

Netanyahu is undermining Israel's economy

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Since the mid-1990s, Israel and its supporters have touted the country's remarkable economic success. The globally connected "Startup Nation" became celebrated as an economic miracle and an exemplar for other technologically ambitious countries, producing companies such as Check Point, Waze and Wiz. Fast forward 30 years and Israeli Prime Minister Benjamin Netanyahu is now vowing autarkic survival and talking about Sparta rather than start-ups.

As the UK, France, Canada and Australia recognise Palestinian statehood, the EU contemplates sanctions and Germany imposes an arms embargo, the true cost of Israel's democratic backsliding is becoming clear. Netanyahu's rule is causing the structural decline of Israel's economy.

In late 2022, Netanyahu's government — dependent on the ultra-Orthodox and the far right — assumed power and immediately began a drive to dismantle democracy. It diverted public funds to unproductive uses by core constituencies of the governing coalition and pursued a judicial overhaul designed to weaken the supreme court, which is the main check on government over-reach. Mass protests caused a delay but not an end to these policies.

Then came the brutal Hamas attacks of October 7 2023. Under the cover of war, democratic backsliding worsened. For Netanyahu, there is an incentive for perpetual war. It allows him to stay in power in the face of a majority that has turned against him and to avoid prosecution in ongoing corruption trials. For the far right, it is a golden moment to advance their messianic vision of Israel.

Repeated warnings of the economic risks — from 25 top scholars, including Nobel laureates, and 84 leading Israeli economists — have now materialised.

Official data indicates that business sector GDP in real terms went up by a meagre 0.2 per cent cumulatively in

2023 and 2024, after growing 7.4 per cent in 2022; real aggregate investment declined by a cumulative 17 per cent in those years, while GDP per capita has declined by over 1 per cent as output growth slows.

Since early 2023, nearly 170,000 people have left the country, with fewer than 60,000 returning. (Israel's famed high-tech sector, producing one-fifth of GDP and over half of service exports,

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employs only 400,000 workers.) Military reserve duty and democratic backsliding will intensify this outflow. These days, start-ups are incorporating in the US, not locally, as potential investors flee. At current rates, the sector could largely vanish as an Israel-based industry in a few years.

Given that Europe is Israel's main

trading partner (45 per cent of imports and 38 per cent of exports), European sanctions would be a significant blow to foreign trade. Inevitably there will be a rise in taxes, cuts in government services and rising income inequality. Domestic fissures in Israeli society will worsen: most ultra-Orthodox do not serve; their share of the population will rise above 20 per cent over the coming decades, worsening the unequal burden of military service.

The rise in the debt-to-GDP ratio will accelerate, with additional credit rating downgrades. A vicious circle may ensue: decline in investment, fall in output per capita and consumption, and slower growth. Israel is in the process of turning from a flourishing, human capital-based economy to one that risks dropping out of the group of advanced economies if its military burden does not diminish. Forecasts of 3-4 per cent annual GDP growth are highly unrealistic, given emigration, trade sanctions and the huge fall in investment.

But there are economic incentives for outside players to take action. US President Donald Trump's interests ulti-

mately align with Israel's, not Netanyahu's. After all, Israel is a "high maintenance" ally for Washington; it received about \$18bn in US military aid in the year after the October 7 attacks. Trump does not want to spend US taxpayers' money on foreign wars, especially in the Middle East. He wants to hold on to Gulf deals that enrich his family.

No stranger to shifting allegiances, Trump could still pressure Netanyahu to change course. He holds many cards vital to Israel, including military assistance and economic support. Such pressure could topple this government and lead to elections that halt Israel's democratic backsliding, economic decline and regional aggression. Instead, a regional accord, including normalisation with Saudi Arabia, could be negotiated, changing political and economic dynamics by slowing emigration, and enhancing trade and foreign investment. Without it, the Israeli economy's further decline seems inevitable.

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