

## CHAPTER V

# DOMESTIC INVESTMENT

### 1. MAIN DEVELOPMENTS

AFTER EXPANDING rapidly for several years until 1964 and declining slightly in 1965 (by about 2 percent), gross domestic capital formation during the year reviewed fell off by a further 18 percent in real terms, and totalled some IL 2,500 million—about the same level as in 1962 and 1963. Both dwelling and nondwelling investment were nearly 20 percent lower than in 1965, while inventories of raw materials and finished goods rose by almost 30 percent. The weight of gross investment in domestic uses fell to 19 percent, compared with an average of nearly 25 percent during 1960–65. There were no marked structural changes in 1966, and as in previous years, construction accounted for about two-thirds of the total.

The downward trend in fixed investment began in early 1965 and was especially strong in 1966. Partial indicators show that during the last quarter of 1966 the volume was 25 percent below the first quarter, and as much as 30 percent below the average quarterly level in 1964.<sup>1</sup>

The decline in gross capital formation, particularly in 1966 when it totalled IL 560 million at 1965 prices, had a marked contractionary effect on economic activity, which itself further dampened investment. The smaller volume of investment, both private and public, was the most decisive change in domestic demand in 1966. It had a cumulative contractionary effect on the national product and employment; this applies especially to construction activity, which has a low import and a high labor component. In this connection it should be noted that a slower growth in the capital stock, in line with that of the national product,<sup>2</sup> is reflected by a greater decline in investment.

Real gross investment expanded rapidly between 1956 and 1964, at an average rate of 12 percent per annum; in 1964 alone it advanced 21 percent. Expectations that the economic boom would continue, based on the steady and rapid rise of the national product at about 11 percent per annum during 1961–

<sup>1</sup> This estimate is based on a quarterly index of total investment in fixed assets, constructed mainly from the following data: average area of building starts and completions, value of new publicly financed residential construction, imports of investment goods, and the production indexes for the relevant industries.

<sup>2</sup> The country's capital stock increased by 7 percent in 1966, which in the long run may result in an annual growth of about 7 percent in the national product. In 1966, however, the national product did not increase at all.

Table V-1  
GROSS AND NET INVESTMENT, 1960-66  
(IL million)

	1960	1961	1962	1963	1964	1965	1966	Percent increase or decrease (-) as against preceding year					
								1961	1962	1963	1964	1965	1966
<b>At current prices</b>													
Gross fixed nondwelling investment	775	992	1,291	1,499	1,933	1,996	1,631	28	30	16	29	3	-18
Gross investment in dwellings	347	472	687	726	866	974	776	36	46	6	19	12	-20
Change in inventories	86	92	125	103	182	86	110	7	36	-18	77	-53	28
Total gross investment	1,208	1,556	2,103	2,328	2,981	3,056	2,517	29	35	11	28	3	-18
Less: Depreciation	364	438	631	765	878	1,022	1,144	20	44	21	15	16	12
Net investment	844	1,118	1,472	1,563	2,103	2,034	1,373	32	32	6	35	-3	-32
<b>At 1965 prices</b>													
Gross fixed nondwelling investment	1,213	1,434	1,485	1,630	2,010	1,996	1,606	18	4	10	23	-1	-20
Less: Depreciation	413	461	537	617	686	773	852	12	16	15	11	13	10
Net fixed nondwelling investment	800	973	948	1,013	1,324	1,223	754	22	-3	7	31	-8	-38
Gross investment in dwellings	536	656	827	819	909	974	776	22	26	-1	11	7	-20
Less: Depreciation	157	170	187	207	227	249	273	8	10	11	10	10	10
Net investment in dwellings	379	486	640	612	682	725	503	28	32	-4	11	6	-31
Total gross fixed investment	1,749	2,090	2,312	2,449	2,919	2,970	2,382	19	11	6	19	2	-20
Change in inventories	109	110	140	109	188	86	112	1	27	-22	72	-54	30
Total gross investment	1,858	2,200	2,452	2,558	3,107	3,056	2,494	18	11	4	21	-2	-18
Less: Depreciation	570	631	724	824	913	1,022	1,125	11	15	14	11	12	10
Total net investment	1,288	1,569	1,728	1,734	2,194	2,034	1,369	22	10	—	27	-7	-33

SOURCE: Central Bureau of Statistics and Bank of Israel.

64, were responsible for this big increase. Although supply was slow to adjust to mounting demand between 1961 and 1964, it eventually caught up and the first signs of excess supply appeared in 1964. There was even overinvestment in several sectors, while fears of Government restrictions on building touched off a strong upsurge in construction starts and led to the accumulation of a large stock of unsold completed buildings, chiefly dwellings and business and industrial premises.<sup>1</sup> It should be noted that in some cases the concentration of investment in a single year may be purely fortuitous. This applies to ships and aircraft<sup>2</sup> and to changes in inventories, which are influenced by factors quite different from those determining the volume of investment in fixed assets.

The immediate effect of the various factors depressing investment demand is limited, the full impact only being felt in subsequent years. The implementation of investments is normally a lengthy process, which cannot easily be adjusted to rapid changes in demand. It takes one to two years to put up a building, while equipment must be ordered many months in advance, from both Israeli and foreign suppliers. A quick reaction is possible mainly during periods of rapidly falling demand, when planned projects or equipment orders can be deferred. Presumably there were also special factors in 1966 which had an effect here, such as declining profitability and a slower population growth. The fact that investment decreased chiefly during the second half of the year, and that the level in the last quarter of 1966 was about 25 percent lower than during the first quarter, supports this assumption.

The principal cause of the change in investment demand was the drop in immigration in the last two years, and especially in 1966.<sup>3</sup> In 1961–64 net immigration was about 50,000 per annum, dropping to about 20,000 in 1965 and less than 5,000 in 1966. The demand for three types of investment was directly and indirectly affected by this: immigrant housing, buildings for public institutions and various essential services, and fixed assets required to supply the additional demand generated by the newcomers (for both consumer and capital goods). The decline in housing demand was especially pronounced during the last two years, but since the supply of dwellings in a given year is somewhat inelastic, a stock of vacant units accumulated. An indirect effect of reduced immigration, reinforced by other factors, is reflected in the drop of more than IL 50 million in 1966 in purchases of construction machinery and equipment.

Another exogenous factor depressing housing demand was the decline in

<sup>1</sup> See also Chapter XIII, "Construction and Housing", section 2(b).

<sup>2</sup> Real gross investment in fixed assets other than ships and aircraft increased by 13 percent in 1964 and by 8 percent in 1963, while the increase in total gross investment was 21 and 5 percent respectively.

<sup>3</sup> According to the assumptions and calculations of M. Merhav in his article, "Some Economic Consequences of a Large-Scale Renewal of Immigration", Bank of Israel Bulletin No. 17, January 1963, with the data updated and adjusted. About half the decline in gross investment between 1964 and 1966 can be attributed to immigration.

private transfers from abroad, particularly personal restitution payments from Germany.<sup>1</sup> These transfers have been contracting gradually since 1963 (in 1966 receipts were 40 percent less than in 1963), after expanding during the years 1956–63. Taking into account a lag in the outlay of these funds, it appears that their influence on investment demand reached a peak in 1964 and has been diminishing since then.

Capital transfers from abroad for investment purposes, which influence the demand for investments other than dwellings, also fell off during the last two years—by about 40 percent in 1965 and 10 percent in 1966.<sup>2</sup> These flows include the purchase of shares, the ploughing-back of profits, and capital transfers in cash or in kind. It should be noted that this type of receipt depends to some extent on developments in domestic demand, and a decline therein partly reflects the contraction of domestic demand and investment. The smaller volume of foreign transfers received by nonprofit institutions in 1966 was one of the major reasons for the contraction of their investment.

Added to these factors which slowed down the growth of domestic demand and the national product—a development in which the construction sector played a predominant role—was the Government's retrenchment policy. The Government's measures were also aimed first and foremost at reducing investment, chiefly through cuts in the development budget, and by deferring or shelving major projects. Investment plans were apparently examined more scrupulously in view of the considerable losses incurred by a number of public sector companies. However, at the end of 1966 there was a change in Government policy, and deliberations were initiated with a view to granting further concessions under the Law for the Encouragement of Capital Investments. Direct public sector<sup>3</sup> investment other than in housing declined by nearly 16 percent, compared with a drop of 6 percent in 1965 and a rise of almost 30 percent in 1964. Most of the contraction in 1964–66 was due to reduced purchases of ships and aircraft by public sector companies, and to smaller investment in ports (after the completion of the first stage of Ashdod Port), the Dead Sea Works, and public buildings (schools and health institutions). On the other hand, public sector investment in telecommunications (by the Post Office), the railway, and water projects remained virtually unchanged.

Nondwelling investment of private enterprises (excluding nonprofit institu-

<sup>1</sup> Total restitution received less current pensions. The amount of nonrecurrent restitution income invested in dwellings was estimated in saving surveys at about IL 200 million in 1964 and IL 160 million in 1966.

<sup>2</sup> See Table III–18 in Chapter III, "The Balance of Payments". The item "liquidation of foreign investments in Israel" should be deducted from total foreign investment.

<sup>3</sup> Including the Government, National Institutions, local authorities, Government enterprises, and public sector companies (see also Table V–2). This definition differs from that used in Chapter VII, "Public Sector Operations", which does not include public sector companies.

tions) fell off even more, by nearly 25 percent, after rising by about 5 percent in 1965 and 20 percent in 1963 and 1964. The decline, reflecting sagging demand and the official retrenchment policy, was aggravated by the expectations of private investors in 1966, which were accentuated by the substantial drop in profitability<sup>1</sup> during the year.

Industrial investment (including construction equipment) showed a particularly steep decline of 32 percent at constant prices. Purchases of construction equipment were very heavy in 1962–65 and by 1966 there was a surplus, so that this type of investment came to a virtual standstill. Labor shortages and a prolonged rise in the relative price of labor had induced the substitution of equipment for labor in this sector—a trend brought to a stop by the crisis in construction. Another direct effect of the building slump (together with other factors) was the 30 percent drop in purchases of transport equipment, especially tenders and trucks. Private investment in commercial and office premises and hotels also fell off, by approximately 30 percent. This steep downward trend, which carried over into 1967,<sup>2</sup> can be partly attributed to the decline in the capital utilization rate and reduced profitability.

The value of new residential construction was down 20 percent in 1966. However, in contrast to other sectors, the decline was greater in public than in private investment<sup>3</sup>—26 as against 17 percent. The curtailment of public housing was due chiefly to the virtual cessation of immigration and the creation since 1964 of a surplus supply, resulting in the accumulation of a large stock of vacant dwellings. In private housing, the recession, the decline in personal restitution receipts from Germany, the existence of surplus public housing, and expectations that housing prices would decline, all these combined to dampen demand.<sup>4</sup>

The decline of nearly 20 percent in total fixed capital formation was reflected by the slower growth of the gross capital stock.<sup>5</sup> Nondwelling capital stock grew by 7 percent, compared with 10 percent in 1965 and an average of over 11 percent per annum during 1960–64. However, even the 1966 growth rate is sufficient to sustain a rapid economic expansion, provided it is maintained in the coming years.

The value of assets discarded, which represents assets withdrawn from produc-

<sup>1</sup> The reference is to the ratio between returns to capital and the nondwelling capital stock. Returns to capital fell off appreciably in 1966, when wages rose two-and-a-half times faster than national income.

<sup>2</sup> As indicated by data on building starts.

<sup>3</sup> Public and private residential construction are defined according to the initiating sector, whereas nondwelling investment is defined according to the sectors acquiring the assets.

<sup>4</sup> See also Chapter XIII, "Construction and Housing".

<sup>5</sup> For an explanation of this and other terms used here, see A. L. Gaathon, *Capital Stock, Employment and Output in Israel, 1950–1959*, Jerusalem, 1961, Chapter 1. A detailed discussion of the differences between gross and net capital stock can be found in A. L. Gaathon, "Mutual Relations between Gross and Net Capital", *The Economic Quarterly*, Vol. 13, No. 49–50, June 1966, pp. 89 ff.

tion because of wear and tear and obsolescence,<sup>1</sup> came to about 25 percent of total fixed nondwelling investment. This relatively high rate was due to the fact that plant, equipment, and vehicles acquired at an accelerated rate in the mid-1950's are reaching the end of their economic life-span. There is a wide sectorial disparity in the weight of discards, depending mainly on the ratio of equipment to buildings and the age of the stock. In industry, discards are estimated at over half of gross investment in 1966.

Changes in the composition of the capital stock followed the pattern of recent years, with the services and transportation and communications displaying a long-run rising trend; in 1966 over 60 percent of the increment went to these sectors. Most of the new investment was in assets required to satisfy domestic demand or to expand the economy's infrastructure in such spheres as telecommunications, rail transport, water projects, and equipment for business, personal, and other services.

Only 11 percent of the incremental gross capital stock in 1966 went to industry, although it accounted for 21 percent of total gross investment, a fact reflecting the high value of discards in this sector. In 1962-65 industry also contributed only some 15 percent to the total increase in the capital stock.

The positive effect of the contraction of investment in 1966 was felt chiefly in the balance of payments. The financing of investment in Israel depends on the inflow of capital, owing to the low level of national saving. The decline in the capital inflow in 1966 was accompanied by a 19 percent drop in imports of machinery, equipment, and transport vehicles, compared with an increase of 5 percent in 1965 and 11 percent in 1964.

## 2. INVESTMENT, BY TYPE OF INVESTOR<sup>2</sup>

The public sector and public sector companies were responsible for about 45 percent of total fixed nondwelling investment during the last five years. The direct investments of the Government, local authorities, and National Institutions are usually of an infrastructural nature, such as roads, Government offices, afforestation, sewerage, etc. The investments of Government enterprises are of a similar nature, though their activities may be conducted along business lines and their investments may be evaluated in terms of anticipated profits. The capital outlays of public sector companies are mostly in mining and quarrying, electric power, water projects, shipping, and civil aviation; they display sharp annual fluctuations, largely owing to the irregularity of investment in ships and aircraft and in the implementation of special projects such as the National Water Carrier. In general, it may be said that Government and public sector company

<sup>1</sup> Discards are measured according to the estimated economic life of the assets; the figure for any year represents the order of magnitude only.

<sup>2</sup> The reference is to the sectors purchasing the capital assets, i.e. the final owners. See also the notes to Table V-2.

Table V-2

## GROSS FIXED INVESTMENT, BY TYPE OF INVESTOR AND INITIATING SECTOR, 1962-66

(IL million, at 1965 prices)

	1962	1963	1964	1965	1966	Percent increase or decrease (-) as against preceding year			
						1963	1964	1965	1966
<b>Nondwelling investment, by investing sector</b>									
Government, local authorities, and National Institutions	226	255	298	351	299	13	17	18	-15
Government enterprises <sup>a</sup>	103	115	188	211	183	12	63	12	-13
Public sector companies <sup>b</sup>	399	336	424	289	235	-16	26	-32	-19
<b>Total public sector investment</b>	<b>728</b>	<b>706</b>	<b>910</b>	<b>851</b>	<b>717</b>	<b>-3</b>	<b>29</b>	<b>-6</b>	<b>-16</b>
Nonprofit institutions	83	115	133	130	122	39	16	-2	-6
Private business enterprises <sup>c</sup>	674	809	967	1,015	767	20	20	5	-25
<b>Total private sector investment</b>	<b>757</b>	<b>924</b>	<b>1,100</b>	<b>1,145</b>	<b>889</b>	<b>22</b>	<b>19</b>	<b>4</b>	<b>-22</b>
<b>Total nondwelling investment</b>	<b>1,485</b>	<b>1,630</b>	<b>2,010</b>	<b>1,996</b>	<b>1,606</b>	<b>10</b>	<b>23</b>	<b>-1</b>	<b>-20</b>
<b>Investment in dwellings, by initiating sector</b>									
Public	390	310	338	353	261	-21	9	4	-26
Private	437	509	571	621	515	16	12	9	-17

<sup>a</sup> The trading enterprises of the public sector, including the Post Office, Israel Railways, air and sea ports, and local authority enterprises.

<sup>b</sup> Companies in whose management the public sector has the decisive voice.

<sup>c</sup> Calculated as a residual.

SOURCE: 1962-65—Central Bureau of Statistics, after adjusting for differences in definitions; 1966—Bank of Israel estimates.

Table V-3

**GROSS FIXED NONDWELLING INVESTMENT, BY ECONOMIC SECTOR AND  
TYPE OF INVESTOR, 1962-66**  
(percentages)

Sector Type of investor	Total	Agri- culture and irriga- tion	Industry and con- struction	Mining and quarrying, electricity	Trans- port and com.	Com- merce and serv- ices
Government, local authorities, and National Institutions	100	13	—	—	24	63
Government enterprises	100	1	2	2	87	8
Public sector companies	100	29	8	43	16	4
Total public sector	100	18	4	20	33	25
Nonprofit institutions	100	—	—	—	—	100
Private business	100	13	43	—	24	20
Total private sector	100	12	37	—	21	30
Grand total	100	15	22	9	26	28

SOURCE: Based on Central Bureau of Statistics data.

investments are motivated primarily by macroeconomic considerations and Government policy, while profitability plays only a subsidiary role. Consequently, the annual changes in such investments may be regarded more as influencing the level of economic activity rather than as being influenced by it.

Private enterprises<sup>1</sup> are undoubtedly more sensitive to boom and slump conditions, and their investments are determined by expectations of future profits. These expectations are based partly on current profitability trends and the rate of economic activity as reflected chiefly by the national product in the current year or in the recent past. After increasing rapidly in 1963 and 1964, private sector investment grew only slightly in 1965 and declined by nearly 25 percent in 1966.<sup>2</sup> These developments were more or less in line with the GNP growth pattern: a rapid rise in 1962-64, deceleration in 1965, and a standstill in 1966. The profitability of industry, where over 40 percent of all private investments have been made, did not rise in recent years, and apparently even fell in 1966 owing to the substantial increase in production costs (especially wages), which exceeded output and production growth in this sector. There was a particularly steep decline in the overall profitability of the economy in 1966,<sup>3</sup> and this tended to deter new investments already in that year.

<sup>1</sup> Including enterprises of the Histadrut sector.

<sup>2</sup> The estimate for this sector, calculated as a residual, is not very reliable, especially when the percentage change is small.

<sup>3</sup> See note <sup>1</sup>, p. 101.

The decline of nearly IL 250 million (at 1965 prices) in private sector investment other than housing was almost double that of IL 130 million in Government and public sector company investment. In order to determine the share of each sector's total investment, residential construction must also be taken into account. The value of new residential construction sponsored by the Ministry of Housing, Jewish Agency, and local authorities fell off 26 percent in 1966, so that total public sector investment contracted by 19 percent. Total private sector investment declined at a similar rate, by 20 percent. Since the private sector accounts for a larger proportion of total investment, its contribution to the overall decline was greater—IL 360 million as against IL 225 million for the public sector.

### 3. INVESTMENT, BY ECONOMIC SECTOR

In 1966 real gross investment in fixed assets other than housing declined by about 20 percent, and net investment by 40 percent. Net investment, which measures the changes in the production potential of the economy's capital assets until the end of their economic life, came to only about half the gross investment. The estimate of depreciation does not depend on gross investment in the current year; it actually increased faster than the capital stock, owing to the growing weight of items with a relatively high depreciation rate, such as motor vehicles, aircraft, and industrial equipment. In 1966 the sector showing the steepest decline in net investment was industry—down nearly 80 percent. The share of industry in gross and net investment also fell in the year reviewed (see Table V-6), while the weight of commerce and services rose. This striking structural change has continued since 1960. The annual changes in the weight of transportation and communications chiefly reflect the irregularity of investment in ships and aircraft, which reached a peak in 1964 when the figure came to IL 175 million (including the liner *Shalom*).

#### (a) *Agriculture and irrigation*

The downward trend in farm investment, which began in 1958, continued in 1966, when net investment was almost zero. The decline affected most items (see Table V-7). It was especially marked in orchards, where it exceeded 20 percent, and was connected with the restrictions imposed on planting because the supply of fruit in coming years is expected to exceed the demand at the prevailing prices. Capital outlay on irrigation installations has also been declining for several years, since there is not enough water for extending the irrigated area. In 1966 expenditure on farm structures rose slightly, while the increase in livestock was double that of 1965. Both developments were apparently connected with the expansion of dairy farming.

Expenditure on agricultural machinery and tractors has held steady for the last three years, so that the weight of this item in total farm investment has

Table  
GROSS FIXED NONDWELLING INVESTMENT, BY  
(IL)

	1960	1961	1962	1963	1964	
					Buildings	Equip-ment
						<b>A. At current</b>
Agriculture	122	124	137	131	34	46
Irrigation	57	70	111	124	73	10
Industry and construction	183	234	299	364	126	287
Mining and quarrying	14	28	65	76	47	35
Electricity	37	41	77	64	32	31
Transportation and com.	155	234	282	331	166	463
Ships and aircraft	66	102	66	50		175
Mobile transport equipment	41	67	102	140		181
Other items	48	65	114	141	166	107
Business premises, hotels and other guest accommodation	207	261	320	409	69	168
Public buildings					274	
<b>Total</b>	<b>775</b>	<b>992</b>	<b>1,291</b>	<b>1,499</b>	<b>821</b>	<b>1,040</b>
						<b>B. At 1965</b>
Agriculture	190	178	168	149	36	47
Irrigation	82	94	129	136	76	10
Industry and construction	302	348	341	388	132	296
Mining and quarrying	23	41	75	84	50	36
Electricity	60	59	88	69	34	32
Transportation and com.	237	348	308	352	175	474
Ships and aircraft	108	167	66	50		175
Mobile transport equipment	54	85	106	148		188
Other items	75	96	136	154	175	111
Business premises, hotels and other guest accommodation	319	366	376	452	73	172
Public buildings					287	
<b>Total</b>	<b>1,213</b>	<b>1,434</b>	<b>1,485</b>	<b>1,630</b>	<b>863</b>	<b>1,067</b>

SOURCE: Central Bureau of Statistics.

## ECONOMIC SECTOR AND TYPE OF ASSET, 1960-64

million)

		1965				1966			
Farm output	Total	Build-ings	Equip-ment	Farm output	Total	Build-ings	Equip-ment	Farm output	Total
<b>prices</b>									
72	152	27	46	71	144	26	47	68	141
	83	59	16		75	61	15		76
	413	122	314		436	68	234		302
	82	32	18		50	19	18		37
	63	37	75		112	37	52		89
	629	206	378		584	164	288		452
	175		92		92		47		47
	181		184		184		137		137
	273	206	102		308	164	104		268
	511	82 330	183		595	57 293	184		534
72	1,933	895	1,030	71	1,996	725	838	68	1,631
<b>prices</b>									
80	163	27	46	71	144	26	46	62	134
	86	59	16		75	61	14		75
	428	122	314		436	68	229		297
	86	32	18		50	19	17		36
	66	37	75		112	37	51		88
	649	206	378		584	162	284		446
	175		92		92		48		48
	188		184		184		135		135
	286	206	102		308	162	101		263
	532	82 330	183		595	57 293	180		530
80	2,010	895	1,030	71	1,996	723	821	62	1,606

Table V-5

CHANGES IN GROSS FIXED NONDWELLING INVESTMENT, BY ECONOMIC SECTOR AND TYPE OF ASSET, 1961-66  
(percent increase or decrease [-] as against preceding year)

	Agriculture <sup>a</sup>	Irrigation	Industry and construction	Mining and quarrying	Electricity	Transportation and communications	Commerce and services	Total	Total excl. ships and aircraft
<b>Total investment</b>									
1961	-4	15	15	78	-2	47	15	18	15
1962	-6	37	-2	83	49	-11	3	4	12
1963	-11	5	14	12	-22	14	20	11	13
1964	9	-37	10	2	-4	84	18	22	15
1965	-12	-13	2	-42	70	-10	12	-1	4
1966	-7	—	-32	-28	-21	-24	-11	-20	-18
<b>Construction</b>									
1961	-17	15	23	23	-4	36	12	8	8
1962	-3	37	-1	125	19	18	3	11	11
1963	-2	2	5	44	-3	38	23	18	18
1964	-1	-37	32	-4	13	58	16	10	10
1965	-15	-22	-8	-36	-94	18	14	3	3
1966	-12	3	-44	-41	56	-23	-15	-19	-19
<b>Machinery, equipment, and transport equipment</b>									
1961	26	14	13	150	—	50	21	28	22
1962	-12	37	-2	56	73	-19	2	-3	13
1963	-33	45	17	-18	-32	6	15	5	8
1964	43	-37	3	13	-18	97	22	35	21
1965	-4	6	6	-50	132	-20	6	-4	5
1966	4	-14	-27	-6	-32	-25	-2	-20	-17

<sup>a</sup> Including assets from farm output.

SOURCE: Table V-4.

**Table V-6**  
**GROSS AND NET FIXED NONDWELLING INVESTMENT,**  
**BY ECONOMIC SECTOR, 1960-66**  
 (percentages)

	Agriculture	Irrigation	Industry, mining and quarrying	Electricity	Transportation and communications	Commerce and services	Total
<b>Gross investment</b>							
1960-63	12	8	28	4	22	26	100
1964	8	4	26	3	32	27	100
1965	7	4	24	6	29	30	100
1966	8	5	21	5	28	33	100
<b>Net investment</b>							
1960-63	9	9	23	3	22	34	100
1964	4	4	20	1	38	33	100
1965	2	3	18	5	32	40	100
1966	1	5	6	5	30	53	100
<b>Share of depreciation in gross investment</b>							
1960-63	53	24	47	57	33	15	35
1964	67	40	49	73	23	17	34
1965	81	49	56	45	32	19	39
1966	92	52	86	62	49	25	53

risen. This change is connected with the substitution of equipment for labor, a trend which has been going on in agriculture for a considerable time. However, despite the easier terms of institutional financing granted in 1966 for agricultural mechanization and a rise of nearly 18 percent in agricultural wages, there was no increase in this type of investment. A possible explanation may be the failure of farm production to expand during the last two years, and the drought which hit unirrigated crop cultivation in 1966 (such crops normally require considerable equipment).<sup>1</sup>

Investment in national and regional water development projects remained at the 1965 level, the completion of the National Water Carrier being offset by work on various regional projects.

(b) *Industry and construction*

Gross investment in this sector, which includes mining and quarrying, manufacturing, and construction equipment, was down 32 percent in 1966.

<sup>1</sup> See Chapter XI, "Agriculture", section 5.

The figure for mining and quarrying fell off sharply in 1965 and 1966, after holding steady for three years at approximately IL 80 million (at 1965 prices). Most of the decline occurred at the Dead Sea Works, which completed the first stage of its expansion program and which is now preparing for the second stage.

Industrial investment decreased by nearly 24 percent in 1966,<sup>1</sup> after levelling off in 1964 and 1965. Outlay on equipment was stable in 1963-65, while that on buildings rose substantially in 1964, owing partly to the expanded construction of centers for light industry and crafts. These consisted of rental premises, and were erected mainly by local authorities with the encouragement of the Ministry of Commerce and Industry. Since the demand for such premises fell considerably short of construction, a stock of empty buildings accumulated. Private investment in industry, which was fairly stable in 1963-65, fell off in 1966. This was apparently due to the decline in profitability.<sup>2</sup> The pessimistic expectations generated thereby and the general contraction of demand discouraged potential investors.

Despite the contraction of total industrial investment, its branch composition did not change much. Nearly 20 percent (about IL 45 million) was invested in the food and tobacco industries and a similar percentage in the textile, clothing,

**Table V-7**  
**GROSS INVESTMENT IN AGRICULTURE, 1958-66**  
(IL million, at 1965 prices)

	Orchards	Land reclamation, afforestation, drainage, etc.	Farm buildings and local irrigation networks	Machinery and equipment	Livestock	Total
1958	54	44	67	31	27	223
1959	51	49	63	40	18	221
1960	45	43	55	40	7	190
1961	44	32	43	47	12	178
1962	45	34	37	41	11	168
1963	43	32	39	35	—	149
1964	42	36	36	47	2	163
1965	38	31	27	46	2	144
1966	30	28	26	46	4	134

SOURCE: Central Bureau of Statistics.

<sup>1</sup> This figure is no more than a rough estimation, as there are no reliable data on purchases of construction machinery and equipment, which are lumped together with industrial equipment. Moreover, it should be noted that investment in industrial equipment is calculated as a residual, by subtracting the investment estimates for the other sectors from the aggregate figure. Hence all errors accumulate in the estimate for this sector.

<sup>2</sup> See also Chapter XII, "Industry", section 4.

and leather industry. However, the share of the printing and paper industry rose, while that of chemicals and petroleum refining declined following the establishment or expansion of several plants.

(c) *Transportation and communications*

The public sector determines the size of most investments in this sector, except for that in motor vehicles. After a steady rise in 1960–65 in outlay on the railway, ports, roads, and communications (mainly by the Post Office), in 1966 there was a decline in the figure for ports with the completion of work at Ashdod, and in that for roads, mainly because of the paring of local authority development budgets; investment in the railway and communications, on the other hand, tapered off. All told, there was a decrease of nearly 15 percent in this sector, excluding mobile transport equipment, ships, and aircraft (see Table V-8).

**Table V-8**  
**GROSS INVESTMENT IN TRANSPORTATION AND COMMUNICATIONS, 1960-66**  
(IL million, at 1965 prices)

	1960	1961	1962	1963	1964	1965	1966
Railway	3	6	4	4	12	17	18
Ports	11	13	25	31	66	60	40
Roads <sup>a</sup>	27	40	42	58	77	95	81
Communications <sup>b</sup>	27	25	51	51	115	119	112
Other <sup>c</sup>	7	12	14	10	16	17	12
<b>Total excl. transport equipment</b>	<b>75</b>	<b>96</b>	<b>136</b>	<b>154</b>	<b>286</b>	<b>308</b>	<b>263</b>
Motor vehicles	54	85	106	148	188	184	135
Passenger cars and commercial vehicles	43	72	91	129	165	160	112
Buses	11	13	15	19	23	24	23
Ships	108	131	16	50	173	94	28
Aircraft	—	36	50	—	2	-2	20
<b>Total, incl. transport equipment</b>	<b>237</b>	<b>348</b>	<b>308</b>	<b>352</b>	<b>649</b>	<b>584</b>	<b>446</b>

<sup>a</sup> Includes local authority investment in traffic equipment, sidewalks, etc.

<sup>b</sup> Mostly Post Office outlay on construction and equipment.

<sup>c</sup> Airports, oil and gas pipelines, storage, etc.

SOURCE: Central Bureau of Statistics.

A steeper drop—about 30 percent—occurred in purchases of passenger cars for business purposes, trucks, and other commercial vehicles. These vehicles are acquired mainly by the private business sector, and in 1966 purchases were greatly affected by the general decline in demand, and especially by the curtailment of construction activity.

(d) *Public services*

Most investments here are in educational and health institutions (see Table V-9). The 1966 decline in these services was particularly marked compared with the considerable increase during 1963-65. Investment in educational services contracted by about 9 percent, and that in health services by 19 percent. These investments are implemented by the Government, local authorities, and nonprofit institutions. The Government's policy of moderating economic activity was particularly effective in these services; another limiting factor was the smaller volume of institutional transfers from abroad. The sharp fall in expenditure on cultural services in 1966 reflects the completion of the Israel Museum. In social welfare and religious services and trade union and political organizations, the level of investments did not change much in 1966, but their weight in total public services is rather small (about 7 percent).

**Table V-9**  
**GROSS INVESTMENT IN COMMERCE AND SERVICES, 1962-66**  
(IL million, at 1965 prices)

	1962	1963	1964	1965	1966
<b>Public services</b>					
Education, research, and science	100	137	151	182	166
Culture <sup>a</sup>	15	16	22	23	13
Health	29	36	47	52	42
Social welfare	7	13	5	4	3
Religion	5	9	9	12	11
Labor and other organizations, political parties	5	9	14	13	13
Other public services <sup>b</sup>	85	83	93	98	94
<b>Commerce and personal services</b>					
Business enterprises, hotels and other guest accommodation	130	149	191	211	188
<b>Total</b>	<b>376</b>	<b>452</b>	<b>532</b>	<b>595</b>	<b>530</b>

<sup>a</sup> Including libraries, museums, cultural centers, etc.

<sup>b</sup> Including administrative services of the public sector, entertainment and sports, and miscellaneous. This item was calculated as a residual, and is of doubtful reliability.

SOURCE: 1962-65—Central Bureau of Statistics; 1966—Bank of Israel estimates based on Central Bureau of Statistics data.

(e) *Commerce and personal services*

After growing rapidly for several years and especially so in 1964, investment in businesses and in hotels and other guest accommodation declined by about 11 percent in 1966; this was entirely due to the 30 percent decrease in construction expenditure, outlay on furniture and equipment rising somewhat. The

economic slowdown affected each type of investment differently, for several reasons: there may be a lagged effect in respect of purchases of equipment from abroad, such as computers; moreover, it is more risky to establish an entire new enterprise than to buy equipment, especially for replacing items that have become obsolete or worn out. Equipment is usually purchased for new buildings as they are finished, and building completions declined less than total investment in 1966.

#### 4. INVESTMENT, BY TYPE OF ASSET

The real decrease of 20 percent in the value of new nonresidential construction in 1966 was steeper than that in investment in machinery and equipment (other than vehicles, ships, and aircraft), which declined by 15 percent. The weight of nontransport equipment in total investment thus rose somewhat. This does not necessarily mean that there was a shift to investment with a high equipment component. Equipment is often purchased only when a project is nearing completion, so that a time-lag is to be expected before equipment is affected by a recession. Moreover, there may be a considerable interval be-

**Table V-10**  
**GROSS FIXED INVESTMENT, BY TYPE OF ASSET, 1962-66**  
 (IL million, at 1965 prices)

	1962	1963	1964	1965	1966	Percent increase or decrease (-) as against preceding year			
						1963	1964	1965	1966
Dwellings	827	819	909	974	776	-1	11	7	-20
Nonresidential buildings	346	411	489	534	427	19	19	9	-20
Other construction work	304	352	374	361	296	16	6	-3	-18
<b>Total value of new construction</b>	<b>1,477</b>	<b>1,582</b>	<b>1,772</b>	<b>1,869</b>	<b>1,499</b>	<b>7</b>	<b>12</b>	<b>5</b>	<b>-20</b>
Assets from farm output	90	75	80	71	62	-17	7	-11	-13
Machinery and equipment									
Locally manufactured	172	187	236	252	244	9	26	7	-3
Imported	401	407	468	502	394	2	15	7	-21
<b>Total</b>	<b>573</b>	<b>594</b>	<b>704</b>	<b>754</b>	<b>638</b>	<b>4</b>	<b>18</b>	<b>7</b>	<b>-15</b>
Motor vehicles	106	148	188	184	135	40	27	-2	-27
Ships and aircraft	66	50	175	92	48	-24	250	-47	-48
<b>Total fixed investment</b>	<b>2,312</b>	<b>2,499</b>	<b>2,919</b>	<b>2,970</b>	<b>2,382</b>	<b>6</b>	<b>19</b>	<b>2</b>	<b>-20</b>

SOURCE: Central Bureau of Statistics.

tween the order and delivery of equipment, particularly as two-thirds of the equipment is imported. Purchases of motor vehicles, on the other hand, react very quickly to the market and to investors' expectations, so that the steep decline in these purchases is understandable.

The 1966 decline in machinery and equipment was entirely in imported items, investment in locally manufactured equipment remaining at the 1965 level. Consequently, the weight of domestic equipment continued to rise, continuing a trend that began in 1962, when the proportion of equipment produced or assembled in this country was about 30 percent. The trend is explained by the fact that the 1962 devaluation raised the relative price of imported equipment. By 1966 the local industry supplied 38 percent of total demand for equipment (see Table V-11). The big change in 1966 is partly explained by the sharp drop in purchases of construction equipment, which has a relatively high import component. On the other hand, there was a relatively big outlay on machinery and equipment for agriculture, commerce, and the services, which have a high domestic component.

**Table V-11**

**SHARE OF LOCALLY MANUFACTURED EQUIPMENT IN TOTAL EQUIPMENT EXPENDITURE,<sup>a</sup> 1962-66**

(percentages)

	Agri- culture	Industry and electricity	Construc- tion	Transporta- tion and communica- tions	Commerce and services	Total
1962	57.2	22.7	13.6	27.1	51.4	30.1
1963	65.0	23.2	15.0	39.3	47.0	31.5
1964	58.8	25.8	17.4	33.9	47.3	33.5
1965	63.8	25.3	18.1	37.0	47.4	33.5
1966	62.9	27.2	29.9	51.0	43.5	38.2

<sup>a</sup> Calculated at current prices; however, presentation of the data at constant prices would not alter the picture, since the prices of local equipment went up to the same extent as those of imported equipment during the period 1962-66.

SOURCE: Central Bureau of Statistics.

In 1966 equipment prices rose by about 2 percent. On the other hand, nominal hourly wages in industry rose by nearly 16 percent. As a result, the relative price of industrial equipment fell more steeply than in any year since 1963—by about 12 percent (see Table V-12). The relative price of other types of equipment apparently declined at a similar rate, and this may have prevented investment in machinery and equipment contracting more than it did, for capital assets continued to replace labor in some sectors.

Table V-12

**INDEX OF THE PRICE OF INDUSTRIAL EQUIPMENT  
RELATIVE TO THE PRICE OF LABOR, 1962-66**

	Index of nominal hourly wages in industry	Index of industrial equipment prices	Index of the relative price of equipment
1962	100	100	100
1963	112	106	95
1964	124	108	87
1965	137	111	81
1966	159	113	71

### 5. INVESTMENT PRICES

Investment prices rose by only 1 percent in 1966, compared with approximately 4 percent in both 1964 and 1965.

In contrast to previous years, prices of buildings did not rise at all,<sup>1</sup> owing to the sharp decline in demand. On the other hand, prices of earthwork apparently continued upward, reflecting the appreciable increase in wages, the main cost component of this item.

As in previous years, prices of local and imported machinery and equipment rose by 2 to 3 percent; motor vehicle prices went up to a similar extent.

### 6. CAPITAL STOCK

The principal change in the composition of gross capital stock from 1960 to 1966 was the decline of nearly 30 percent in the share of agriculture and the rise, by about the same percentage, in the weight of commerce and the services (private and public). The share of transportation and communications also went up by about 20 percent (See Table V-13). The share of industry has remained remarkably constant over this seven-year period; if anything, it has declined slightly and stands at around 25 percent of the total nondwelling capital stock.

Dwelling and nondwelling gross capital stock grew at the same rate in 1966. The addition to the stock of dwellings was almost equal to gross investment, since discards amounted to only 3 percent of investment. However, discards come to about one-quarter of gross investment in other types of assets, as the machinery, equipment, and vehicles acquired at an accelerated rate in the mid-1950's are becoming worn out or obsolescent. In industry, discards are

<sup>1</sup> This is little more than a guess, since there is no suitable index of construction costs which includes both actual wages and contractors' profits. See Chapter XIII, "Construction and Housing", section 3.

<sup>2</sup> See note <sup>1</sup>, p. 102.

**Table V-13**  
**GROSS CAPITAL STOCK, BY SECTOR, 1966**  
 (IL million, at 1965 prices)

	Capital stock at end of 1965	Gross investment in 1966	Discards in 1966	Incremental capital stock in 1966	Capital stock at end of 1966	Weight in total capital stock (%)		Change in weight from 1959 to 1966 (%)	Weight in incremental capital stock in 1966 (%)
						End-1959	End-1966		
Agriculture	3,043	134	43	91	3,134	22	16	-6	8
Irrigation	1,469	75	5	70	1,539	9	8	-1	6
Industry <sup>a</sup> and construction	4,560	333	195	138	4,698	26	24	-2	11
Electric power	1,105	88	1	87	1,192	7	6	-1	7
Transportation and com.	3,879	446	104	342	4,221	18	22	+4	28
Commerce and services	4,141	530	46	484	4,625	18	24	+6	40
<b>Total nondwelling capital stock</b>	<b>18,197</b>	<b>1,606</b>	<b>394</b>	<b>1,212</b>	<b>19,409</b>	<b>100</b>	<b>100</b>	<b>—</b>	<b>100</b>
Dwellings	10,926	776	19	757	11,683				
<b>Total stock of fixed assets</b>	<b>29,123</b>	<b>2,382</b>	<b>413</b>	<b>1,969</b>	<b>31,092</b>				

<sup>a</sup> Including mining and quarrying.

SOURCE: Based on estimates of A. L. Gaathon. For definitions and explanations see: A. L. Gaathon, *Capital Stock, Employment and Output in Israel, 1950-1959*, Bank of Israel, Jerusalem, 1961, p. 2.

Table V-14

**GROWTH OF REAL CAPITAL STOCK, BY SECTOR, 1960-66**  
(percentages)

	Agri- culture	Agri- culture and irri- gation	Industry, water, elec- tricity	Trans- portation and communi- cations	Com- merce and servi- ces	Total non- dwelling capital stock <sup>a</sup>	Dwell- ings	Total fixed assets
1960	8	8	10	11	17	11	8	10
1961	7	8	11	17	17	12	9	11
1962	7	8	14	12	15	12	11	12
1963	5	7	11	12	16	11	10	10
1964	5	5	9	21	16	12	10	11
1965	4	5	7	15	15	10	9	10
1966	3	4	4	9	12	7	7	7

SOURCE: See source to Table V-13.

estimated at over 50 percent of investment, in agriculture at one-third, and in transportation and communications at one-quarter. In electricity and irrigation, most investments were made after 1958, so that discards are minimal.

The growth of the industrial capital stock has slowed down considerably since 1962; this reflects the high weight of equipment, whose economic life is much shorter than that of buildings. The smaller the annual investment, the greater the ratio of discards. The deceleration in agriculture represents a long-run trend, reflecting reduced investment in orchards, farm buildings, irrigation, and—since 1964—also in national water projects.

Table V-15

**GROWTH OF REAL CAPITAL STOCK PER GAINFULLY EMPLOYED,<sup>a</sup> BY SECTOR, 1961-66**  
(percentages)

	Agriculture and irrigation	Industry, water, electricity	Transporta- tion and communica- tions	Commerce and services	Total non- dwelling capital stock	Dwelling capital stock per capita
1961	7	3	8	12	6	3
1962	9	2	12	11	6	7
1963	11	6	6	8	7	6
1964	6	6	4	10	6	6
1965	6	7	17	11	8	5
1966	9	12	17	10	10	8

<sup>a</sup> Data on capital stock relate to the beginning of the year, while the number of gainfully employed is an annual average.

Capital stock per gainfully employed expanded in 1966 at a similar rate as in previous years, and at the same rate as aggregate capital stock, since employment did not rise. The growth of the capital stock was not accompanied by any increase in the real national product; the rise in the capital/product ratio apparently indicates a lower utilization rate of the stock of capital assets.<sup>1</sup> This tendency was very striking in construction, where there was considerable idle equipment—especially heavy equipment used for big projects such as the National Water Carrier, Ashdod Port, and the Dead Sea Works. There was a large outlay on construction equipment even in 1965, when the deceleration of building activity was in full swing—apparently because of the time-lag between the submission and delivery of orders. Owing to the smaller demand for building materials, firms producing them worked below capacity, and several suspended production altogether. There was also underutilization of plant and equipment in other sectors—for instance, in the trucking industry and the elimination of extra shifts.

## 7. INVESTMENT IN INVENTORIES

In 1966 inventories expanded by 30 percent;<sup>2</sup> most of the increase was in Government inventories and in involuntary stockpiling of manufactured goods due to the lag in adjusting production to the smaller domestic demand. On the other hand, it is reasonable to assume that enterprises which reduced output in response to declining demand for their products also ran down their stocks of raw materials.

Government stocks, which had contracted in 1965, were expanded in order to take advantage of the favorable world prices prevailing in 1966. The Government also aimed to concentrate imports as far as possible in the last months of 1966, so as to free the ports for the citrus export season at the beginning of 1967.

Industrial inventories grew by about 7 percent in 1966,<sup>3</sup> compared with 10 percent in 1965. The biggest increase was in minerals, owing to the irregularity of potash exports. Inventories also expanded in the textile and clothing industries.

<sup>1</sup> Since the capital stock increased chiefly in commerce and services, where the capital/product ratio is low, and in transportation and communications, where the ratio is high, the two trends more or less offset each other.

<sup>2</sup> Investment in inventories is estimated as the physical change in stocks between the beginning and the end of the year, valued at the average prices prevailing during the year. The estimate is thus not consistent with the inventory changes reported by the concerns. The difference between the two depends on changes in prices during the year and the value of the total stock of each product.

<sup>3</sup> This estimate is very unreliable. It is based on a preliminary sample of enterprises, and past experience has shown that there is a strong response bias in the reports submitted by firms just after the end of the year.

## 8. PUBLIC FINANCING OF INVESTMENT

The weight of public financing<sup>1</sup> within total investment went up in 1966, after having remained more or less at the same level during 1961–65. The 1966 rise, at a time when total investment fell steeply, reflects the stability in the volume of loans granted (mainly by the Government) for investment purposes. However, this rise does not necessarily reflect an increase in public sector influence on investment, owing to the arbitrary conceptual distinction between public and private financing. In recent years a considerable part of the investment finance was provided by financial institutions, which mobilized funds from various Government-controlled sources, such as the sale of bond issues to social insurance funds and foreign loans. The Government exerts considerable influence on these institutions, and not necessarily through the funds placed at their disposal. The Government thus effectively controls the allocation of most of the loans granted—for instance, those by the Industrial Development Bank—and the fact that only 11 percent of industrial investment is directly financed by the Government is of little significance.

Table V-16

### SHARE OF GROSS INVESTMENT FINANCED BY THE PUBLIC SECTOR, 1960-66 (percentages)

	1960	1961	1962	1963	1964	1965	1966
Agriculture and irrigation	84	81	75	86	93	92	86
Industry	39	36	24	27	11	7	11
Mining and quarrying	50	10	11	21	13	24	57
Electricity	5	8	26	23	30	38	21
Transportation and com.	77	56	48	44	38	53	72
Commerce and services	57	42	44	45	46	43	48
Housing	38	29	36	30	36	33	37
Total	54	43	41	40	38	39	47

## 9. GROSS INVESTMENT, BY DISTRICT

The considerable (direct and indirect) share of the public sector in investment gives it—at least theoretically—the possibility of implementing the population dispersal policy. The regional distribution of investment during the last four years (see Table V-17) may serve as a measure of the effectiveness of this

<sup>1</sup> I.e. direct investments of the public sector (e.g. in roads and ports), as well as loans granted for investment purposes—either directly or through banks and financial institutions. It should be noted that the provision of financing and the actual implementation of investments often do not coincide.

**Table V-17**  
**GROSS FIXED INVESTMENT, BY DISTRICT,<sup>a</sup> 1963-66**  
 (percentages)

District	Total fixed investment <sup>a</sup>				Of which: Dwellings			
	1963	1964	1965	1966 <sup>b</sup>	1963	1964	1965	1966 <sup>b</sup>
Jerusalem	7	7	8	8	8	7	8	9
Northern	16	15	14	17	10	12	11	14
Southern	18	19	17	16	12	13	13	11
<b>Total development areas</b>	<b>41</b>	<b>41</b>	<b>39</b>	<b>41</b>	<b>30</b>	<b>32</b>	<b>32</b>	<b>34</b>
Haifa	15	15	17	17	14	15	13	12
Central	18	19	18	17	19	20	20	21
Tel Aviv	26	25	26	25	37	33	35	33
<b>Total central area</b>	<b>59</b>	<b>59</b>	<b>61</b>	<b>59</b>	<b>70</b>	<b>68</b>	<b>68</b>	<b>66</b>
<b>Grand total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

<sup>a</sup> Excluding motor vehicles, ships, and aircraft.

<sup>b</sup> Provisional estimate.

SOURCE: Economic Planning Authority, Central Bureau of Statistics, Ministry of Agriculture, and Bank of Israel.

policy. The distribution of investments more or less corresponded to that of the population increment. The Jerusalem, Northern, and Southern Districts, which are regarded as development areas, accounted for about 40 percent of total fixed investment in 1963-66,<sup>1</sup> while 45 percent of the country's additional population during 1962-66 was in these three districts. The central area, which includes the Tel Aviv, Central, and Haifa Districts, accounted for over 60 percent of total investment, and the Tel Aviv District alone for about one-quarter.

There is a wide disparity between the distribution of investment in housing—30 percent in the development areas and 70 percent in the central area—and the distribution of other investments, which were more or less equally divided between the two. About one-third of the total housing investment was concentrated in the Tel Aviv District.

A striking fact revealed by Table V-17 is the stability in the distribution of total investment between development areas and the central part of the country

<sup>1</sup> Excluding motor vehicles (chiefly because of statistical difficulties), ships, and aircraft.

during the last four years. The weight of development areas in housing investment has risen slightly, while its weight in other types of investment has fallen off.

The fairly large weight of the Southern District in investment, and its decline between 1964 and 1966, reflect the concentration of mines and quarries in this part of the country. Most of the industrial investment is concentrated in the Tel Aviv and Haifa Districts, while the Northern District accounts for about two-thirds of the investment in agriculture and irrigation.