

CHAPTER I

MAIN ECONOMIC DEVELOPMENTS IN 1958

THE NATIONAL PRODUCT continued to expand at a considerable pace in 1958, rising by 8 per cent. A high level of employment likewise prevailed. These developments contrasted sharply with the situation in many foreign economies, and particularly in the United States and Western Europe, where the level of output and employment did not rise, owing to the recession. Insofar as the recession affected the Israel economy, its effect was favourable, as the drop in import prices retarded the increase in the trade deficit and the rise in the domestic price level. Lower export prices had only a slight impact on the Israel economy, as the prices of citrus—Israel's major export commodity—rose in the 1957/58 season, while the total volume of exports remained limited. Capital imports, which constitute an appreciable part of Israel's resources and are largely channelled to investment, did not decline in 1958. Their high level relatively to the size of the economy contributed to the intensification of economic activity in Israel, in contrast to the trends prevailing in other countries.

During 1958, the rate of increase was most rapid in agriculture, industry and transport, where output rose—in real terms—by 13 per cent, 10 per cent and 12 per cent respectively. Building activities, which had reached a very high level in 1957, as compared with previous years, expanded only moderately. The expansion in Government and other services was slower than in other economic branches.

The number of gainfully employed workers increased by 2 to 3 per cent, immigration—together with the absorption of unemployed workers and younger age groups entering the labour cycle—accounting for the increment. Moreover, there was a rise in the average number of hours per worker. The expansion of employment was slower in 1958 than in the preceding year, mainly owing to the reduced volume of immigration.

The national product expanded more rapidly than employment, output per worker rising at the considerable rate of over 5 per cent.

A considerable increase in output—amounting to 8–10 per cent per annum—and a high level of employment have been characteristic features of the Israel economy during the last few years.

In 1958, the national product expanded at a somewhat lower rate than in the two preceding years; however, on a per capita basis, the increase totalled

TABLE I-1
Indicators of Economic Development, 1955-1958

	Percentage increase or decrease (-)		
	1955 to 1956	1956 to 1957	1957 to 1958
1. Resources and their use—at constant prices			
Gross national product	10.0	11.0	8.1
Output in:			
Agriculture	16.0	10.0	13.0
Industry	9.0	15.0	10.0
Building	— 9.0	32.0	3.0
Private consumption	6.0	9.0	11.2
Private consumption—per capita	1.5	3.3	7.4
Public consumption*	41.0	—15.0	2.2
Gross investment	7.0	21.0	4.6
Imports (goods and services)	18.1	— 0.2	9.2
Exports (goods and services)	15.0	19.0	10.0
Deficit on current account	19.6	— 9.9	8.7
Imports of goods	3.2	11.4	4.8
Exports of goods	14.8	20.6	0.7
Trade deficit	— 1.0	7.5	6.8
2. Population and employment			
Average population	4.5	5.6	3.6
Employment	3.0	9.0	2.5
3. Nominal prices and earnings			
Average wages	13.0	9.0	6.0
Consumer price index	6.4	6.5	3.4
National income	21.0	19.0	13.2
National income—per capita	15.5	12.6	9.3
Private income	20.0	20.0	14.9
Private disposable income	19.0	20.0	15.6
Private disposable income—per capita	13.9	13.6	11.6
4. Finance			
Money supply (annual average)	17.9	19.4	15.2
Bank credit to the public (annual average)	13.4	15.7	18.2
<i>Total resources</i>	12.0	8.0	8.3

* Public consumption includes all current expenditures, except transfer payments of the public sector. However, the "output" of the public sector includes only expenditure on local purchases.

SOURCE: Bank of Israel (based on various sources).

more than 4 per cent, a rate equal to that of 1956 and 1957. It would seem that the slower growth of production in 1958 was due to the lower rate of increase in building and the public services, caused by the reduced volume of immigration.

The expansion of production was facilitated by several factors on the supply side, such as the maturing of investments in certain economic sectors, the fuller utilization of existing capacity in other sectors, the higher level of employment and the availability of larger quantities of imported raw materials. While the production factors at the disposal of the economy increased, there was a simultaneous rise in demand, which enabled their utilization. The greater demand for private consumption goods was particularly marked, demand for investment goods and consumption commodities rising to a lesser extent.

Private consumption expenditure increased following a significant—15 per cent—rise in private income. This rise is attributable to the higher level of employment, wages and profits prevailing in 1958, as well as to the greater volume of transfer payments received by private persons from the Government (mainly premiums to importers of capital and exporters) and from abroad (chiefly personal restitution paid by West Germany). Though direct tax collections likewise expanded, they did so more slowly than disposable income—which rose by over 15 per cent. As in previous years, the growth of private consumption expenditure absorbed 85 per cent of the net addition to private disposable income.

Monetary expenditure on consumption increased by some 14 per cent, i.e., at a rate similar to that of 1957. However, since the prices of consumer goods rose only to the insignificant extent of 2 to 3 per cent, real consumption expanded considerably—by some 11 per cent. Real consumption per capita increased by 7.5 per cent in 1958, as against only 3.5 per cent in 1957. The greatest expansion took place in food consumption, particularly as regards agricultural products. Altogether, the increase in private consumption absorbed about 73 per cent of the real increment in resources created by the larger national product and the bigger volume of imports.

Public consumption expenditure rose slightly—by 2 per cent—mainly as a result of increased Government outlays on education and health services. However, the proportion of additional resources allocated for this purpose was relatively small in comparison with those channelled to private consumption.

Gross investment rose by about 5 per cent. It also underwent a structural change, the share of investments in agriculture and industry increasing considerably. Some of the investments in these sectors were made in branches whose products are intended to raise the level of domestic consumption. However, as public investment in these branches did not increase, it would seem that this expansion was financed from non-governmental sources. It is also possible that higher gross profits permitted companies and other enterprises to increase their investments in their own concerns, replace obsolete equipment

and develop their activities. Investment in the transport sector declined considerably after the acquisition of the new "Britannia" aircraft and several ships in 1957. The level of building activity rose to a limited extent. Immigrant housing construction financed from public sources contracted somewhat, since fewer immigrants arrived in the country. However, there was an upturn in public and private residential building for the established population, as well as in the erection of industrial and public buildings. The volume of earth-works likewise expanded.

Only a negligible portion of the additional output was directed to the expansion of exports. Exports of commodities and services rose—in real terms—by 10 per cent, the increment being wholly due to larger exports of services, particularly in the shipping, aviation and tourism branches. The level of commodity exports remained unchanged. Industrial exports did not expand; however, their composition improved, since exports to countries protected by trade agreements—such as Turkey—were reduced. On the other hand, there was a marked tendency to expand exports to countries more open to competition, and particularly to Asia and Africa. The added value of industrial exports has probably increased somewhat.

The drop in world prices affected Israel exports; yet, their prices declined by an average of only 2 per cent, mainly because higher prices were received for citrus during the 1957/58 season.

Though total exports rose relatively little, the balance of payments did not deteriorate, since the 6 per cent drop in import prices enabled the real volume of commodity and service imports to be expanded by about 9 per cent, at an additional outlay of only 3 per cent.

Services for the Government (chiefly for defence purposes) constituted the bulk of the additional imports. However, when imports of services are deducted, it becomes apparent that the real volume of commodity imports rose by about 5 per cent, foodstuffs—and in particular surpluses of agricultural produce from the United States—accounting for most of the increase.

Capital imports through unrequited transfers and long-term foreign loans totalled \$330 million in 1958, as against \$312 million in 1957. There was also an increase in short- and medium-term loans. This was offset by a \$46 million rise in foreign currency reserves.

One of the most striking developments in 1958 was the moderate rise in prices, which did not exceed 2 to 3 per cent—the lowest rate recorded during the last few years. This stability was due to several factors:

On the cost side, the drop in import prices exerted a downward pressure on local prices, as in certain branches producers paid lower prices for their raw materials. In some other branches, the lower import prices enabled the Government to raise imposts without affecting production costs.

An additional factor tending to keep prices stable were the firm consumer prices of agricultural produce, the supply of which was expanded.

Higher wages did not affect the prices of locally produced commodities in 1958, the 6 per cent increase in wages being largely offset by higher output per worker, expanded investment, and longer hours of work in certain branches.

As prices were not pushed up by increased production costs, the 2-3 per cent rise in the domestic price level seems to have been due to inflationary pressures generated by demand, and reflected by the expansion of credit.

The expansion of bank credit to the Government and to the public contributed to the raising of the price level in 1958 as well, but monetary developments during 1958 were different in certain respects from those of the preceding year.

The total volume of credit granted to the Government by the banking system rose by an average of IL. 61 million during 1958—a smaller increase than in 1957, when bank credit to the Government rose by IL. 79 million.

Recourse to bank credit constitutes only part of the Government's financial activities. The impact of the Government on total demand is determined by the scope of its financial transactions with the rest of the economy and by its own demand for commodities and services. If all the financial transactions of the Government are taken into account, it will appear that the net money outflow from the Government to the economy (i.e., the net amount of long-term loans granted to local residents or bodies, less the increase in the Government's short- and long-term local liabilities) was smaller in 1958 than in the preceding year.¹

Inflationary pressures generated by the local financial activities of the Government were thus reduced, though the expansion of its purchases abroad was clearly an inflationary factor.

A similar development occurred in respect of the Jewish Agency, whose local financial activities, however, are more limited than those of the Government.

On the other hand, credit extended to the non-governmental sector increased in 1958 by an annual average of IL. 59 million, as against IL. 44 million in the preceding year.

The expansion of credit to the public was, to a certain extent, proportional to the real increase in output. Nevertheless, the latter was not its sole cause. Other factors characteristic of the Israel economy contributed as well. These included the persistent inflation, an interest rate legally fixed at a level too

¹ An analysis of the overall monetary impact of the Government and other public bodies is presented in this Report for the first time (see Chapter XV—"The Financial Activities of the Public Sector").

low to bring about an equilibrium between the demand for credit and its supply, and the dynamic tendency towards expansion inherent in the Israeli economy. An additional factor was the smaller share of the enterprises' own capital in the financing of current production. Had the demand for credit been satisfied beyond the real output capacity of the economy, this might undoubtedly have generated inflationary pressures. Another factor markedly increasing the demand for credit in 1958 was the competition among producers caused by increased production, which led to credit selling on the local market.

All these factors contributed to the considerable expansion of credit to the public. Moreover, the rise in foreign currency reserves increased the money supply, the growth of which, however, was slowed down by substantial increases in the deposits of various saving schemes and other time deposits.

On the average, the total money supply was 15 per cent larger in 1958 than in the preceding year, as against an increase of 20 per cent between 1956 and 1957.

The relative importance of the factors expanding the money supply (and other deposits of the public) changed in 1958: In 1957, additional credit to the Government caused 62 per cent of the increase, the other 38 per cent being due to the expansion of credit to the public, while foreign exchange reserves remained unchanged. In 1958, the comparative shares of these factors were: Credit to the Government—43 per cent; credit to the public—42 per cent; increase in foreign exchange reserves—15 per cent.

The distortions of the price system, caused by varying premium rates for different exports and by the granting of subsidies to certain branches of production with high real production costs, were not abolished in 1958.

In conclusion, it may be said that the expansion of the national product—particularly in agriculture and industry—continued during 1958, and that a high level of employment prevailed in the economy. The price level showed marked stability and net foreign exchange reserves increased. However, as the bulk of the additional production was channelled to the expansion of private consumption, the ratio of savings to private income did not rise. No significant improvement occurred in the balance of payments.