

המכון למחקר כלכלי בישראל  
על-שם מוריס פאלק בע"מ (חל"צ)  
The Maurice Falk Institute for  
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## **Early Economic Research in Israel: the Falk Project**

by

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## Introduction

The new State of Israel inherited a wide body of knowledge about its economy accumulated during the Mandatory period by the mandatory government and by research carried out by the Jewish Agency for Palestine, the Histadrut, and private groups and individuals. The most important of the economic studies were Gruenbaum's estimates of national product, separating the Jewish and Arab economies,<sup>1</sup> and the survey prepared by three American economists to strengthen the Jewish Agency's argument that the economy had substantial absorptive capacity.<sup>2</sup> The new state took over the mandatory government's Central Bureau of Statistics; Gruenbaum (Gaathon) headed an economic planning unit, and domestic economists and men of economic affairs, mainly connected to the ruling political party, headed the Government's ministries. However, faced with major economic problems in the formative years, the Government still relied heavily on *ad hoc* foreign US and UN experts for advice on various economic matters.

Important developments affecting domestic thinking about economic problems took place in 1953-54. One was the creation of an economic advisory committee, headed by Oscar Gass, in the Prime Minister's office. Though its core consisted of six foreign experts, each was matched by a domestic counterpart and assistants; these then continued as advocates of the way economic problems were to be studied. A second was the entry into the labor market of the first graduates of the new economics program of the Hebrew University, students of Don Patinkin, an American economist who joined the economics department and reshaped its program along American lines. These young graduates brought new ways of thinking to the various Governmental economic departments, in particular to the Ministry of Finance budget planning unit. A third development was the creation of an economic research department, manned by these graduates, in the new central bank, the Bank of Israel. This department has developed into Israel's most important economic research organization. The fourth development was the creation of a private economic research institution, financed by grants from the Maurice and Laura Falk Foundation. Called "The Falk Project for Economic Research in Israel". This research program lasted for ten years, after

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<sup>1</sup> Gruenbaum (Gaathon) (1941).

<sup>2</sup> Nathan, R.R., O. Gass and D. Creamer, (1946).

which it was transformed into a separate research institute as part of the Hebrew University. This paper discusses the objectives, activities and achievements of the Falk Project during its ten years. Though the new permanent institution, the Maurice Falk Institute for Economic Research in Israel, has continued the objectives of the original project, but by the time of its creation the Falk Project had concluded its pioneering contributions.

### **Establishment and Structure of the Falk Project**

The creation of the Falk Project was initiated by a meeting between Leon Falk and Steele Gowe, director of the Laura and Falk Foundation,<sup>3</sup> with Abba Eban, Israel's ambassador to the U.S., in March 1952. This was followed by a memorandum by Eban outlining the need for an independent economic research institution in Israel, then by an initial grant of \$10,000 for a survey and recommendations by A.D.H. Kaplan of the Brookings Institution. Simon Kuznets agreed to head an advisory committee, and Daniel Creamer<sup>4</sup> agreed to serve as first Director of Research. They visited Israel in the winter of 1953-54 in order to set up the new institution. In January 1954 the Project began operations with a five-year grant of \$430,000. A second five-year grant, the two totaling \$814,573, continued the work of the Project until it was replaced by a new institution, as part of the Hebrew University – as recommended by Kuznets - with a \$500,000 grant by the Falk Foundation matched by an equal amount by the Hebrew University. The older institution had both American and domestic advisory committees, made up of economists, other academics and representatives of financial institutions. The new institution had only a domestic advisory committee, though Kuznets remained as a member of the committee.

The two objectives of the Falk Project were to foster research on the Israel economy and to train young local economists in economic research. The choice of a private institution was

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<sup>3</sup> The Maurice and Laura Falk Foundation was founded in 1929 and over the years gave substantial grants for education, health and welfare in Pittsburgh, Pennsylvania, as well as grants for research in economics and education, starting with one to the Brookings Institution in 1931. See Starrett (1966).

<sup>4</sup> Kuznets, at that time a professor of economics at The Johns Hopkins University (later at Harvard and a Nobel Prize recipient) had pioneered national income accounting. Creamer was an economist familiar with the Israel economy from his work as part of the three-man team that had written *Palestine, Problem and Promise*, in 1946.

based on the idea that the pressures of government often limit the resources (if not the will) for objective serious basic research. Moreover, it was felt that in light of the special problems faced by the young State of Israel foreign economic experience and policies should not be automatically copied without serious consideration of their applicability to local conditions. As to scope, all aspects of the economy were considered worthy subjects for study: population, labor force, national product and its components, and the structure of individual industries, agriculture, industry, and financial institutions.<sup>5</sup>

Whereas the arguments for a private institution for economic research are clear, the need for a private institution to train empirical economists is not that obvious. There already existed a fine, private university. However, the Hebrew university had only recently restructures its economics program, not as yet stressing research methods, and it was only later that this area was developed at that institution and the universities founded later: Tel Aviv, Bar Ilan, Haifa and Ben Gurion. For this reason the first director of research, Daniel Creamer, was a seasoned American research economist, and after his two-year tenure he was replaced for one year by another American economist, Harold Lubell, who had been part of the first research program. Don Patinkin, essentially a theoretician, took over as Director of Research in late 1956, not till after he had spent a sabbatical year at Johns Hopkins University with Kuznets, familiarizing himself with empirical research. Patinkin, then virtual (though not yet official) chairman of the Hebrew University economics department, continued as Director of Research after the creation of the new institution.

### **Research Program**

With its limited resources the Project could not conduct major surveys, but had to rely on available data, most of which were at the Central Bureau of Statistics (CBS), and kept only a very small permanent staff, hiring part-time researchers. As stated in its first annual report: “The individual studies that compromise the research program provide, in essence, a list of seized opportunities: whenever a mature investigator expressed an interest in research that promised to add to our knowledge and understanding of the economy, and there was a body of data that could

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<sup>5</sup> The objectives are set out in the First Annual Report , (1954).

be used or secured, the opportunity was translated into an individual study.”<sup>6</sup> In fact, this was the general policy throughout the ten year period: individuals suggested research projects that interested them, and the director of research accepted or rejected them. There was one major exception to this rule. The background of both Kuznets and Creamer was in studies of aggregate economic performance, thus the most important initial program, conducted by Creamer himself, was to revise the estimates of domestic product made by Gaathon, with the help of the staff at the CBS that had worked with Gaathon.<sup>7</sup> To complement these estimates, H. Lubell was chosen to estimate national income, and N. Halevi to estimate international transactions.

The first sixteen research projects were classified in three areas. One was the measures of aggregate economic performance. A second group included studies on human resources. These studies gave several members of the CBS and other researchers a chance to summarize and analyze in different ways the data available at the CBS relevant to the major specific experience of Israel’s early years: mass immigration. Thus, M. Sicron undertook to study immigration; B Gil, places of settlement of the immigrants; A. Hovne, the labor force; H.V. Muhsam, the supply and demand for professional manpower, and S.N. Eisenstadt, a sociological study of occupational mobility.

Whereas this second group had at least a general unifying area – human resources - the third was an *add hoc* assortment of studies on specific aspects of economic performance. It clearly illustrates that topics were chosen without an overall plan. This group included studies on family farms (an exception to the general rule, since this entailed expensive field work undertaken with the cooperation of the Jewish Agency, the department of Agriculture, and Bank Leumi), value added in international prices, rents and housing, inflation and credit policy of commercial banks, saving and investment through provident funds, interrelations of public budgets, and Israel’s terms of trade under clearing and barter agreements. Except for the three supervisors of the aggregate performance studies, all the other researchers were part time. In

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<sup>6</sup> Falk Project (1955, p.11).

<sup>7</sup> Gaathon’s earlier estimates, (Gaathon, 1941), were later published by the Falk Project and the Central Bureau of Statistics.

addition to the research projects, the Project financed a training fellowship in agricultural marketing as part of its training program.

During the second and third year there were few *ad hoc* studies added, with most of the original studies nearing completion. However, data problems led to abandonment or to limiting the scope of several projects. Some studies were curtailed; the explanation given was that the original supervisor could not give the project sufficient time. In several cases the research assistants were promoted to project supervisor. In September 1956, Patinkin took over as director of research; from then on the project had one supervisor, one closely connected to the Hebrew University though the Project was still independent.

A new approach to the selection of research projects is noticeable from 1957, and is clearly stated in the *Fourth Annual Report: 1957 and 1958*, the first under Patinkin's administration. "During the last two years it has proved possible to shift the major resources of the Falk Project to the new program, which is to emphasize more intensive analysis of data bearing upon a few problems central to the understanding of the Israel economy - the structure of expenditure and savings, the supply of capital, the effect of mass immigration on the structure of wages, the supply and demand for skilled manpower."<sup>8</sup> Clearly, the emphasis is on studies that are relevant for economic policy. The paramount example of policy implications from analysis of previous studies is Patinkin's own essay "The Israel Economy: the First Decade", included in the *Fourth Report*. After surveying Israel's development, pointing out impressive achievements, in a concluding chapter Patinkin maintained that Israel's main problem was and continued to be its balance of payments deficit and reliance on foreign aid, and he suggested how this problem should be dealt with.<sup>9</sup>

New areas of research inaugurated in the following years included human capital, consumption savings and income patterns, the structure of Israel's manufacturing, the effects of

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<sup>8</sup> Falk Project (1959. p.5).

<sup>9</sup> Patinkin's conclusions were hotly debated, particularly by M. Michaely, who raised a methodological question: he claimed that the relative size of foreign aid (the ratio of the balance of payments deficit to GNP or total resources) should be measured in constant prices, and not, as Patinkin did, in current prices. Measuring in constant prices alters the conclusions.

immigration on wages, income distribution, and the size of the Government, Histadrut and the private sector in Israel's economy.

### **Relations with the Department of Economics**

It could be expected that being located in Jerusalem, the cite of the only higher education institution in Israel with an economics department, the project would rely for its project supervisors on faculty members of the Hebrew University. Though two of the seven members of the Israel advisory committee were professors in the department, no permanent member of the department was among the first project supervisors. The new, American style, economics program was still in its early stages, and Patinkin had just sent his first students for doctoral studies abroad, thus only one, an American trained external teacher (A Kessler) supervised a research topic. The rest of the original project supervisors consisted of several American economists, including recent immigrants, CBS staff and other civil servants, and several economists in the business and banking community who suggested projects in their specialties. On the other hand, those projects which were located in Jerusalem itself mainly relied for research assistants on students at the Hebrew University. In some cases where the project supervisor could not continue or the project was cut down in size, these assistants took over, and some presented the finished work as a master's thesis to the economics department.

For several years after Patinkin took over as Research Director, and was at the same time Chairman of the Department of Economics, the research staff still had few department members. Even when the first group of students which Patinkine had sent abroad returned with their PhD degrees they did not work for the Project. In fact, several were employed in a department-initiated research project headed by Professor Bonne. For several years, Patinkin also acted as official Economics Department faculty advisor for MA projects conducted at the Project, sometimes even in areas for which the Department had a specialist. In 1957, N. Liviatan of the Economics Department (working on his doctorate) and Y. Mundlak of the Economics Department in the Faculty of Agriculture were the first to start a new trend which marked the 1960s: HU economists doing their research with the aid of supplemental funding from the Falk

Project.<sup>10</sup> These two, later joined by Y. Grunfeld, brought with them new econometric methods both to the research programs and to the teaching of economics.<sup>11</sup> The newer research tools are evident in the nine theoretical Research Papers which later were published in academic journals.

The separation between the Falk Project and the Economics Department made it possible to avoid the unpleasantness within the Department caused by some members getting additional pay and others not. While an argument can be made that those willing to work on empirical research on the Israel economy, on projects that take years, and end up in form unsuitable for publication abroad – a necessary condition for academic advancement – deserve some recompense, the theoreticians still see this as bias.<sup>12</sup>

### **Appraisal**

Because the present writer, the first researcher hired locally, was involved in four of thee early projects, his objectivity is subject to question. Consequently, this appraisal will not deal with individual reports, but only with the influence of the Project

In the ten year report Patinkin states that there were too many projects not completed. He describes this as arising primarily from the fact that the research supervisors were part time and therefore some could not give the research their full attention. Actually, after the first two or three years there were only rare cases of studies that did not reach some sort of publication. In all, forty three empirical research projects initiated during the ten year period were completed and published (some in the two following years): 25 books in print or mimeograph (6 published jointly with the CBS) and 18 research papers, 9 of which were theoretical papers presenting methods of analysis, based on those used in the empirical studies. The theoretical papers were later published in academic journals, as were several condensed versions of the empirical studies. Though all publications were subject to Kuznets' approval, quality varied. Some sere simple,

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<sup>10</sup> This section is based on Michaely (2007).

<sup>11</sup> Grunfeld's tragic early death was a great loss to both institutions.

<sup>12</sup> The econometricians were able to publish abroad theoretical papers based on their work, others wrote papers additional to their empirical work, and some published abroad papers "examples from the Israel economy". When the Falk Institution was set up, connected to the HU, this problem caused some friction.

though original, statistical surveys; some had more penetrating analysis, and others more originality in approach.

Their influence must be judged by the extent that to which the Falk Project in its ten-year career attained its basic objectives: fostering empirical research on the Israel economy and training of young researchers. The Project's official mandate was not to present policy papers, despite clear indication by his choice of subjects that Patinkin was interested in influencing policy,<sup>13</sup> but rather to add to empirical knowledge, which of course could be used for developing rational economic policies. Perhaps shorter delays in publication and more aggressive dissemination of research results would have led to more influence on policy. Since the research projects usually took a long time before completion, preliminary results were presented in the annual reports, some in Discussion Papers (several of these were final reports of smaller projects and some were theoretical papers) or in local periodicals, such as the *Jerusalem Quarterly*. Final reports appeared in book form, sometimes only in mimeograph, usually in both Hebrew and English.<sup>14</sup> Three Annual Reports included complete essays: Patinkin's "The Israel Economy: the First Decade" in the Fourth; G. Hanoach's "Income Differentials in Israel", in the Fifth; and H. Barkai's "The Public, Histadrut, and Private Sectors in the Israeli Economy", in the Sixth. The last Annual Report, *A Ten Year Report 1954-1963*, presents short descriptions of all the completed projects

Of paramount and of more lasting importance was the work on creating a system of national economic accounting, mostly carried out with the CBS, on which the CBS has continued to base its estimates, of course with continuous improvements in definitions and estimation methods. Most projects did try to concentrate on areas of the economy in some way special to Israel. Because the main factor unique to Israel in its formative years was mass immigration it was quite reasonable to devote much of the early research program to studying the effects of this phenomenon: its size, composition, place of settlement, occupational structure and effects on human capital, wages and income distribution. Other factors of particular importance to the

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<sup>13</sup> Even after the Project was replaced by the newer institution, the board of directors voted down a proposal that short-term policy papers be added to the program.

Israel economy in its early years include the dominant role of Government in directing and controlling the economy, the role of agriculture and the small family farm, the importance of foreign aid, the complicated exchange rate system, and the Arab labor force. Though some of these factors have changed gradually over the years, all of these studies were of great immediate interest and, in later years, remain important for historic analysis.

As previously mentioned, all the research assistants (other than some of the CBS staff) were students, usually after completing their first degree, in economics, agricultural economics, or statistics. Over the ten-year period the Falk Project included among its research staff seven newly appointed faculty members and eighteen students who went on to become faculty members at the Hebrew University or other Israeli universities. Others went on to senior positions in Government economics departments and at the Bank of Israel. The Project certainly fulfilled its aim of provided training opportunities for young researchers. Thus, it is fair to conclude that, in general, the Falk Project lived up to the expectations of its founders.

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