

CHAPTER VI

PRICES

THE AVERAGE price level of commodities and services for private consumption and investment rose by nearly 8 per cent in 1961, while public consumption prices increased at a similar rate.¹ This was the steepest rise since 1957, and it reflected the intensification of a trend already apparent during the second half of 1960 and which continued throughout most of the year reviewed (see Table VI-1 and Diagram VI-1).

TABLE VI-1

*Average Increase in the Prices of Resources Available to the Economy,
by Final Domestic Uses, 1956-61*
(in percentages)

	1956 to 1957	1957 to 1958	1958 to 1959	1959 to 1960	1960 to 1961	Weight in 1961
Private consumption	7	4	2	3	7	61
Public consumption ^a	6	5	6	6	8	18
Investment	6	2	1	4	9	21
<i>Total</i>	7	4	3	4	8	100

NOTE: A new set of weights is determined each year to measure the relative share of the various uses within total available resources during the year.

^a The weighting was changed in 1959, and this explains the difference as compared with the figures cited in Chapter II—"Resources, Uses, and Incomes". A detailed explanation is given in the Appendix to this report (in Hebrew only).

SOURCE: Central Bureau of Statistics and Bank of Israel.

1. FACTORS IN THE PRICE INCREASES

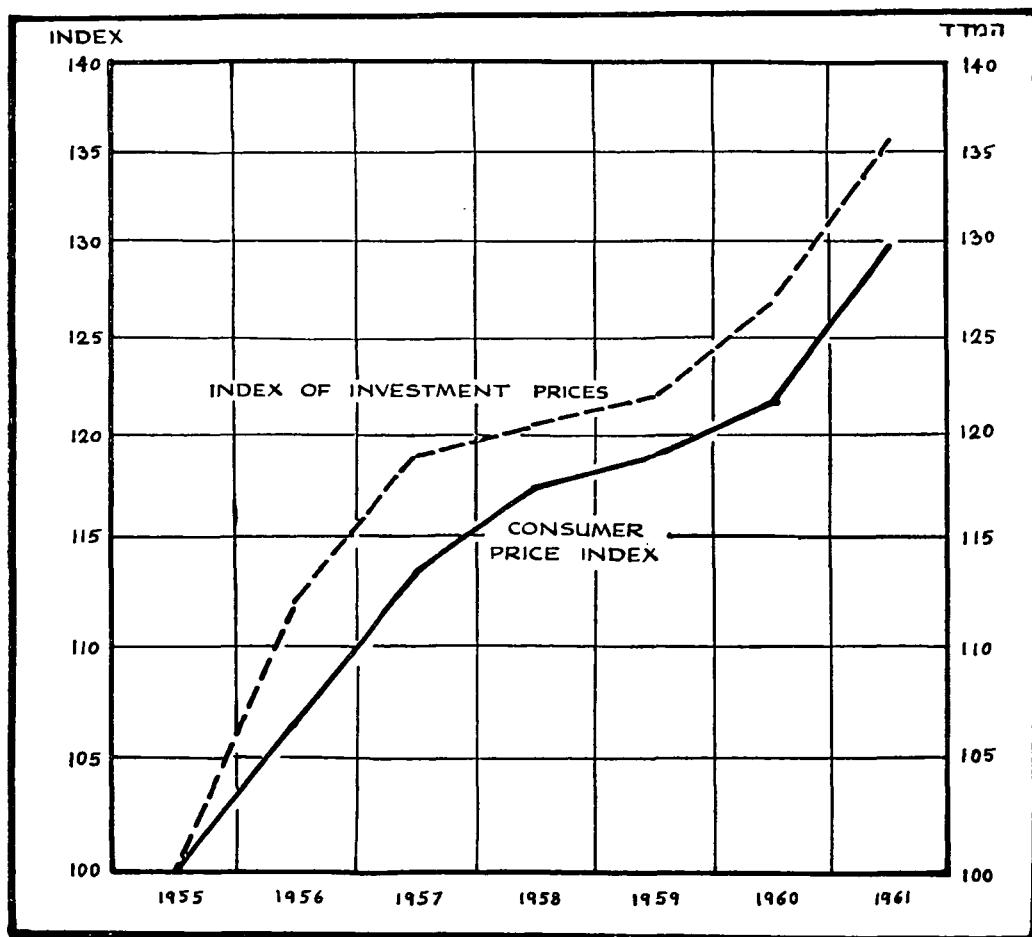
The steep rise in prices during 1961 was due to the big expansion of demand. Its origins may be traced back to 1960, when the money supply grew rapidly following the large expansion of credit and the accelerated pace of foreign currency conversion. The rapid rise in the price level began in the second half

¹ Calculated on the basis of the rise in wages and salaries per time unit in the public sector, as well as the sector's purchases of imported and locally produced items. The figures cited should be regarded as indicators only, rather than actual prices.

of 1960 and continued until the middle of 1961. The rise was slower in the sectors where supplies could be expanded by imports, and steeper in sectors where bottlenecks or deliberate restrictions on production prevented increases in supply.

In the second half of 1961 the rise in the price level was slowed down. This was due to the checking of the increase in demand following the deceleration of the rate of monetary expansion; the latter development resulted from the restraining measures adopted by the Bank of Israel during the year, the conversion of local currency into foreign currency (i.e. a decline in Israel's foreign currency reserves) during the second half of 1961, and the disinflationary steps taken by the Government throughout most of the year. The deceleration of the

DIAGRAM VI-1
Indicators of Price Increases, 1955-61



price increase in the last half of 1961 occurred despite a rise in production costs during that period.

Factors on the cost side did not have a marked impact on the general price level, since they tended to lag behind price increases. Their effect was restricted chiefly to the distribution of income among the various economic sectors.

The Government's economic policy has been based on the fundamental assumption that full employment must be assured. Consequently, any rise in production costs necessitates an expansion of the money supply in order to prevent unemployment and a decline in output. An increase in production costs therefore causes a rise in the general price level. The monetary expansion, which accelerated in the second half of 1960 and continued through the first half of 1961, was in the main unconnected with production costs, and hence the price increases during that period cannot be ascribed to this factor.

The rapid rise in prices began in the second half of 1960, a period during which production costs hardly increased at all. The increase in wages did not exceed the rise in productivity, so that there was no increase in labor costs per

TABLE VI-2

Consumer Price Index and Index of Investment Prices, 1950-61

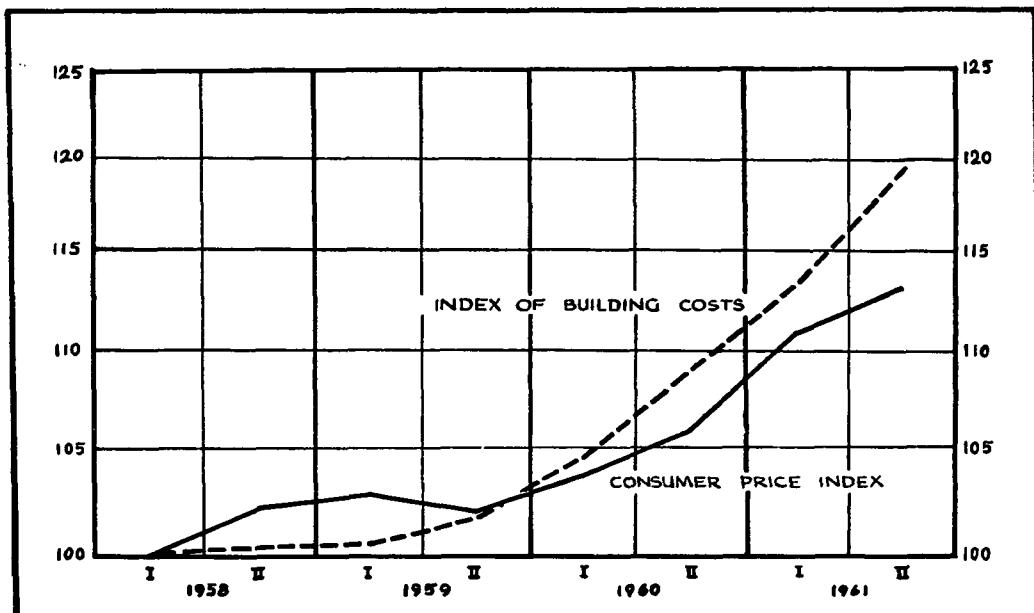
Year	Consumer price index		Index of investment prices	
	Annual average	Per cent increase over preceding year	Annual average	Per cent increase over preceding year
1950	100.0	—	100.0	—
1951	114.1	14.1	136.0	36.0
1952	180.0	57.8	243.3	78.9
1953	230.6	28.1	322.7	32.6
1954	258.8	12.2	376.3	16.6
1955	274.1	5.9	414.8	10.2
1956	291.8	6.5	464.0	11.9
1957	310.6	6.4	492.6	6.2
1958	321.2	3.4	500.5	1.6
1959	325.9 ^a	1.5	505.4	1.0
1960	333.4 ^a	2.3	525.9	4.1
1961	355.6 ^a	6.7	562.7	9.0

^a In 1959 a new consumer price index was introduced. To allow comparison, the new index has been chained to the old.

SOURCE: Consumer price index—Central Bureau of Statistics. Index of investment prices: 1950-59—Dr. A. L. Gaathon, "Capital, Employment and Output in Israel, 1950 to 1959"; for 1960-61—Bank of Israel.

unit of output. Moreover, import prices were stable throughout most of the period,¹ while import duties were not raised very much. Broadly speaking, developments were similar during the first quarter of 1961. But as from the second quarter of the year, when the retroactive wage increment due under the new collective labor agreements were paid, production costs per unit of output began to rise. The process continued in the third quarter, when a higher cost-of-living allowance was paid. Nevertheless, the rise in the general price level was slowed down. This was apparently due to the relative stabilization of demand, following the curbing of the monetary expansion. The increase in production costs was absorbed by profits, which seem to have grown during previous periods when price increases were not accompanied by corresponding increases in costs.

DIAGRAM VI-2
Development of Prices, by Half Years, 1958-61



In certain sectors, where taxes were raised or subsidies abolished, commodity prices did go up, but this cannot be regarded as a factor changing the general price level.

¹ The effective exchange rate for imports was approximately 2 per cent higher in 1961 than in 1960.

2. RELATIVE CHANGES IN PRICES

The changes that occurred in the general price level in 1961 were due, as already mentioned, to the monetary expansion which increased demand. Changes in the relative prices of various groups of commodities or services were determined by special factors which influenced supply and demand in each of the groups concerned.

(a) *Prices of private consumption*¹

Prices of private consumption rose in 1961 by approximately 7 per cent, which was much faster than in any of the preceding three years. The increases were not equal in the different items, being above average in fruits, vegetables, housing, and personal services, and below average in other foodstuffs, textiles, and footwear.

Fluctuations in the index during the year reviewed were caused mainly by extraordinarily sharp movements in the prices of fruit and vegetables (see Diagram VI-3).

1. *Fruit and vegetables*

An especially steep rise of 20 per cent occurred in the prices of fresh vegetables. This represented the continuation of a trend which started as far back as 1957 (see Table VI-4).

This development was caused by the relative decrease in the supply of vegetables following the growth of the population and the rapid increase in private disposable incomes, which stimulated the demand for vegetables.² The quantity of fresh vegetables marketed per capita declined by 10 per cent between 1957 and 1961.

The continuous rise in the relative prices of vegetables was connected with a deliberate policy of inadequate increases in supply. The limiting of supplies was due to restrictions on production and, during certain periods, to the deliberate contraction of marketing and the destruction of surpluses. The Government paid subsidies on these surpluses, the amount in the 1960/61 agricultural year coming to IL. 3.2 million. It seems that the marked rise of 25 per cent in the prices of canned vegetables in 1961 was partly caused by the higher prices of fresh vegetables,³ since the canned products are a close substitute for them. Other factors were the increased customs duty on the tin used in the manufacture of the cans, the higher prices of vegetables serving as raw material

¹ The analysis is based on the consumer price index, which rose by 6.7 per cent. Consumer prices shown in Table VI-1, which rose by 7 per cent, were obtained by dividing the index of the nominal value of consumption by the index of real consumption.

² The income elasticity of demand for vegetables is estimated at about 0.3. Accordingly, demand should have risen by 10 per cent between 1958 and 1961.

³ The prices of most canned vegetables were raised simultaneously.

DIAGRAM VI-3
Consumer Price Index, 1957-61

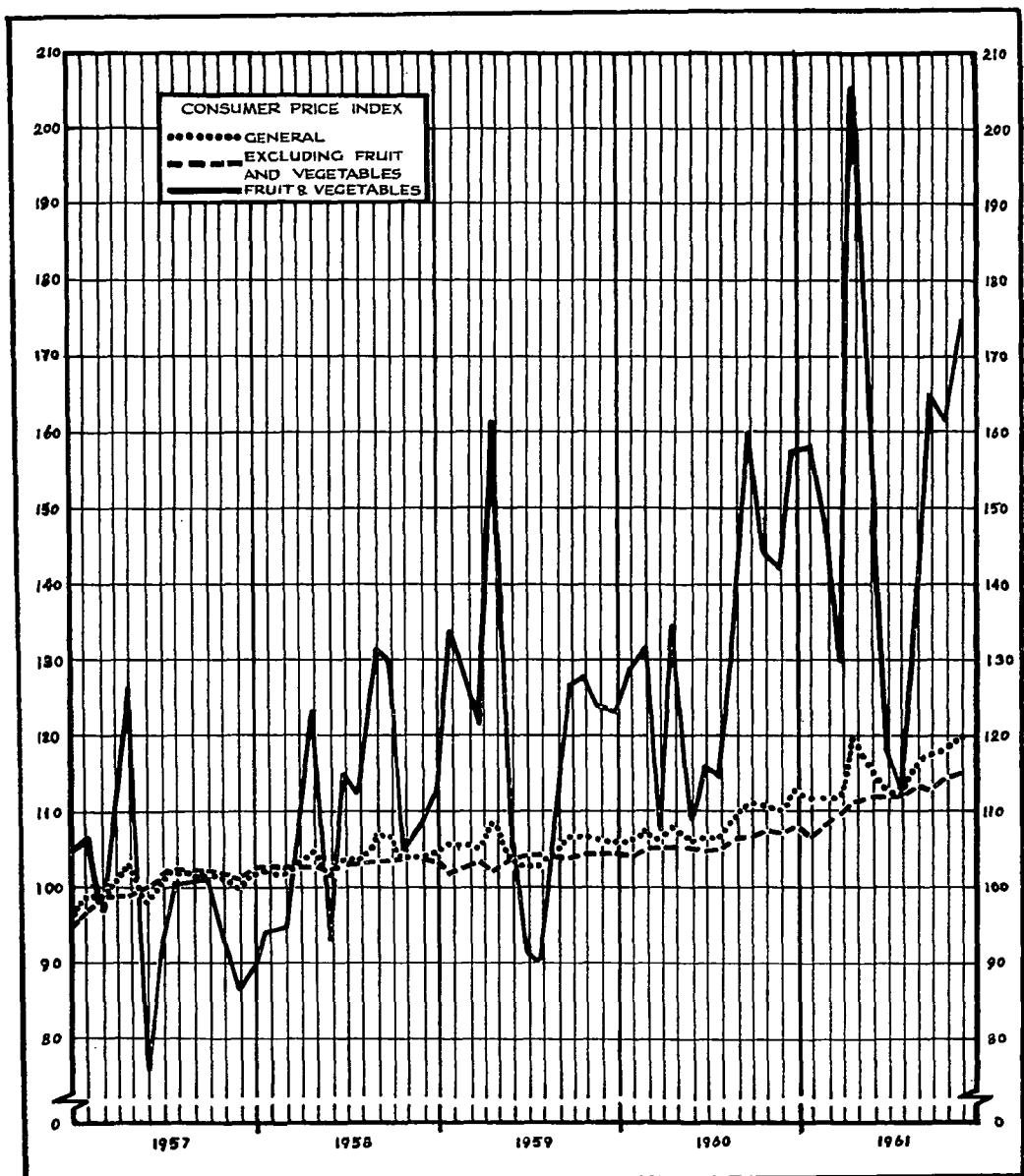


TABLE VI-3
Changes in the Consumer Price Index, by Origin of Items, 1960-61

	<i>Per cent increase from 1959 to 1960</i>	<i>Per cent increase from 1960 to 1961</i>	<i>Weight</i>
Agricultural products			
Fruit	8.0	12.0	43.0
Vegetables	11.0	16.5	45.5
Other agricultural products ^a	-5.5	0.5	124.0
<i>Total</i>	1.0	7.0	212.5
Industrial products			
Foodstuffs	2.5	5.5	174.0
Textiles	-3.5	5.0	87.0
Footwear	1.5	3.0	28.0
Other industrial products ^b	2.5	4.5	64.0
<i>Total</i>	1.0	5.0	353.0
Imported foodstuffs	1.0	8.0 ^c	45.0
Fuel	0.5	4.5	32.0
Personal services	6.0	10.0	164.0
Housing	5.5 ^d	13.0 ^d	123.0
Items not elsewhere specified ^c	3.5	5.0	71.5
<i>Grand total</i>	2.5	6.5	1,000.0

NOTE: The figures have been rounded to the nearest half per cent or half mill.

^a Poultry meat, beef, eggs, and fresh fish.

^b Chemical, furniture, metal, electrical, glass, and ceramic products.

^c This estimate is biased owing to the methods of calculation employed.

^d See footnote 1 on page 76.

^e Histadrut dues, local property rates, books, newspapers, jewelry, bicycles, etc.

SOURCE: Central Bureau of Statistics. Classification of items by the Bank of Israel.

for the food industry, and the exceptionally sharp fluctuations in vegetable prices during the year.¹ The appreciable rise in the prices of canned fruit was due both to the higher customs duty on tin and to new taxes on the finished products.

¹ See the explanation in Chapter IV—"Consumption".

Prices of fresh fruit also rose more than the general price level—by 12 per cent. This was due to smaller supplies and to the Citrus Marketing Board's raising local citrus prices by 30 per cent.

Prices of other fruit rose only slightly, by 2 per cent, since the quantities offered for sale increased.

TABLE VI-4
Changes in Vegetable Prices, 1958-61

	Average annual increase or decrease (-) as compared with previous year—in per cent				Weight in 1960 and 1961*
	1958	1959	1960	1961	
All fresh vegetables ^b	8.0	16.5	10.5	20.0	100
<i>Of which:</i>					
Tomatoes	1.5	14.0	13.5	26.0	28
Cucumbers	49.5	-25.5	16.5	22.5	10
Potatoes	16.0	38.0	11.0	12.5	23
Index of consumer prices	3.5	1.5	2.5	6.5	—

NOTE: Figures have been rounded to the nearest half per cent.

* The weights relate to 1960 and 1961 only. During 1958 and 1959 weights were calculated on a different basis. An explanation will be found in the Appendix to this report (in Hebrew only).

^b Groundnuts have not been included in this table, though they are included with vegetables in Table VI-3.

SOURCE: Central Bureau of Statistics.

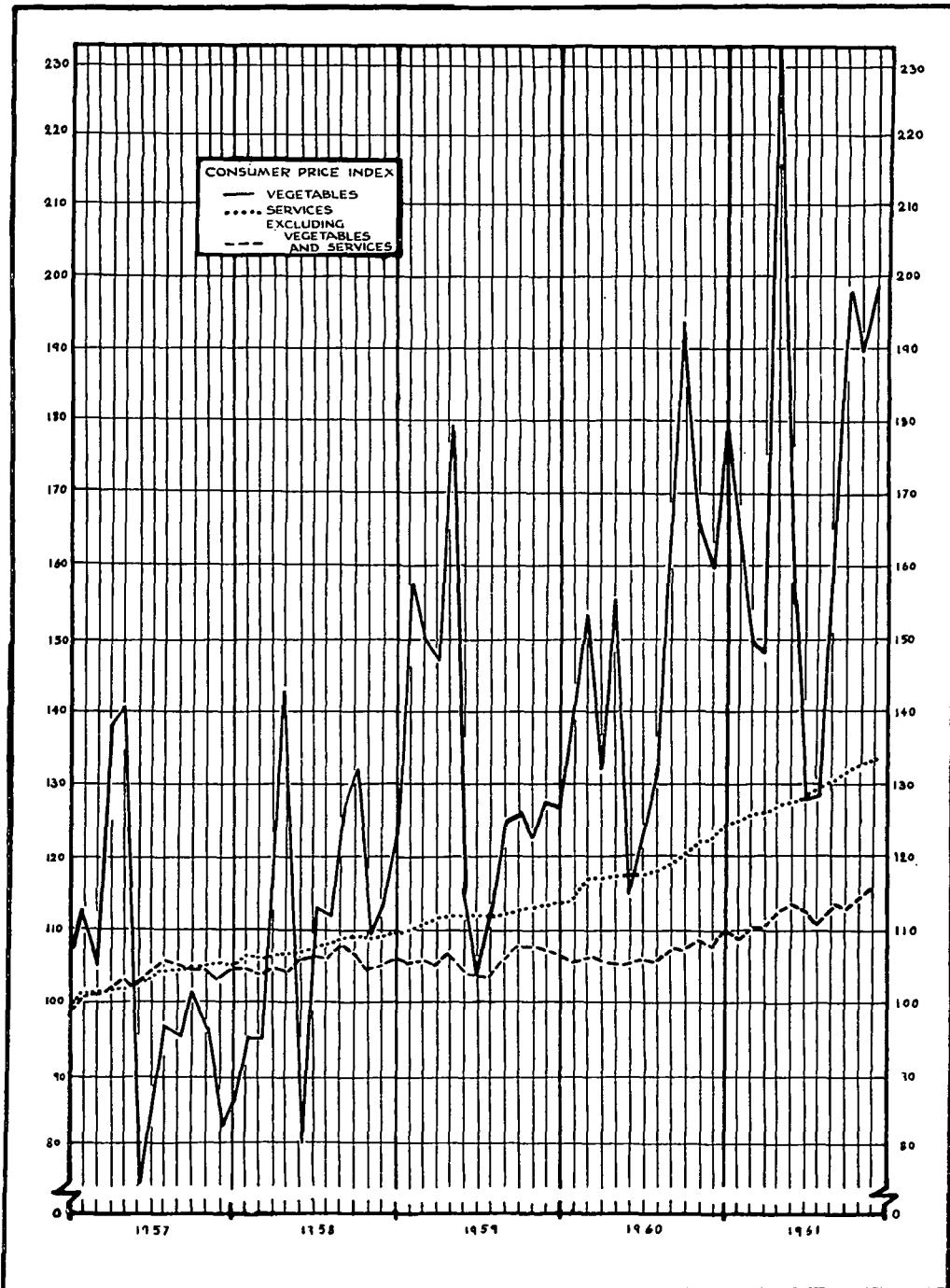
2. Services

The steep rise in the prices of services covered most items in this category, including travel, the cinema, theater, concerts, house repairs, holidays and convalescence, restaurants, beauty parlors, etc.

The relatively high increase in the prices of services has characterized every one of the past few years. It has been caused partly by the rapid increase in the demand for services which accompanied the rise in incomes, and partly by the special character of this sector. There are virtually no import substitutes for services and the possibilities of mechanization are restricted, so that it is difficult to increase productivity. Thus wage increases, which in other sectors are absorbed by increased productivity, are expressed here chiefly by a rise in prices.

Besides the general factors common to the entire sector, there are special factors operating in certain spheres, such as big real estate investments in urban business centers. The large number of special factors is due to the highly varied composition of the sector.

DIAGRAM VI-4
Consumer Price Index, by Components, 1957-61



3. Imported foodstuffs

The rate of increase in the prices of imported foodstuffs appearing in Table VI-3 was biased, owing to the methods employed in measuring beef imports.

The rise in the average price for this category was due to the 26 per cent increase in the price of sugar following the abolition of the partial rationing of this commodity which was still in force in 1960. Hardly any change took place in the prices of other imported foodstuffs.

4. Industrial products

The prices of most locally manufactured industrial products rose by 5 to 6 per cent, i.e. at about the same rate as the general price level. The increase in footwear prices, however, amounted to only some 3 per cent.

5. Housing services

Housing prices went up by about 13 per cent.¹ The index comprises indicators for both owner-occupied and rented housing, as well as property taxes. The steepest rise was in property taxes, which were increased by some 50 per cent at the beginning of 1961. Prices of owner-occupied housing climbed by at least 14 per cent, reflecting the great demand for housing by both the private and public sectors. This demand was not paralleled by an adequate increase in supply, owing to the full employment prevailing in the economy. There was also a steep rise in the prices of urban building plots, due to the limited supply.²

6. Fuels³

Fuel prices rose by 4.5 per cent. Electricity rates, which constituted 40 per cent of this category, remained unchanged, but the other items showed increases ranging from 1.5 per cent in the case of matches to 12.5 per cent in the case of ice. The prices of electricity, kerosene, and gasoline are to all intents and purposes fixed by the Government. Ice, gas, and matches are sold by firms which exercise a considerable control over the market.

7. Other agricultural produce

There was virtually no change in the prices of other agricultural products, chiefly because of the Government's subsidization policy which greatly increased supplies (especially as regards eggs and poultry meat, the major items in this category). In order to prevent an increase in beef prices, the Government im-

¹ This estimate measures the change between the prices prevailing during the months April-September, 1961 and those in the corresponding period of 1960. An explanation of measurement methods for housing services, as used in the preparation of the consumer price index, was given in the "Statistical Bulletin of Israel", February 1962, pp. 13 and 44.

² See Chapter II—"Building"—regarding the increase in building costs.

³ This category includes electricity, kerosene, gasoline, gas, ice, and matches.

ported 4,635 tons of fresh and frozen meat during the year to supplement local production.

(b) *Investment prices*

In most components of investment, prices rose more sharply during 1961 than in 1960 (see Table VI-5).

The higher cost of building and earthworks was caused mainly by a rise of 14 per cent in wages and by considerable increases in the prices of building materials.¹ The big wage increases were due to the large-scale expansion of building under conditions of full employment.

The prices of imported equipment rose because of the customs duties imposed in 1961 and the higher prices charged for equipment in the international market.

TABLE VI-5

Changes in Investment Prices, 1960-61

(percentages)

	<i>Increase from 1959 to 1960</i>	<i>Increase from 1960 to 1961</i>	<i>Weight</i>
Building and earthworks	6	11	620
Equipment	1	6	307
<i>Of which:</i>			
Locally manufactured	1	5	89
Imported	1	6	218
Prices of investments			
in agriculture	3	9	73
<i>Total</i>	4	9	1,000

NOTE: Figures have been rounded to the nearest unit.

SOURCE: Central Bureau of Statistics and Bank of Israel.

(c) *Public consumption prices*

In recent years public consumption prices have been rising faster than those of private consumption. This is due to the big weight of wages in the public consumption basket (over 50 per cent), and to the fact that in the last few years wages have been rising much faster than the consumer price index.

The very steep rise in public consumption prices in 1961 was caused by the increase in wages (continuing a trend apparent in the last few years), as well

¹ See Chapter XII—"Building".

as by the considerably higher prices of the public sector's other purchases, in contrast to their relative stability in the two preceding years.

3. CHANGES IN THE CONSUMER PRICE INDEX, BY INCOME GROUPS

The consumer price index shows the changes that have occurred in the expenditure on a constant basket of commodities, representing the composition of urban wages-earners' consumption.

However, the composition of the consumption basket varies in different income groups, and the "average" basket does not faithfully mirror the situation at various income levels. Consequently, it is of interest to examine the relative increases in the cost of the baskets of different income groups. Table VI-6 does this for the period 1956 to 1961.

TABLE VI-6
Price Indices of Baskets of Various Income Groups,^a 1957-61

Monthly income per capita	Average monthly per capita expenditure on consumption ^b (IL.)	1957	1958	1959	1960	1961
Under IL. 50	43.1	107.7	110.3	110.1	112.1	119.4
IL. 50 to IL. 79	69.0	108.1	110.8	110.6	112.7	119.9
Over IL. 80	111.2	108.1	111.1	111.0	113.5	120.8

^a Excluding the cost of housing.

^b Expenditure on consumption is a better indicator of economic capacity than income, as measured at present.

SOURCE: Central Bureau of Statistics.

As shown in the table, price changes affected the various income groups to a very similar extent. Hence it must be concluded that, if the structure of indirect taxes and subsidies is intended to make the baskets of the low income groups relatively cheaper than those of the higher income groups, this objective has, to all intents and purposes, not been achieved. At the same time, one cannot draw conclusions from the table concerning the progressive or unprogressive nature of indirect taxation.

There appear to be two reasons for the similarity of the increases in the cost of the baskets of the different income groups:

(1) There is little difference in the composition of expenditure in the three income groups examined. An increase in the price of a certain commodity

affects the total cost of the baskets in varying degrees only when the weight of that commodity is not equal in the different baskets.

(2) The rise in the price level covered a wide range of commodities, and did not by-pass even the so-called "poor man's commodities", such as bread and grains.

Items whose weight varies considerably in the different income groups are vegetables, bread and grains, furniture, cigarettes, general services, and health, educational, and entertainment services. The increase in the prices of grains (including bread) and furniture was fairly close to the average, but since the weight of bread declines as income goes up, while that of furniture rises, the increases in their prices taken together did not cause a change in the relative cost of the baskets of the different income groups. On the other hand, the prices of cigarettes, vegetables, general services, and health, educational, and entertainment services rose steeply. Vegetables are most significant in the consumption basket of the lower income groups, and the rise in their prices was thus an important factor in the higher cost of these groups' consumption basket. In contrast, cigarettes, general services, and health, educational, and entertainment services are all more heavily weighted in the higher income groups, and the increase in their prices raised the relative cost of the consumption baskets of these groups.