

CHAPTER II

RESOURCES, USES, AND INCOMES

DEVALUATION affected the national accounts in two different ways: in a purely accounting sense, and concretely through its effects on the behavior of the different units of the economy. Before devaluation, the effective exchange rate for foreign currency transactions exceeded the official rate, and that part of the increase in rate which replaced duties and subsidies did not constitute a real change affecting economic behavior, but involved an accounting change only. This change raised the value of imports and exports and their weight in relation to the other resources and uses: the weight of exports in total resource use went up, as did imports in relation to product; while the import component of each use and the weight of the import surplus in total resources at the disposal of the economy likewise rose.

The substantive effects of devaluation show up in the composition of product and resource use and in price changes. With devaluation, there was an intensification of the inflationary pressures on the demand side which had been evident since the end of 1960. The increased demand of enterprises and households was accompanied by the expansion of public construction and public sector investment, and this combination of factors led to general boom conditions accompanied by an appreciable growth in product, as well as by price rises and considerably higher imports.

A major source of the boom was the increase in the IL counterpart of transfers received from abroad by households and institutions, as well as the increase in the value of foreign currency already held by them.

Ordinary disposable income rose by 2 per cent per capita in real terms, compared with 8 per cent in 1961.

The rise in incomes and liquid assets held by the public, together with expectations of a post-devaluation price increase, led to a growth in consumer and investment demand. Exports continued to expand—at an even slightly faster rate than in 1961. Public consumption—especially defense expenditure—rose sharply, and there was also considerable growth in public sector investment, both in dwellings and in development projects, which were among the major causes of the buoyant level of economic activity.

The higher aggregate demand accelerated the growth of product and, even more so, that of imports. The full employment which in fact already existed in most sectors of the economy did not permit production to expand as fast as

Table II-1
RESOURCES AND THEIR USES, 1958-62

	IL million					Per cent increase or decrease (-) as against preceding year			
	1958	1959	1960	1961	1962	1959	1960	1961	1962
At current prices									
Resources									
Gross national product	3,542	4,066	4,543	5,388	6,464	14.8	11.7	18.6	20.0
Imports ^a	1,034	1,096	1,246	1,507	2,664	6.0	13.7	20.9	76.8
Total resources	4,576	5,162	5,789	6,895	9,128	12.8	12.1	19.1	32.4
Use of resources									
Private consumption	2,473	2,777	3,107	3,639	4,401	12.3	11.9	17.1	20.9
Public consumption	677	755	856	1,006	1,348	11.5	13.4	17.5	34.0
Gross investment ^b	1,006	1,116	1,183	1,494	1,963	10.9	6.0	26.3	31.4
Exports ^a	420	514	643	756	1,416	22.4	25.1	17.6	87.3
At 1958 prices									
Resources									
Gross national product	3,542	3,937	4,269	4,692	5,248	11.2	8.4	9.9	11.8
Imports ^a	1,034	1,125	1,275	1,534	1,723	8.8	13.3	20.3	12.3
Total resources	4,576	5,062	5,544	6,226	6,971	10.6	9.5	12.3	12.0

Use of resources

Private consumption	2,473	2,710	2,940	3,243	3,603	-9.6	8.5	10.3	11.1
Public consumption	677	703	773	853	948	3.8	10.0	10.3	11.1
Gross investment ^b	1,006	1,096	1,129	1,316	1,454	8.9	3.0	16.6	10.5
Exports ^a	420	553	702	814	966	31.6	26.9	16.0	18.7

Price indices (1958 = 100)

Resources

Gross national product	100.0	103.3	106.4	114.8	123.2	3.3	3.0	7.9	7.3
Imports ^a	100.0	97.4	97.7	98.2	154.6	-2.6	0.3	0.5	57.4 ^c
Total resources	100.0	102.0	104.4	110.7	130.9	2.0	2.4	6.0	18.2

Use of resources

Private consumption	100.0	102.5	105.7	112.2	122.1	2.5	3.1	6.1	8.8
Public consumption	100.0	107.4	110.7	117.9	142.2	-7.4	3.1	6.5	20.6
Gross investment ^b	100.0	101.8	104.8	113.5	135.0	1.8	2.9	8.3	18.9
Exports ^a	100.0	92.9	91.6	92.9	146.6	-7.1	-1.4	1.4	57.8 ^c

^a At the official exchange rate. Imports plus duties and exports plus subsidies for 1961 and 1962 are shown in Table II-2. Imports include factor payments to the rest of the world, and exports include factor payments received from the rest of the world.

^b Including investment in stocks.

^c The figures represent a 2 per cent decline in the c.i.f. prices of imports, and a 60 per cent rise in the average official exchange rate; for exports—a decline of 1 per cent in f.o.b. prices and a 58 per cent rise in the average official exchange rate.

SOURCE: Central Bureau of Statistics.

demand, and the demand pressure found expression in a rise in prices exceeding that which was warranted by devaluation.

Real national product rose by 11 to 12 per cent, the highest rate in the last few years. The annual average increment from 1956 to 1961 came to 9 per cent, and in no single year did it exceed 11 per cent.

Imports were up 12 to 13 per cent. The rise was actually much greater in most items, but on the other hand there was a sharp decline in imports of ships, whose weight in total import was considerable in 1961. If ships and aircraft are deducted, the import growth came to 20 per cent, compared with 17.5 per cent in 1961.

The large increase in product, consumption, and investment was accompanied by an increase of 12 to 13 per cent in the average price of domestic uses. Public consumption and investment prices rose by about 20 per cent, while for private consumption the price rise was lower, amounting to 9 per cent.¹

The international prices of imports and exports declined by 1 to 2 per cent. The official exchange rate was raised by 67 per cent in February, so that the average increase for the year as a whole was about 60 per cent. Import and export prices in IL therefore rose on the average by 57-58 per cent, according to the official exchange rate.

GNP prices were up 7 to 8 per cent, and explain more than half the increase in the price of domestic uses.

However, owing to the subsidies and duties in force, the official exchange rate did not reflect the real prices of imports and exports in 1961. A calculation based on the change in effective prices (see Table II-2) shows that they actually rose less than the prices at the official rate: import prices by almost 40 per cent on the average, and export prices by 35 per cent.² The weight in GNP of import taxes net of export subsidies continued to increase in 1962. The rise in GNP prices as calculated according to the effective rates is somewhat lower than that according to the official rate, but is still within the 7 to 8 per cent range.

Wages per employee rose by 13 per cent in 1962. Real average output per employee advanced by 5 to 6 per cent, and nominal wage outlay per unit of output therefore went up by about 7 per cent. The rise in wages was in part connected with the cost-of-living allowance arrangement, and in part resulted

¹ These are implicit price changes which take into account the changes in the weights of the components; therefore they are generally lower than those shown in the chapter on prices which are based on the fixed weights of a specific past year.

² These are also implicit price changes, and therefore differ from changes in the effective exchange rate calculated on the basis of fixed weights. Both imports and exports here include imports-for-export, for which the rate is actually not defined. For such imports, devaluation raised the price by the maximum of 67 per cent. If imports-for-export are netted out, the real effect of devaluation is therefore lower, both as regards imports for domestic use, and as regards the value added of exports.

from market forces which reflect supply and demand relations, and therefore should not be regarded as an autonomous factor in the price increase.

There was only a slight connection between the magnitude of the price increase of the different commodities and the weight of their import component; the largest increases did not necessarily take place in those commodities which were decisively influenced by devaluation. This is strikingly illustrated in the case of dwellings and services, in both of which there was a marked price rise despite a relatively low import component. This development indicates that the rise in prices essentially derived from the demand side, and not from the increase in import prices. The average increase in prices covers commodities which should have been considerably affected by devaluation, but which in fact showed a more moderate price rise. This implies a decline in GNP prices, or in other words, the absorption of the increased costs at the expense of either profits or wages, or through subsidization or tax reduction on the part of the Govern-

Table II-2
RESOURCES AND THEIR USES, AT OFFICIAL AND EFFECTIVE
EXCHANGE RATES, 1961-62
(IL, million)

	1961	1962		Per cent increase from 1961 to 1962	
		At 1961 prices	At current prices	Volume	Price
Resources					
Gross national product	5,388	6,014	6,464	11.6	7.5
Imports at the official exchange rate	1,507	1,692	2,664	12.3	57.4
Total resources	6,895	7,706	9,128	11.8	18.5
Use of resources					
Private consumption	3,639	4,041	4,401	11.1	8.9
Public consumption	1,006	1,118	1,348	11.1	20.6
Gross investment ^a	1,494	1,650	1,963	10.4	19.0
Exports at the official exchange rate	756	897	1,416	18.7	57.9
Imports including duties	1,935	2,173 ^b	3,038	12.3	39.8
Exports including subsidies	904	1,073 ^b	1,446	18.7	34.8
Gross national product excluding import duties and including export subsidies	5,108	5,709	6,120	11.8	7.2

^a Including investment in stocks.

^b Assuming that tax and subsidy rates remain constant.

SOURCE: Central Bureau of Statistics.

ment. On the other hand, there were commodities which, owing to the pressure of demand, went up in price to a greater extent than they should have as a result of devaluation. Contributing to this were the various arrangements made with producers and importers in an attempt to curb the raising of prices. However, in the absence of monetary restraint, such arrangements could not prevent an increase in the general price level. They did succeed in slowing down the rise in the prices of commodities covered in the arrangements, which were precisely the ones which devaluation was intended to make dearer; but at the same time they shifted the demand pressure to other commodities.

A rise of 40 per cent in the effective price of imports as compared with one of 7 to 8 per cent in domestic product prices means that imports became, relatively, about 30 per cent dearer.

Despite such a marked increase, there was apparently no import substitution, and the import component of the different uses rose. The absence of import substitution must apparently be ascribed to the fact that a considerable part of imports are not sensitive to price changes, at least in the short run, so that changes in the volume of imports can come about only through changes in the structure of the economy.

Nevertheless, the figures indicate the possibility of inventory accumulation in 1961 and the running down of stocks in 1962, so that imports did not have to grow for a few months toward the end of the latter year.

1. INCOMES

The most striking development as regards incomes in 1962 was that 36 per cent of the increment to disposable money income derived from foreign transfers, and only two-thirds from economic activity. In 1961, only 7 per cent of the increment came from abroad.

National income rose by 18 to 19 per cent, the same as in 1961. The national income estimates are derived by deducting depreciation on a replacement cost basis. As a result of the steep increase in investment prices in 1962, depreciation for the year was 43 per cent larger, at current prices, than in 1961, and this caused a 2 per cent difference between the rates of growth of gross and net national product.

Although national income rose at roughly the same rate in 1961 and 1962, the growth of direct taxation was twice as rapid in the latter year, as a result of more efficient collection methods and the introduction of the Absorption Loan and the Compulsory Saving Program. Despite the faster increase in population and prices, disposable income from domestic sources grew more slowly than in 1961—a real per capita increase of 2 per cent, as compared with 8 per cent. Wage earnings and other incomes grew at the same rate.

However, it appears that the full extent of the price increase was not always taken into account by the enterprises in recording depreciation, and therefore

NATIONAL INCOME AND PRIVATE DISPOSABLE INCOME, 1960-62

Table II-3
(IL million)

	1960	1961	1962	Per cent increase over preceding year	
				1961	1962
National income ^a	3,448	4,084	4,835	18.4	18.4
Public sector transfers (net) ^b	145	166	203	14.5	22.3
Private income from domestic sources	3,593	4,250	5,038	18.3	18.5
Less: Direct taxes ^c	419	506	693	20.8	37.0
Private disposable income from domestic sources	3,174	3,744	4,345	18.0	16.1
Transfers from the rest of the world	328	372	718	13.4	93.0
Total disposable income	3,502	4,116	5,063	17.5	23.0
Increase over the preceding year					
National income		636	751	104	79
Public sector transfers (net)		21	37	3	4
Private income from domestic sources		657	788	107	83
Less: Direct taxes		87	187	14	20
Private disposable income from domestic sources		570	601	93	63
Transfers from the rest of the world		44	346	7	37
Total disposable income		614	947	100	100

^a Excluding interest on the public internal debt.

^b Including interest payments of the public sector, less its interest receipts and income from property.

^c Income tax, Absorption Loan, Compulsory Saving, and National Insurance.

the depreciation charges were less than what they should have been on a replacement cost basis. Various sources indicate that depreciation was understated by more than IL 100 million, with the result that profits were inflated by this amount, and income as recorded by the enterprises was about 3 per cent greater than true economic income.

One-third of the additional disposable income was derived, as stated, from foreign transfers. These totalled more than IL 700 million, or 16.5 per cent of private disposable income from domestic sources. While the latter item rose by 16 per cent (compared with 18 per cent in 1961), total disposable income rose by 23 per cent, compared with 17.5 per cent in 1961. Devaluation therefore brought about a change in the distribution of incomes.

At the same time, a marked change also occurred in the distribution of assets. The value of foreign currency deposits soared by IL 200 million following de-

valuation, and capital gains likewise accrued to holders of dollar-linked assets, especially various types of securities.

As against this, the indebtedness of recipients of linked loans, including a large number of mortgagors, rose with devaluation. Even when borrowers converted their linked loans to short-term unlinked loans, they had to increase their current repayments. It is difficult to estimate the overall effect of the devaluation on the distribution of assets, but it seems that those who benefited from the larger IL proceeds of foreign transfer receipts were by and large the same ones who reaped the capital gains; in other words, the change in asset distribution intensified the trend in the distribution of income in favor of foreign currency recipients.

2. THE USE OF RESOURCES

(a) *Private consumption*

In 1962 real private consumption rose by 11 per cent, or 6.5 per cent per capita. Consumer prices went up 9 per cent.

Consumption expenditure rose by 21 per cent and reached IL 4,400 million—slightly more than private disposable income from domestic sources, which advanced by 16 per cent. Consumption financed from such sources presumably did not grow at a much faster rate than this; the additional consumption was most likely financed principally from foreign transfers, as well as from past savings and from the fictitious profits resulting from the underestimate of depreciation.

The composition of private consumption expenditure differed from that of the preceding year: the relative share of imports going to consumption rose by 15 per cent, and the domestic product component by 10 per cent, so that the total import component of consumption increased somewhat.

There was a striking 30 per cent growth in imports of final consumer goods and services, mainly durables and various household goods, as well as tourist expenditure abroad. Nevertheless, imported final consumer goods still accounted for only a small part of consumption expenditure—3.5 per cent as compared with 3 per cent in 1961.

Private consumption absorbed 44 per cent of the additional imports and about half the incremental product. The growth of consumption led to a considerable expansion in several branches, especially livestock and vegetables in agriculture; textiles and clothing, wood and carpentry, and rubber and plastics in the industrial sector, as well as in commerce and services.

(b) *Public consumption*

In public consumption as well, the import component, especially imports of final goods, grew faster than the domestic component, so that the share of the former increased. This was due to the large import for defense needs.

Public consumption accounted for 22 per cent of the additional imports, and for 9 per cent of the additional product. Production destined for public consumption has a low weight in the output of the various branches, except of course Government services, and therefore the rise in public consumption did not particularly stimulate expansion in any of the branches.

(c) *Exports*

The volume of exports rose by 19 per cent in 1962; because of the decline in the prices of citrus and several other products, foreign currency proceeds rose at a somewhat lower rate—17 per cent. In exports too there was a shift to products with a higher import component, and the overall import component rose. The 19 per cent gain in exports entailed a 23 per cent expansion of imports, so that value added rose by only 17 per cent.

The high import component of exports is an important factor in the growth of imports: in 1962, 37 per cent of the import increment went to export production, whereas the share of exports in the incremental product was only 17 per cent. Nevertheless, exports were an important factor during the year reviewed in the expanded output of textiles and clothing, wood and carpentry, paper and printing, rubber and plastics, diamonds, and shipping and aviation services.

(d) *Investment*

Gross investment rose by 10 to 11 per cent. This consists of a 15 per cent increase in construction, a 3 per cent decline in investment from agricultural output, a 22 per cent increase in equipment, and a 65 per cent fall in ship and aircraft acquisitions. The smaller import of ships and aircraft led to a decline in total imports of equipment, so that the import component of investment contracted. If ships and aircraft are excluded from the calculation, the import component of investment remained almost unchanged.

Construction investment was concentrated mainly in dwellings, the volume of which rose by more than 20 per cent. The largest expansion—by about 30 per cent—was in public immigrant housing, while private building rose by 13.5 per cent. In both categories, the rate of growth was the highest in recent years. The growth of industrial and construction investment led to greater activity in the glass, cement and ceramics, and metal products branches.

Investment in motor vehicles also rose, and the output of the vehicle production and repair branch was higher.

3. RESOURCES

(a) *Product and output*

In 1962 gross national product rose by 11 to 12 per cent. Gross output increased at a somewhat faster rate—apparently 12 to 13 per cent.

The number of gainfully employed was up 5.7 per cent, and product per

person employed thus rose by 5 to 6 per cent. The stock of productive capital rose by 11 to 12 per cent, and productivity by 3 to 4 per cent.

The biggest growth was in transportation, the output of which went up more than 17 per cent owing to increases in shipping and aviation services and an especially marked expansion in railway output. The second highest rate of growth was in construction, reflecting the increased investment in both dwellings and earthwork. Manufacturing output rose by 14 per cent, most sub-branches sharing in the increase. A particularly large increase occurred in branches affected by the building boom, such as wood and carpentry, non-metallic minerals, and metals. There was also strong growth in diamonds, as well as in rubber and plastics, where the weight of private consumption is very considerable. Agricultural output rose relatively little, principally owing to the decline in the output of intermediate products—after the appreciable growth of the previous year; these variations reflected mainly changes in weather conditions.

Table II-4
INCREASE IN OUTPUT AND GAINFULLY
EMPLOYED, BY SECTOR, 1962

(percentages)

Sector	Gross output	No. of gainfully employed
Agriculture	7	1.5
Industry	14	9.5
Construction	15	9.9
Transportation	17	4.6

In all branches output rose faster than the number of gainfully employed, i.e. there was an increase in output per worker.

(b) *Imports*

In 1962 the volume of imports grew by 12.3 per cent: raw materials rose by 13.4 per cent, final consumer goods by 30 per cent, public sector imports by 23 per cent, while investment goods declined. At 1958 prices, the import component of all final uses rose, except for investment, where the decline was due to the smaller import of ships and aircraft.

The import component has, in fact, tended to rise since 1957. From 1958 to 1962, imports went up by two-thirds, while product expanded by only 50 per cent. Imports have risen faster than product because of shifts in the composition of output and demand, products and branches with a higher import

component having increased their share. There has been practically no change in the technical import component of the individual branches.

From 1958 to 1962, imports rose by IL 690 million, at 1958 prices. The increase in final uses, with composition held constant, explains 78 per cent of the additional imports, while the change in the composition of the final uses explains a further 25 per cent. On the basis of these two factors, the import increment should have been 3 per cent higher than it actually was during this period (see Table II-7 and Diagram II-1). The difference, which comes to less

Table II-5
PRODUCT AND IMPORTS, BY FINAL DESTINATION, 1958-62

(IL million, at 1958 prices)

	Year	Private consumption	Public consumption	Gross investment ^a	Exports	Total ^b
Imports of finished goods and services	1958	70	138	190	—	398
	1959	66	154	182	—	403
	1960	77	156	249	—	482
	1961	98	185	277	—	560
	1962	127	227	264	—	618
Imports of raw materials	1958	325	33	111	167	636
	1959	355	35	113	220	722
	1960	384	39	112	258	793
	1961	459	55	134	326	974
	1962	513	56	140	395	1,105
Total imports	1958	395	171	301	167	1,034
	1959	421	189	295	220	1,125
	1960	461	195	361	258	1,275
	1961	557	240	411	326	1,534
	1962	640	283	404	396	1,723
Gross national product	1958	2,079	506	704	253	3,542
	1959	2,290	514	800	333	3,937
	1960	2,479	578	768	444	4,269
	1961	2,686	613	905	488	4,692
	1962	2,963	665	1,050	570	5,248
Total final uses	1958	2,474	677	1,006	420	4,576
	1959	2,711	703	1,096	553	5,062
	1960	2,940	773	1,129	702	5,544
	1961	3,243	853	1,316	814	6,226
	1962	3,603	948	1,454	966	6,971

^a Including investment in stocks.

^b Discrepancies in total are due to rounding.

than \$ 15 million over the four years, is negligible, and the calculation would seem to show that the technical import components have, on the whole, remained constant.

The changed composition of final uses can be attributed to three factors. First, there was a rise in the share of exports at the expense of the other uses. Since the import component of exports is high, this implies a greater increase in imports than would result from a corresponding rise in the other uses. This factor explains 8 per cent of the import increment from 1958 to 1962. Second, there was a shift in all final uses from domestic products to imported products, and this explains 7 per cent of the increment. Third, in the demand for locally produced goods, there was a shift to goods with a higher import component. This process took place in private consumption, investment, and exports, and explains 10 per cent of the import increment.

In practice, the unexplained increment includes, along with import substitution, changes in inventory and estimating errors, so that it is difficult to ascribe any particular significance to the annual fluctuations in this item.

Table II-6
IMPORT COMPONENT OF FINAL USES, 1958-62
(percentages, at 1958 prices)

	Year	Private con- sumption	Public con- sumption	Gross invest- ment ^a	Exports	Total
Total import component	1958	16.0	25.3	29.9	39.8	22.6
	1959	15.5	26.9	26.9	39.8	22.2
	1960	15.7	25.2	32.0	36.8	23.0
	1961	17.2	28.1	31.2	40.0	24.6
	1962	17.8	29.9	27.8	41.0	24.7
Import component in gross output ^b	1958	13.5	6.1	13.6	39.8	15.2
	1959	13.4	6.4	12.4	39.8	15.5
	1960	13.4	6.3	12.7	36.8	15.7
	1961	14.6	8.2	12.9	40.0	17.2
	1962	14.8	7.8	11.8	41.0	17.4
Imported finished goods and services component of final uses	1958	2.8	20.4	18.9	—	8.7
	1959	2.4	21.9	16.6	—	8.0
	1960	2.6	20.2	22.1	—	8.7
	1961	3.0	21.7	21.0	—	9.0
	1962	3.5	23.9	18.2	—	8.9

^a Including investment in stocks.

^b National product plus imported raw materials.

Nevertheless, it may be that the rise in 1961 and the decline in 1962 tend to confirm the hypothesis that 1961 saw a building up of stocks of imported commodities, with a decline in the latter months of 1962.

Table II-7
CHANGES IN IMPORTS DUE TO CHANGES IN FINAL USES AND
COMPOSITION THEREOF, 1959-62
 (IL million, at 1958 prices)

	1959	1960	1961	1962	Total 1959-62	
					IL million	Per cent of total
Increase in imports due to:						
Increase in final uses	109	109	153	170	541	78.5
Change in composition of final uses	15	15	17	11	58	8.4
Increase in imported finished goods in each final use	-25	52	13	7	47	6.8
Change in composition of demand in each final use	7	11	31	18	67	9.8
Total increase due to changes in final uses	106	187	214	206	713	103.5
Imports not explained by changes in final uses	-15	-37	45	-17	-24	-3.5
Total actual import increment	91	150	259	189	689	100.0

An analysis of imports since 1958 reveals two important characteristics. First, the economy's import requirements are mounting steadily, and at a faster rate than product and final uses. Imports have risen not only because of the expansion of economic activity, but also because of changes in its composition. The growth of final demand together with changes in its composition from 1958 to 1962 entailed a 48 per cent rise in product and a 65 per cent rise in imports. Second, the actual increase in imports is consistent with that implied by the given final demand. In other words, since 1958 there has been no import substitution in the productive branches.

The absence of import substitution and the rise in the import component may be regarded as a natural development up to the devaluation, in view of the steady decline in the relative price of imports over the last few years. Import prices lagged far behind domestic product prices, despite the fact that import duties were raised from time to time (see Table II-9 and Diagram II-2). Such a trend, of course, is not likely to encourage import substitution, either

Diagram II-1

ACTUAL INCREASE IN IMPORTS AND INCREASE DUE TO CHANGES
IN FINAL USES AND COMPOSITION THEREOF, 1959-62

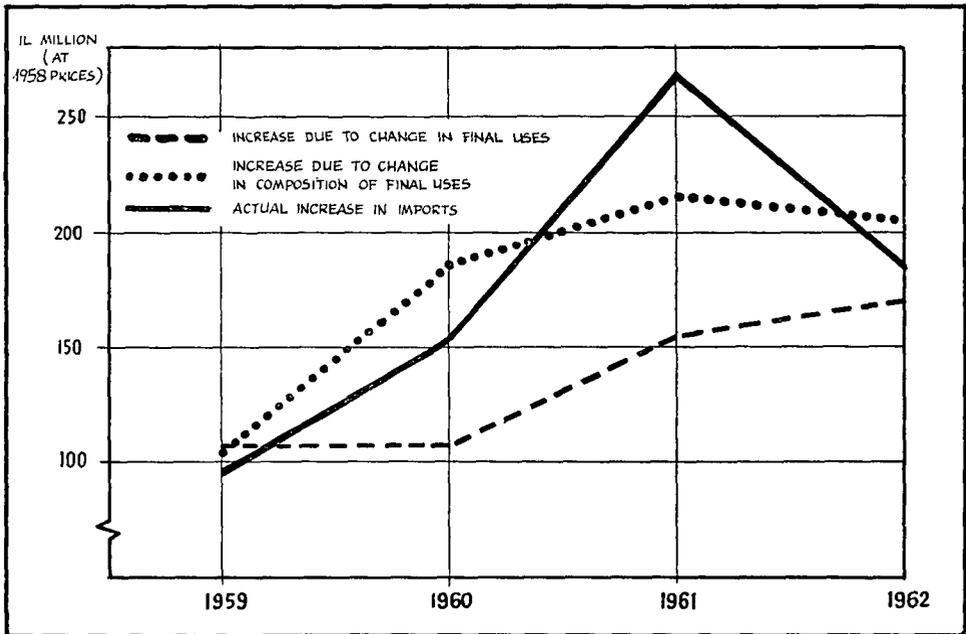


Table II-8

RISE IN IMPORTS DUE TO STRUCTURAL
CHANGE IN USES, 1959-62

(IL million, at 1958 prices)

	Final commodities	Raw materials
Private consumption	25	34
Public consumption	34	—
Gross investment	-12	29
Exports	—	4
Total	47	67

through changes in the composition of demand or through a change in the composition of output.

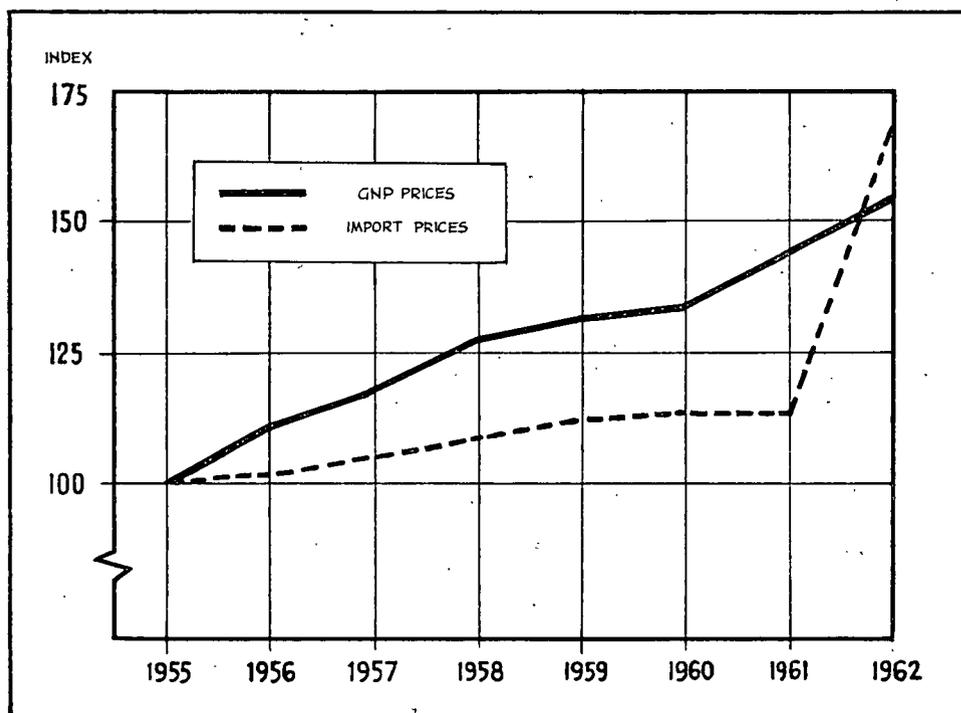
The tendency for import requirements to rise, not only absolutely but also relative to product, was evident in 1962 as well, although less markedly than in

Table II-9
**CHANGES IN IMPORT PRICES RELATIVE TO
 GNP PRICES, 1956-62**
 (1955 = 100)

	Index of local currency prices of imports ^a	Index of GNP prices	Index of relative import prices
1956	107.6	110.3	97.6
1967	117.3	118.1	99.3
1958	119.0	126.2	94.3
1959	111.1	130.4	85.2
1960	113.9	134.3	84.4
1961	114.5	144.9	79.0
1962	164.5	155.5	105.8

^a Includes changes in c.i.f. prices, the official exchange rate, and import duties.

Diagram II-2
INDICES OF IMPORT^a AND GNP PRICES, 1955-62
 (1955 = 100)



^a Based on provisional data.

Table II-10
IMPORT COMPONENTS, BY FINAL USE, 1962

	At 1958 prices					At current prices ^a				
	Private consumption	Public consumption	Gross investment ^b	Exports	Total	Private consumption	Public consumption	Gross investment ^b	Exports	Total
IL million										
Imports of finished goods and services	127	227	264	—	618	197	351	408	—	956
Imports of raw materials	513	56	140	396	1,105	793	87	216	612	1,708
Total imports	640	283	404	396	1,723	990	438	624	612	2,664
Gross national product	2,963	665	1,050	570	5,248	3,411	910	1,339	804	6,464
Total use of resources	3,603	948	1,454	966	6,971	4,401	1,348	1,963	1,416	9,128
Percentages										
Import components										
Total import component	17.8	29.9	27.8	41.0	24.7	22.5	32.5	31.8	43.2	29.2
Import component in gross output ^c	14.8	7.8	11.8	41.0	17.4	18.9	8.7	13.9	43.2	20.9
Imported finished goods and services component of final uses	3.5	23.9	18.2	—	8.9	4.5	26.0	20.8	—	10.5

^a In the absence of accurate data, it was assumed that changes in the international prices of imports (a 4 per cent decline) applied equally to each use.

^b Including investment in stocks.

^c National product plus imported raw materials.

1961. It may therefore be asked why the considerable rise in the price of imports in 1962 did not lead to any import substitution.

The answer to this question is to be found first and foremost in the composition of imports. In respect of final goods, two categories can be distinguished. The first consists of imports that are completely insensitive to price changes—at least in the short run—such as those for defense purposes and certain investment items such as ships and aircraft and equipment not manufactured locally. But these are precisely the ones whose prices were most affected by devaluation, going up to the maximum possible extent of 67 per cent, because they had previously been duty-free. In the second class of final goods, especially consumer goods for which demand is presumably elastic, the rises were much more moderate, reaching 20 to 25 per cent. Taken together with the domestic price increase, this represents a relative price rise of only 10 to 15 per cent.

This figure certainly has an upward bias, since before devaluation the effective exchange rate for part of the imports, especially foreign travel, exceeded the official rate even with taxes included. A factor which countered the increased price of imports was the rise in incomes, which offset the tendency for import demand to shrink as a result of higher prices.

Demand for intermediates is inherently inelastic in the short run, since any substitution of raw materials and unfinished goods requires the development of new branches. Demand for raw materials that cannot be produced in the country can change only as a result of changes in the volume of output of user branches, and such changes, of course, also involve long-run processes.

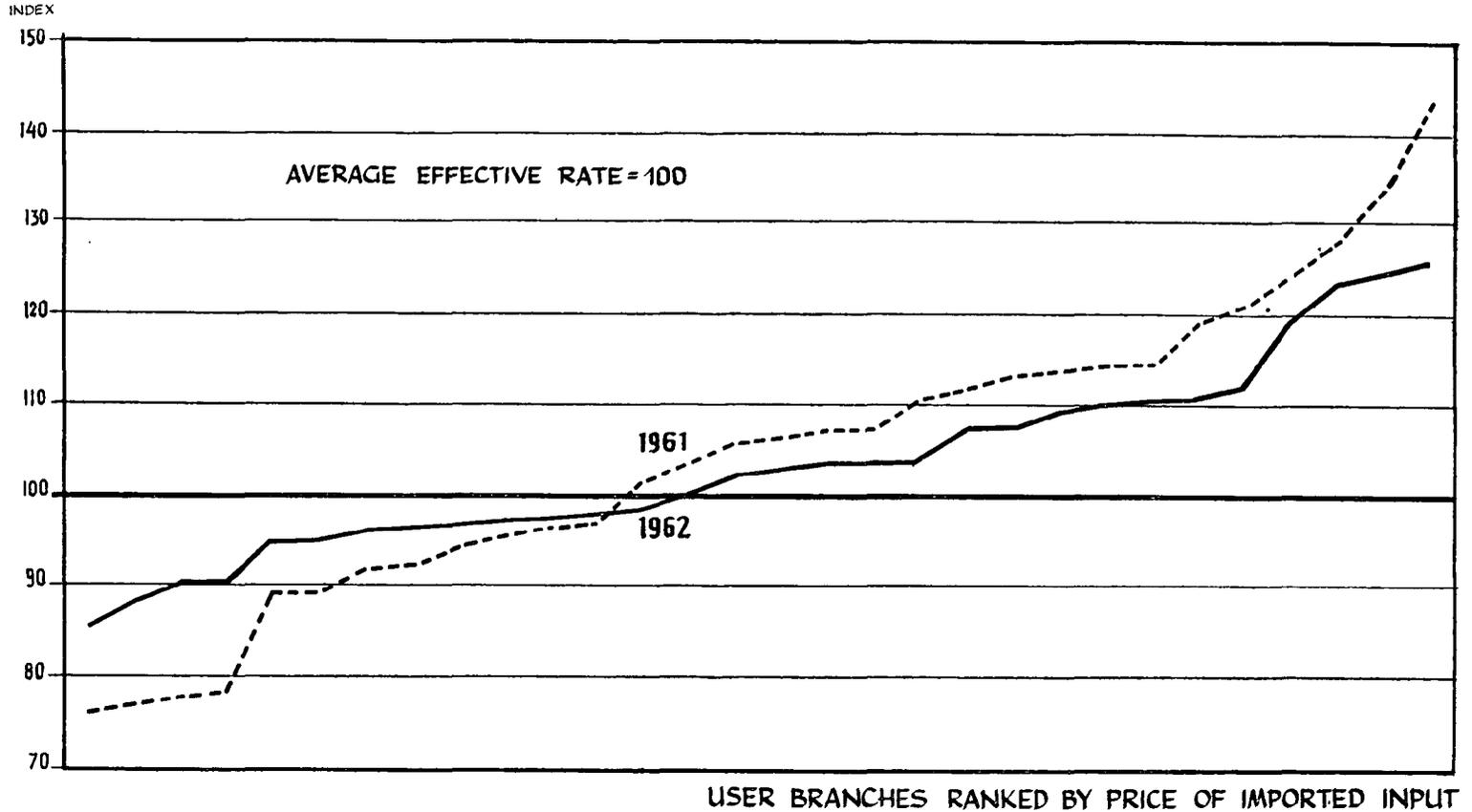
Import liberalization, which of late has been introduced to a growing degree, also inhibits import substitution. The extent of import substitution in the future is connected not with the direct effectiveness of the devaluation, but first and foremost, with the development of various industrial branches.

Table II-11
IMPORTS, EXPORTS, AND THE IMPORT SURPLUS, 1958-62
(IL million, at 1958 prices)

	1958	1959	1960	1961	1962	Average 1958-62
Imports	1,034	1,125	1,275	1,534	1,723	1,338
Exports	420	553	702	814	966	691
Import surplus	614	572	573	720	757	647
Domestic use of resources	4,156	4,509	4,842	5,412	6,005	4,985
Exports as a per cent of imports	40.6	49.2	55.1	53.1	56.1	51.6
Import surplus as a per cent of domestic use of resources	14.8	12.7	11.8	13.3	12.6	13.0

Diagram II-3

IMPORTED RAW MATERIAL INPUTS: USER BRANCHES RANKED BY RELATIVE IL PRICES OF INPUTS, 1961-62



The rise in the exchange rate naturally raised the share of imports in each final use, and the total import component in 1962, which was 25 per cent at 1958 prices, came to more than 30 per cent at 1962 prices.

(c) *The import surplus*

Exports have generally expanded faster than imports, but since the absolute export increment is smaller than that of imports, the import surplus has been growing steadily.

The ratio of the import surplus to total domestic uses has in recent years shown only insignificant fluctuations, averaging 13 per cent at 1958 prices; a revaluation at current prices would raise the 1962 figure from 12.6 to 16.2 per cent.

Since 1958 the import surplus has on the whole risen *pari passu* with domestic uses. Although the weight of exports has risen steadily—from only 40 per cent of imports in 1958 to 56 per cent in 1962—the share of the import surplus in total domestic uses has remained more or less constant, since imports have risen faster than product. At the same time, the import surplus has continued to grow in absolute terms.

4. SECTORIAL DISCRIMINATION THROUGH EFFECTIVE EXCHANGE RATES FOR IMPORTS

One of the aims of the exchange rate unification, which was one of the basic principles of the New Economic Policy, was the elimination of distortions in the productive system and of discrimination between the various sectors. In 1961 the effective exchange rates for imported goods ranged from IL 1.70 to IL 10 and more per dollar, although in respect of 90 per cent of the value of imports, the rate did not exceed IL 3.50/\$ 1. The inter-quartile range¹ of the effective exchange rate dispersion dropped from 40 agorot in 1961 to 6 agorot in 1962.

In both years the average rate for raw materials was 10 to 12 per cent lower than that for final goods. This was a reflection of the general protective policy through the imposition of higher duties on imports of finished goods.

However, this protection was extended only to consumer goods. In 1961 the effective exchange rate for public consumption and investment was 7 per cent below the rate for raw materials, and in 1962 it was also slightly lower. On the other hand, a high duty was imposed on consumer goods, and in 1961 the effective rate for these was one-third higher than for raw materials, and in 1962, 30 per cent higher.

But even in respect of the raw material imports themselves, the rates were

¹ The range between the rate which is higher than that of one-quarter of imports and that which is higher than that of three-quarters, covering therefore that half of imports in the middle of the exchange rate scale.

not uniform, neither in 1961 nor in 1962. Customs rate differentials have a two-way effect: discrimination works in favor of a branch insofar as the duty on its own imported inputs is lower, and insofar as the duty on competing imports is higher. Rate unification means that duties are the same for all branches and for competing products.

An examination of the average price of inputs to each of the various branches shows that rate differentials narrowed from 1961 to 1962 (see Diagram II-3). In 1961 the highest branch average was 90 per cent above the lowest, while in 1962 the figure was slightly more than 50 per cent.

As stated, this is only one aspect of the matter. In order to gauge the effect of effective import exchange rates on the position of a given branch, it is also necessary to take account of the protection accorded it through the taxation of competing imports. A comparison of the effective rates of the imported inputs in each branch with the effective rates of competing imports reveals a somewhat surprising phenomenon: those branches whose inputs were highly taxed were generally the ones whose products were protected through tariffs, while branches with a low rate of taxation on their imported inputs did not as a rule enjoy tariff protection on their manufactures.

This manifestation characterized most branches before devaluation; in a few exceptional instances where this was not so, the situation has improved since devaluation and there is now a greater degree of consistency.

Appendix to Chapter II
RECONCILIATION BETWEEN RELATED NATIONAL ACCOUNTS
AGGREGATES, 1960-62
(IL million)

	1960	1961	1962
Private consumption	3,107	3,639	4,401
Plus: Public consumption ^a	856	1,006	1,348
Gross investment ^b	1,183	1,494	1,963
Equals: Domestic use of resources	5,146	6,139	7,712
Plus: Exports	643	756	1,416
Equals: Use of resources	5,789	6,895	9,128
Less: Imports	1,246	1,507	2,664
Equals: Gross national product at market prices	4,543	5,388	6,464
Less: Depreciation	364	430	616
Equals: Net national product at market prices	4,179	4,958	5,848

Appendix to Chapter II

RECONCILIATION BETWEEN RELATED NATIONAL ACCOUNTS
AGGREGATES, 1960-62 (continued)

(IL million)

	1960	1961	1962
Less: Net indirect taxes	557	745	899
Errors and omissions	174	129	114
Equals: National income ^a (net national product at factor cost)	3,448	4,084	4,835
Plus: Public sector transfers to households and non-profit institutions	231	264	309
Interest on the internal public debt	53	58	91
Less: Transfers from households and non-profit institutions to public sector	46	59	79
Interest receipts of public sector	62	64	71
Other public sector income from property	31	33	47
Equals: Private income from domestic sources	3,593	4,250	5,038
Less: Income tax	316	376	490
Absorption Loan and Compulsory Saving	—	4	57
National Insurance contributions	103	126	146
Equals: Private disposable income from domestic sources	3,174	3,744	4,345
Plus: Personal transfers and restitution payments from abroad ^b	242	280	582
Transfers of non-profit institutions from abroad ^c	86	92	136
Equals: Private disposable income	3,502	4,116	5,063

^a Does not include interest on the public debt.

^b Including investment in stocks.

^c In \$ million:

	1960	1961	1962
Transfers of households	134.6	155.5	201.4
Transfer of non-profit institutions	47.8	51.0	47.0

The 1960 and 1961 figures in the table were converted at IL 1.80/\$ 1, and the 1962 figures at an average rate of IL 2.89/\$ 1.

SOURCE: Private consumption through national income—from the Central Bureau of Statistics; other figures are Bank of Israel estimates.