

Subsidized Sacrifice:
STATE SUPPORT OF RELIGION IN ISRAEL

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ABSTRACT

This paper offers three economic arguments for ending discriminatory religious law in Israel. First, the current set of subsidies have created massive poverty and welfare dependence in the Israeli Haredi community. With men remaining in Yeshiva till an average age of forty and the Haredi population doubling each 16 years, that community is dangerously dependent on transfers which are unlikely to grow fast enough to support it. Previous work developed a model to explain why fathers with families in poverty choose *Yeshiva* over work. This paper explores policy implications of that analysis, stressing the extreme distortions that result from subsidizing membership in a community that requires personal sacrifice as an entry requirement. Subsidies are largely dissipated by the induced increase in sacrifice. A second argument for ending discriminatory religious law is that the monopoly status granted to Haredim limits competition in the market for religious services, resulting in underprovision to the remainder of the Jewish population. Finally, the opportunity to draw transfers that discriminate in favor of their own constituencies provides a strong incentive to organize political-religious parties, which have destabilized Israeli politics. The paper offers a set of equitable reforms which would compensate the Haredi community for their loss of subsidies and religious monopoly status by expanding needs-based social welfare programs. By limiting the discriminatory rents that a religious-political can aspire to, such reforms would reduce the incentive of religious groups to organize politically, thus serving as an alternative to (the failed) electoral reform.

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1. INTRODUCTION

The Israeli Ultra-Orthodox community is threatened by economic crisis [Dahan 1996; Berman and Klinov 1997]. Berman [1999] documents four components of that impending problem: 1) low labor force participation rates by prime-aged males, 60% of whom are in *Yeshiva* (religious schooling with no secular training component); 2) low market wages for *Yeshiva* graduates; 3) low current incomes of families; 4) population growth rates of 4-4.5% annually, which imply a community doubling in size each 16-18 years, and rapidly outgrowing its resources.

In the face of poverty among their families, why do men remain in *Yeshiva*? Part of the explanation must be draft deferments, which effectively subsidize *Yeshiva* attendance. Yet, *Yeshiva* attendance typically continues long after the deferment subsidy has run out. Could the explanation simply be a pious devotion to studying holy texts? That seems unlikely for two reasons: first, Ultra-Orthodox men outside Israel, even followers of the same streams, are rarely in full time *Yeshiva* attendance beyond age 25; second, there is no historical precedent for the current duration of full-time *Yeshiva* attendance which now extends till age 40 on average!

Previous work [Berman 1999] offered an explanation based on the club good model¹ of Iannaccone [1992]. It describes a community in which members benefit from the religious and social activity of other members within the community. In the Haredi context that is a natural argument, as this community practices a remarkable degree of mutual insurance through charitable acts by individuals and institutions. Religious prohibitions can be understood as an extreme tax on secular activity outside the club that substitutes for charitable activity within the club. A religious community lacking tax authority or unable to subsidize unobservable religious activity may choose prohibitions to increase religious activity among members. Sabbath observance and dietary restrictions, for instance, can be rationalized with that approach. A view of religious behavior as a social activity does not deny the importance of faith but attempts to provide a positive theory orthogonal to explanation based on faith.

Rationalizing irreversible destruction of resources such as burnt offerings or public vows of celibacy or abstinence takes more effort. For that Iannaccone augments the model with heterogeneous agents who signal their commitment to the religious club by incurring costs or "sacrificing," allowing the club to exclude free-riders, choosing only the most committed among potential entrants. In that context, *Yeshiva* attendance can be understood as a costly signal of commitment to the Ultra-Orthodox community, or club. This model clarifies the inefficiency in the draft deferment system and other subsidies to community members, such as stipends to *Yeshiva* students. Intuitively, subsidizing a costly signal is inherently wasteful as it destroys signaling value, inducing an even more costly signal. More generally, subsidizing any aspect of membership in a club that has a costly signal as an entry requirement induces a more expensive signal that dissipates the initial subsidy. It may be the ultimate in distortionary public policy. Equity and efficiency are aligned in this case, as a subsidy that does not favor membership for

¹ See Cornes and Sandler [1986] for a clear explication of club good theory.

the potential entrant will not induce an inefficient increase in the signal. Equitable, Pareto-improving subsidies are possible.

This paper reviews that analysis, providing an intuitive explanation of the major findings and discusses in detail the implications for welfare and public policy. It also refers to the literature on monopoly provision of religious services and the distortions due to religious monopolies. The major conclusion of all these lines of argument is that state support of a particular religious group introduces inequities that generate inefficiencies of two types: first, subsidizing groups that use sacrifices as signals of commitment causes increased sacrifice; second, restriction on the entry of providers of religious services results in underprovision of services. Furthermore, the existing system provides incentives for religious and ethnic groups to organize politically, forming political-religious parties that destabilize Israeli politics. It concludes with an explicit set of policy recommendations that would correct the distortions implied by the current treatment of religion by the Israeli government. These reforms would allow a strong Haredi community to prosper through self-sufficiency without the need for divisive religious politics based on the pursuit of discriminatory rents.

A brief description of State support of religion is instructive. Israel inherited from the British Mandatory government a legal system in which various aspects of family law are the jurisdiction of religious authorities, according to the religion of residents.² (This paper is concerned with Israeli Jews, though the analysis could generalize to other Israelis.) For Jews, Rabbinical courts have exclusive jurisdiction over marriage and divorce and share jurisdiction with Civil courts in issues of alimony, child support, custody, inheritance and personal status. Israeli law recognizes the Chief Rabbinate as the supreme authority in religious law. Two Chief Rabbis, a Sephardi and an Ashkenazi, alternate in the presidency of the Rabbinate.

In addition to the Rabbinate and the Courts, Israel's Ministry of Religious Affairs distributes funding to Yeshivas, ritual baths and other religious bodies. It supports local religious councils for each religion that (for Jews) supervise dietary laws, synagogues, ritual baths, the performance of marriages and burial services. The ministry appoints local Rabbis. It has a large staff who are responsible for providing religious services. For Jews these include protecting holy places, religious instruction and conversion of new immigrants, and organizing religious celebrations. The Ministry's budget is 1.6B NIS³ (~\$400m), which amounts to about 0.4% of GDP. Over half the budget is distributed to Yeshivas, (not including 110m NIS in income support to Yeshiva students). The Jewish part of this bureaucracy, including the religious councils, was initially dominated by the Orthodox National Religious Party but control has passed to the Ultra-Orthodox over the past two decades.

Section 2 introduces the Economics of Religion with a discussion of Adam Smith's approach to market power in the provision of religious services. Section 3 discusses the political economy of religious-political parties in Israel. Section 4 provides background on the Israeli Ultra-Orthodox, reviewing the logic of mutual insurance communities and how that logic can

² For a full description see the Israel Government Yearbook (1998).

³ Proposed budget for 1999 in the Israel Ministry of Finance Budget Proposal (<http://www.mof.gov.il/>).

explain three extraordinary aspects of Haredi society: the increasing demands it places on followers, extremely low employment rates of adult men, and high and rising fertility rates. Section 5 examines the implications of this logic for welfare, including the effects of public policy on the economic welfare of Haredim; relations between Haredim and other Israeli Jews; and relations between Israeli and Diaspora Judaism. Section 6 provides policy suggestions and Section 7 concludes.

2. ADAM SMITH AND THE BURDEN OF MONOPOLY IN RELIGIOUS MARKETS

As an introduction to the Economics of Religion, consider Adam Smith's argument in the *Wealth of Nations* [1776, Book V, Chapter I]. Smith assumed that the market for religious services operates like other markets in the sense that state-provided monopoly power compromises incentives to provide a high level of service. Consider competing streams of Jewish practice as firms competing for market share. As in any market, that competition could result in an enhancement in the quality and variety of service. (This argument should be familiar to any Israeli old enough to contrast the current level of telephone service to that a decade ago.) Smith presented this as an argument against state monopolies in religion, stressing that the state-endorsed religion would attempt to use the state to restrict the entry of other religious groups. He offered as evidence the contrast between religious strife in Europe and the peaceful coexistence of diverse religious groups in the colony of Pennsylvania. Low quality religious services will in turn lead to low levels of affiliation, activity and belief.

Iannaccone [1998] summarizes the considerable evidence consistent with Smith's hypothesis. Market power of churches (as measured by the concentration of members of the same denomination) has a strong negative correlation with a variety of indicators of religious activity across countries and regions. This pattern is reflected in Figure I, which is reproduced from Iannaccone [1991]. In a cross section of 12 predominantly Protestant countries..

"Weekly church attendance rates range from over 40% in the United States (where the constitution guarantees religious competition), to less than 10 percent in Scandinavian countries (where a single state-run Lutheran church dominates the market, runs on tax dollars and pays its clergy as civil servants). Indeed, every available measure of piety, including frequency of prayer, belief in God and confidence in religion, is greater in countries with numerous competing churches than in countries dominated by a single established church, and these relationships remain strong even after controlling for income, education or urbanization." [Iannaccone, 1998 p. 1486]

The same negative correlation of concentration and attendance has been reported in several countries. The U.S., Korea and Japan show evidence of sharp increases in the number of denominations and in membership associated with "deregulation" of religion, suggesting improved levels of service. In Japan the abolition of state-Shinto religion after World War II set off a five-year period known as "The Rush-Hour of the Gods."

Comparable measures for Israel aren't available, but Israelis are clearly located much closer to the doubting Scandinavians than they are to the more devout Americans. Like the

Scandinavians, Israel has very little competition in the religious services market for the less-than-Orthodox population and low levels of religious activity.

Considering the wealth of spiritual raw material in the geographical and archeological environment, the paucity of activity in the Israeli religious spectrum between the secular and the modern Orthodoxy is striking. That is especially striking considering that most North American Jews are either Conservative or Reform, precisely the part of the spectrum that is so sparsely occupied in Israel. There are many possible explanations for this phenomenon, including the anti-clerical socialism of Israel's founders and the legacy of the Holocaust of European Jewry. Yet religion is thriving in formerly communist societies. Ashkenazi Jews abroad share the same history, yet seem to be much more attracted to religion than are Israelis.

The contrast between the diversity of Jewish religious practice in the diaspora and that in Israel suggests that the State monopoly granted to Orthodox and Ultra-Orthodox streams of Judaism has resulted in significant underprovision of religious services in Israel. The Orthodox established a monopoly early in Israel, with the agreement of the secular socialists, leaving a hole in the middle ground of traditional Judaism. This contributed to the culture shock of Jews arriving from Arab world, who suddenly had to choose between extremes of secular and orthodox practice, neither of which matched their moderate, traditional practice. With time, the Orthodox ceded monopoly power to the Ultra-Orthodox and the schism in religious practice widened further. Today, rather than receiving services from the Ministry of Religious Affairs, large segments of the secular population are hostile to its employees, resenting their control over marriage and family law.

Relations with Diaspora Jewry

The contrast between the dichotomy of religious practice in Israel and the continuum in the West is the source of a cultural disconnect between the less-than-Orthodox majority in Israel and that abroad. When Haredi or Modern Orthodox Jews look to Israel as a source of culture, then find rich and vibrant communities producing books and newspapers and prayers, places to visit and to send their children to study in.

But the majority of diaspora communities are Reform and Conservative. They look to Israel for Jewish culture that they can identify with, and find nothing at their position on the continuum of religious practice. Secular Israeli culture is remarkably rich in every dimension, except the religious, to which it is frequently antagonistic. To Diaspora Jews, religious identity is important. It's what makes them Jewish and keeps their communities from disintegrating through assimilation. Yet when they look to Israel, on the one hand the Orthodox are intolerant of their form of practice, rejecting their converted spouses as non-Jews and on the other, the secular culture of Israel doesn't understand the need of Diaspora Jews cling to the religion abandoned by the secular Zionists. And to add insult to injury, the same secular Israelis continue to allow the Orthodox to define Judaism for legal purposes, including the so called *Law of Return*, which grants citizenship to any Jew on arrival.

3. THE POLITICAL ECONOMY OF RELIGIOUS PARTIES

Adam Smith points out in the same chapter the dangers of alliances between political parties and religious groups. He recounts the bloody religious wars of 17th century Europe, which had depopulated half of Germany, and was probably also referring to the disaster of the Puritan role in England's civil war in the 1640s. In contrast, he describes with admiration the separation of Church and State in Pennsylvania, where

“though the Quakers happen to be the most numerous, the law in reality favours no one sect more than another, and it is there said to have been productive of this philosophical good temper and moderation.” [Smith, Volume II, p. 317.]

He goes on to describe the dangers to the sovereign of a powerful state-supported religious group which could be avoided if the State treated all religious groups equally, since free entry would prevent any one religious group from becoming politically powerful.

“In a country where the law favoured the teachers of no one religion more than those of another, it would not be necessary that any of them should have any particular or immediate dependency upon the sovereign or executive power; or that he should have any thing to do, either in appointing, or in dismissing them from their offices. In such a situation he would have no occasion to give himself any concern about them, in the same manner as among the rest of his subjects; that is, to hinder them from persecuting, abusing or oppressing one another.”

Though Smith is nowhere explicit about it, he implicitly argues that if the law is committed to equal treatment of religious groups, they have no incentive to organize politically.

The American Constitution, written a few decades later against the same historical background, takes the same approach to separating Church and State and to guaranteeing religious freedom for all denominations in the First Amendment. The American guarantee of freedom of religion is coupled with a commitment that there may be no discrimination along religious lines by the federal government.⁴ This effectively reduces the incentive of religious groups to organize politically, since the rewards they can aspire to from political power are intrinsically limited.

A 1st Amendment style separation of religion and state can be thought of as a substitute for electoral reform in Israel. Electoral reform was introduced a few years ago in an effort to decrease the influence of small parties and thus increase the stability of governments. The small parties holding the balance of power at the time were Ultra-Orthodox, and their agenda was mostly concerned with religious issues and support for their community. Precisely for that reason they have held the balance of power for two decades in Israeli politics, as they are the only small parties which can consistently exploit the even split in Israeli politics over foreign policy by

⁴ The relevant language of the the First Amendment is "Congress shall make no law respecting the establishment of religion, or prohibiting the free exercise thereof.." It has been interpreted liberally by the courts to imply a complete separation of Church and State, and no discrimination on the basis of religion. States were allowed to have official religions, though they had all stopped doing so by the mid 19th century.

credibly threatening to join either left- or right-wing coalitions. Electoral reform attempted to limit this destabilizing influence of small parties by reducing their representation. A credible promise not to practice discriminatory public policy along religious (or ethnic) lines would limit that power much more effectively, removing this form of rent-seeking from the political arena, even under the current system of proportional representation.

A glance at currently successful democracies in the OECD is consistent with this argument. They have all avoided religious parties and the accompanying extraction of rents, while respecting the rights of religious groups. They either have strict rules forbidding public policy to discriminate along religious lines, like the American first amendment, or have generous social welfare systems as in much of Western Europe, or a combination. The social welfare systems are important, as they undermine the ability of a particular group to deliver a voting bloc by providing a discriminatory system of social services to their constituency alone. State social welfare reduces the appeal of social welfare services provided by a religious group, such as the Israeli Ultra-Orthodox. In contrast to the success of the Western democracies (since the 18th century) in avoiding religious antagonism, Middle Eastern and Asian democracies from Turkey to India remain subject to the destabilizing influence of religious-political parties.

Israel is culturally and religiously diverse, has no first amendment and high income inequality. Even her relatively generous social welfare system still leaves sufficient room for an ethnic or religious group to entrench itself by providing publicly funded social services in a discriminatory fashion. The success of the Muslim Brothers among Israeli Arabs may be due to the same mechanism: they can aspire to extracting rents from the government, then to use those rents to increase their own power by providing social services which the government does not.

4. THE LOGIC OF MUTUAL INSURANCE CLUBS⁵

Prohibitions and Mutual Insurance

Viewing the continuing debate over the place of Reform and Conservative Judaism in Israeli civil law, a nonaligned spectator may ask herself what good would come of allowing streams of Judaism other than Orthodox and Ultra-Orthodox a foothold in Israeli public life. Each of the existing streams has created a political-religious party that, in representing its own interests, has contributed to the instability of Israeli politics. Would the new entrants not do the same, contributing further to political fragmentation? The short answer is, *probably not*, but an explanation requires a review of the history of modern Jewish religious practice, and an examination of the economics underlying each of these movements. Along the way, I want to point out various puzzles in the economic behavior of the Ultra-Orthodox, the solutions to which have strong implications for policy.

⁵ The material in this section draws heavily on Berman [1999].

Ultra-Orthodox and Reform Judaism are both rather recent developments, born in 19th century Eastern and Central Europe.⁶ Their spread dates back to emancipation: the linked developments of increasing economic opportunity outside the Jewish community and the newfound ability of Jews to work and live among Gentiles. In response to these economic opportunities, many Jews did exactly what an economist would predict, mixing themselves into the secular world around them and abandoning the time-consuming rituals and practices of traditional Judaism. Reform Judaism adapted to the increased value of time by providing a time-saving form of Jewish practice requiring, for example, less time in prayer and in the study of Hebrew [Chiswick 1995].

The development of Ultra-Orthodox Judaism (and to a lesser extent Modern Orthodox Judaism) is more of a puzzle to an economist. It became increasingly demanding of the time of adherents, despite the increased value of their time in the market. Prohibitions that Jews had traditionally observed, such as dietary restrictions, sabbath observance and sexual propriety are augmented by the Ultra-Orthodox. For example, some Ultra-Orthodox refuse to use a delineated area (*Eruv*) which allows one to carry objects on the sabbath, geographically limiting the size of a synagogue community. Moreover, many traditions in use of language, diet, clothing and synagogue practice have been elevated to the status of religious imperatives among the Ultra-Orthodox, and deviations can result in social ostracism. The customs of 19th century Eastern European Jewry are currently preserved quite precisely in New York and Israel. Yet despite the conservative appearance of the culture, Jewish Ultra-Orthodoxy is radically more stringent in its demands than pre-modern European Jewry and less tolerant of deviation.⁷ One aspect of this increased stringency of dietary and other laws is the segregationist nature of Ultra-Orthodoxy, which broke with a longstanding tradition of unity within Jewish communities. By making it difficult to eat with, and unacceptable to worship with Reform or even Orthodox Jews, including relatives, the Ultra-Orthodox consciously reduced social contact between the Ultra-Orthodox minority and the rest of the Jewish community.

The Ultra-Orthodox explanation for this increase in the stringency of practice is that it represents a protective reaction to the threat of reform Judaism. Historians agree, though they see

⁶ The origins of Jewish Ultra-Orthodoxy are well described in Friedman [1991], Heilman [1992] Katz [1961] and Silber [1992].

⁷ “Of all the branches of modern-day Judaism, ultra-Orthodoxy is undoubtedly the most tradition-oriented. Its rallying cry is “All innovation is prohibited by the Torah!” a clever wordplay on a Talmudic ruling first coined by Rabbi Moses Sofer in the early nineteenth century that captures the essence of its conservative ideology. And yet, like other antimodern conservative movements, ultra-Orthodoxy is clearly a recent phenomenon. Belying the conventional wisdom of both its adherents and its opponents, it is in fact not an unchanged and unchanging remnant of pre-modern, traditional Jewish society, but as much a child of modernity as any of its “modern” rivals.” Silber [1992, p. 23].

it as a reaction to assimilation and emancipation.^{8 9} This latter view is supported by the observation that Ultra-Orthodoxy¹⁰ did not develop among Jews from North Africa and the Arab world until faced with the option of assimilation into secular (not Reform) culture in Israel.

One line of defense against assimilation was the expansion of Yeshiva study, first among Lithuanians and later among *Hassidim*. The prototype was the Volzhin *Yeshiva* in Lithuania, established in 1802 as a boarding school and supported by donations from outside the community. Teenage boys were sent there to study the holy texts and commentaries in an effort to protect them from corrupting secular influences.¹¹ The study of religious law in *Yeshiva* “became an absolute prerequisite for religious behavior throughout the traditionalist world.” [Heilman 1992, p. 20.] In contrast, secular studies beyond literacy and numeracy at a junior high school level are viewed as a necessary evil. The Ultra-Orthodox have consistently attempted to resist attempts by governments to impose curricula of secular studies.¹²

Yet why would a religious community choose to make increasingly costly demands of members’ time, many of whom lived near poverty in the Shtetls of Eastern Europe? And why would individuals choose to remain in, or even join such a community if it did? A possible explanation is that the Haredi community offered spiritual sustenance, yet that only begs the question of why the spiritual content could not be provided in a more time-efficient package.

Berman [1999] offers an explanation based on the logic of *mutual insurance* clubs. The Haredi community provided, and continues to provide, a remarkable degree of mutual insurance, to an extent believed to be unprecedented in Jewish history.¹³ Charity is common and free loans abound, both in money and in kind [Landau, 1993]. No sick member is without visitors and no single member is without an arranged match. Anecdotally, we observe remarkable altruism in

⁸ See, for example, Friedman [1991], Heilman [1992], Katz [1961] and Silber [1992]. As evidence, Heilman presents quotations from various Ultra-Orthodox leaders of the time.

⁹ Katz [1961], Ellenson [1992] and Silber [1992] make the same claim about Orthodoxy. German Orthodoxy and especially Hungarian Orthodoxy certainly had elements of increased segregation in them and increased stringency of religious prohibitions. Silber [1992] interprets early Ultra-Orthodoxy as an extreme offshoot of Hungarian Orthodoxy.

¹⁰ Within the Ultra-Orthodox there are considerable differences between groups. For instance, the *Lubavitch* Hassidim are openly messianic and many believed their last leader to be at least a potential Messiah, while the *Satmar* dismiss any such possibility. Most are hierarchical communities that seek the advice of their leader, either *Rebbe* or *Rosh Yeshiva*, on any decision, religious or secular. Common among these groups, as among Mennonites, Amish, and adherents of “fundamentalist” Islam, is the rejection of almost all of modern culture, which they view as corrupt and corrupting. That includes modern literature, sport, music, film and television.

¹¹ Friedman [1991] p. 11.

¹² The Volzhin Yeshiva was eventually closed rather than ceding to a (Russian) government demand to include a secular curricula [Heilman 1992].

¹³ Menachem Friedman, quoted in Landau [1993], p. 255.

donation of time and money to community charities, which provide insurance to community members in the form of job search, spouse search, and transfers of food, clothing, medical services and cash. Haredi Jews insure each other to the extent that one would insure their immediate family.

A key aspect of mutual insurance clubs is a tension between the club and its members in how they allocate time between activities that benefit the community (the club) and activities outside the club. The community has an interest in members spending as much time as possible in charitable activity, while the individuals may be attracted by uses of their time on the outside, such as earning wages and consuming.¹⁴ The community can resolve that tension by finding a way to effectively tax wages on the outside through a set of prohibitions on consumption enforced through community pressure. For instance, keeping glatt kosher restricts my ability to use earnings to buy food or eat among the Gentiles, which makes earning less attractive. The greater the benefit the community derives from charitable acts by members, the greater its' ability to keep members affiliated and the more extensive will be the prohibitions it chooses to enforce. Those that do not observe the prohibition could be expelled or sanctioned. This is the rationalization that Iannaccone [1992] offers for religious prohibitions, such as dietary laws, sabbath observance, dress codes and language codes.

This line of argument should not be unfamiliar to observers of other groups that benefit from the voluntary good citizenship of members. Families, university departments, kibbutzim, workplaces and military units all provide examples of institutions attempting to provide incentives for good citizenship within the group by limiting outside opportunities.

Returning to the 19th century armed with the logic of exclusive mutual insurance clubs, we now have an explanation for increased religious prohibition among the Haredim. Traditional Eastern European Jewish society before emancipation acted as a mutual insurance club in which defection was impossible, as living among the Gentiles was not an option. When emancipation and higher wages became an option, some communities attempted to protect themselves against members defecting (and possibly buying their insurance on the market) by offering a “take it or leave it” deal: either agree to a higher level of religious prohibition or leave. That higher level of religious prohibition would be one that taxes wages enough to retain the necessary level of charitable works even at the new, high wage level, which would otherwise distract members with market activity.

So, in broad terms, the fairly uniform religious practice of 18th century European Jewry diffused into a spectrum. Many Jews assimilated altogether. Reform created communities that offered much lower levels of mutual insurance and a time-efficient set of spiritual services. The Ultra-Orthodox isolated themselves from other Jews (who elected to “leave it”), offering high levels of mutual insurance accompanied by a time-intensive set of religious practices. This diffusion would later repeat itself with Jews from Arab lands arriving in Israel.

Could Reform Jews create a viable political party in Israel? History argues against it. Their

¹⁴ A formal version of this argument and the analysis that follows in terms of externalities and public finance is presented in Iannaccone [1992] and in Berman [1999].

degree of communal affiliation is much weaker than that of the Ultra-Orthodox, which is bound together by the tight forces of a mutual insurance community. Thus the ability of Reform Jews to vote as a co-ordinated bloc is not nearly as strong. Besides, the returns to affiliation are smaller for the wealthier Reform community, as we will see below.

Destruction and Renaissance

The argument above suggested that for the Haredi community to retain members in the long run it must enhance the value of the services it provides at the rate that wages rise and lure members away from the community. Indeed, the community experienced growth followed by attrition in the 19th century. Yet the 20th century provided a much greater threat. Unlike millions of Eastern European Jews, the Ultra-Orthodox rejected the option of emigration abroad (mostly to America) in the beginning of this century because America was considered too secular. Likewise, the Ultra-Orthodox declined to join the generally secular Zionist migration to Israel in the 1930s. As a consequence, more than any other segment of Judaism, Ultra-Orthodox Jews were trapped in Europe to be nearly annihilated by the Nazis.

In the aftermath of the Holocaust, the Ultra-Orthodox established communities of survivors, with centers in New York, Jerusalem, Bnei Brak (in metropolitan Tel Aviv), Amsterdam and London. These communities regard themselves as a pious elite, charged with the sacred duty of perpetuating the correct form of devotion by reestablishing their shattered Eastern European cultural tradition.

This fervent desire for cultural preservation was acknowledged by the first Israeli government in an agreement to allow about 400 *Yeshiva* students, many of them refugees from destroyed European *Yeshivas*, exemption from military service so that the study of the *Talmud* could be nurtured [Friedman 1991, Landau 1993].

Subsequently, Ultra-Orthodox Jews have enjoyed an astounding cultural and demographic renaissance. Of all the cultures of Eastern European Jewry, that of the Ultra-Orthodox is undoubtedly the most faithfully preserved. Their demographic success is due to extremely high birth rates. *Israeli Ultra-Orthodox women averaged seven and a half lifetime children* in the mid 1990s.¹⁵ While fertility dropped between 1980 and 1995 for other Jews, Muslims and Christians in Israel, the fertility of Ultra-Orthodox women *increased* by over a child per woman.

The Israeli Ultra-Orthodox population doubled from about 140,000 in 1979 to about 290,000 in 1995. Figure II illustrates the implication of current Ultra-Orthodox fertility rates by simulating population growth for the next 50 years. Population will continue to double every 15-16 years, reaching a half million by the year 2010, one million by the year 2025, two million by 2041 and three million by the middle of the next century.¹⁶ These projections take into account

¹⁵ Based on a total fertility rate calculated using the Labor Force Survey. See Berman [1999] for details.

¹⁶ These estimates do not include Ultra-Orthodox living in boarding schools, who are not sampled in the LFS. They represented an additional 9000 individuals in 1983, or an additional 5% of the population. See Berman

only natural population increase and do not include net migration and net conversion. The Ultra-Orthodox population share is projected to increase from 5.2% in 1995 to 12.4% in 2025 to 28.5% in 2050. Fully 22.5% of Israeli children are predicted to be Ultra-Orthodox by the year 2025.¹⁷

These remarkable population growth rates present a second puzzle. While the vast majority of the world's population is undergoing a "fertility transition" of falling fertility rates, the Israeli Ultra-Orthodox have increasing fertility. The Ultra-Orthodox often explain this as an attempt to compensate for the losses of the Holocaust. While that is an argument that should not be refuted, high and increasing fertility is apparently not common to other communities of Holocaust survivors.

Yet another possible explanation is the increased generosity of child allowances in Israel over the 1980s. While the Ultra-Orthodox benefitted disproportionately from this change, which increased the concavity of the per-child schedule in the number of children, so did Muslims and Druze, who also had large families and whose fertility rates have continued to *decline*.

The logic of mutual insurance clubs and the prohibitions they enact provides an alternative explanation for increased fertility. Development economists generally believe that interaction with labor markets contributes to fertility decline, arguing that as women's wages increase they choose to enter the market and earn, reducing the quantity of children while increasing the consumption and education of each child.¹⁸ Yet prohibitions that effectively tax real wages can forestall that transition, forming a force that slows the entry of women into the labor market. As prohibitions increase in stringency, which they apparently have over the past generation among Israeli Ultra-Orthodox, one may expect to see an increase in fertility. Moreover, increased transfers to Ultra-Orthodox families would also tend to increase fertility for two reasons. First, the income effect on fertility is generally believed to be positive [Becker, 1991], though small. Second, and more importantly, transfers allow the community to increase religious prohibitions without risking attrition, providing further increases in the effective tax on real wages.¹⁹ I return to that point below, offering evidence that increased fertility among the Ultra-Orthodox is a response to increased subsidies.

[1999] for details.

¹⁷ Those proportions are likely to underestimate the growth in the Ultra-Orthodox population share as they do not take into account: a) the trend decrease in the fertility of other segments of the population; and b) migration to Israel of Ultra-Orthodox Jews, which accounted for about 10% of the community's population growth between 1979 and 1995, so that net migration was probably positive.

¹⁸ This argument was most strongly proposed by Becker [1960, 1991]. See Ray [1997] for a summary.

¹⁹ See Berman [1999] for a formal explanation of this point.

Looming Bankruptcy

Population growth has led to increasing political power, which has been translated into increasing government support for the community, and particularly for Yeshiva students. Yet that support has produced a set of disincentives to work that, in turn, now leave the Ultra-Orthodox dangerously dependent on welfare.

Much of the political influence of the Ultra-Orthodox is derived from their status as a swing voting block in the *Knesset*. Ultra-orthodox politicians have been able to threaten to vote with either large block, the right or left wing, on foreign policy. This status has allowed disproportionate influence in every government since the first right-center coalition took power in 1977. This influence has been translated into an expansion of government support to the Ultra-Orthodox community, including stipends for married men in *Yeshiva*, reduced tuition in preschool, elementary school and boarding schools, reduced property taxes and reduced health insurance premiums. Ultra-Orthodox pressure has also helped bring about an expansion in the generosity of various general support systems, most notably child allowances.²⁰ The Ultra-Orthodox have pursued a contentious political agenda, attempting to impose religious restrictions in the form of secular law in such areas as dietary restrictions (*kashrut*), sabbath observance and abortion. They have also insisted on an Orthodox interpretation of conversion law in the legal definition of Judaism in Israeli civil law. This constitutes an important and emotional issue in Israel and among Jews abroad since Israel's "*Law of Return*" grants any (recognized) Jew citizenship upon arrival.

Of all these, the most controversial of all points of contact between Ultra-Orthodox and secular society in Israel is draft deferments and exemptions, which are granted to full time *Yeshiva* students. Deferment of regular service (three years) and reserve duty (about 30 days annually) can be extended and eventually converted to an exemption by remaining in *Yeshiva* till age 41, or till age 35 with five children [Ilan 1998b]. Restrictions on the maximum number of exemptions from required military service were lifted by the government in 1977. Since then, the number of deferments has increased to 3000 per year, or 7.5% of males newly eligible for the draft. These deferments and exemptions are granted only to full-time *Yeshiva* students, who are liable to be drafted if they work even part time.

In 1984 a Sephardi²¹ Ultra-Orthodox party organized nationally, partially as a reaction to the preferential treatment given to Ashkenazi (European) Ultra-Orthodox Jews by the Ashkenazi-dominated institutions and political party. It immediately became the largest of the Ultra-Orthodox parties as it managed to draw increasing numbers of votes from traditional Sephardi Jews who had previously supported non-Ultra-Orthodox parties. It quickly became the fulcrum of

²⁰Ilan [1998a] estimates that an Ultra-Orthodox family with six children is eligible for 6,500 NIS (\$1850) per month in government support from all sources.

²¹ Sephardi, which literally means "Spanish" is a common misnomer describing Jews from Arab countries.

Israeli politics and rapidly translated its political leverage into sharp increases in funding of its own system of schools, Yeshivas and social welfare institutions.²²

Increased subsidies to the Ultra-Orthodox community have been accompanied by a surprising increase in fertility. Did increased subsidies cause increased fertility? Table I provides evidence that this link is indeed causal. The Table reports the differential increase in fertility between Sephardi and Ashkenazi Ultra-Orthodox between the early 1980s and the mid 1990s, the period of differentially sharp increase in the flow of resources to the Sephardi Ultra-Orthodox community. Sephardi Ultra-Orthodox women had a total fertility rate of 4.57 children per woman in the early 1980s, *which rose by two children* by the mid 1990s to reach 6.57 children per woman! The velocity of this remarkable increase in fertility may be unparalleled in modern demography. It dwarfs even the 0.71 child increase in total fertility experienced by Ashkenazi Ultra-Orthodox women over the same period. The difference between the Sephardi and Ashkenazi increases in fertility rates is 1.29 children per woman and is statistically significant (at $\alpha=0.03$ for a one-tailed test.)

The three right columns of the table report that fertility *declined* for the non-Ultra-Orthodox population in Israel, including Jews, Christians and Muslims. Note that all these groups are subject to the same increase in child allowances (in the mid 1980s) as are the Ultra-Orthodox. Thus it's hard to explain increased fertility among the Ultra-Orthodox with the increased generosity of the child allowance system.. In particular, Muslim women began the period averaging one and a half children more per woman than the Sephardi Ultra-Orthodox and ended the period with two children less. In contrast, *the table provides strong evidence that transfers to the Ultra-Orthodox community have brought about a remarkable increase in fertility.*

Increased subsidies to *Yeshiva* students, in combination with draft deferments and exemptions have made *Yeshiva* attendance increasingly attractive, even to older men. Berman [1999] reports that the proportion of prime-aged Ultra-Orthodox Jewish males (aged 25-54) not working because of full time *Yeshiva* attendance is high and rising: from 41% in 1980 to 60% by 1996.²³ These levels are unprecedented among Jews,²⁴ far exceeding historic levels of *Yeshiva* attendance in Europe and current rates of *Yeshiva* attendance among Ultra-Orthodox abroad, where young men are rarely in *Yeshiva* past the age of 25. The combination of increased *Yeshiva* attendance and rapid population growth have resulted in a sharp increase in the number of Ultra-Orthodox children whose father does not work because he is in *Yeshiva*. The proportion

²² Friedman [1991, chapter 11] provides a detailed description of the rise of this political movement.

²³ *Yeshiva* attendance may be somewhat, but not grossly, exaggerated. A government commission reported on cases in which a *Yeshiva* student was investigated on suspicion of violating the deferment agreement. 40% of these were found to be in violation, either by working or by being in a different *Yeshiva*. The army claims that the figure is 20% [Ilan, 1998b]. The violation rate in a random sample of *Yeshiva* students would presumably be lower.

²⁴ Friedman [1991] describes the history of *Yeshiva* attendance in Europe.

of Israeli children with a (labor force nonparticipant) father in *Yeshiva* more than doubled between 1980 and 1996, from 2.7% to 5.9%.

Table II provides evidence that this rapid decrease in labor force participation is due to subsidies. It reports how *Yeshiva* attendance among Sephardi Ultra-Orthodox rapidly caught up with that of the Ashkenazim with the ascendance of *Shas*, the Sephardi Ultra-Orthodox party. In the early 1980s, before *Shas*, only 38% of Sephardi Ultra-Orthodox men aged 25-5 attended *Yeshiva* full time, as opposed to 46.8% among the Ashkenazim. By the mid 1990s, the Ashkenazi attendance rate had increased by 7.6 percentage points, to 54.4%, while the Sephardi attendance rate had increased by more than twice that amount, to reach 53.9%. *Yeshiva* attendance, like fertility, is highly responsive to subsidies.

Families with fathers in *Yeshiva* have very low incomes. The average family with a father aged 25-54 in *Yeshiva* is large, with 4.5 children at home. Their monthly income in 1995 averaged about \$1150 (US), only 42% of the income of the average two-parent Israeli family²⁵ (which has 2.1 children). Measured income does not include imputed rent for a population that generally owns its own housing. It's worth stressing, though, that the common practice of conditioning marriage on the provision of an apartment by parents exists precisely because young Ultra-Orthodox couples cannot afford to pay rent. This average family with a prime-aged father in *Yeshiva* is below the poverty line.

Families with fathers in *Yeshiva* are extremely dependent on government support. Only 18% of family income is earned, with almost all of that coming from the wife's earnings. Transfers from institutions (other than the National Insurance Institute) account for 39% of income. This is almost entirely stipends granted to *Yeshiva* attendants. Child allowances make up another 32% of income. These transfers, mostly from government, account for at least 70% of the income of these families, not counting pensions, disability and other National Insurance programs. In short, the combination of increased *Yeshiva* attendance and natural population increase has created a rapid increase in the absolute number and proportion of Ultra-Orthodox families dependent on government support. To maintain this standard of living at current levels of *Yeshiva* attendance and Ultra-Orthodox fertility, outside support of the community would have to continue to increase at 4-5% annually, or double each 15-17 years, a growth rate much higher than Israel's rate of per capita output growth. *At current levels of transfers and taxes the Ultra-Orthodox population growth rate will make Israel's welfare system insolvent and bankrupt municipalities with large Ultra-Orthodox populations.*²⁶ The status quo is not sustainable without transferring an ever-increasing proportion of output to welfare programs.

²⁵ Under-reporting of income would bias estimates downwards. *Yeshiva* nonparticipants may be more likely to under-report income since, in principle, they face larger potential penalties than do most taxpayers: they could lose both their stipends and draft deferments as well as having to pay taxes. In practice there is evidence that these sanctions are not strictly enforced [Ilan 1998c].

²⁶ Dahan [1998] analyzes the effect of *Ultra-Orthodox* demographics and earnings on Jerusalem's municipal finances.

This condition cannot be quickly reversed by current *Yeshiva* students entering the work force. *Yeshiva* students face low wages. While the return to secular schooling rose in Israel over the 1980s and early 1990s rose from 7.8 to 9.4 percent, the return to *Yeshiva* education was low and possibly decreasing, from 2.3 to 1.8 percent. Compared with secular education, which is a remarkably good human capital investment in Israel, *Yeshiva* has become an increasingly poor investment.²⁷ Yet Ultra-Orthodox men are choosing it in increasing numbers and for longer durations of study.

Is this all due to the distorting influence of draft deferments? If a father's *Yeshiva* attendance is being extended in order to qualify for a draft exemption we would expect that as soon as the exemption is granted, he would leave *Yeshiva* for the labor force, either to work or to seek work. Exemptions are achieved at age 35 for men with at least five children and at age 41 regardless of the number of children. Yet, as pointed out in Berman [1999], *not only does Yeshiva attendance not disappear at age 41, there is no sharp decline of Yeshiva attendance rates at either age. Fully 46% of Ultra-Orthodox men aged 41-45 chose Yeshiva rather than the labor market despite already being exempt from military service for life.*

The choice of studies over work is especially puzzling considering the high marginal utility of income in a large family. At 35 years old a *Yeshiva* student could earn more than twice his monthly stipend by working. That ratio would rise to about 250% by age 45 with 10 years labor market experience. A 25-year old *Yeshiva* student could earn twice the stipend by working, would incur perhaps a month a year of reserve duty till his exemption (generally at age 35), and would gain returns to experience which would increase future earnings. Compounding the puzzle is the fact that, beginning in their late 30's, a typical Ultra-Orthodox couple will have children marrying. That rarely occurs without the parents guaranteeing minimal financial security by purchasing an apartment for the young couple, since the groom will certainly be in *Yeshiva* and the couple will be too poor to pay rent.

Could extended *Yeshiva* attendance be out of the sheer love of learning? That explanation is inconsistent with the fact that in much wealthier communities abroad, often followers of the same *Rebbe*, the men seldom attend *Yeshiva* past their mid-twenties. In the Montreal Hasidic community, for example, only 6% of men aged 25 or older attend *Yeshiva* full time [Shahar, Weinfeld and Schnoor 1997], as opposed to 60% in Israel in the mid-1990s. Moreover, despite the traditionalism of Ultra-Orthodox culture, a situation in which the average man stays in *Yeshiva* till age 40 is unprecedented, both in Israel and abroad. Even in Israel, *Yeshiva* attendance rates have risen by almost a half since 1980 for men aged 25-54.

In summary, *Yeshiva* attendance by adult men after the benefits of the draft deferment subsidy have been exhausted presents a third puzzle, especially considering the fragile economic state of their families. This puzzle exists both at the level of the individual, whose family is in

²⁷ The standard caveat about the causal interpretation of regression coefficients is in order. For instance, if years of schooling in *Yeshiva* are positively correlated with an unobserved variable such as preference for work which allows study during work hours, low wages may represent a compensating differential and bias the estimated coefficient downward. It seems unlikely that the entire gap between the returns to secular and *Yeshiva* education can be due to such biases.

poverty, and at the level of the community, which is pushing itself into bankruptcy. I turn now to an explanation of efficient sacrifices and to rationalize the behavior of individuals, and return to the problem of the larger community in the next Section.

Mutual Insurance and Efficient Sacrifice

Exclusive clubs tend to be selective. So too with mutual insurance clubs, which can strengthen themselves by choosing members who contribute to the common good by doing charitable acts and being good citizens. Yet how can one tell who will be a committed member and who will defect? The nightmare of Ultra-Orthodox parents would be a son-in-law who looks fine initially but eventually turns out to be a closet secularist, exposing their child and grandchildren to insidious secular influences, or even defecting.

In the presence of uncertainty about how tempted a young man will be by high market wages and a secular lifestyle, a good way for him to signal commitment to Ultra-Orthodoxy would be to forgo a few years of earnings as a sort of initiation rite. That costly signal would be prohibitively expensive for high wage types, or materialists, but would be an acceptable cost of entry for low wage types, or those who have a stronger preference for charitable acts within the community over consumption. Yeshiva attendance as an expensive signal satisfies that criterion exactly. It is an alternative use of time that could have been spent earning wages or invested in increasing future earnings through education.^{28 29}

That rationalization for Yeshiva attendance provides an explanation on the one hand, for the contrast between attendance rates in Israel and abroad and on the other for continued attendance in Israel among men who are already draft-exempt: In New York, a few years in Yeshiva after high school may be sufficiently costly to signal commitment. Yet in Israel, the subsidy inherent in the draft exemption deflates that signal. Till age 35 one cannot be sure if a man in Yeshiva is there because he is truly a committed member of the community or because he is merely trying to avoid reserve duty in the military. Remaining in Yeshiva till age 40, the Israeli average, provides an sufficiently expensive signal.

Many groups ask for signals of commitment, which can be rationalized in the same way. For instance, elite military units require a painful training period (*gibush*) in order to select only the most committed recruits. The more prestigious the unit, the greater the sacrifice required of recruits.

The signaling explanation implies that as subsidies to the Ultra-Orthodox increase, a more costly signal of commitment is necessary in order to exclude "free-riders." (I.e., those that

²⁸ Other benefits of Yeshiva, according to attendants, are direct utility from the enjoyment of study and benefits to the individual and the community from the accumulation of denomination-specific religious capital [Lehrer and Chiswick, 1993]. The logic of the argument allows utility from learning, which is omitted only for simplicity. Note the more utility derived from *Yeshiva* attendance (for all types), the longer the duration necessary to provide the necessary signal of commitment, which necessarily involves a sacrifice of utility.

²⁹ Yeshiva attendance may also be

would benefit from the advantages of membership but eventually defect.) That is consistent with the facts since 1977: as subsidies to the Ultra-Orthodox have increased per capita,³⁰ duration of *Yeshiva* attendance has increased as well.

The comparison with communities abroad also rules out the possibility that *Yeshiva* attendance of men in their forties is due to the combination of high income from other subsidies and a high income elasticity of demand for learning, since the communities outside Israel have higher income. I conclude that the Israel-abroad difference is due to the combination of subsidy and signal. Abroad, in the absence of a subsidy, a few years in *Yeshiva* are a sufficient sacrifice of time to signal commitment to the Ultra-Orthodox community.³¹

In summary, an approach that stresses the importance of mutual insurance provides an explanation for three striking puzzles in the economics of Ultra-Orthodoxy, the increasing time-intensity of practice, high and rising fertility rates and low employment rates. It is worth repeating that this approach doesn't preclude the importance of spiritual values or an ethic of cultural preservation, but does stress that among possible choices of religious practice the time-intensity of Ultra-Orthodox practices, which are reforms of traditional practice, requires some explanation. I turn now to a discussion of public policy implications.

5. WELFARE IMPLICATIONS - THE INEFFICIENCY OF INEQUITY

Section 4 indicated that the Haredi community is headed for economic impoverishment. The population doubles each 16-18 years. It is hard to imagine that transfers from the community's sources of support, the Israeli government and donors abroad, or what remains of reparations payments, can come close to keeping pace with that growth rate. Approximately 110,000 children currently live in households headed by a *Yeshiva*-attending father. These households average very low income, below the Israeli poverty line. The number of children in this situation is rising exponentially. What is worse, if those fathers chose to enter the labor market immediately, their earning capability is quite low. How then to transfer funds to these families, who support many children, without compromising the incentives of their fathers to work? In the longer term, is it possible to design a politically feasible policy that would bring the Haredi community into self-sufficiency?

An answer to that question requires an analysis of the extreme distortion of subsidized sacrifices.

³⁰ See Berman-Klinov [1997] for a discussion.

³¹ Yoram Weiss raised a puzzle associated with this explanation, namely that by age 40 the community is so familiar with an individual that there should be little left to signal. A possible answer comes from the attitudes of students: A typical older Kollel students' explanation for his *Yeshiva* attendance is that it insulates him from the corrupting influences of the secular world. When asked if at the age of 40, with 6 children, he is still a candidate for defection or backsliding, he answers: "Of course, I haven't been tested till I leave." Note also that this is the age at which a signal of commitment may be the most valuable, as the father will soon depend on the community to raise funds for apartments in order to allow his children to marry.

Subsidized Sacrifice

The logic of Yeshiva as a costly signal of commitment implies that any public policy that discriminates in favor of the Ultra-Orthodox will have an implication for the duration of Yeshiva attendance. That's true not only of subsidies, like stipends to Yeshiva students, but also of taxes which fall only on non-Ultra-Orthodox citizens, such as the military draft. The same argument applies to enforcement of restrictions on Sabbath travel or dietary restrictions in civil law. Anything that makes membership in the community relatively more attractive to the potential entrant will induce an increase in the initiation cost, which imposes an added distortion on the economy. The monopoly status of the Ultra-Orthodox in local religious councils provides another such distortion, as they decrease the quality of religious services provided to the non-Ultra-Orthodox majority, a point I return to below.

Interpreted in this context, the cumulative effect of discriminatory subsidies to the Ultra-Orthodox is extreme. The average age of leaving Yeshiva, at 40, implies a 15-18 year delay of entry into the labor market, when compared to Ultra-Orthodox Jews abroad! This delayed entry into work is the single most important factor in the welfare-dependence of the Ultra-Orthodox community.

That welfare dependence, combined with population growth, poses problems at the municipal as well as national level. As increasing numbers of Ultra-Orthodox qualify for exemptions from local property taxes on the basis of low income, the tax bases of B'nei Brak and Jerusalem are compromised [Dahan 1998]. This inevitably sets into place a self-defeating dynamic of reduction in the quality of local service (or an increase in local tax rates), followed by migration of wealthier households, which accelerates the problem. Other municipalities have a disincentive to welcome young Ultra-Orthodox migrants who cannot afford property prices in Jerusalem, fearing that the same dynamic of shrinking tax base will occur in their cities as well.

The choice of Yeshiva over higher education among Ultra-Orthodox is not only an Israeli phenomenon. Ultra-Orthodox men in the Diaspora commonly avoid Universities and Colleges because of the perceived threat of ethical relativism and other insidious ideas. This choice has dangerous economic implications for the world Ultra-Orthodox community. Most of the growth in Jewish national product this century, both in Israel and abroad has been the result of human capital accumulation. The current wave of skill-biased technological change, which has lasted at least for two decades, has benefitted Jews disproportionately. Yet the underside of that trend has been worsening economic outcomes for those with a High School education or less, throughout the OECD. Since this is the educational level of the majority of Ultra-Orthodox men, they may well be facing worsening economic outcomes both in Israel and abroad. It seems that the ongoing Ultra-Orthodox negotiation with the modern world must now include coming to terms with postsecondary technological education in a way that least threatens social cohesion.

6. POLICY SUGGESTIONS - THE EFFICIENCY OF TOLERANCE

The perceived inequity of the draft deferral arrangement has been a traditional divisive force in Israeli public life. The secular and mainstream religious population (including some

non-Jews such as Bedouin and Druze) generally regard military service as a necessary public service, some of which is quite dangerous, and resent the Ultra-Orthodox exemption. In contrast to that debate over equity per se, the inequity in the draft deferment system creates an *inefficiency* that has aided in driving the Ultra-Orthodox community toward economic crisis.

In previous work [Berman and Klinov 1997] we argued that draft deferments conditioned on *Yeshiva* attendance are an obstacle to the self-sufficiency of the Ultra-Orthodox community as they provide strong disincentives to earning and human capital accumulation. The conditioning of draft deferment and of stipends on not working is an enormous tax on the first hour of work. The same is true of the requirement that men over the age of 30 must have studied full time in *Yeshiva* continuously in the past in order to qualify for stipends and deferments. That continuous study requirement discourages *Yeshiva* students from even experimenting with work or from working temporarily to provide for their families in a crisis. Furthermore, the conditioning of deferment and stipends on full-time study in *Yeshiva* leaves little time for secular, work-oriented studies.

That previous argument was incomplete as it misses the main point of the efficient signaling model of Section 4: Any subsidy that increases the return to joining for a nonmember will be canceled and wasted by a counteracting increase in the optimal sacrifice. To be efficient a subsidy must be equitable, in the sense that they do not enhance the benefits of joining any religious club.

Here *equity and efficiency dictate the same policy*. Transfers to the Ultra-Orthodox that do not discriminate between members and nonmembers will not induce an offsetting sacrifice since they don't increase the attractiveness of membership to nonmembers. Equitable subsidies would include, for example, job training, conditioned only on employment status, or the child allowance system, which is conditioned only on the number of children. These are much more efficient than subsidies such as stipends or support of Ultra-Orthodox schools, which are conditioned on membership in the Ultra-Orthodox community or on *Yeshiva* attendance.

Applied to the subsidy implicit in draft deferments, this logic has a clear implication: Easing the conditions of exemption from military duty, such as the reduced *Yeshiva* attendance requirements proposed in September 1997 by the Finance Ministry, would provide an increase in the already inequitable subsidy to the Ultra-Orthodox. That implies an increase in the compensating sacrifice, probably not in the form of increased *Yeshiva* attendance but in some other inherently inefficient form. Universal equitable application of the draft would avoid that distortion.³² The model predicts that the welfare loss to the Ultra-Orthodox community from equitable application of the draft would be small (literally zero). They could be efficiently compensated with a general increase in other forms of income support or child allowances or job training, equitably applied to all needy Israelis. Such a policy reform would benefit a large

³² A third option which also has the advantage of efficiency through equitable treatment is a volunteer military. That's a complex question which is not currently under consideration. In short, it has the usual advantages of efficient allocation through market wages but the disadvantages of the necessity to raise revenue to pay higher salaries through distortionary taxation and the loss of the draft's current function of promoting cultural cohesion and promoting an equitable distribution of the special tax of military service.

population of low-income children. It would also promote tolerance, reducing the incentive of the Ultra-Orthodox to put themselves in conflict with Jews of other traditions by reducing their need to exclude free-riders through costly sacrifice.

More generally, any action that makes membership more attractive, relative to nonmembership will also induce an inefficient increase in sacrifice. Thus use of civil law to enforce prohibitions for nonmembers will also induce increased sacrifice as a signal. That includes legal enforcement of Sabbath observance laws, dietary laws, marriage laws, conversion laws and any other restrictions on activities of competing religious traditions, such as the modern-Orthodox, Conservative and Reform.

Rapid population growth, combined with low human capital accumulation imply threats to the economic viability of the Israeli Ultra-Orthodox community both in the long term and in the short term. In the long term transfers from parents will be necessarily exhausted. It is also hard to imagine government support or donations from abroad doubling every 16-18 years. In the shorter term, the dependency of the Ultra-Orthodox on donations makes them vulnerable to two types of risk. First, a recession abroad may severely reduce donations. Anecdotally, a large proportion of those transfers come from diamond and real estate wealth, two highly cyclical industries. Second, a realignment in Israeli politics may bring to power a center-left or center-right coalition with a majority that does not depend on Ultra-Orthodox support. Such a coalition could exploit secular resentment of Ultra-Orthodox political success by promising to reduce transfers to the Ultra-Orthodox. Reform of the draft deferral regulations would help insulate the community against both of those risks.

A Package of Reforms

A possible solution to all these issues would be a two-part package of reforms, which would be equitable and thus efficient, on the one hand, and provide sufficient compensation for the Ultra-Orthodox to be politically feasible, on the other. The first part would guarantee equity and the second would replace discriminatory subsidies with a nondiscriminatory safety net.

Part I. Equity. Introduce a constitutional item guaranteeing equal treatment under the law for religious groups and denominations. While that would be interpretable by the courts, the intended effect would be to a) equalize treatment under the draft; b) equalize support of education and other social services across religious denominations; c) ending the monopoly of any religious denomination in the provision of religious services and in the application of civil law.

Part II. Safety Net. Provide a generous set of “safety net” items, provided equally on the basis of some objective indicator such as income or number of children. In the immediate future these should include job training, in an effort to move tens of thousands of Ultra-Orthodox men into employment, if they so choose.

The equity proposal is quite flexible. For example it allows for considerable leeway in the draft, including “Hesder” like arrangements that accommodate the special needs of Haredi draftees, national service, or even a volunteer military.

The safety net portion should include job training in programming and computer-related skills. The exception to the world trend toward skill-biased technological change is computers, which offer high productivity jobs to smart high-school graduates with relatively short courses in programming and related skills. Experience suggests that Yeshiva students have done quite well with a few months' training.

The equitable public policy rule would end subsidized sacrifice, end state-sanctioned monopoly in religion and strongly reduce the incentives of political-religious groups to organize at all. Note that the latter is only true if a government can *guarantee* not to discriminate on the basis of religion or religious denomination, which would require a constitution-like commitment.³³

With a generous enough additional "safety net," the constituents of the Ultra-Orthodox community should be willing to accept the package, since it would mean trading a set of subsidies that induce a countervailing sacrifice of time for a set of subsidies that require no sacrifice. Recall also that the status quo is not sustainable for the Ultra-Orthodox community at current levels of overall support.

While the safety-net proposal is expensive, the alternative could be worse. Consider the long term gains from removing a community growing exponentially from the Yeshiva subsidy rolls and starting to collect taxes from them. Alternatively, consider the political and social costs of the fathers of 100,000 Haredi children looking for support and work at once, with little human capital to offer. Consider also the benefits of a functioning, responsive political system able to push forwards major policy initiatives.

7. CONCLUSIONS

The postwar Haredi community has achieved a breathtaking cultural and demographic renaissance, preserving to a remarkable degree the culture of prewar Europe and achieving an astounding rate of population growth. Yet, the Israeli branch of that community, which numbers about 300,000 people, now faces a new threat to its' well-being: the economic consequences of outgrowing its' resources.

As in many other areas of the Israeli economy, Israel's founders granted a monopoly on religion, which created a vested interest that is hard to displace. The state carries out a set of discriminatory policies, which imply extreme distortions: the institutional welfare dependence of the Haredi community, which has over 100,000 children in state-supported households with precious little human capital; the distortion of the political culture through rent-seeking of religious-political parties; the underprovision of religious services to the majority of secular and less-than-Orthodox Jews.

³³ Note that none of this precludes the same guarantee of equal treatment for ethnic groups, including groups from various countries of origin, though it may make sense to allow for affirmative action, which Israel has been fairly aggressive about in the past.

The dominant culture in Israel is a Jewish form of Western Liberalism. The economics underlying that ascendant force are based on the productivity of individual creativity, as complemented by education. Jews in the West have done well by this economically and have thrived in the open and tolerant general culture, even as we grope for and redefine our Jewish cultural identity.

Like Reform Judaism, Ultra-Orthodoxy is a reaction to that success. Economically, Ultra-Orthodoxy is the poor cousin of that tradition, intellectually, culturally and spiritually vibrant but economically impoverished. It feels threatened by the secular culture and so isolates itself. The largest cost of that isolation is the refusal to participate in secular education, which has been the engine of Jewish economic growth over the past century, both in Israel and abroad. Communities that hitched themselves firmly to the mule of secular education have thrived.

This reaction has survived so far, despite not getting on the cart, because of a combination of commitment to cultural preservation, high birth rates and transfers from other Jews, both from the Israeli government and from donors abroad. Unfortunately, those transfers have also reinforced the logic of isolation as a cultural preservation strategy, sowing the seeds of economic collapse.

Most Israeli Ultra-Orthodox families have not yet felt the weight of that economic pressure, because their communities have insulated them with an admirable level of mutual insurance. Each couple, each family, each yeshiva, feels strapped but knows it can rely on a generous community to support it. But the community is just the collection of families. It doesn't take a prophet to see that with the growth in human and physical capital lagging behind the growth rate of population, the community as a whole faces economic bankruptcy.

Many Israelis outside the Ultra-Orthodox community may view the population projections in Figure II with trepidation. This paper should make two points clear in that regard. First, the current fertility rates of the Ultra-Orthodox community and their current degree of isolation and radicalism are unsustainable. In the absence of a widespread the community will bankrupt itself and collapse long before those projections are realized. Second, current rates of fertility and Yeshiva attendance are clearly the result of distortionary subsidies so that they are quite likely to respond to the inevitable reductions in those subsidies.

The current Israeli government has an unprecedented opportunity to correct distortions that handicap Israeli society and politics. The Israeli Haredi community can act in concert with government to avert its impending bankruptcy. It must move most of the current Yeshiva students into work. Removing discriminatory treatment by the State, beginning with the draft deferment for Yeshiva students, would serve that purpose in two ways. First, it would remove the distorting incentive to remain in Yeshiva till age 40. Second, it would heal a festering wound in the relations between the Haredim and other Israeli Jews, averting the potential for an opportunistic politician to trigger a nasty cultural confrontation by proposing a sudden, mean-spirited reduction in support for the Haredi community. The world Ultra-Orthodox community has accomplished a remarkable cultural and demographic renaissance over the past half century. It may now be strong enough to relinquish its special status in Israel in order to restore self-sufficiency and thrive in the next century.

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Figure I: Religious Market Power and Church Attendance

Note: Concentration is measured as a Herfindahl index of Protestant denominational shares in the population. Countries included are all less than 50% Catholic. Reproduced with permission from Iannaccone (1991). Based on data from the International Survey of Values, collected 1981-1983.

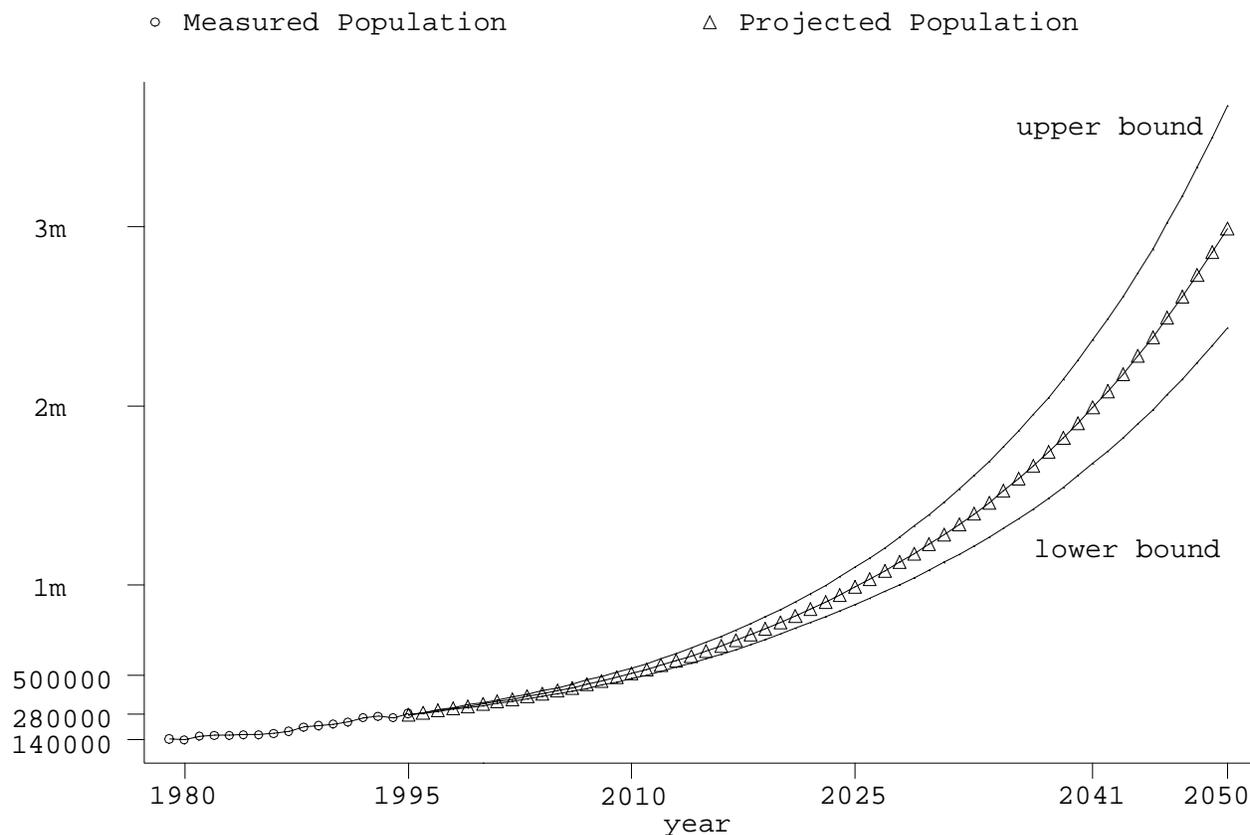


Figure II: Population Projection for Ultra-Orthodox Jews

Note: Demographic projections are calculated using age-specific predicted fertility rates and mortality rates. Predicted fertility rates are calculated using estimated coefficients from a regression of births on a quartic in age. Mortality figures are from the Population Registry, as reported in the 1993 Statistical Abstract of Israel. The base population for the projection is the 1995/96 sample. Projected population (1996-2025) is calculated by iteratively calculating age and gender specific cells using 1995/96 LFS figures as a base. Upper and lower bounds for population projections are calculated using the upper and lower bounds of 95 percent confidence intervals for predicted age-specific fertility rates to predict births. While this is likely to be the major component in variance of a projection, these bounds understate the true 95 percent confidence interval as they do not reflect: sampling variance in age-specific populations for women of childbearing age in the base year; projection variance in age-specific populations of women of childbearing age; variance in actual mortality; and variance in actual fertility. See Appendix II of Berman [1999] for details.

TABLE I
FERTILITY BY RELIGIOUS AFFILIATION AND ETHNIC ORIGIN

Period	Sephardi ^a Ultra- Orthodox	Ashkenazi ^a Ultra- Orthodox	Ultra- Orthodox with Native Parents ^a	Non Ultra- Orthodox Jews	Christians	Muslims
Source:	Labor Force Survey micro data				Population Registry	
1980-1984	4.57 (0.36)	6.91 (0.32)	8.70 (0.72)	2.63 (0.03)	2.66 ^b	5.98 ^b
obs.	613	764	194	38909		
1993-1996	6.57 (0.41)	7.62 (0.38)	8.51 (0.77)	2.26 (0.04)	2.19 ^c	4.65 ^c
obs.	531	673	372	33738		
Change	2.00 (0.55)	0.71 (0.50)	-0.18 (1.06)	-0.37 (0.05)	-0.47	-1.33
Difference in difference:						
Sephardi/Ashkenaz		1.29 (0.67)				

Notes. "Sephardi" Jews are identified by own or fathers' birthplace in Africa or Asia. "Ashkenazi" Jews are identified by own or fathers' birthplace in Europe, America or Oceania. Native born parents are generally Ashkenazi, especially in the 1980s, since the majority of Sephardi Jews arrived in Israel after 1950.

b. Population Registry, 1980

c. Population Registry, 1995/96

Total Fertility Rates in left four columns are calculated from micro data using the Israel Labour Force Survey (LFS) question "own children aged 0-1 at home." These may include a small number of adopted children. Age specific fertility rates are calculated for 6 age categories for women aged 18 through 54. Heteroskedasticity-consistent standard errors in parentheses. Ultra-Orthodox Jews are identified in the survey as individuals living in a household in which at least one male declares his last school attended as yeshiva. LFS samples include all unique rotation groups the first time they are observed. Population Registry figures are from the Statistical Abstract of Israel 1982 and 1997.

TABLE II
FULL-TIME YESHIVA ATTENDANCE RATES BY ORIGIN: 1980-1996
 Men aged 25-54

Period	Sephardi ^a	Ashkenazi ^a	Native Israeli Parents ^a	All Ultra- Orthodox Jews
1980-1984	38.0 ^b %	46.8	55.1	45.4
	(3.0) ^c	(2.2)	(5.1)	(1.7)
obs.	260	520	98	880
1993-1996	53.9	54.4	72.2	57.6
	(2.9)	(2.3)	(3.3)	(1.6)
obs.	299	464	182	796
Change	15.9	7.6	17.1	12.2
	(4.2)	(3.4)	(6.1)	(2.5)
Difference in difference:				
Sephardi/Ashkenazi		8.4		
		(5.7)		
Sephardi / Ashkenazi & Native			5.0	
			(5.4)	

Source: LFS, 1980-1984, 1993-1996.

Notes: a. "Sephardi" Jews are identified by own or fathers' birthplace in Africa or Asia. "Ashkenazi" Jews are identified by own or fathers' birthplace in Europe, America or Oceania. Native born parents are generally Ashkenazi, especially in the 1980s, since the majority of Sephardi Jews arrived in Israel after 1950.

b. An attendance rate is the ratio of yeshiva nonparticipants (who list full time yeshiva study as their reason for nonparticipation) to Ultra-Orthodox Jews. Ultra-Orthodox Jews are identified in the survey as individuals living in a household in which at least one male declares his last school attended as yeshiva.

c. Heteroskedasticity-consistent standard errors in parentheses.