1985. Against the backdrop of the end of the Lebanon war and rising domestic economic pressures, Prime Minister Shimon Peres and Defense Minister Yitzhak Rabin began Israel's own defense conversion in 1985. Prime Ministers Shamir and Rabin have both maintained this policy, and defense purchases have continued to fall steadily since 1985, to approximately 8 percent of GDP in 1993. Defense conversion in Israel has placed additional pressure on the labor market, as it attempts to absorb the recent immigrants and young entrants into the labor force.

Investing in Israelis

Prime Minister Yitzhak Rabin focused much attention on the need to build and maintain Israel's physical infrastructure, and his budget reflects this shift in priorities. Investment in fixed assets rose by 22 percent and 48 percent in 1990 and 1991 respectively, primarily as a result of construction to house the massive inflow of immigrants from the former Soviet Union. The decline in the number of new immigrants caused investment in residential construction to flatten in 1992 and fall 30 percent in 1993. Nonresidential construction rose by more than 10 percent in 1992 and 1993. Investment in machinery and equipment grew by over 5 percent in both years. Much of this investment is either directly financed or indirectly encouraged by the Israeli government. As evidence, the 1993 budget called for a 30 percent expansion in the capital budget, in particular for road construction and education.

The Clinton campaign called for encouraging private investment through targeted investment tax credit, tax incentives for small businesses, and a permanent R & D tax credit. The structure of Israel's tax system already serves to encourage investment rather than consumption. The primary mechanism for collecting government revenue is the value-added tax (VAT), which is applied to almost all products sold in Israel. The VAT was reduced from 18 to 17 percent in 1993. Israel does not tax capital gains; thus this disincentive to investment is absent. In addition, there was a 50 percent increase in accelerated capital depreciation allowances in 1993. The Israeli government also encourages research and development through direct grants and subsidies.

Opening up world markets to exports was a central theme in candidate Clinton's trade policy. Israel's efforts toward opening world markets to its goods in exchange for opening its markets to foreign goods began several years ago. Israel is a signatory to free trade agreements with the European Community (1975) and the United States (1985). The EC-Israel agreement has recently been extended to include the countries of the European Free Trade Area (EFTA). In addition, Israel has unilaterally converted its remaining import restrictions—primarily licensing requirements—for countries other than the United States and European Community (now European Union) members ("third" countries) into tariffs, with a commitment to phase them out by the year 2000. All these decisions predate the current government, but Prime Minister Rabin appears to be committed to them.

Another important ingredient of Governor Clinton's strategy of investing in people was a system of lifetime learning. This includes reforming basic education, creating new programs to assist the transition from school to work, improving worker training, and consolidating and expanding programs for displaced workers.

There was also considerable debate over education reform during Prime Minister Rabin's first year in office. Two issues dominated the debate: length of the school day and control over the curriculum. One of the by-products of Israel's party electoral system is that in the past small religious parties were granted control of the country's education system in return for their participation in successive coalition governments. Many believe that as a result of their control, the quality of the country's nonreligious schools was compromised.

In forming his government, Yitzhak Rabin transferred the responsibility of the nation's education system to the Citizens' Rights Movement (CRM), predominantly composed of liberal, secular Israelis. Under the new leadership, one of the first actions was to extend the school day. Lengthening the school day meant increasing teacher salaries, which was achieved after a rather unpleasant strike. There have also been several changes to the curriculum, which have raised the ire of the religious community, cost the job of one education minister, and almost brought down the government. In all, education reform is gaining public attention, and some small steps have been taken to improve the quality of education students receive.

In the area of worker training, many Israelis already have access to something similar to an "individual training account." Workers and employers make regular contributions, and after a certain period, workers can begin to use this money, within certain restrictions, to improve their skills. The government also has a program of wage subsidies to encourage employment of certain segments of the economy. The Rabin government has not introduced any new initiatives in this area, although the Israeli social safety net is already rather tightly woven.

One of President Clinton's top concerns is health care reform. Interestingly enough, the Clinton reform proposal incorporates many of the aspects of Israel's current health care system. The Israeli system is based on an assortment of "sick funds," and every citizen joins one. Each fund offers a basic coverage plan and operates very similarly to a health maintenance organization. Individuals can supplement this coverage at their own expense. Government subsidies to the sick funds, as well as to individuals for their membership fees, account for about half of the nation's total health bill.[7]

At the same time that the United States is attempting to move toward the Israeli system, Israel is trying to move in the direction of the U.S. system. Government subsidies have removed any incentives for the sick funds to be run efficiently. Medical personnel are frequently involved in labor disputes over wages and hours, and a two-tier system of health care has evolved. Israeli reformers want to move more of the health system into the private sector.

Israel's health care system already meets many of the criteria set out by President Clinton. There is universal coverage, provided in large part by "managed care networks," which offer a core benefit package. The great missing link is the absence of a cap on national health care spending, which is where the Israeli system serves as an ominous lesson to U.S. reform efforts.

The last area of Governor Clinton's campaign strategy was "reinventing government." Here too, the Rabin government has taken the lead in translating campaign rhetoric into policy. Near the end of the Shamir government term, the Knesset passed a bill similar to the Gramm-Rudman Amendment, fixing the path of the government's budget deficit, which was planned to reach zero in 1995.[8] The Rabin government weakened the existing targets, requiring only that the deficit as a percent of GDP fall each year and removed the zero target date. The government, however, introduced multiple-year budgets, further encouraging the shift in spending priorities toward investment and away from consumption and entitlements. The budget deficit fell to approximately 3 percent in 1993 (see Table 11.2), down from almost 5 percent in 1992.[9]

Conclusion

Prime Minister Rabin has had relative success in implementing policies consistent with his campaign promises of increasing investment in physical and human capital and removing barriers to job creation and economic growth. Although he was afforded a favorable starting point, Prime Minister Rabin has been able to achieve many of his stated goals. The critical test will be whether he can convert the current economic upturn into long-term improvements in the standard of living for all Israelis. There is no doubt that his peace efforts with Yasser Arafat and King Hussein have already won him a place in history. This is also a critical time for the Israeli economy, and if Prime Minister Rabin can navigate the economy through its ups and downs, then he may also secure a place in Israel's economic history. There is currently quite a void there.

Notes

1. Several caveats should be kept in mind in analyzing these data. First, unilateral financial assistance is qualitatively different from trade and investment flows. Second, exports and imports are added in this case to measure the value of total bilateral trade flows. Third, investment data represent the value of investment in a given year, not the change from year to year and therefore are not exactly comparable to the aid and trade data.

2. In 1990, Israel accounted for 37 percent of U.S. military assistance and 17 percent of U.S. economic assistance. Other significant recipients included Egypt ($2.2 billion), Turkey ($515 million), and Greece ($349 million). Together, these four countries accounted for half of all U.S. military and economic assistance in 1990.

3. The Begin election in 1977, the election in 1984 that led to a Likud-dominated National Unity government, the Shamir election in 1988, and the Rabin election in 1992.

4. Shimon Peres is the only prime minister who not only took a deep interest in the Israeli economy but also concentrated during most of his term in office (1984 to 1986) on addressing critical economic issues.

5. Israel faces two challenges that the United States does not: absorbing a half million new immigrants and continuing the process of economic liberalization begun in 1985. However, both the United States and Israel face the common challenges of maintaining fiscal discipline in spite of growing demands on government resources, defense conversion, and responding to structural change.

6. Rabin's success may be a reflection of the differences between a parliamentary and a constitutional system with a clear separation of power between the executive and legislature.

7. The government also "bails out" several large sick funds at the end of every year, by offsetting deficits in their annual operating budgets.

8. It is interesting to note that the Israeli version targeted the size of the deficit relative to GDP, whereas the original Gramm-Rudman Amendment employed nominal dollar levels. In economic terms, the Israeli version is preferred.

9. In contrast, the U.S. budget deficit declined by 1 percent of GDP over the same period.