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THE ISRAELI ELECTIONS:

WHAT DO THEY MEAN FOR THE UNITED STATES?

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P R O C E E D I N G S

MR. BYMAN: Good morning and welcome. I'd like to thank you all very much for braving the snow, I guess more accurately, braving the traffic that comes with the snow, and joining us here this morning.

I'm Dan Byman. I'm the research director of the Saban Center for Middle East Policy here at Brookings as well as a professor at Georgetown, and I'm delighted to welcome you to this event on Israel's elections.

When we conceived of this event, we knew that Israel's elections were going to have important consequences, but at least I was not anticipating that they would be particularly exciting. For the sake of this event and perhaps in general, I'm actually quite pleased that the elections proved surprising, again, at least to me, in so many ways.

What happens in Israel, of course, is important not only for Israelis and their immediate neighbors, but is also tremendously important for U.S. policy in the Middle East, and as a result, who's at the helm and the strength of the coalition and other basic questions that were decided, in part, yesterday and will be decided over the next few days, are of vital importance to U.S. foreign policy in general.

And that's why I'm delighted to have two excellent speakers from Brookings to educate us further on what happened.

Our first speaker today is going to be Natan Sachs. Natan is a fellow at the Saban Center. He is a specialist on Israeli politics and he's writing a book on Israeli domestic politics and the linkages with Israel's foreign policy.

Our second speaker today is, I think, well known to almost all of

you. This is the director of the foreign policy program, Ambassador Martin Indyk. Ambassador Indyk, among his many accomplishments was the senior person for the Middle East under the Clinton Administration, ambassador to Israel for the United States during many of those years, and has long been a watcher of Israel and an observer of Israel's interactions with its neighbors.

I'm going to, rather than have them give formal presentations, I thought it might be best if we did this really as a conversation and I'll kick off the conversation with some questions for both of our speakers today, and then I'd like to open it up to all of you for your questions.

Natan, if I can really begin with you, give us a sense of this election. It was a surprise in many ways, but what are the possible coalitions that are going to come out of this? What's the government going to be or at least what are the different scenarios for what we can expect in the weeks to come?

MR. SACHS: Well, the surprise that we saw is, in some ways, dramatic. The event is, indeed, much more interesting than we thought. But I just say that the surprise is probably less dramatic than it might seem. If you think of the coalition today, the graph you have in front of you is actually just off by one. We've got the final tally today with votes of soldiers and the right-wing as one more -- the Jewish Home on the far right has one more while Raam-Ta'al, one of the Arab parties, has one less.

So, at the end of the day, the right wing has about 61, the right and center and religious have -- sorry, right and religious have 61, and most of our projections said 34 -- 63, 64, 65, so it's not really off by much.

The drama is that it is not nearly as -- that the center has done much better than many people think, and in particular, the party of one Yair Lapid called Yesh Atid, There is a Future.

So, the star of these elections, the one everyone in Israel is talking about today, is Yair Lapid. You can see him in the center above 19, it's his name rather than the party's name under the graph there, and he's now the kingmaker. In many respects, there is no coalition without Lapid, and that's a bit of a surprise.

If you think of the summer, Netanyahu was described in *Time Magazine* as King Bibi and he brought Kadima in, the largest party, Kadima, from the center into government. He had options and then they left. He had options on right, on center, he could do almost whatever he wants.

That has changed. Now he needs Lapid and if you count the numbers, even with Lapid, it's not enough. He needs others as well.

So, the coalition is much more constrained than it used to be, the leeway is much less than it was, and this means that Netanyahu's probably going to have to make certain decisions on what kind of coalition he wants and what coalition Lapid can swallow, and then that will determine a lot of the policy.

So, I think we can start with the assumption that Lapid is going to be in. Nothing is certain, but that is a given and everyone's talking about that. In fact, they're talking about what post, exactly, he will take.

Former Foreign Minister Avigdor Lieberman is trying to urge him towards finance so that he doesn't steal the foreign ministry from Lieberman himself. Lapid will probably prefer the foreign ministry because finance entails

terrible cuts in the upcoming budget, and that's not something anyone wants to do, and the finance minister also works very hard and has little time for politics.

But a lot of it very much depends on who the other partners are, and there are basically two options. If you look at the graph, and especially the second one with the blocks, one option is to go with the ultra orthodox, the classic perennial partners of almost any coalition in Israel, and the other is to go with the right wing, the Jewish Home, or a combination of both.

If you do the math, you need 61 for a coalition in Israel and even 61 is very close, and I'll get to that maybe a bit later about why 61 would be very unstable in Israel right now.

And so, this choice entails a lot of what the government what the agenda will be. Going with the ultra orthodox will be very difficult for Lapid to swallow in some respects. He'll have to curtail some of his promises about religion and state and especially about conscription of ultra orthodox into the military in Israel. These are issues that get less attention, naturally, abroad, but are extremely contentious in Israel. They're really one of the core issues that Israelis care about and especially the Lapid voters.

But the other option, then he would go with Naftali Bennett, the leader of the Jewish Home, on the far right, and that would entail some compromises from the left side of Lapid's new party, which includes a whole host of new politicians, not one of them was a member of Knesset before. This was a promise Lapid made.

That would be one choice. And then he could go -- so, he could go

with (inaudible) with their ultra orthodox and then opt to compromise on issues of religion and state, or he could go with the right wing, have what is known as a civic kind of government pushing on conscription, pushing on questions of religion and state, but then compromising on issues of classic right and left Palestinian issue, assuming they are even part of it.

If I had to venture a guess, and it's only a guess, we're just two days away, it looks very clear that we're going to have something reminiscent of ten years ago, 2003. Two-thousand and three, there was a sitting Prime Minister from the Likud. There was a center party headed by a journalist named Lapid, and he was the surprise of the elections. He won 15 seats. This Lapid has 19. That Lapid was Yosef "Tommy" Lapid. He happened to be the father of this journalist, Yair Lapid -- the late father.

Tommy Lapid ran on a secular agenda with the Shinui party, and his biggest achievement, and the one that made his voters very happy, was that there was a government without the ultra orthodox, at least at first.

Sharon, then the Prime Minister of Likud, before he formed Kadima, formed a government with Lapid, Tommy Lapid, and the other partner was the National Religious Party from the right, the modern orthodox. That is now today called the Jewish Home.

So, in 2003, we saw the fundamentals of a coalition between the Likud, between the National Religious Party, and between, Lapid, journalist Lapid, in the center.

The most likely scenario, I would guess, although Netanyahu and

Sharon are very different individuals, would be Likud with (inaudible), Lieberman's party in alliance with Likud, then Jewish Home, which is strongly based on the National Religious Party, and the new Lapid, Lapid the younger and called Yesh Atid. He was a very loyal son. He's less of a staunch secularist, less of a firebrand than his father, much more consensual. He's a very famous person in his own right in Israel. He's a celebrity, that's really the appropriate word, very much a TV personality, movies, heartthrob kind of figure. But his platform -- and so his platform is much more moderate. He has religious in his party, but nonetheless, he's a Lapid, he is the son of his father and a very loyal son.

That's sort of where we'd guess it would go, and this has implications for what it says for the agenda. That means going for the civilian agenda and it means, perhaps, doing much less on, if there was any chance of anything, on the Palestinian question with Bennett and party.

MR. BYMAN: Let me follow up with a question. I can look at these elections and see the narrowing of support for Netanyahu and say it's going to be a weaker government, but since he can go both right and left, that seems to give him a lot of options and a lot of flexibility in a way that actually makes him stronger, or at least strong. Do you feel that whatever emerges will actually be a fairly strong and stable coalition that will enable the government to act or not act, but in a fairly decisive manner as opposed to some of the governments we see in Israel that were quite weak and really unable to accomplish any other agenda?

MR. SACHS: The short answer is no, but I'll qualify that in a minute. The weak Likud, if you look at the numbers, Likud plus the center is just not

enough. Likud has -- and Yisrael Beiteinu, and Lieberman's party together have only 32 -- 31, excuse me, which is a drop from 42 of their combined parties last time. Plus Lapid, plus Kadima with two, still exists, plus Tzipi Livni's party known as The Movement, all that together is simply not enough for a stable coalition, so there has to be either religious, ultra orthodox would be the obvious choice, or a Naftali Bennett, the modern orthodox.

But then we have strong conflicting agendas, Naftali Bennett is very rightwing and most importantly his back benchers are very right wing, and between him and the movement of Tzipi Livni, for example, there is strong tension on that.

So, in the summer we had exactly Netanyahu reigning as a sort of (inaudible), kind of in the center, he can choose right and left, he can do whatever he wants. Now we have a very different situation. The one qualified, that I know, is that the scenario described earlier, the Sharon 2003 scenario, it can be stable. It is stable if the agenda is very clearly focused on domestic things, if it is things that both Bennett and Lapid can agree on, and Bennett can agree on quite a bit. He's been signaling this as well. He's modern orthodox. He's much less orthodox than some, and even in the National Religious Party, he is sometimes derided as "religious lite".

He lives in Ra'anana, a very central kind of Israeli town, very Anglo-Saxon, so there's stuff they can agree on as long as that pesky issue of the peace process, the United States, the future of Jewish Democratic state, all these questions -- as long as that doesn't bother anyone, they can live harmoniously.

If that comes up, if one settlement outpost is withdrawn, Bennett's

backbenchers will throw a fit and it is worse than Netanyahu saw in '98 when he had trouble from the right. He now has backbenchers not only from Bennett, but from his own party as well, who are very rightwing in some respects, at least.

So, in short, there is a stable coalition to be had, perhaps, assuming Lapid's party can stay coherent, and we don't know much about it yet, but only if the issue that Washington cares about most, besides Iran, is left aside.

MR. BYMAN: Martin, can I ask you exactly that?

It's not exactly a secret that the Obama Administration has not seen Prime Minister Netanyahu as their favorite partner, and there have been remarks that have slipped out in the media here and there that have made that -- the tension and the dislike rather clear.

Is this good news for an American Administration? Is this a government that the United States could work with better than in the past?

MR. INDYK: It's better news than we thought we were going to have, but let me, if I might, just comment -- make one comment on what Natan said in I think a very compelling analysis. And it's simply, *cherchez la femme*. The first woman that we need to keep our eye on is Sara Netanyahu, Bibi's wife, who has a real problem with Naftali Bennett, who used to be Bibi's director in his office and was forced out, according to press reports, by on Sara Netanyahu's insistence.

The bad blood between Bibi and Naftali Bennett is extreme, particularly because of the campaign where Bibi really did a lot to go after Bennett in order to stop the erosion of the good voters to Bennett, to the right, and in fact,

the apparent explanation for this surprise result that none of the pollsters predicted, was that in the last 72 hours, Bibi went after Naftali Bennett so effectively that he drove voters away from Bennett, but not back to the Likud, but back to Yair Lapid, and that explains the dramatic numbers that Yair Lapid ended up with, I think to his surprise as well, and why the pollsters didn't pick it up.

So, there's a lot of bad blood there and Bibi has to be very worried, precisely as Natan said, about leakage. If Bennett is in the government, about leakage of the Likud, which has become a very hard right party in its constituencies now, in it's members of Knesset, for them to start moving towards Naftali Bennett.

So, I suspect that for a combination of reasons, he doesn't actually want Bennett in the coalition, would rather have him languish outside, hasn't, as far as we know, even called him, whereas the first call he made even before he claimed victory was to Yair Lapid, and that the coalition may end up with being more restricted in the sense of Lapid and Yesh Atid on the center, and Shas, the Sephardi religious party, and that would be the core of the coalition, and then presumably add Kadima and Livni to that, and that would be kind of interesting, to come back to your point, your question, Dan, which is, it would change that dynamic that you described so well of within the government, because if you had a coalition of Likud, Beiteinu, Shas, and Lapid, Kadima, and Livni, then it looks more like a centrist religious coalition than a center-right coalition. And then things become more possible on the Palestinian issue in a way that they would not in the scenario that Natan explained.

Now, before you get your hopes up and before the administration

gets its hopes up, there are a number of very important points to bear in mind about this election. First of all, the Palestinian issue was only promoted by one party, that was Livni's party, and she got six seats, you could say merits also, on the left, but essentially, that is the constituency for a government that wants to move on the peace process.

Lapid and Shelly Yachimovich of Labor, stayed away from the Palestinian issue with a passion because they understood that the voters had no interest in this issue. And I do not believe that Lapid is going to make it a strong point in his demands for joining the coalition. He's going to be far more focused on the things that his voters wanted when they voted for him, which is the social agenda, it's about housing prices, it's about jobs, it's about making ends meet, and it's about fear of an austerity budget that's coming, which, by the way, I think he would be wise to actually take on the finance ministry, but I'm sure Natan is right that he won't. But he should because he'd have much more control about who gets the cut in that situation.

So, what does it mean, bottom line? There's a sliver of hope, no more than that, that with a more centrist coalition than we had expected that there will be a greater willingness to move forward on the Palestinian issue, but it's not at the top of the agenda. It will be a minor key in any coalition agreement.

And this is one other point that I think is important to make here. Lapid's leverage is now, before he goes into the coalition, before he signs the agreement. Afterwards, Prime Minister has immense authority and all of the cabinet ministers that he will have been responsible for getting into their seats will

quickly discover that there's a very special glue that adheres to cabinet seats in Israel, and once they sit in them, they somehow get stuck there and don't want to leave, and so if Lapid doesn't make the Palestinian issue his -- one of his causes going into the coalition, I don't see that he'll have much of a chance to do it when he's in.

MR. BYMAN: In your book, you -- I could say warn, I could even say mock, several U.S. attempts to try to shape Israeli domestic politics in pursuit of U.S. foreign policy goals, but does the United States have any ability to influence this, to try to take that sliver and at least make it, you know, something that has a fighting chance?

MR. INDYK: Well, it -- I think, yes, but it's on the margins. Senator Kerry is going through his confirmation hearings today. Is he going to put down a marker that Yair Lapid would hear and think that maybe it's important to be responsive to the United States? We just have to see how that plays out. As I say, it's a sliver of hope.

I think that President Obama's supposed comments that were leaked to and reported by Jeffrey Goldberg in a piece that got huge play in Israel in which the President was reported to believe that Prime Minister Netanyahu is a political coward who doesn't have the best interest of his country in his mind, those, which I think came out three days before the election, may have had a marginal impact, I think nothing more than that, together with the fact that Bibi has mishandled his relationship with the United States and everybody in Israel knows that. I don't think that either of those things helped Netanyahu.

But I don't think it was, in any way, decisive. Maybe it made a one- or two-seat difference, but I guess we'll never know, and the same thing applies to whatever it is that the Administration might put down as a marker now. Because the Palestinian issue was not an issue in the campaign, because the Israeli public, in what looks to me, personally, like a head in the sand attitude towards the Palestinians, simply has convinced itself that they don't have a partner on the Palestinian side, there simply isn't a pressure on the politicians from left to right to take this issue seriously.

And I'm afraid that until Israel runs into a brick wall on this issue, or a train wreck, we're not going to see the Israeli government, that's about to be formed, take seriously the idea of an initiative towards Palestinians -- an American initiative towards Palestinians.

MR. BYMAN: Natan, if I could ask you if you want to, first of all, comment on that, but also, when we say the Netanyahu government or likely Netanyahu government, what's the security cabinet going to look like? I realize it's speculative at this point, but we probably have some sense.

MR. SACHS: Yeah, I'd say that -- Martin's put it exactly about the religious party, it points us exactly to the fascinating previous mavericks of election. We were always obsessed with Shas, those of us who are completely obsessed with Israeli politics, if there are any here, I don't know, Shas was always the one we cared about, that was the maverick party of the '90s, they did whatever they wanted.

And now, again, to a certain degree, we come back exactly to this

question. Yair Lapid, as I mentioned, is not his father. He has, for example, number two is a rabbi, an orthodox rabbi, in his own party, which he handpicks. He has the right to pick his list for ten years in his party, that's actually the constitution of the party. Number two is a rabbi, and he's not the only one, and he has signaled that he does not rule out anyone.

His voters and his constituencies were chanting, "anyone but Shas", the old chant that Ehud Barak got when he was elected Prime Minister and defied in '99, this is what Yair Lapid got in his victory speech, "anything but Shas", (speaking in Hebrew). But he may well go with Shas, and the reason is two-fold. First, he is not the same as his father, and part of what he said just in the last two days since the election is that we need to go together, we're facing terrible things in the world, we want normalcy, that's the word he uses. He is the center of Israeli sort of discourse, he's the most Israeli of Israelis in his mind and he wants normalcy.

But to do that, he says, we have to go together. No more divisions, no more sectors, et cetera.

So, for that, he's come a long way from his father's rhetoric, and that would make it, perhaps, possible to go with Shas.

Secondly, we need to look at Shas. The Shas and National Religious tension, for one, is very, very interesting. That's part of what led the National Religious Party into government in 2003.

They had lost a tremendous amount of jobs in the rabbinate and the interior ministry, and a whole host of state institutions, to Shas that had become

ascendant in the '90s. Two thousand three was payback. They wanted to be in the government while Shas was outside, for internal, religious community reasons.

The same, to a certain degree, is true today and there's a lot of animosity between them, and so Bennett and Bennett's party may well want to come in despite the left wingers on Lapid's list, and there are a few, for this reason. For the same reason, Shas will have a big impetus to try and stave this off, and they have signaled very clearly that they do not -- that, as well, they will sit with anyone. They don't (speaking in Hebrew), they will go with anyone, right? Even Eli Yishai, the person on the rightwing of Shas says.

The final word, just on the religious part of politics, which actually is consequential for relations with the U.S., oddly enough, inside Shas there's a tremendous power struggle. The old charismatic leader of the '90s, Aryeh Deri, who had to resign because of a prison term, actually, for bribery, but very charismatic, very intelligent, very consequential for the peace process in the '90s, he's back. But he is co-chairman, that's actually the term, with Eli Yishai, the man who inherited it, who's much more rightwing, much less charismatic, less impressive in some respects, but now quite experienced, himself, and there's a third wheel, Ariel Atias, and above them all there's a very aged, Rabbi Ovadia Yosef, who just had a minor stroke.

Things are going to change in Shas. They had a disappointing number; that was Deri's task to bring the votes as the charismatic leader. He failed to do it. They're stuck. They're stagnant. Eli Yishai is very happy about this. But there's going to be a struggle in there and it's very hard to predict. It depends

partly on rivalry between the different sons of Rabbi Ovadia Yosef and we all wish him well, of course, but no one goes beyond 120 in Jewish tradition.

So, as I said, after 120 many things can happen.

So, that can be consequential. To your question, the short answer is, of course, I don't know. What we do know, that Yair Lapid will probably have his choice of position. He's going to be the senior partner, and an Israeli, it's usually a team of rivals, that's actually the norm, and so he can probably choose his post. Defense is very unlikely.

There was an experience in Israel, considered to be a bad experience, with the Civilian Defense Minister, and Yair Lapid has no military experience at all, so probably not that. It could be Treasury, I guess Foreign Ministry, but of course, Lieberman is in the wings.

The interesting thing is that the two most important people from a national security standpoint, one is Avigdor Lieberman, who's the partner of Netanyahu and is still a very important and influential man. We should not count him out, but he has had to resign from posts at least temporarily, hand it back to Netanyahu, because of an indictment over a much more minor, but nonetheless, corruption charge involving his post.

If he's cleared, which is not clear, but if he's cleared, he may come back, certainly to his senior post, he will come back, Ehud Barak, the Defense Minister, who's really there on his own ticket, had left the labor party, but was very important also as the de facto Foreign Minister, in a certain respect, because Lieberman was persona non grata in many places -- not quite as strongly as that,

but was not very welcome in many places.

Ehud Barak resigned from the Knesset, or retired, I suppose, he didn't run. He does no political backing.

Who Netanyahu appoints to Defense Minister is the big question. It could be Barak again -- personally, you do not have to be a member of Knesset to be a minister. But that would be -- and it could happen. His weakness may be an asset from Netanyahu's standpoint. A weak Defense Minister means a loyal Defense Minister in some respects.

It could be Shaul Mofaz, who has two seats and is also weak, but the animosity there is big. Mofaz, after all, left the government. I doubt that would happen. It could.

The natural choice is actually a strong candidate, Moshe Bogie Ya'alon, another former Chief of Staff like Barak and Mofaz, who is a member of Likud and sees himself as one of the successors to Netanyahu. This strength, this power of Likud, which is sometimes exaggerated, perhaps, is exactly his liability in Netanyahu's eyes.

So, I don't know, of course, who Netanyahu will pick, but these are sort of the options, and there could be a maverick choice. Some people have floated the name Tzachi Hanegbi, who used to be a young sort of radical, but became a trusted ally of Sharon and others and served in Parliament in the Security Committee. And so he actually could be a choice, he just rejoined Likud from Kadima, and apparently, Netanyahu and he get along very well these days. There are people who probably know about this, including in the audience.

This is sort of the lay of the land. At the end of the day, like Martin said, though, national security in Israel, first and foremost, is made in the Prime Minister's office. That's where most things are done. The Defense Minister is very important, partly because he has a statutory role in the West Bank, and has a huge budget, but the Prime Minister is what really counts.

So, continuity, more or less, will probably be the answer.

MR. BYMAN: Martin, one quick follow up on this point, one thing we haven't discussed is the Iran situation, and a number of the commentators who are frankly celebrating what seems to be the -- defeat is too strong a word, but the setback of Netanyahu at the polls were also pleased that this seems to decrease the chances of an Israeli confrontation with Iran over its nuclear program.

Do you agree with that? And what are the broader implications for kind of Israel-U.S.-Iran relations?

MR. INDYK: I don't. I'd be interested in Natan's view on this, but my sense is that it wasn't as if the rightwing was pushing for an attack on Iran. It was Netanyahu and Barak who felt this was important and several important rightwing members of their cabinet, including Bogie Ya'alon, who Natan mentioned as a possible Defense Minister, including Lieberman himself, were not in favor of a strike, certainly not rushing into it in the way that Bibi appeared to want to do that.

It's much more a split between Netanyahu and Barak, who's no longer relevant, on the one side, and the national security establishment of Israel on the other, which came out very vocally and forcefully, in an unprecedented way, against an Israeli strike or at least an Israeli strike in a situation which the United

States was opposed to it. And that happens to be popular opinion as well. A majority of the public don't support an Israeli strike on Iran unless it's done in coordination with the United States.

And I don't think that's going to change. The election results are not going to change that or the composition of the government. Lapid is a newcomer to all of these issues. He has no standing, no -- I mean, he has 19 seats, but he has no knowledge on this issue. I don't think he expressed an opinion on it in the campaign, so I don't see that that's going to make a significant difference.

And so the makeup is basically the same. The issue in 2013 is much more an issue for decision here by the President of the United States than it is, I think, by the Prime Minister of Israel, and people keep on focusing on, you know, what will Bibi do as the clock is ticking, and so on, but I do not believe that in the end Netanyahu will act against the will of the United States if it's clear that the President is going to live up to his word of preventing Iran from acquiring nuclear weapons.

If we move to a policy of containment, as some here suggest in the debate here, then I think all bets are off in terms of what Netanyahu might do, but as long as the President sticks with his current policy, which is to exhaust the negotiations, to try to get the Supreme Leader of Iran to accept curbs, meaningful curbs, on his nuclear weapons program. And if that doesn't work, then I think the President is the one, not the Prime Minister of Israel, that's going to have to make a very tough decision about whether he takes military action against Iran's nuclear facilities, whether he decides to let Israel do it, which I think would be a far more

complicated decision -- I mean, far more complicated in its consequences and therefore far more dangerous for the United States, or whether he's going to go to a policy of containment. But that's on Obama's desk, not on Bibi's desk.

MR. BYMAN: Natan, did you want to chime in on this?

MR. SACHS: I agree completely and I think that this is one of the points where it's very lamentable that the relation is bad. I mean, we can all have opinions on why it is and whose fault it is, et cetera, but the fact remains that the relation between the President and the Prime Minister is not as good as it usually is between these two posts, and in most respects it doesn't matter that much. Relations between the Administrations are very close. There's the cooperation on intelligence and on Iran on many issues. It's perhaps unprecedented, according to many reports, and people I speak to in Israel.

But the simple trust in what Martin described as the President's commitment, the idea that the President, when he said, I do not bluff as President of the United States, and that containment is not an option -- all options are on the table, containment is not one of them -- if the Prime Minister of Israel were convinced that that is the case, and previous Prime Ministers would have been by previous Presidents, it is lamentable as the case.

Again, I don't mean this to any attribution of blame, but regardless of how one thinks of Netanyahu, it is a shame that it is not -- that the U.S. is not able to imprint on Israelis this kind of commitment, not because Israelis deserve it in some respect or that the U.S. should be obsessed with Israel, but rather that this is potential for upheaval, and (inaudible) Israeli strike on Iran would change the

Middle East or have the potential to change the Middle East, at least in the short term, tremendously, and not for the better.

And so it is very important that this coordination be maintained. And this is, of course, the opinion of many of the most senior security officials in Israel.

MR. BYMAN: Natan, let me ask you one last domestic politics question before I open it up to our audience. One thing that we all talked about before this election was that Israel as a country has moved to the right and, in fact, a number of people commented that the Netanyahu government seemed to be the new center, which was striking for a number of observers.

This election seems to directly contradict that. Is that contradiction actually accurate? And how do you assess kind of the broad trends within Israel that this election reflects?

MR. SACHS: Well, the classic answer to that over really the last decade, is that the left won in some ideological sense in the idea that the land between the sea and the river, the Jordan River, has to be partitioned for Israel to continue as the country it wants to be, but that the rightwing, since the second intifada, has won in its deep skepticism of Palestinian tensions and in its deep concern over security issues, and that is part of the move toward unilateralism and part of the consensus in Israel that there is no point in talks with Palestinians.

What we're seeing today, to my mind, is a continuation of this trend. Neither rightward turn nor center turn, but rather a desire to move away from that issue entirely. When people voted for Lapid, some of them came from Bennett's party, some of them came from Millets.

I heard people debating in Israel, ten years ago, I heard people debating between Bennett, Lapid, Millets, Livni, seemly contradictory things because most of what people were thinking about was not the Palestinians, because there seems to be little point. It doesn't matter what people believe in the end game for Palestinians. It's not going to happen anyway. So, let's debate extremely important issues for Israelis such as ultra orthodox secular variations, such as economics, such as housing, et cetera.

So, this is what Lapid also ran on.

I will say one thing, though. So, the rightwing shift was very much exaggerated in the sense that Israelis did not move right/left on the Palestinian issue, which is how we usually define right and left in Israel. There we didn't have movement, but we did have a profound change in the rightwing, in Likud. It was more subtle than perhaps reported, but it was profound.

There are quite a few backbenchers inside Likud now and they're actually quite high on the list now who are very different from the old Likud. It's not Menachem Begin's old Likud, which was nationalist, but also very liberal. Menachem Begin always spoke about the Supreme Court with reverence; he spoke about minority rights with reverence. Jabotinsky, the ideologue of the rightwing, always spoke of the rights of Arabs in the future state.

This is very different for some of the backbenchers in the Likud, and certainly among Bennett's party. So, it's not necessarily rightwing on territories. Many of them never accepted the two-state solution anyway. It is more radical or it is less mainstream Israeli, sometimes in profound ways, on issues of rule of law,

issues of minority rights, issues of democratic rules, things that Secretary Clinton spoke at our forum two years ago, I believe, publically.

In this sense, there has been a shift and Lapid's victory only mitigates that somewhat. These people are still in and more importantly, I should also just mention, last thing, several of the counters to that, Dan Meridor, Benny Begin, Michael Eitan in the Likud, people right and left on Palestinian issues -- Benny Begin, very rightwing, but very liberal on issues of democracy, Benny Begin, the son of Menachem Begin -- these were all kicked out of the Likud list. Netanyahu's hinted, maybe, to appoint them to ministers anyway, but that remains to be seen.

MR. Byman: Good. Thank you. I'd like to open it up to the audience. If I could ask you please wait for -- do we have microphones? If not, please speak loudly and introduce yourself. Great. Sir, in the front. Stand up and speak loudly.

SPEAKER: If Yair Lapid is going to take on the portfolio Foreign Minister, would it not make sense for him to push the Palestinian negotiation issue to give him leverage as a viable Foreign Minister? And how does he square this need to -- in a sense, can he give up his demand for universal conscription, sit with the religious party -- what would he have to do to kind of square that circle?

MR. BYMAN: Natan, if I could ask you to repeat the gist of the question because the microphone came late.

MR. SACHS: Sure, the question was, if Yair Lapid takes the Foreign Ministry, wouldn't it make sense for him to try and use the ticket of the

Palestinian issue to make a mark there and especially if he has to give up his central -- his core issue or what I describe as a core issue, of conscription?

Yes, but a very qualified yes. First, on the conscription question, there is already a lot of movement. It is not the same debate of old. The law that allowed religious, ultra orthodox men, not to conscript, expired in August, and so we already have a new situation and this can give a lot of political leeway for the parties to say, well, we're just going to amend it somewhat, throw it to the military to have to deal with the conscripts, in some respect, and buck a bit of the issue.

So, Lapid and Shas, perhaps, if it's Aryeh Deri, may be able to come up with very creative ways to get around this problem. And even what they put forward now, Yair Lapid and especially Ofer Shelah, a sports but also political journalist, actually a very intelligent man worth watching, especially if you like NBA, he is now on the list -- high on the -- he's one of our main politicians now, but a serious man, they have spoken about conscription in ways that are not nearly as stringent as Yair Lapid's father, for example, did. So, there may be leeway here.

On the Foreign Ministry, yes, except if you're not going to go anywhere on the Palestinian issue, then making that your central tenant, your central ticket as Foreign Minister, is not necessarily a winning card, and the firm belief, certainly shared by the Center and certainly shared by Lapid, is that it's not going anywhere.

On the other hand, in their list of demands they have now, they had two red lines. They had demands, they had two red lines, one is the issue of conscription, a creative one, and second, resumption of talks. This is a bit of lip

service because the natural response from Netanyahu and Lieberman is, yes, we've been calling for talks since day one, since the Bailan speech, Abu Mazen won't talk to us. We will talk tomorrow, no preconditions today -- Netanyahu's been saying this for four years. It's actually true. One can qualify that for other reasons, but technically that is true.

And finally, I would just caution, Yair Lapid's party is very diverse on many issues -- religious and others, but also right and left. There are real right-wingers there, there are real left-wingers there. Yair Lapid is no left-winger. When he talks about a two-state solution, it's united Jerusalem, it is -- when he talks about the leftwing, in particular, he's not a lefty, he's a real centrist. His father was a classic rightwing, actually, sort of between (inaudible) and (inaudible) somewhere, it was never labor and certainly never socialist. These are rightwing economic people.

And so, so I'll just qualify, this is not Tzipi Livni, who used to be rightwing herself who's now firmly in the peace camp, that's not her. He really is centrist, this is actually true.

MR. INDYK: I think that Lapid is in a very new situation that he himself did not expect to be in. Nineteen seats, second largest party, expectations now of him are much higher than he could have ever anticipated. You know, if you get 10, 12 seats and you go into the coalition and take the Education Ministry, you know, it's enough for the first step. Now he's got 19 and he's got to worry, more than anything else, about the fate of center parties, which is there one election round wonders, they disappeared. Look what happened to Kadima. It went from

28 to 2.

So, he's going to have to deliver on the expectations. The expectations are not about the Palestinians. Now, that could change, but for the time being, that's not what it's about. And so, that's why I said, to take the Foreign Ministry, in a way it's a trap for him. He should take the Finance Ministry, the Interior Ministry, the Education -- he should take those portfolios because that's what his constituents care about.

Take the Foreign Ministry, the Prime Minister will run circles around him. It's the Prime Minister that decides foreign policy, not the Foreign Minister. But we'll see what happens. Maybe he'll be lured by the idea of being in the Oval Office instead of outside the Oval Office reporting about it. I don't know.

But I think that's critically important. Now, there's one issue, which we haven't discussed at all, which could still fit within what I just described and that is the issue of settlements, not because he thinks there needs to be a settlements freeze so there can be a negotiation with the Palestinians, but because he may feel that the best way to show his constituents that there is a shift in the priorities of the government that he's going into, is that the money spent on settlement activity is going to be spent on the domestic priorities that his constituents care about.

And there, Natan's point about him being a centrist, is not inconsistent with this, that is to say, he could insist on settlement activity only in the settlement blocks along the green line, and only in Jerusalem, but not anywhere else. That, by the way, is the settlements freeze which Bibi could accept as well. He's been kind of saying that that was a settlements freeze that Olmert, when he

was Prime Minister essentially had in place with agreement with George W. Bush. It's not really a freeze, but it's a restriction in activity throughout the West Bank area.

And it will be interesting to see whether he makes that a demand because it would be a -- if he could get it and it would be a way of saying to his people, we changed the priorities of the government that I'm joining.

MR. BYMAN: Garrett in the front.

MR. MITCHELL: Thanks very much. I'm Garrett Mitchell and I write the Mitchell Report and I want to ask, you've given us kind of a really wonderful analysis of what just took place in these elections and what might be the results.

I'm interested to know, to the extent that you do, what the reactions of three constituencies either are or should be, one you've talked a bit about, two I don't think we have. The first is, although Martin did make reference to it, is the folks over at the, you know, Executive Office building, the National Security -- what should they -- although you could say we -- but what are they making of this now and the ways in which this affects what the new national security team ought to be focused on?

MR. INDYK: Here? You're talking about here?

MR. MITCHELL: Yeah. Right. The second is, in Israel itself, the sort of entrepreneurial business folks who are so important to driving the economy, how are they reacting to this election? What's their view of it?

And the third is, what do you suppose President Morsi is thinking about all of this?

MR. BYMAN: I have a guess on the latter. Martin, let me ask you to start this off and then we can pass it to Natan for further comments.

MR. INDYK: Well, first, in terms of what are people in our national security establishment thinking about this, I don't know. I haven't spoken to them, so I'm -- this is pure speculation on my part. I think they're relieved that they're not going to have to deal with a, kind of, rightwing to far rightwing coalition government, religious government that would just be very problematic. It's already -- we got a taste of that before the elections when Bibi was trying to play to his rightwing -- settlement activity, provocative settlement activity, as a (inaudible) of that kind of government.

And that looks like -- it looks unlikely now, so I think -- so, relief is the first thing.

You know, I don't get the sense that President Obama is looking to make peace in the Middle East as part of his legacy. You know, I mean, he's ending wars in the Middle East, he'll be ending America's dependence on Middle Eastern oil, and I sense that he's basically ending American leadership in the Israeli-Palestinian arena.

His Secretary of State will have a different thing in mind. I think his Secretary of State, John Kerry, if he's confirmed, will want to work this issue, although I suspect he'll do it quietly because I suspect he understands that the chances of failure are very high. But I think he will want to work it. I think he wanted to work it before these results, and these results will probably give him some encouragement to go on the road that he intended to go on anyway.

MR. BYMAN: Natan?

MR. SACHS: Well, the business community, I would say one important aspect of the Lapid party is that it is economically, or at least Lapid himself, is identified as economically rightwing, very business-friendly. So, this grew out of the -- some of this grew out of the social protests of 2011, but unlikely labor that took the red, social democratic overtly, social democratic mantle of those demonstrations, there was a part of those demonstrations that was just about the cost of living in Tel Aviv.

I have the numbers with me here. This is a Tel Aviv party. I mean, speaking figuratively. But also the numbers bear it up. In Jerusalem, I think the largest -- I could check the numbers -- it's the religious, it's the Likud that wins in Jerusalem, Israel's largest city. Tel Aviv, Israel's economic capital, that's where the center really thrives, that's where Lapid thrives, there's where Lapid lives.

So, the business community is very happy and the market went up the day after. It also is happy with Netanyahu. Netanyahu is economically rightwing, very business friendly, and Lapid is literally friends with many of these business people. Israel's a very small place. His advisors are some of Sharon's advisors, (inaudible) Shanee for example, is a very close advisor. These are people who are thoroughly enmeshed in Israel's business community.

So, what some people dreamed of in Rothschild Avenue in 2011, the huge demonstrations -- it's not Occupy Wall Street, it was much, much, much bigger -- what some of them dreamt, a red dream of (inaudible) to the left, that did not win these elections, but the cost of living aspect of it, of where is the money,

that's actually his tagline for the elections, Lapid, "where is the money?", that won.

And so Education Minister or Finance, that could do something about housing, this could be a winning ticket with that. Or conscription, that could be a winning ticket with the secular side. But both aspects are very important.

What should Morsi think, I'll leave this to Martin.

MR. INDYK: What should he think? I don't know what he should think, but what will he think, well, we kind of had an insight into what he thinks about Jews and Israelis, unfortunately, and if that's, in fact, his attitude, I doubt that the elections changed anything.

But let me twist the question, if you'll allow me, and say, what does it mean for Egyptian-Israeli relations? And I think that the same thing is true, that it relieves some of the pressure. If Bibi had a rightwing government that was pushing actions which would have been seen by the Egyptians as provocative, then Morsi's task of trying to reconcile an ideology that is fundamentally anti-Israel and anti-Semitic in the (inaudible) with his need as the President of Egypt to maintain the Egyptian-Israeli peace treaty, that's a real tension between those two.

It's much better if you've got a government in Israel that's, you know, trying to do something on the Palestinians, not engaged in provocative settlement activity, not looking to reoccupy Gaza, that that makes it easy for Morsi to balance between this anti-Israel ideology on the one side and his need to maintain the peace treaty on the other.

MR. BYMAN: Yes, in the back. Right there.

MR. ARIKAT: My name is Said Arikat from Al-Quds daily

newspaper. My question to Martin Indyk, what is the primary message conveyed to the Palestinian by this election? And to Natan Sachs, what are the implications in the long-term for Arab Israelis? Thank you.

MR. INDYK: Well, the message -- I don't know whether everybody heard the question, but the question to me was, what is the message of this election to the Palestinian people? And I think the basic message is, you're not on our radar screen, you're not the issue for us, we're more concerned about our domestic issues, our social issues, the relationship between -- as Natan said -- between religious and secular, issues of the draft, but the Palestinian issue is not on our radar screen.

And that's true, essentially, from left to right. Shelly Yachimovich, the Labor Party, avoided any talk about the Palestinian issue because she -- why? Because she knew she wasn't going to get votes if she pushed that. So, if -- so, I think that's the message. I lament that. I think it's a bad message to send because what will the Palestinians conclude from this? That they don't have a partner. So, both sides conclude that they don't have a partner, then what hope is there for a negotiating process?

Natan, if I can push this question just a little bit for you. Is there any reason to think this might change in the next two years? Or is this the wave of the future?

MR. SACHS: No. We described earlier what coalitions look like. And slightly less than we expected before the election, but there is a lot of potential for instability here. A lot of things could go wrong, especially from the

backbenches of the Likud, and then if there is movement, if Senator Kerry becomes Secretary of State and does things, revolts are quite likely.

And besides, in Israel, the average of a government, the average of a Knesset is very short. It is not the four years we saw just now, and even this was shorter than the term. It was supposed to last until October 2013, it ended now, and even this was considered very long and stable.

So, we could easily see another Israeli election before Obama leaves office and things could change.

More importantly, and Martin alluded to this earlier, they could change if something dramatic happens. Israelis ignore the Palestinian issue for two reasons. One, they feel that there's just no point. We tried, and if they really wanted to have an independent state, a Singapore in Gaza, they could have had it -- could have had it -- I'm not saying this is right, but this is the common Israeli perception -- they could have had it in 2000 with Barak, they could have had it in 2008 with Olmert, if they really had their act together, they would do it. They didn't, and so we need to just stop subsuming every other issue to this abnormality of Israel. We want to be a normal country, that is the message of Lapid, and he said "normalcy" that was one of his main points in his first talk.

And so, in a sense, what they're saying is, we couldn't get normalcy through the peace process, we're just going to decree normalcy. We're now normal. We forgot about our problem.

The second reason -- second reason -- that they can ignore the Palestinian issue is that it's been quiet. This is the sad truth. If there were a

second intifada going on, that would be -- or third intifada now, that would be the issue.

The second intifada was traumatic; it was on the streets of Israel. If something as traumatic as that were happening, or if a peaceful third intifada were happening on a mass scale, Israelis could not ignore. The West Bank is not somewhere far away. It is right there. Jerusalem is Israel's largest city and East Jerusalem is going to be the capital of Palestine, according to Palestinians.

So, this is where it is and so Israelis won't be able to ignore it.

The last thing is, to quote a certain Martin Indyk, many times, the Iran question can have a lot of effect on this. The Middle East may change a lot. Iran is still the number one issue. As the Israelis say, it's the three most important issues for Netanyahu are Iran, Iran, and Iran, and this is still true in the next year or two. If things move on that, one way or another, a lot could change, and if there is linkage between that and other issues, if the U.S. takes some leadership on this, a lot could still happen.

So, I would say that the glimmer of hope, if one hopes for some movement, it's not very hopeful, is that nothing is that stable in the Middle East, partly because the situation is inherently unstable. This is not a normal situation despite the self-decree of Israelis.

MR. BASHIR: Adham Bashir, the Embassy of Iraq. I was curious what effect the recent military Israeli operation into Gaza has had on voters, if any.

MR. SACHS: Not large. This may be surprising in Washington; it was very popular in Israel, going to the operation. The sense was that the south of

Israel -- and the south of Israel, again, Israel is tiny, so the south of Israel is very close to the center of the country -- was under rocket fire constantly, and so Israelis were demanding some kind of action.

Moreover, one of the paradoxes of Netanyahu is that he speaks very loudly, but he is, in fact, much less warlike than most Israeli Prime Ministers in actually going to war. And so, even this operation, which was the first major military operation with Netanyahu as Prime Minister, and he's the second longest serving Prime Minister ever after David Ben-Gurion. This was the first major operation he undertook, and even this lasted eight days, was far less -- far less bloody than the one under Prime Minister Olmert from the center. It was very, very different.

If anything, there was a reverse -- there was anger that it ended so quickly and it hardly had to do with a sort of cognizant dissonance. There was a huge call up of reserves, huge, much bigger even than Lebanon, which was a bigger war, and they were not used. They were used basically as a threat; they were used as leverage, which, from a strategy point of view, made a lot of sense, but there were so many reservists in a very small country that everyone knows someone, and they were called up, they had to leave their families -- reservists are people of, you know, 30, 40 -- they had to leave their families, leave their jobs, go south, train, and then they went back home.

And so there was this sense that Netanyahu didn't have the guts to carry through on what his own rhetoric and Lieberman's rhetoric always was, which was going to topple Hamas, not let this terrorist entity exist, et cetera. They didn't

deliver. At the end of the day, they did exactly what Olmert did.

It had a marginal negative effect, perhaps, on Netanyahu in some respects, but I think in a slightly longer term, it coincides with the sense of Netanyahu as, although belligerent in words, actually sort of a steady hand and delivering on quiet, not peace, but some kind of quiet, an Israeli perspective.

MR. INDYK: I wonder whether, just to dwell on that for a moment, because after all, as I think the *Haaretz* headline today said it all, Bibi plummeted to victory. He lost a lot of seats. And why did he lose? I mean, I suspect that there's a disillusionment with Bibi himself that's reflected here. Why is that?

MR. SACHS: This is very speculative; I don't have a definitive answer. I think it's a combination of maybe three things. The first is that Netanyahu himself, he's popular, he's the second longest leader since Ben-Gurion, but he's not revered. This is not King Bibi of the *Time Magazine*. This is not true.

He has a core constituency that admires him, but it's not even the '90s where they really loved him. People trust him today and they see absolutely no alternative. They see him as a steady hand, someone who knows the job, and let's be perfectly honest, it's true. He's been Prime Minister for a long time and it's a very, very difficult job in Israel, security-wise as well. There are many aspects of it that we don't see.

And he just has the experience, that is actually true. He has many faults, but that is not one of them. But he's not loved, he's not revered, and this is partly to his detriment.

The second is that this flux -- in a sense, the rightwing won on the

skepticism, but that defeats the rightwing itself. The rightwing is defined in Israel on opposition to Oslo, on opposition to compromise, on being tough, but if everyone agrees and we're not going anywhere, then there's no rightwing. There's no need for that. You can debate (inaudible), the ultra orthodox, (inaudible).

So, the very reason of being for the rightwing sort of disintegrates -- it's also partly true of the left, by the way -- and it breaks up the tribes into their different elements, and Lapid enjoyed that, he received several seats from the right, probably Likud and probably Bennett as well.

And lastly, there probably was movement towards Bennett's party. Bennett -- we should just say that him -- we were talking only about him two weeks ago and now it's only Lapid, but Bennett also had a big success. This is the Jewish Home on the far right. Bennett is a very young, impressive, charismatic man on Palestinian -- on his vision on the territory is very extreme, but on most issues, not extreme, domestic and others. He's also -- he's pragmatic in a sense. His English is excellent too, but he also -- he can speak to all these guys.

He and Lapid probably have common language. And he was a big success. Voters were very impressed with him and they still are and he's going to be around for a long time and he's only 40 or 42.

So, that also probably hurt Netanyahu (inaudible).

So, and finally one last note is that the joining of Lieberman and Netanyahu, oddly enough, probably hurt them in the sense that some of the constituency of Lieberman found that Netanyahu and Likud unappealing and visa

versa, so their internal sort of domestic -- dynamics of the rightwing, between religious and very secular Russian speakers, mostly secular Russian speakers that Lieberman represents and more religious traditionalists that are in Likud, this probably hurt them quite a bit as well.

MR. BYMAN: Thank you. Yes, in the back along the aisle.

MR. WEINTRAUB: Thank you. I'm Leon Weintraub, University of Wisconsin, formally of the diplomatic service. I'd like to address some remarks by Ambassador Indyk. I think his remarks about the message to the Palestinians was very accurate, but I'd also like to ask him about the remarks about the Israeli public having their head in the sand about the peace process.

I think when you consider what we hear from President Abbas recently about continuing to deny a Jewish historical kind of a connection to Israel, the stories that emerged this last week about alleged Zionists and Nazi kind of collaboration, continuing to insist upon the right of return, other things of this nature, I don't expect him to surrender all his points before going into negotiations, but I'd like to see a stronger differentiation between Hamas and the Fatah line -- I'm sorry, between -- yes, between Hamas and Fatah on the part of Abbas, that the Israelis could see, here, really is a potential for a partner.

MR. BYMAN: Martin, may I expand on that slightly, which is, given the election results and given that both you and Natan believe that this further marginalizes the Palestinian issue, does it also give incentives for Abbas to play to his right, to play to the conservatives that are more critical of a peace process in part because there's no hope to be -- there's nothing to be gained by trying to

make gestures of good will?

MR. INDYK: I think Fatah-Hamas divide is a lot deeper than any divide that we've been talking about on the Israeli side, and I don't think that what happens in Israel is going to really change that. They are rivals for power in a very tribal way and so I think there may be reconciliation process, there has been in the past, it's essentially because that's popular amongst the Palestinians, unity is popular on both sides of this conflict.

But I don't imagine that he's about to get into bed with Hamas and there's a real doctrinal difference as well. For all of the complaints that can be leveled at Abbas for things that he has said, he's committed to peace with Israel and Hamas is committed to the destruction of Israel, and it's a fundamental difference. And the fact that Israelis can't see that difference is why I say they've got their heads in the sand.

And, you know, everybody can build up a narrative of how the Palestinians are extremist in this way or in that way, and God knows the Palestinians help reinforce that narrative, but there's also an element of continually raising the bar. We had Foreign Minister Lieberman at -- when he was Foreign Minister -- at the Saban Forum this year and he said that until the Palestinians have -- I don't remember how much --

MR. SACHS: Ten thousand --

MR. INDYK: -- \$10,000 per capita GNP and studied Rousseau and

--

MR. SACHS: Voltaire.

MR. INDYK: -- and Voltaire, then they'll deserve a state.

So, you know, turns out Israel got a state, but its standard of living is well under \$1,000 equivalent and it turns out that Palestinians actually do have Rousseau and Voltaire in their curriculum. But it doesn't matter. But the point is that all of this argument about, you know, whether the Palestinians have met the latest test -- used to be recognizing Israel, then it had to be recognizing Israel's right to exist, now it has to be recognizing the Jewish state of Israel -- and all the time that that's been going on, the Palestinian Authority has been doing something which the Israeli security establishment is ready, consistently, to acknowledge publically, which is, that it's fighting terrorism and preventing violence, which used to be the most important condition and now the Israelis simply don't take that seriously anymore until we see some more violence or terrorism and then suddenly it will all come back and there will be another reason why we can't deal with the Palestinians.

So, you know, I don't have a lot of sympathy or patience for this attitude because it is, as I said, it's a head in the sand attitude. Israel has so many of the cards. Israel can do so much to help the Palestinians be responsible partners.

But if you start from the premise that they're not a partner, you're not even beginning to think about what Israel can do to help achieve this. They're not victims anymore and it's about time that they realized it. If they want a normal life, if that's what they really want, then they're going to have to solve the Palestinian problem.

MR. BYMAN: Sir. One second please, wait for the microphone.

MR. CHANDLER: Gerald Chandler. Could you just give us a background on the economic situation in Israel? Apparently the parties have been complaining that the standard -- some parties have been complaining the standard of living has gone down. How much has it gone down? Is it in their imaginations given that Israel, as we've just heard, over the last 60 years has gone from almost a zero to a very, very high standard? When did they reach their peak? And what has happened now to make it go down?

MR. SACHS: It hasn't gone down. My macroeconomic standards, Israel's been doing very well and it weathered the economic crisis very well. It is very dependent -- it's very exposed to Europe, so what happens in Greece and Spain matters even more to Israel than it does to Wall Street.

So, you know, nothing is sure, but by and large the macroeconomics in Israel have been very good and there have now been also large discoveries of natural resources, mostly natural gas, in the Mediterranean, which could have also a positive effect, and to Israel -- to the Israeli economy's credit, these huge discoveries from Israel standards, huge discovers if natural gas are not even the only issue in the Israeli economy because the economy is big enough now to contain this without the damage that natural resources sometimes have.

Israel is now a member of the OECD, that's new, that's this past term. So, it's officially an advanced country and that is, in many respects, true.

So, standards of living have gone up considerably and consistently,

but I will caveat that strongly in three ways. First, there is fiscal -- there are fiscal problems on the horizon. There is a big, big hole in the budget coming up. It's not nearly as big the U.S., we're not talking those kinds of scales, but for Israel it's a considerable cut.

Israel will succeed. This is not a huge economic crisis looming, but it's a political crisis looming.

The second is that this dramatic rise in standard of living was accompanied -- it was perhaps caused, some would say, Netanyahu would say, by a Thatcherite revolution, by privatization, by a movement very strongly to the right. So, Israel left what was a welfare state, officially a welfare state, and became a very Western oriented economy. And, not surprisingly, the polarization in income has risen dramatically. The difference between rich and poor is huge in Israel now.

And a second issue is structural, not so much in class, but rather across sectors of the population. The Israeli tax base is very narrow. There are two important populations, mostly the ultra orthodox and Israeli-Arabs, whose participation in the workforce is low. They are very poor. I say this not judgmentally, I say, they are very poor populations, both of them, for different reasons.

This has consequences for the rest of the population, which carries most of the burden of the tax base. So, taxes -- the cost of living is very high in Israel. It is true. Those demonstrations did not come out of nowhere. The salaries are much lower. Tel Aviv is very expensive and the salaries are not very high. It is simply true. And that's Tel Aviv, the richest one, the richest part of Israel.

So, the problems are real. It's not in their imagination, but it is rich people's problems, severe, but rich people's problems.

I'll stop there. I lost my train of thought. I think I've covered it.

MR. BYMAN: Fair enough. Yes, sir.

MR. SHEHABI: Omar Shehabi, Palestine Works. What's next for Livni? Is she on her way to being the next Shimon Peres, the perennial loser? And what happens to the people she brought along, Amram Mitzna and Amir Peretz?

MR. BYMAN: I think you have insight to this.

MR. INDYK: I think there's a good chance that Livni will be in the cabinet. She may very well end up being the Foreign Minister. She has six seats, right, and that six is worth something to Netanyahu.

She's not going to be influential -- very influential on the issue that she cares about, which is the Palestinian issue, but I could imagine a situation in which Bibi wants to present this government as a centrist government, and Livni, as Foreign Minister, could serve that purpose and, you know, Peretz played an important role as President in legitimizing the Netanyahu government. I think he's gone sour on that idea for the time being and is not willing to play that role, but for four years, he did play that role, and if Bibi can't use Peretz to legitimize him in the international community, Livni could be quite useful in that regard, and much more useful than Yair Lapid, who's not a known entity, whereas Livni is, you know, Kadima, Olmert, Sharon -- she was part of that effort to make peace, so she has much greater credibility on the international stage.

So, expert her in the government and maybe as Foreign Minister.

There's one other surprise scenario that I have in mind, because Israel always surprises us. It doesn't look very likely today, but I wouldn't rule out - I'd be interested in what Natan thinks about this -- I wouldn't rule out that Shelly Yachimovich, the third woman in the *cherchez la femme*, could join the government, even though she's made a clear commitment not to, that her party made a decision not to, today suddenly we hear voices around speaking to the press, testing the proposition that they would go in.

Now, she has a good relationship with Netanyahu, even though they're ideologically opposite. She has a good relationship with Gideon Sa'ar, the guy who ran the Likud campaign and was the Education Minister, very close. And if Bibi could actually entice her to change her mind, he's suddenly in a different position because then he can play Shelly off against Lapid in terms of who joins the coalition from the center left, and Bibi is a palace master, he has a lot of experience with this, and what Shelly Yachimovich and Yair Lapid both know is that it's better to be in the government than out of the government in Israeli politics.

So, that's just one to watch, probably in the unlikely category, but not impossible.

MR. BYMAN: Natan, my head is hurting, but can you expound on this as well?

MR. SACHS: Yeah, we didn't even talk about Labor, which actually is fascinating. So, Labor has undergone a revolution, led by Shelly Yachimovich, but the list has also changed. For people in Labor it's exciting, it was a dead party

after Oslo and Ehud Barak was not kind to his party, nor was it to him.

Shelly Yachimovich changed that quite a bit, but the result was disappointing for them. They got 15, in some respects a success, but it was very disappointing, and moreover, her move to completely avoid the Palestinian issue was not popular. Labor is still a dovish party, so the knives -- as we say, the knives are already coming out, and Labor is very bad to its leaders, very bad.

So, there's already opposition. In one respect I agree with Martin. This is -- I mean, it's an intriguing possibility I'd say perhaps more likely with Lapid, so Yachimovich, Lapid, and Bibi would have a very different feel, that's a different government, it really would be, actually, and then also maybe she could swallow it.

Anecdotally, I heard an online conversation where someone was saying -- sort of polling their friends. If Yachimovich joined with Lapid and Bibi and kept the rightwing out, would she be betraying you? And the answer was, no. That would be worth it. That would be worth breaking her word, especially given that the promise was very new.

But I don't believe it's going to happen and I don't believe it's going to happen for two reasons. First, she kind of lost. She is not second in parliament, which is what she wanted, so being head of opposition is maybe the best post she can hope for. And it's not a bad post.

She's an oppositionary figure, she has a very different message. But more fundamentally, the economic issue is not just a ploy. She really is social democratic and the party now is social democratic, and Netanyahu is not and Lapid is not, and this budget is not going to be. The upcoming budget is going to have

big cuts to a lot of the promises that were given in 2011.

So, this would be a huge thing to swallow on her core issue, not to mention the others, which she didn't even raise. So, I doubt it, but never say never in Israeli politics and especially the budget is very soon. We're already in January. So, the budget needs to happen now, which means that, you know, in four years who knows who's going to be head of Labor, who knows where Amir Peretz is going to be. He might be back in Labor. Amram Mitzna now is head of Labor. We have no idea what's going to happen.

Don't forget, you know, the previous election, Ehud Barak was head of Labor. He split, he joined Netanyahu, he split Labor, kicked them out, new party, Shelly -- this is Israel, anything can happen. In two years, it can be different.

SPEAKER: Sherry (inaudible) National Academies of Science. Quick, mundane kind of question. What's the scoop with Yair Lapid's relationships outside of Israel? Does he have any trusted relationships with the United States, any other international -- either on a diplomatic front or an economic front?

MR. SACHS: Do you know of any?

MR. INDYK: No. I mean, he may have some personal relationships but, look, he was a journalist, a television journalist. To the extent that anybody knows him here, it's journalist, and I don't know that many that know him. We had hoped to bring him here last year and he canceled on us because making an impression here was not important to his election campaign. And so, no, he's an unknown figure.

I'm sure, quite sure, that the invitations are being printed as we

speaking, including here, but it's -- he really -- that's why I think it's so unlikely that he would be Foreign Minister, famous last words.

He just doesn't have that kind of relationship interest. I mean, he never really cultivated relationships here. I mean, contrast him with John Kerry; he's been cultivating relationships abroad for 30 years. That's not Yair Lapid.

MR. SACHS: May I say just one last word, is that the one thing about Lapid that qualifies that is that he's very close, oddly enough, to Olmert. Olmert was a very close, personal friend of his father, Tommy Lapid, and Yair Lapid in fact said, I will criticize everyone in politics, but not Ehud Olmert. He was with my father at his deathbed. I will never say a bad word about him.

And Ehud Olmert -- it's not Olmert, Olmert is a group, that's a lot of trusted people who are very loyal to Olmert, by the way, have a lot of experience. So, I mentioned (inaudible), more of a Sharon person, but (inaudible) is close to Lapid and Olmert, to campaign for Kadima, he's still a member of Kadima, everyone knows that he's also close to Lapid, at least personally.

So, if any connection abroad, I would say it's from that angle, from the Olmert, Kadima, Sharon type.

MR. BYMAN: Thank you. In the very far back.

MR. MORGENSTEIN: My name's Jonathan Morgenstein. I'm with the Pell Center for International Relations, and you were mentioning that Lapid, his main focus was kind of an economic justice sort of thing, associated with all of the protests from previous years. If he is going to become finance minister, how does that connect with what you were just saying about the very kind of more libertarian

perspective of Likud and Netanyahu's parties and the need for budget cuts? It seems like fundamentally contradictory the need to dramatically reduce the budget while simultaneously addressing what was the surprise success political position of this election.

MR. SACHS: So, I want to clarify my point about the 2011. Some of his support, not all of it, some of it is the same central support -- if you look at the numbers, it's the same center. Some of it grew out of 2011, but not the social justice red socialist aspect of 2011. That is where Shelly Yachimovich places herself.

Lapid -- no one has any doubts in Israel that Lapid is economically rightwing or somewhere in that world. No one has any doubts. He doesn't try to fool anyone; he says this. But 2011 was complicated, that was hundreds of thousands of people on the street in a country of less than eight million, and by polls it was about 70 percent of Israelis that supported this. This wasn't Occupy Wall Street. This was something different, much bigger, and he had -- so, naturally, 70 percent of the population was not radical leftwing economically, right. There was a big chunk that is not necessarily radical, but that is social democratic, it's much more popular in Israel than it is in the United States, and Shelly Yachimovich and others capitalized on that.

Lapid, to a certain degree, I don't want to over blow this, capitalizes on the cost of living aspect. It is the middle class -- he talks about the middle class. It sounds almost like a Barack Obama campaign event, the middle class, the middle class, the middle class, which I hear as upper middle class, northern Tel

Aviv middle class. We can't afford an apartment in Tel Aviv, okay, which is like saying I can't afford an apartment in Manhattan, which I can't. That's not a cause for protest. That's how many people saw it, but that's not the message that Shelly Yachimovich ran on.

So, it's a very different aspect of the same event that coincided quite comfortably in the streets of Tel Aviv, and by the way, not just Tel Aviv, all over the country, because the demands were similar. It was, fear us, fear middle Israel, stop fearing the sectors -- the ultra orthodox, everyone else, the settlers -- no one said that, but they meant that -- start fearing us, the middle class Israelis. And everyone talks about the failure of 2011. I will just say that I think this was a success -- politicians, fear the Israeli middle class. And this means that in minute decisions in the Ministry of Finance, this, I know for a fact, it is taken into account.

MR. BYMAN: Yes, sir, right in front.

MR. GLUCK: Thank you. My name is Peter Gluck. It's probably fair to say that the Palestinians enjoy much more sympathy, if not support, at the UN, certainly in the General Assembly and perhaps even in the Security Council. So, what is the Administration -- U.S. Administration and the Israeli government reaction, if the UN creates a state of Palestine the same way it created a state of Israel, using the 1967 borders? I mean, that action in 1948 was accepted internationally as legitimate. Why wouldn't it be accepted internationally as legitimate if the same thing happened with the Palestinian state?

MR. INDYK: Well, in one sense it's already happening, the UN General Assembly resolution, which took place at the end of last year, which

recognized the State of Palestine as a non-member observer state based on the '67 lines, that's what the resolution says. So, essentially what you're talking about is already underway.

But just back in the 1960s and '70s, when the PLO was being recognized as the sole legitimate representative of Palestinians, it was very nice for them to get that kind of recognition, but it didn't count for anything until Israel and the United States recognized the PLO, and that took another, what was it, 20, 25 years for that to happen.

And so that's the heart of the matter. If you had an Israeli government that wanted to take that resolution and use it as the basis of negotiating a two-state solution, it could serve that purpose. But as long as that's not the case, I don't imagine that the U.S. position is going to change on this issue and we'll have to see on the Israeli front.

I think that Netanyahu has embraced the two-state solution, but for him in the past, a territorial compromise has been very dangerous politically, and that's why the transition from declaring a willingness to accept a Palestinian state to actually making it happen, did not occur in the last government because it would have brought his government down.

If that is the case when they form a coalition this time around, then we'll see no progress. In effect, you will have a situation in which Netanyahu is not prepared, willing, capable of making a territorial compromise, Hamas is not willing to make an ideological compromise, and the status quo ends up suiting both sides in those circumstances with Hamas ascendant on the Palestinians.

But if we get a different kind of government, with a more centrist coalition, with Tzipi Livni as Foreign Minister, maybe Bibi's political calculus changes. Maybe. I don't hold out high hopes for it, but it's possible. And then a lot of other things become possible, but on -- yeah, the heart of the matter is, from my point of view and long experience, this problem cannot be resolved in the United Nations. It cannot be resolved by fiat of either side. It can only be resolved through a direct negotiation on the final status issues and the sooner the parties get back to the table and negotiate the substance, the sooner we'll get to a solution.

I think Abu Mazen's detour to the UN is just that and it really isn't helpful.

MR. BYMAN: With apologies to the large number of questions I haven't had time to get to, we're going to have to wrap up our event now. However, before we leave, I'd like you all to join me in thanking both our speakers today for a really educational, excellent presentation. Thank you.

(Applause)

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