

The mirage of a home and a car

Car and housing prices are sky-high in Israel. Yet it has no viable alternative to home and car ownership in the form of cheap rent or efficient public transportation

By Efrat Neuman and Daniel Schmil

Lately, the dream of owning a home seems to have grown increasingly distant for the average Israeli without one. More than a mere economic decision, home ownership is a compulsion hard-wired into the Israeli DNA. It gives us a sense of security and peace of mind. To achieve it, we are willing to accept the bank as our constant companion for the next 30 years.

The fact that double-digit inflation has recently hit Israeli real estate prices means that buying a home has become even harder, perhaps impossible. According to the Central Bureau of Statistics, housing costs are the Israeli household's largest monthly expense: NIS 3,200. In 2010, the average apartment cost just over NIS 1 million, according to Housing Ministry data, but this includes low-priced housing in peripheral areas of the country. Anyone looking for a place in the bustling center of the country would be thrilled to cut a check for NIS 1 million if something satisfactory could be found at that price.

The ministry's summary report for 2010 said that while the average-priced home in 2007 and 2008 cost the equivalent of 105 average monthly salaries, in 2010 this jumped to 129 average monthly salaries.

A study published in 2010 by the BDO Ziv Haft consulting group showed that the situation in Israel is extreme compared to most other countries: Whereas in Israel, an average-priced home was equivalent to 114 average monthly salaries at the time of the study, the corresponding figures elsewhere were 90 in France, 71 in Britain, 60 in the United States, 54 in Germany, 42 in Switzerland, and a paltry 30 in Sweden.

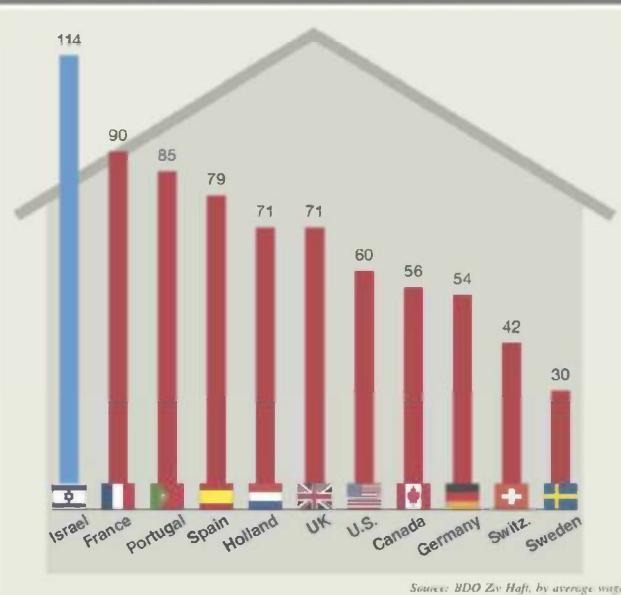
Israel's pricey real estate can easily be explained as a case of supply and demand: This is a small country with very little land and great demand. Another reason is its dreadful transportation network, which discourages Israelis from commuting any distance, but this is also a cultural matter: As opposed to Israelis, Americans, for instance, think nothing of a daily hour-and-a-half commute by car or train and are likelier to settle for cheaper homes in the far reaches of suburbia. The U.S. is also a much more transient society with less longing to live close to family, so folks there aren't as determined to live in a specific locality.

The high demand for property in Israel is also due to a social convention that it is a parent's duty to assist grown children in acquiring their first home. Long-term tenancy hasn't become a norm and rental housing projects hardly exist, so Israelis usually have little choice but to turn to home ownership. In countries like the U.S., in contrast, renting is an accepted and established alternative.

Where rentals are available in Israel, usually for privately-owned apartments, the cost isn't high in nominal terms. But in terms of per capita gross domestic product, it hits the top of the worldwide charts. And many think that rental charg-



No. monthly salaries to buy an apartment



es will soon go even higher to more fully reflect rising property costs.

Here are a few examples of monthly rental prices around the world: A two-bedroom apartment in Little Rock, Arkansas or Portland, Oregon costs about \$850; in Manhattan, the same can easily cost \$3,000; in London, 2,000 pounds (about \$3,200); and in Paris, 2,000 euros (\$2,800).

In Tel Aviv, the average monthly rent for a two-bedroom apartment is NIS 5,000 – about \$1,400. In less centrally-located Hadera, it would be NIS 2,400 a month, or roughly \$660. In a typical suburb of Sydney, Australia, the price for a two-bedroom unit might reach \$2,000 a month, but Australia's per capita GDP is double that of Israel.

Double the U.S. price

A quick scan of new car prices in the U.S., Europe and Israel is enough to show that here, too, we pay more, much more. In Israel, a family car is double the cost of an equivalent-sized compact in the U.S., notwithstanding the average Israeli salary being one-third lower. For Americans, it is much easier to buy a car, and much cheaper to maintain it, too.

Consider the popular Mazda 3 with a 1.6 liter engine: An Israeli will spend NIS 120,000 at the showroom, while its sticker price in the U.S., with a 2.0 liter engine, is \$15,800 – about NIS 56,000. Drivers in France, Germany and Britain will pay the equivalent of NIS 94,000 to NIS 96,000 for the same car, and in Australia its price is about NIS 86,000. The Volkswagen Golf, previously dubbed the Rabbit in North America, costs NIS 140,000 in Israel, but only NIS 72,000 in the U.S., NIS 90,000 in Australia, and NIS 100,000 to NIS 108,000 in Europe.

Factoring in income and per capita GDP, the comparative

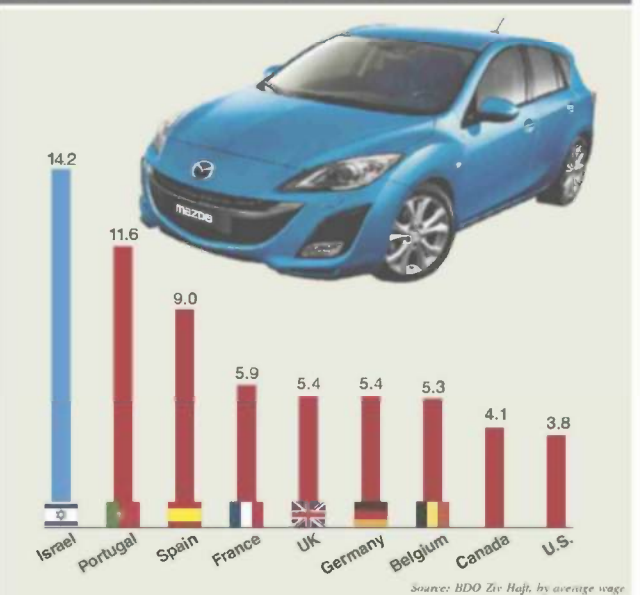
figures become starker yet: Average paychecks are considerably higher in the U.S., Britain, France and Australia than in Israel. To illustrate this, it would cost an Israeli 14 average monthly salaries to purchase a Mazda 3. But according to BDO Ziv Haft data, only four months of the average salary are sufficient to buy the same car in the U.S., reflecting both higher wages and lower car prices. In Western Europe, a Mazda 3 costs about six average salaries.

Are we paying an exorbitant amount at the gas pump too? When the public outcry against rising gasoline prices began in February, the Finance Ministry quickly whipped out a comparative price chart to show that Israelis aren't being gouged any more than the rest of the world: In comparing the cost of 95-octane gas, it turns out that drivers pay more per liter in 13 out of 27 countries. Whereas in Israel, the price at the time was 1.41 euros (it has since gone up), the price was 1.70 euros in Norway, 1.48 euros in France and Finland, and 1.47 euros in Germany, Britain and Sweden.

In the other 14 countries it was cheaper, particularly in Eastern Europe: A liter of gas cost less than 1.20 euros in Bulgaria, Latvia, Estonia and Poland. In the U.S., which didn't appear on the list, gasoline prices are much lower: approximately 0.70 euros (\$1) per liter. So besides their cars being less expensive, so is their gas.

Thus Israel is comfortably located right in the middle of the chart for gasoline prices. But this comparison is misleading, because it lists nominal prices, while average wages in Europe are higher than in Israel. Europeans also have an alternative mode of travel – efficient public transportation. If they feel like polluting and paying less, they

No. monthly salaries to buy a Mazda 3



can leave the car at home. But in Israel, there is no effective alternative, so the demand for private transportation is fairly inelastic.

Why are cars in Israel so expensive?

Automobile prices in Israel are among the highest in the world. Except for Singapore and Denmark, the sticker price on any model in Israel is sharply higher than anywhere else in the world. What Israel, Singapore and Denmark have in common is steep purchase taxes on private vehicles arising from a similar consideration: too small an area to accommodate masses of cars.

But as opposed to Israel and its dearth of appropriate alternatives to private car use, Singapore and Denmark have well-developed and efficient public transport systems.

In Israel, every new car gets slapped with a basic 83% purchase tax, slightly less if the vehicle is considered environmentally friendly. Added to that is 7% in customs duties for imports from Japan and South Korea. Value-added tax, at 16%, needs to be paid on the entire amount as well, bringing the total tax rate on the purchase as high as 120%.

The original reason for the hightaxation, which dates from the early days of the state, was that a car was deemed a luxury item and therefore easier to tax. Afterward, it was claimed that the tax was meant to prevent overcrowding on Israel's meager road system. The Israel Tax Authority has now finally begun admitting that the income the state derives from direct taxes on vehicles is too substantial to sacrifice. In 2010, the treasury raised NIS 8 billion through these taxes, 8.6% of all direct taxation income.

There's more to this story:

The largest new car buyers in the country are the leasing companies, which enjoy 15% to 20% discounts, if not more. To maintain this discount margin and at the same time maintain high prices in the used car market, where the companies earn additional income, consumer prices are inflated even further. Prices in Israel for family cars are nearly all identical – between NIS 118,000 and NIS 120,000. If there is any competition, it doesn't apply to individual car buyers, but only to the leasing companies.

It would be some consolation if vehicle usage costs were low, but this isn't the case. There is a NIS 2.90 tax on every liter of gasoline, and this too comes with a VAT surcharge. Surprisingly, however, fuel prices in Israel aren't high compared to Europe: They are lower than in Holland, Norway and Britain, though higher than in Spain and eastern Europe.

Gasoline taxes generate NIS 12.7 billion a year for the treasury. Like with cars, demand for gasoline is considered rigid. Lacking a viable alternative in the form of convenient and efficient public transportation, the public is forced to grit its teeth and continue paying through the nose.

The Finance Ministry has begun considering changes in taxation for the automotive industry. The idea is to reduce purchase taxes and raise taxes on usage, such as fuel taxes and licensing fees. Under the proposal, taxes would be based on the car's contribution to environmental damage and road congestion. This approach holds that there is no need to tax vehicle ownership, as the purchase tax does, only vehicle usage.

It is hard to believe that the tax burden on drivers will be lighter following the reform. But at least it will be distributed more fairly.