

CHAPTER VI

PRICES

THE GENERAL upward trend of prices persisted in 1956. Commodity prices were 8 per cent higher than in 1955. This is reflected by a rise of the average level of the consumers' price index by 6.4 per cent, a rise of the prices of public consumption goods and services by 8 to 10 per cent, and of those of investment goods by 10 to 12 per cent.

Table VI-1 shows the rise in the prices of the output of various sectors.

TABLE VI-1
*Average Prices of Certain Commodities and Services
in 1956 as compared with 1955*

	<i>Increase per cent</i>
Agricultural Products	+ 2.0
Industrial Products	+ 9.0
Transport	+ 6.0
Building	+15.0

SOURCE: Calculations of the Bank of Israel.

1. THE CAUSES OF PRICE INCREASES

The factors chiefly responsible for the rise of the price level in 1956 were higher production costs and indirect taxes, as well as rising effective demand. On the other hand, there was a considerable real increase in the supply of resources, which somewhat mitigated the upward trend.

The rise of production costs is the result of changes of the various input prices. The main increase occurred in wages, which rose by 13 per cent. and since wages constitute about 60 per cent of the total value added by the economy, (in some services the percentage is even higher) the contribution of this item to the raising of production costs was considerable.

The prices of imports also rose by an average of 7 per cent, increases occurring in all classes of imports serving as input for domestic production.

Together, the above price increases created inflationary pressures on the cost side of agriculture, industry and the services.

The prices of consumption goods were also affected by indirect taxes, some of which were raised in 1956.

The volume of available resources in physical terms was expanded by about 14 per cent as regards agriculture and by about 9 per cent in industry. This attenuated somewhat the upward pressure on prices.

Besides the inflationary pressure on the cost side, there was a concurrent pull from the demand side. In the public sector this stemmed mainly from greater requirements for defence, and for the absorption of the new immigration, simultaneously with increased government borrowing from the banking system. In the private sector, demand rose as a consequence of better export earnings and, to a certain extent, the inflow of personal restitution monies from Germany. Personal income rose by some IL.50 million from each of these two sources.

Effective demand was perhaps checked somewhat by a certain expansion in the volume of saving in 1956.

2. THE CONSUMERS' PRICE INDEX

The average level of the consumers' price index in 1956 rose by 6.4 per cent to 248 points, as against 233 points in 1955. The monthly index numbers are given in Table VI-2.

TABLE VI-2
The Consumers' Price Index, 1956
(September 1951 = 100)

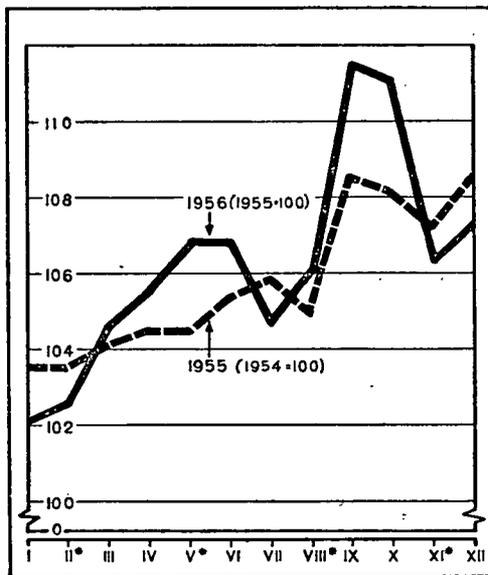
1955 Average	233
1956 January	238
February	239
March	244
April	246
May	249
June	249
July	244
August	247
September	260
October	259
November	248
December	* 250
1956 Average	248

* Key month for wage adjustments according to the new cost-of-living allowance agreement.
SOURCE: The Central Bureau of Statistics.

Diagram VI-1 illustrates the monthly fluctuations of the index in 1955 and 1956. In both years, the upward slant was particularly marked in the last six months, especially in September and October. Moreover, it appears that, while in 1955 the rise of the index was temporarily checked by means of Government subsidies in each of the months which are decisive for the adjustment of the cost-of-living allowance, this was done once only in 1956, in November, a month when the index tends to fall in any case. It should be pointed out that the decisive factor in the fluctuations of the general index are movements in vegetable prices, as described below.

DIAGRAM VI-1

The Consumers' Price Index, 1955-1956 as Compared with the Preceding Year



* Key month of the new cost-of-living allowance agreement.

Table VI-3 shows the change of the average of the main components of the consumers' price index in 1956 as against 1955. The classification is that used by the Central Bureau of Statistics.

The relatively largest rise occurred in the items "Fees" and "Education and Culture", but as the weight of these items is comparatively small, the increases are not reflected in the index as a whole. The items "Food" and "Miscellaneous" each of which rose by about 7 per cent, account for nearly two-thirds of the index. The remaining three items did not increase very considerably.

TABLE VI-3
Consumers' Price Index, Annual Average of Components
1955 and 1956
(September 1951 = 100)

	<i>General index</i>	<i>Food</i>	<i>Clothing and footwear</i>	<i>Rent and electricity</i>	<i>Furniture and household utensils</i>	<i>Fees</i>	<i>Educational and culture</i>	<i>Miscellaneous</i>
Weight in Index	1,000	410	130	76	73	65	40	206
Average for 1955	233	244.1	241.4	216.2	187.9	203.8	248.7	234.5
Average for 1956	248	262.2	246.6	225.0	192.2	231.2	271.2	250.2
Rise, per cent	+ 6.4	+ 7.4	+ 2.2	+ 4.1	+ 2.3	+ 13.4	+ 9.0	+ 6.7

SOURCE: The Central Bureau of Statistics.

(a) *Monthly Fluctuations in the Components of the Consumers' Price Index*

In the following the seven items listed by the Central Bureau of Statistics are collected into three groups: The first includes only the item "Food", the second, "Clothing and Footwear" and "Furniture and Household Utensils", the third group, "Various" comprising the remaining items, i.e. "Rent and Electricity", "Fees", and "Education and Culture", which are services, as well as "Miscellaneous" which includes a number of goods and services which cannot be covered by a single definition though most of them are in the nature of services.

(1) *Food*

Diagram VI-2 illustrates the fluctuations of the index of (retail) food prices in 1956.

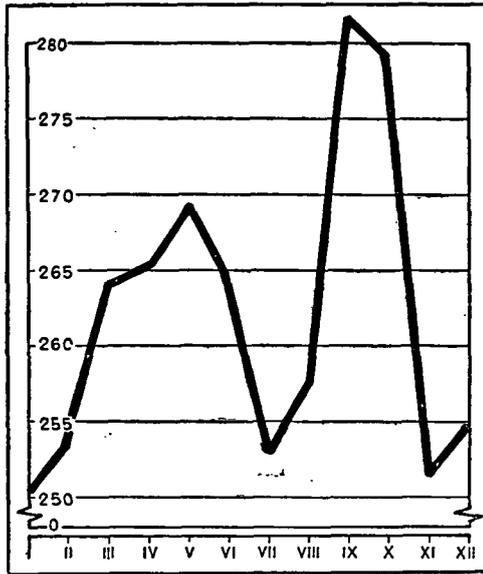
In 1956, the prices of processed foodstuffs exceeded the previous year's average by 6.5 per cent, on account of higher wages and prices of foreign raw materials, and despite the fact that raw materials produced by local agriculture were being supplied at cheaper prices than last year.

Prices of imported foodstuffs rose by 8 per cent, in consequence of the higher world market prices in 1956 which had risen after the temporary recession in 1955. Another factor that raised the prices of imported foodstuffs was the abolition of subsidies on such products as margarine, oil and preserved fish. The products referred to are not those sold in the so-called "grey market", where imported foodstuffs are sold with Government permission at relatively high prices—including customs and other imposts. Price increases in this market are estimated to have ranged from 10 to 20 per cent.

In the sub-division "Local Agricultural Products" of the "Food" item, prices rose by some 6 per cent during 1956. However, changes in the consumption pattern of the population—as reflected by agricultural production and the survey of consumer families undertaken by the Central Bureau of Statistics—appear to

DIAGRAM VI-2

*Monthly Fluctuations in the Food Retail Price Index in 1956
(September 1951=100)*



indicate that this rate of increase is exaggerated. If local fruit and vegetables are weighted according to actual consumption, the rise in the prices of local agricultural produce is no more than 2 per cent.

The prices of fruit and vegetables undergo sharp fluctuations during the year, which necessarily affect the corresponding item in the index. Fluctuations sometimes occur even in the course of a month, between the dates of measurement. The index of fruit and vegetable prices stood 2.6 points lower at the end of 1956 than at the beginning of the year, yet the average for 1956 was about 11 per cent above that for 1955. Vegetable and fruit prices were high during most months of the year, prices falling steeply only in two periods—June–July and October–November. Prices declined as a result of plentiful seasonal supplies of fruit and vegetables and of Government subsidies. For these reasons the decline was particularly sharp in November.

In view of these sharp fluctuations, which are liable to raise the index as a whole and thus require the payment of additional cost-of-living allowances, the Government took steps to check especially steep increases of the food item by granting subsidies—usually for short periods—whenever a shortage of vegetables threatened to raise prices to a considerable degree. Moreover, the Government also used to subsidize fruit and vegetables in order to offset rises in other items of the index. When fruit and vegetable supplies were plentiful, it was possible to

affect the index by subsidies costing relatively little compared with the extent of their influence. This was done towards the end of the year.

Table VI-4 compares the monthly fluctuations of the "Fruit and Vegetables" item with the movements of the index as a whole.

TABLE VI-4
Consumers' Price Index Monthly Changes in 1956^a
(September 1951=100)

<i>Month</i>	<i>"Fruit and Vegetables"</i> <i>(weight = 91)</i> <i>points</i>	<i>All items^b</i> <i>(weight = 1000)</i> <i>points</i>
January	-1.2	- 1
February	+1.4	+ 1
March	+1.5	+ 5
April	+0.6	+ 2
May	+2.5	+ 3
June	-3.5	—
July	-5.2	- 5
August	+1.8	+ 3
September	+8.3	+13
October	-0.8	- 1
November	-9.5	-11
December	+1.4	+ 2
Total Rise (+) or Fall (-)		
Dec., 1955-Dec., 1956	-2.7	+11

^a Difference in points, between each month and the preceding month.

^b Rounded figures.

SOURCE: The Central Bureau of Statistics and calculations of the Ministry of Finance.

Some inordinate fluctuations stand out in table VI-4, especially the rise of the "Fruit and Vegetables" item by 8.3 points in September and its fall by 9.5 points in November.

The changes in vegetable prices determined the fluctuations of the index as a whole for most of the year. Only in March and June, and to a lesser extent in April, was there a change in other index components: in March in the items "Other Foodstuffs" and "Fees" and in June in the item "Education and Culture".

The increases in the periods April-May and August-September were seasonal, while the declines in July and November were partly seasonal and partly induced by Government subsidies.¹

¹ The subsidy policy is discussed in chapter IX (Agriculture).

(2) *Clothing and Footwear, Furniture and Household Utensils*

The average index of clothing prices was only 1 per cent higher than the average index of this item for 1955 owing to weak demand for textile goods generally and for those textiles represented in the consumers' price index in particular, in the first half of 1956. Some of the fluctuations observed during the year were caused by the price reductions during the prolonged seasonal sales. Prices rose slightly as the market recovered in the second half of the year. It should be noted that production costs in the textile industry increased by some 8 to 10 per cent, chiefly because of higher wages. But in so far as these higher costs were passed on to the consumer, it was mainly by raising the prices of better quality goods.

Prices of *footwear* were on the average about 5 per cent higher in 1956 than in 1955. Here also, there was a distinct decline in prices during the seasonal sales, and a rise following the general revival of the market in the second half of the year for reasons similar to those mentioned above in connection with clothing; had large stocks of finished footwear not accumulated in the first half of 1956, the price increases may well have been larger.

The index of *furniture* prices remained stable throughout the year under review at the approximate level of the last months of 1955. Sales of those types of furniture included in the index were of limited quantitative importance and there seems to have been a tendency of consumers to switch from "utility" furniture represented in the consumers' price index to other types, the prices of which rose somewhat, particularly towards the end of the year. It seems that the transition to higher quality goods was a general phenomenon affecting many kinds of industrial manufactures. This trend was also reflected in the movement of prices, though its full extent was not mirrored by the consumers' price index. The price index of *household utensils* rose by about 3.5 per cent in 1956. In this branch, too, price movements were affected by seasonal sales.

In the second half of the year prices rose, probably because of increased demand and higher costs of production.

(3) *Various*

Table VI-5 illustrates the changes in this group of index items in the course of the year under review.

In the item "*Rent and Electricity*" included in this group there was a general rise of about one point, chiefly caused by the revision of electricity rates. The item "*Fees*" reflects increases in Histadruth dues and municipal rates. The changes in the item "Education and Culture" were caused by higher secondary school fees and higher prices of newspapers. The "*Miscellaneous*" group includes items the cost of which largely consists of wages. Prices in this group increased steadily throughout the year, almost without fluctuation.

TABLE VI-5
Consumers' Price Index
Monthly Changes in the "Various" Group of Items, 1956^a
(September 1951 = 100)

<i>Month</i>	<i>Change</i>
	Points
January	+0.8
February	-0.7
March	+0.6
April	+1.1
May	+1.1
June	+1.6
July	+0.7
August	—
September	+1.8
October	+0.7
November	—
December	+1.2
Annual Rise ^b	+9.1

^a Difference in index points, between each month and the preceding month.

^b Discrepancy due to rounding.

SOURCE: Central Bureau of Statistics.

(b) *Limitations of the Consumers' Price Index*

The consumers' price index is the most important economic index in this country, since it measures price changes affecting the greater part of national expenditure. It has, however, certain limitations due both to the rigidity of the "consumption basket" on which it is based and to the functions that it has come to fulfil.

The present index measures the consumption expenditure of an urban wage-earner's family at current prices as compared with the prices of the years 1950/51. It ignores the consumption of rural or of self-employed families. The consumption survey on which it is based was made in years of widespread rationing, a fact which greatly affected the consumers' choice, and thus the consumption basket. Moreover, the population structure has since changed fundamentally, especially in the years immediately following the base year. On the supply side, too, great changes have meantime taken place. The rapidly growing supply of local agricultural and industrial products brought with it a greater variety of goods, thus allowing the consumer a far wider choice. The abolition of controls, and the consequent changes in demand, likewise led to certain shifts in the relative prices of goods available in the market, and have caused a substitution of cheaper for more expensive commodities.

In addition to its original function, which was to measure the level of retail

prices, the index has become instrumental in the periodic revision of the cost-of-living allowances to wage earners: if in certain key months the index had risen by 3 points or more the allowance was increased.² This has led to a situation where efforts which might have contributed to a stabilization of the general price level in order to restrain the inflationary process—have been concentrated on lopping points off the index. This course of action was made easy by the changing consumption habits and the subsidization during the key months of commodities which now appear overweighted in the index.

As this report is being written preparations are being completed for the compilation of a new index of retail prices, based on an up-to-date consumption basket.

3. INVESTMENT PRICES

The two major investment items are construction, and machinery and equipment. The index of building costs shows an average rise of 14.8 per cent in 1956. The prices of machinery and equipment rose by 8 per cent.

TABLE VI-6
Index of Building Costs, 1956^a
(July, 1950 = 100)

<i>Month</i>	<i>Index</i>	<i>Index based on average for 1955</i>
1955—Average	393.4	100.0
1956 January ^b	427.2	108.6
February	427.4	108.6
March	444.9	113.1
April	444.9	113.1
May	450.1	114.4
June	459.4	116.8
July	460.4	117.0
August	461.1	117.2
September	461.1	117.2
October	461.1	117.2
November	461.1	117.2
December	461.1	117.2
1956—Average	451.7	114.8

^a Details of the structure of this index are given in chapter XII.

^b Since the index published in the monthly bulletin of the Central Bureau of Statistics on the first of each month relates to the prices charged during the last week of the previous month, the whole index has here been moved back by one month.

SOURCE: The Central Bureau of Statistics.

² Since this Report was prepared, the system has been changed; see chapter VII, page 111.

The index shows two main rises which have occurred during the year—in March and in June. Both were caused by wage increases due to higher basic rates and cost-of-living allowances. There was also a slight increase in the price of iron in the second half of the year. As a result of a recession in the building market at the same time, contractors reduced their purchases; owing to the decline in demand, small increases in the prices of building materials during the last few months of the year were not reflected in the index of building costs.

Prices of imported building materials increased by 9 per cent in 1956, in consequence of a continuous rise of world prices.

As regards machinery and equipment, price movements were different in the case of locally produced and of imported goods. The prices of imported equipment rose by 6 to 7 per cent, whereas similar locally-produced goods increased from 8 to 9 per cent.