CHAPTER VII

GOVERNMENT AND NON-GOVERNMENT PUBLIC SECTOR

1. CONSOLIDATED ACCOUNT[1]

Public sector operations in 1971 were influenced by the continued but somewhat less vigorous application of the far-reaching restrictive fiscal measures adopted in the previous year, when tax rates were upped, compulsory loans imposed, and the growth of budgetary expenditure of the various public sector authorities was curbed (except for security, housing, and debt repayment).

The public sector's payments grew more slowly in the year reviewed – 24.8 vs. 30.9 percent in 1970 (see Table VII-2); but this was due chiefly to the cutback in defense imports. Total domestic expenditure soared 34.5 percent, as against 5.1 percent in 1970, with the biggest increases being in transfer payments, subsidies, and purchases on capital account. Even though domestic revenue was up by a respectable 35.7 percent, after rising 25 percent in the previous year, it still trailed behind domestic expenditure. The sector's domestic demand surplus therefore grew from IL 774 million to IL 940 million during the year, after declining in 1970.

The sector's overall demand surplus (including foreign currency expenditure) rose 5.1 percent to IL 3,873 million, after swelling by 37.9 percent in 1970 to reach IL 3,684 million. These figures are at current prices; at constant prices there was probably no increase whatsoever in the demand surplus.

The demand surplus has been calculated from data on the direct budgetary operations of the various authorities of the sector. It should be remembered, however, that the Government's influence on economic activity is not reflected solely in its fiscal policy measures but also in its control over public sector companies, financial institutions, the

1. This sector comprises the Government (including the National Insurance Institute), local authorities (including religious councils and the municipal expenditure of cooperative agricultural settlements), and a number of voluntary institutions (the Jewish Agency, World Zionist Organization, Jewish National Fund, and Keren Hayesod) engaged principally in welfare and cultural activities for the general public.

Current income and expenditure of business-type enterprises (e.g. the Post Office, Israel Railways, and municipal waterworks) are not included except for their surpluses or deficits. The data in this chapter are for calendar years, and are based chiefly on financial reports of the various public sector authorities and partly on data from the Central Bureau of Statistics. Some of the data for 1971 are based on provisional summaries, as the financial reports for fiscal 1971/72 had not yet been published when this chapter was prepared. Data for 1970 have been revised.

new issue market for bonds, and the like. If the Government's extrabudgetary operations are also taken into account, it turns out that in the year reviewed the public sector exerted an expansionary influence on aggregate demand in the economy in comparison with the previous year.[2]

Public consumption rose in 1971 by 15.3 percent at current prices, compared with 37.1 percent the year before. At constant prices the level was down 1 percent, owing mainly to the cutback in defense imports: these declined by 11.6 percent, as contrasted with an 8.9 percent growth in other component items.

The smaller defense import reduced the weight of noncivilian consumption in total public sector consumption from 70.5 percent in 1970 to 67.5 percent, and in the gross national product from 25.2 to 22.7 percent. Nevertheless, this figure was still higher than in any year before 1970 (see Table VII-1).

The smaller defense spending in 1971 depressed the share of total public consumption in GNP from the preceding year's 35.8 percent to 33.5 percent, and its share in total domestic uses from 28.6 to 27.3 percent. But here, too, the figures are higher than in any year previous to 1970.

Tax revenue in the year reviewed was up 36.5 percent – the fastest rise in years. Together with compulsory loan collections, the gain was 41 percent (as against 37.1 percent in 1970), bringing the level up to IL 9,531 million. The factor most responsible for this growth was the annual average increase in tax rates, particularly indirect taxes. The hiking of both direct and indirect taxes in 1970 found full expression in 1971. The devaluation of the Israeli pound was responsible for increasing collections of the ad valorem taxes levied on imported goods and on those local goods that became more expensive after the change in the exchange rate. In addition, there were a number of small tax increases in 1971 as well.

Total tax revenue in 1971 amounted to 36.4 percent of GNP, compared with 32.8 percent in 1970 and 26.5 percent in 1967. The addition of compulsory loans brings the figures up to 40.8, 35.6, and 27.9 percent respectively, from which it can be seen that the tax burden has grown in recent years.[3]

Along with the larger amount of funds siphoned off from the public in 1971, there was an increase in the sector's transfer and subsidy payments. Transfers to households and nonprofit institutions climbed 40.2 percent, subsidies and transfers to business by 70.8 percent, and domestic interest payments by 31.8 percent.

Excluding these transfers, net absorption through taxes, compulsory loans, and transfers from the public amounted to IL 5,782 million – up 35.2 percent, compared with a 50.1 percent advance in 1970. Thus it will be seen that the Government continued with its policy of income restraint, though on a smaller scale than in 1970.

The weight of net transfer payments to the public sector in total gross private income from economic activity has moved up steadily in recent years – from 19.1 percent in

2. This is discussed in detail in section 2 below.
3. Some indirect import tax hikes were introduced in lieu of an official devaluation and not for fiscal reasons. Excluding all import levies, tax revenue in 1971 amounted to 31.7 percent of GNP, as against 29.4 percent the year before.

1967 and 25.2 percent in 1970 to 27.6 percent in 1971. This too points to an increase in the tax burden.

As previously noted, the growth of the public sector demand surplus slowed in 1971, when it reached IL 3,873 million as against IL 3,684 million in 1970 and IL 2,671 million in 1969. Excluded from the computation are net compulsory loan receipts and development budget loans granted (chiefly by the Government) for financing investment; these are included under financial transactions. The sector's transactions on financial account show a net credit inflow of IL 80 million, compared with a net credit outflow of IL 91 million in 1970. It is difficult to estimate the combined effect of the sector's credit flow and demand surplus.[4] The impact of the sector's operations on the principal monetary aggregates – the money supply and other liquid assets in the economy – may serve as a partial indicator.

The public sector debt to the banking system rose by IL 1,303 million in 1971,[5] compared with IL 1,128 million in the preceding year. However, it should be noted that this was accompanied by an increased deficit in the sector's foreign currency transactions, which counterbalanced some of the expansionary effect on the money supply of the incremental debt to the banking system. The amount of liquidity pumped into the economy by the public sector (that is, the growth of its debt to the banks, less the increase in its surplus of foreign currency expenditure over revenue) came to IL 893 million in 1971[6] – similar to the figures for 1969 and 1970. But it should not be inferred from the relatively constant liquidity infusion over the last three years and the stabilization of the demand surplus during the past two years that the effect of the public sector's operations on economic activity remained the same during this period. The sizable demand surplus in 1967-69, when the economy pulled out of the slump, was to a certain extent a deliberate reflationary measure. But in 1971 – with a substantial monetary expansion stemming from various balance of payments developments (the growth of exports, a large-scale capital import, and the devaluation of the Israeli pound), along with a smaller increase in the amount of funds mopped up from the public, the mounting of demand pressure, and the fall of the unemployment rate to a very low level – what was called for was a sharply reduced pump-priming on the part of the public sector (i.e. a much smaller demand surplus and liquidity infusion), and not its stabilization or even slight increase.

The public sector's overall demand surplus and net credit outflow to the rest of the economy were financed by credit from the banking system and capital imports. In 1971 the total amount required was IL 3,793 million, similar to that in the previous year.

4. For a discussion of this see section 2 below.
5. The data on financial transactions in this section refer to the flow of credit in the course of the year and do not include changes in the credit or debit balances of the public sector authorities due to the devaluation of the Israeli pound or the rise in the cost-of-living index.
6. This infusion does not include the influence of the Government's extrabudgetary activities. In this context it should be noted that there was a much larger conversion of foreign currency in 1971 by public sector companies and financial institutions, which received Government permits for borrowing abroad in order to finance their local operations.

Table VII–1

INDICATORS OF PUBLIC SECTOR OPERATIONS, 1967-71

(IL million)

	1967	1968	1969	1970	1971	Percent annual increase or decrease (–)				
						Average 1961-66	1968	1969	1970	1971
1. Public sector consumption	3,599	4,152	4,956	6,793	7,829	21.4	15.4	19.4	37.1	15.3
2. Revenue from taxes	3,169	3,932	4,909	6,222	8,490	18.3	24.1	24.9	26.7	36.5
Direct taxes	1,460	1,807	2,237	3,057	3,956	23.2	23.8	23.8	36.7	29.4
Indirect taxes	1,709	2,125	2,672	3,165	4,534	15.1	24.3	25.7	18.5	43.3
3. Total transfer receipts from the public, net[a]	1,898	2,310	2,868	3,805	4,815	18.1	21.7	24.2	32.7	26.5
4. Public sector saving	–1,741	–1,813	–1,985	–2,932	–2,881					
5. Demand surplus	2,175	2,400	2,671	3,684	3,873		10.3	11.3	37.9	5.1
6. Net credit outflow[b]	7	–114	–22	91	–80					
Net credit granted	724	865	920	1,219	1,377		19.5	6.4	32.5	13.0
Net credit received	717	979	942	1,128	1,457		36.5	–3.8	19.7	29.2
Compulsory loans[c]	344	168	235	546	967		–51.2	39.9	132.3	77.1
Other	373	811	707	582	490		117.4	–12.8	–17.7	–15.8
7. Outstanding Government loans on March 31	6,068	8,566	10,328	13,989	17,970		41.2	20.6	35.4	28.5
Domestic[d]	2,280	3,398	4,603	7,299	9,140		49.0	35.5	58.6	25.2
Foreign[e]	3,788	5,168	5,725	6,690	8,830		[illegible]	10.8	16.9	32.0

Percentages

Weight of public sector consumption in total domestic uses	26.2	25.0	25.1	28.6	27.3
Weight of public sector consumption in GNP	30.1	29.6	30.7	35.8	33.5
Weight of public sector consumption expenditure on defense in GNP[f]	17.6	18.0	19.8	25.2	22.7
Weight of public sector tax revenue in GNP	26.5	28.0	30.4	32.8	36.4
Weight of public sector revenue from taxes and compulsory loans[g] in GNP	27.9	28.6	30.6	35.6	40.8
Weight of net transfer receipts[h] in total private income from economic activity	19.1	18.7	19.7	25.2	27.6

[a] Taxes and other compulsory payments, less transfers, domestic interest payments, and subsidies.
[b] Excluding transactions with the banking system.
[c] Including voluntary Defense Loan issues; excluding the special issues for banking institutions.
[d] Excluding loans from the National Insurance Institute, Development Authority, and War Risks Insurance (Arnona) Fund.
[e] Including foreign loans repayable in Israeli pounds.
[f] Excluding defense expenditure not classified as public consumption.
[g] Excluding voluntary Defense Loan issues.
[h] Including net compulsory loan collections.

Table VII–2

PUBLIC SECTOR OPERATIONS, 1969-71

(IL million, at current prices)

	1969	1970	1971	Annual increase or decrease (–)			
				1970		1971	
				IL m.	%	IL m.	%
Demand surplus							
1. Current expenditure	7,687	10,062	12,555	2,375	30.9	2,493	42.8
Public consumption	4,956	6,793	7,829	1,837	37.1	1,036	15.3
Transfers to households and nonprofit institutions	1,316	1,466	2,055	150	11.4	589	40.2
Interest paid	737	904	1,171	167	22.7	267	29.5
Subsidies and transfers to business	603	819	1,399	216	35.8	580	70.8
Misc. expenditure abroad[a]	75	80	101	5	6.7	21	26.3
2. Revenue	5,702	7,130	9,674	1,428	25.0	2,544	35.7
Taxes	4,909	6,222	8,490	1,313	26.7	2,268	36.5
Other domestic revenue	793	908	1,184	115	14.5	276	30.4
3. Saving (2 – 1)	–1,985	–2,932	–2,881	–947	–17.7	51	1.7
4. Purchases on capital account	686	752	992	66	9.6	240	31.9
5. Demand surplus (4 – 3)	2,671	3,684	3,873	1,013	37.9	189	5.1
Net domestic credit granted							
6. Net loans granted	920	1,219	1,377	299	32.5	158	13.0
7. Net credit received	942	1,128	1,457	186	19.7	329	29.2
Compulsory loans[b]	235	546	967	311	132.3	421	77.1
Other credit	707	582	490	–125	–17.7	–92	–15.8
8. Net domestic credit granted (6 – 7)	–22	91	–80	113		–171	

9. Balance to be financed (5 + 8)	2,649	3,775	3,793	1,126	42.5	18	0.5
10. Financing							
Net credit from the banking system	1,505	1,128	1,303	−377	−25.0	175	15.5
Unilateral transfers and net credit from abroad	1,144	2,647	2,490	1,503	131.4	−157	−5.9
Influence of public sector operations on the money supply and other liquid asset holdings							
A. Liquidity infusions							
11. Domestic demand surplus	887	775	940	−112	−12.6	165	21.3
Total demand surplus (5)	2,671	3,684	3,873	1,013	37.9	189	5.1
Less: Purchases and expenditure abroad	1,784	2,909	2,933	1,125	63.1	24	0.8
12. Net domestic credit granted (8)	−22	91	−80	113		−171	
13. Repayment of foreign loans	29	27	33	−2	−6.9	6	22.2
14. Total liquidity injected into the economy (11 + 12 + 13)	894	893	893	−1	–	–	–
B. Surplus of foreign currency expenditure over revenue							
15. Purchases and expenditure abroad	1,784	2,909	2,933	1,125	63.1	24	0.8
16. Less: Unilateral transfers and net credit from abroad	1,144	2,647	2,490	1,503	131.4	−157	−5.9
Repayment of foreign loans	29	27	33	−2	−6.9	6	22.2
17. Surplus foreign currency expenditure	611	235	410	−376	−61.5	175	74.5
C. Increase in public sector debt to banking system (A + B)	1,505	1,128	1,303	−377	−25.0	175	15.5

[a] National Institution expenditure abroad and net participation in the budgets of the administered areas.
[b] Absorption, Compulsory Savings, and Defense Loans, less the Defense Loan issues for banking institutions.

The sum obtained from overseas sources was IL 2,490 million, 5.9 percent less than in 1970 (in dollar terms the decrease was 12 percent). Borrowings from the banking system (mostly the Bank of Israel) were stepped up 12.2 percent to IL 1,303 million.

The "balance of payments" of the public sector is presented in the appendix to this chapter (in Hebrew only). A detailed breakdown of the changes in this statement appears separately for the various authorities – for the Government and National Institutions combined in section 2, and for the local authorities in section 3.

2. THE GOVERNMENT AND NATIONAL INSTITUTIONS

(a) *Influence on domestic demand*

The Government dominates the public sector, accounting, together with the National Institutions, for more than 90 percent of total expenditure. The influence exerted by these two authorities on the demand level is estimated below in terms of their demand surplus, net credit outflow to other domestic sectors, and contribution to the increase in the money supply and other liquid assets. The estimates are based on the budgets of the Government and National Institutions and indicate the direct impact of their operations as reflected in the budgets. It must be stressed, however, that the Government's influence on economic activity is not confined solely to the direct fiscal measures carried out within the framework of the budget. It also exerts a weighty influence, of course, through its power to control and direct activities by means of laws, regulations, ordinances, and the like; but of hardly less importance are the direct economic activities which, though not included in its budget, are carried out on its full or partial responsibility. The financial institutions' operations are largely directed by the Government as regards both the mobilization of funds and their allocation; the Government also controls the new issue market for bonds and completely or partially controls dozens of public sector companies, etc. There is therefore cogent reason to enlarge the discussion of the influence of Government and National Institution operations beyond what is reflected in their budgets.

In 1971 the Government continued the contractionary policy it had initiated in 1970, when a broad range of restrictive fiscal measures were taken: compulsory loans were imposed, taxes increased, and the growth of budgetary expenditure limited, with the exception of defense, housing and debt repayment.

During the first quarter of 1971 the Government absorbed liquidity – a phenomenon that generally repeats itself every year owing to the seasonality in tax collection, which rises strongly at the end of the fiscal year (or the beginning of the calendar year). In the second quarter of 1971 the Government began to operate in accordance with the 1971/72 budget. The fiscal measures in its contractionary policy, as embodied in the new budget, were as follows:[7]

1. The amount of liquidity to be pumped into the economy because of the Government's budgetary operations was projected at IL 400 million, the same as in the previous fiscal year.

7. See the Minister of Finance's Budget Message of January 4, 1971, *Divrei ha-Knesset* (Knesset Proceedings), Vol. 59, pp. 788-89 (Hebrew); and the Bank of Israel Research Department and Economic Advisory Bureau of the Ministry of Finance, *National Budget for 1971*, pp. 24-25.

2. The expenditure budget was enlarged to meet the higher defense requirements, debt repayment, and export subsidies, with the current operations of Government ministries being expanded only insofar as necessary for meeting the needs of the population increment – with the exception of transfer payments and certain outlays on social services.

3. After being cut back in the previous year, the development budget was increased, but the implementation of development projects totalling IL 200 million was nevertheless frozen for the time being.

4. Savings Loan collections from employers were raised from 4 to 6 percent of gross wages and salaries, as part of the "package deal" signed at the end of 1970 by the Government, Histadrut (General Federation of Labor), and Coordinating Bureau of Economic Organizations (representing the employers) and which dealt with wage, price, and tax policy for 1970 and 1971.

5. The boosting of indirect tax rates was planned, in order to preserve price stability – this too as part of the "package deal".

6. A few slight changes in direct tax rates were scheduled: National Insurance contributions were increased somewhat, but as against this certain concessions were projected in the Income Tax Ordinance with a view to improving productivity.

The second quarter of 1971 (i.e. the first quarter of fiscal 1971/72) saw a sizable liquidity infusion on the part of the Government – in excess of the sum projected for the whole of the fiscal year; the strong upward trend carried over into the third quarter of 1971. A large-scale liquidity infusion is a common occurrence at the beginning of the fiscal year, and is explained by the seasonality of tax revenue. However, in the first months of 1971/72 this was accompanied by an increase, beyond that projected, in various expenditure items, mainly the financing of housing.

To cover the expenditure in excess of the estimates, as well as the anticipated further rise in outlays on social services and payrolls, the Treasury drafted a supplementary budget to be financed partly by way of an increase in domestic revenue, including the hiking of indirect taxes from July 1971, and by foreign borrowing. The tabling of the supplementary budget was delayed until November; the revised draft took into account the changes made necessary by the August 1971 devaluation of the Israeli pound.

The devaluation in itself had a contractionary effect as far as the Government budget is concerned, since the additional domestic receipts (from ad valorem taxes imposed on imports and from the surtax on inventories) exceeded the extra domestic expenditure (due to the dearer cost of various commodities and services after the devaluation and the larger volume of grants and subsidies paid in the wake of these price rises); the devaluation was also accompanied by a reduction in indirect tax rebates to exporters.[8] Nevertheless, the supplementary budget was neutral as regards the injection of liquidity into the economy, owing, as noted above, to the increase in various expenditure items.

The demand surplus was estimated in the 1971/72 draft and supplementary budgets

8. The total increase in Government revenue resulting from the devaluation is estimated at about IL 900 million for fiscal 1971/72, while liquidity absorption amounted to an estimated IL 200 million.

Table VII–3

GOVERNMENT AND NATIONAL INSTITUTION OPERATIONS, 1969-70

(IL million, at current prices)

	1969	1970	1971	Annual increase or decrease (–) 1970 IL m.	1970 %	1971 IL m.	1971 %
Demand surplus							
1. Expenditure	7,243	9,592	11,998	2,349	32.4	2,406	25.1
Consumption	4,402	6,153	7,032	1,751	39.8	879	14.3
Transfers to households and nonprofit institutions	1,182	1,319	1,871	137	11.6	552	41.9
Net transfers to local authorities	318	401	521	83	26.1	120	29.9
Interest paid	663	820	1,074	157	23.7	254	31.0
Subsidies and transfers to business	603	819	1,399	216	35.8	580	70.8
Misc. expenditure abroad[a]	75	80	101	5	6.7	21	26.3
2. Revenue	5,196	6,588	9,064	1,392	26.8	2,476	37.6
Taxes	4,606	5,909	8,139	1,303	28.3	2,230	37.7
Other domestic revenue	590	679	925	89	15.1	246	36.2
3. Saving (2 – 1)	–2,047	–3,004	–2,934	–957	–16.7	70	2.3
4. Purchases on capital account	431	493	637	62	14.4	144	29.2
5. Demand surplus (4 – 3)	**2,478**	**3,497**	**3,571**	**1,019**	**41.1**	**74**	**2.1**
Net domestic credit granted							
6. Net loans granted	956	1,246	1,408	290	30.3	162	13.0
7. Net credit received	871	1,035	1,386	164	18.8	351	33.9
Compulsory loans[b]	235	546	967	311	132.3	421	77.1
Other credit	636	489	419	–147	–23.1	–70	–14.3
8. Net domestic credit granted (6 – 7)	**85**	**211**	**22**	**126**	**148.2**	**–189**	**–89.6**

Public sector "deficit" and its financing							
9. Balance to be financed (5 + 8)	**2,563**	**3,708**	**3,593**	**1,145**	**44.7**	**−115**	**−3.1**
10. Financing	2,563	3,708	3,593	1,145	44.7	−115	−3.1
Net credit from the banking system	1,419	1,061	1,103	−358	−25.2	42	4.0
Unilateral transfers and net credit from abroad	1,144	2,647	2,490	1,503	131.4	−157	−5.9
Influence of Govt. and National Institution operations on the money supply and other liquid asset holdings							
A. Liquidity infusions							
11. Domestic demand surplus	694	588	638	−106	−15.3	50	8.5
Total demand surplus (5)	2,478	3,497	3,571	1,019	41.1	74	2.1
Less: Purchases and expenditure abroad	1,784	2,909	2,933	1,125	63.1	24	0.8
12. Net domestic credit granted (8)	85	211	22	126	148.2	−189	−89.6
13. Repayment of foreign loans	29	27	33	−2	−6.9	6	22.2
14. Total liquidity injected into the economy (11 + 12 + 13)	**808**	**826**	**693**	**18**	**2.2**	**−133**	**−16.1**
B. Surplus of foreign currency expenditure over revenue							
15. Purchases and expenditure abroad	1,784	2,909	2,933	1,125	63.1	24	0.8
16. Less: Unilateral transfers and net credit from abroad	1,144	2,647	2,490	1,503	131.4	−157	−5.9
Repayment of foreign loans	29	27	33	−2	−6.9	6	22.2
17. Surplus foreign currency expenditure	**611**	**235**	**410**	**−376**	**−61.5**	**175**	**74.5**
C. Increase in public sector debt to banking system (A + B)	**1,419**	**1,061**	**1,103**	**−358**	**−25.2**	**42**	**4.0**

[a] National Institution expenditure abroad and net participation in the budgets of the administered areas.
[b] Absorption, Compulsory Savings, and Defense Loans, less the Defense Loan issues for banking institutions.

at IL 3,650 million, as compared with an actual surplus of IL 2,950 million in the previous year; the "deficit" (that is, the financing of the demand surplus and the net credit flow) was to total some IL 3,900 million, compared with an actual "deficit" of about IL 3,000 million the year before. But a greater-than-planned rise in domestic loan receipts, following the notable expansion of bond issues in the second half of 1971, brought about a sharp contraction in the net credit flow and thus in the deficit. The Government's liquidity infusion ceased in September 1971, at which point it began to absorb liquidity from the economy.

As may be seen from Table VII-3, the demand surplus of the Government and National Institutions, as calculated from data on their direct budgetary operations, rose only slightly during the year reviewed, from IL 3,497 million to IL 3,571 million at current prices. (In 1967-69 the demand surplus ranged between IL 2,000 million and 2,500 million, whereas in 1965-66 it ranged between IL 300 million and 400 million.) The net credit flow from the Government and the National Institutions fell from IL 211 million in 1970 to IL 22 million. A total of IL 3,593 million was therefore needed to finance the demand surplus and net credit outflow, as compared with the previous year's IL 3,708 million. This sum was obtained by borrowing from the domestic banking system and through capital imports from abroad.

The most pronounced changes in the demand surplus in 1971 were the more rapid growth of current revenue (chiefly from taxes), which advanced 37.5 percent as against the previous year's 27 percent, and the slacker growth of expenditure – 25 as against 32 percent. The net outcome was the virtual stabilization of the demand surplus, after a precipitate rise in 1970.

The main factor in the expansion of the demand surplus in recent years was the increase in direct purchases and outlays abroad, while the domestic demand surplus – i.e. the surplus of domestic expenditure over domestic revenue – rose only slightly or even fell. In 1971, however, direct purchases and outlays abroad edged up by less than 1 percent, and the growth in the overall demand surplus, as already noted, was insignificant.

Defense outlays were responsible for the more sluggish growth of expenditure in 1971 – these went up by only 11 percent after soaring 50 percent in 1970. Defense imports slumped noticeably, but domestic defense spending rose steeply. Total domestic expenditure of the Government and National Institutions went up by IL 2,526 million, but the gain in domestic revenue came to IL 2,476 million, so that the domestic demand surplus rose by IL 50 million at current prices to total IL 638 million, in contrast to IL 588 million in 1970.

The above data are in nominal terms; in real terms there was probably even a decrease in the domestic and overall demand surpluses. If the growth in the indirect import component of Government and National Institution purchases in 1971 is added, it turns out that there was a significant decline in the real domestic demand surplus.[9]

9. Government and National Institution purchases and expenditure abroad include, in addition to direct Government purchases, defense imports through agents. The direct import component of domestic purchases rose by approximately IL 90 million in 1971, according to estimates based on input-output tables for the Israeli economy prepared by the Research Department of the Bank of Israel.

It should be noted that the demand surplus is an aggregate of a number of payments and receipts flows, with disparate stimulative or restrictive effects on final demands in the economy. In the absence of detailed and updated data on the demand surplus components (such as the characteristics of taxpayers, recipients of transfer payments and subsidies, wage and salary earners, etc.) it is difficult to quantify the influence of the demand surplus and the changes therein on the national product.

Excluded from the above computations are two items that are treated as financial transactions but whose stimulative or restrictive effects on final domestic demands are very similar to those of the demand surplus components. The reference is to compulsory loan receipts on the one hand and to the financing of investments in housing and in certain public sector companies on the other.

The liquidity of the compulsory loans is very low, especially in the period immediately after collection. Those imposed on the public in the past two years are completely illiquid and special steps were taken to make them nonnegotiable. The contractionary effect of the compulsory loans exceeds that of any other form of credit absorption, and as regards a large percentage of the purchasers they have a tax-like effect.

The granting of development budget loans by the Government and Jewish Agency is directly connected with the implementation of investments, notably in housing and in projects of public sector companies, which would not have been carried out but for this credit. In terms of its impact on demand, there is little difference between such credit and direct Government investments.

Quasi-financial transactions of the type discussed resulted in a net credit flow of IL 441 million, compared with IL 700 million in 1971. Examination of the component items shows the following changes: Development budget loans granted by the Government and National Institutions rose from IL 1,246 million in 1970 to IL 1,408 million. Net compulsory loan receipts advanced strongly, from IL 546 million in 1970 to IL 967 million; these figures do not include the series issued specifically for banking institutions, but in 1970 they include IL 75 million in proceeds from the semi-voluntary 1969 Defense Loan. The growth of the other compulsory loans was therefore greater and had a very pronounced contractionary effect.[10]

Other financial transactions of the Government consist chiefly of net domestic borrowings. Long-term borrowings (excluding the compulsory loans) went up by a respectable IL 266 million to total IL 417 million. But net short-term credit plunged from IL 338 million in 1970 to a mere IL 2 million (see Table VII-10).

Government and National Institution indebtedness to the banking system increased by IL 1,103 million in 1971, compared with IL 1,061 million the year before, with most of the growth being in the debt to the Bank of Israel. It should be noted here that, because of the "balanced budget" multiplier, the provision of bank credit to the Government has a stronger expansionary effect than the supply of credit to other sectors. But the deficit in the foreign currency transactions of the Government and National Institu-

10. Net compulsory loan proceeds consist of loan collections less redemptions, and are to be distinguished from the data appearing in Chapter II, "Resources, Uses, and Income", where compulsory loan certificates distributed during the year reviewed were also deducted.

tions offset much of this expansionary effect, by helping to keep down the growth of the money supply and other liquid assets held by the public. The increase in the debt to the banking system less the deficit in foreign currency transactions represents the amount of liquidity pumped into the economy by these two authorities. This infusion finances the domestic demand surplus and net credit granted in IL.

The liquidity infusion in 1971 amounted to IL 693 million, as against IL 826 million the year before. This decline in a year of rising GNP indicates that the operations of the Government and National Institutions had a contractionary effect on the level of economic activity in comparison with the previous year.

The foregoing pertains to the direct operations of these two authorities as reflected in their budgets; it should not be inferred from this that the overall activity of the Government had a similar effect. In fact, the contrary was probably true if to the liquidity infusion of the Government and the National Institutions we add the amount of foreign currency converted into Israeli pounds by public sector companies and financial institutions that obtained foreign loans with Government approval in order to finance domestic activities,[11] as well as the incremental bank credit supplied to public sector companies.

It follows from the aforesaid that the Government's budgetary and extrabudgetary operations accentuated the expansionary influence of the nongovernmental sectors instead of mitigating or neutralizing it – in other words, the Government did not adopt countercyclical measures to the degree required.

Despite the slower growth of the demand surplus of the Government and National Institutions in 1971 – and perhaps even a decline in real terms – this was not indicative of any weakening of the inflationary pressures generated by their operations. In 1967-68 – when the economy was emerging from the slump, there was a reserve of idle factors of production, and the stimulative forces at work in the nongovernmental sectors were not strong – the creation of a sizable Government demand surplus actually constituted a reflationary measure and contributed greatly to the upturn in GNP and economic activity. In 1970 the demand surplus of the Government and National Institutions grew, but the expansionary forces in the nongovernmental sector were still comparatively weak, both because of the Government's incomes policy, which checked the expansion of private demand and consumption, and also because of balance of payment developments, which averted an increase in the money supply and other liquid assets of the public. The 1970 growth of public consumption and of the public sector demand surplus was partly at the expense of alternative final uses, thereby weakening somewhat the inflationary pressures latent in the former.

The operations of the Government and the rest of the public sector in 1971 must be viewed against the backdrop of the large-scale monetary expansion, which stemmed chiefly from balance of payments developments: the growth of exports and capital imports and the devaluation of the Israeli pound. While the Government continued with its policy of incomes restraint, it was less intensively applied than in 1970; as a consequence,

11. See Chapter XVI, "Financial Institutions", section 2; and Chapter III, "The Balance of Payments", section 5.

disposable private income, private consumption, and investment all moved up at a faster rate, accompanied by the fall of unemployment to a very low level. In the light of these developments, the countercyclical action called for in 1971 was a significant contraction of the Government's demand surplus and liquidity infusion.

As noted above, the Government and National Institutions required IL 3,593 million in 1971 to fund their demand surplus and net credit outflow; this was obtained from foreign sources and the domestic banking system. Net foreign borrowed receipts and unilateral transfers declined from IL 2,647 million in 1970 to IL 2,490 million, i.e. by 6 percent. These sums are in Israeli pounds calculated at the exchange rates prevailing at the time the foreign currency transactions were executed; in dollar terms, the decline was from $756 million in 1970 to $665 million, i.e. by 12 percent. Receipts from overseas sources provided about 70 percent of the total requisite financing; the remainder was supplied by the domestic banking system. The debt to the latter rose by IL 1,103 million, with most of the sum stemming from an increase in loans and a change in deposit balances with the Bank of Israel, and to a lesser extent from changes in deposit and credit balances with, and sales of securities to, the banking system.

(b) *The "balance of payments" of the Government and National Institutions*

Table VII-4 presents the "balance of payments" of the Government and the National Institutions for 1970 and 1971. The table distinguishes between transfers and transactions in goods and services on the one hand and financial transactions on the other. Transactions with the local authorities have been recorded separately.

Total payments of the Government and National Institutions, including long-term debt repayment, added up to IL 15,572 million, 23.5 percent over the 1970 level. Following are the principal changes in the operations of these two authorities, as reflected in their "balance of payments".

Government tax receipts were up 37.7 percent in 1971, with indirect taxes bringing in 46.7 percent more than in 1970, and direct taxes (excluding compulsory loan receipts) 29.4 percent more. The effect of the direct and indirect tax hikes of 1970 was fully reflected in the data for the year reviewed. In addition, the August 1971 devaluation automatically increased the revenue from ad valorem taxes levied on imports and on domestic commodities made more expensive by the change in the exchange rate. But the predominant factor in the growth of tax revenue was the upward revision of the average rates, mainly of indirect taxes.

Unilateral receipts from abroad were down from IL 837 million in 1970 to IL 746 million.[12] The overseas fund-raising campaigns were continued but yielded less than in the previous year. In contrast to this, sales of Independence and Development Bonds, which also reflect the efforts of World Jewry on behalf of Israel, netted IL 694 million as against IL 475 million in 1970.

Government and National Institution consumption was up 14 percent at current

12. This figure differs from that cited in Chapter III, "The Balance of Payments", where unilateral transfers from abroad are shown net of National Institution expenditure abroad, as well as of changes in the Institutions' financial transactions with the rest of the world.

Table VII–4

"BALANCE OF PAYMENTS" OF THE GOVERNMENT AND NATIONAL INSTITUTIONS, 1970-71

(IL million)

Receipts	1970	1971	Increase or decrease (–)	Payments	1970	1971	Increase or decrease (–)
Transfers and transactions in goods and services							
Taxes[a]	5,909	8,139	2,230	Purchases on current account	6,189	7,068	879
Other revenue				Purchases on capital account	494	640	146
Transfers from the public	229	296	67	Interest paid	820	1,074	254
Interest received	332	414	82	Transfers to households and nonprofit institutions	1,319	1,871	552
Income from property	118	215	97	Subsidies and transfers to business	819	1,399	580
Sales	37	39	2	Misc. expenditure abroad[d]	80	101	21
Unilateral receipts from abroad	837	746	–91				
Total	7,462	9,849	2,387	Total	9,721	12,153	2,432
Transactions in financial claims							
Collections on long-term loans	153	200	47	Long-term loans and participation in share capital	1,367	1,572	205
Long-term loans received				Repayments on long-term loans			
Foreign	2,516	2,479	–37	Foreign	726	903	177
Domestic[b]	1,052	1,771	719	Domestic	355	387	32
Short-term credit, net							
Foreign	20	168	148				
Domestic[b]	338	2	–336				
Credit from the banking system[c]	1,061	1,103	42				
Total	5,140	5,723	586	Total	2,448	2,862	414
Transactions with the rest of the public sector							
				To local authorities (net)	433	557	124
Total receipts	12,602	15,572	3,013	Total payments	12,602	15,572	3,013

[a] Including collections on account of National Insurance.
[b] Excluding credit from the banking system.
[c] Including changes in deposit balances, long-term loans, and purchases of Government bonds.
[d] National Institution expenditure abroad and participation in the budgets of the administered areas.

prices and totalled IL 7,032 million. The largest expenditure item is defense, which accounts for roughly 70 percent of total consumption spending. In the year reviewed this item went up only 11 percent at current prices, with domestic expenditure rising 26.5 percent and imports declining by 6 percent.

Payroll outlays soared 29 percent, the highest rate since 1968. The rise in average earnings per employee added 24.5 percent to the wage bill (part of this represents pay differentials on account of previous years).

At constant prices, Government and National Institution consumption was down 0.5 percent. This was due almost entirely to the cutting back of defense imports; less the latter, there was a rise of 9 percent.

The most striking change was in transfer payments: those to households and non-profit institutions soared 42 percent, domestic interest payments by 34.5 percent, and subsidies and transfers to business on capital account by 70 percent.

Gross long-term loans and participation in share capital rose 15 percent, with the bulk of the increment being in housing and industrial loans.

Details of the changes mentioned above and of others in the "balance of payments" of the Government and the National Institutions follow in sections (c), (d), and (e).

(c) *Receipts*

1. *Taxes*

Government tax revenue was up 37.7 percent, the biggest gain ever recorded. In 1970 growth amounted to 28.3 percent, while the average for the last decade was 19.8 percent.

A number of factors contributed to this increase: the raising of tax rates in 1970 and 1971, the impact of the August 1971 devaluation, and the expansion of GNP, national income, and imports. The influence of these factors will be detailed in sections 2 and 3.

Of the IL 2,230 million incremental tax revenue in 1971, about 60 percent (IL 1,331 million) constituted indirect tax collections. These were, at IL 4,183 million, up 46.7 percent from 1970, when the increase came to 20.4 percent. About 70 percent of the growth derived from import taxes. Direct taxes went up less – by 29.4 percent – and totalled IL 3,956 million. In 1970 revenue from this source expanded by 36.7 percent, mainly because of the stiff increases in rates during the year. Direct taxes and compulsory loan collections[13] combined went up 39.3 percent, compared with 60.2 percent in the previous year.

The share of taxes on income, including the compulsory loans, in total tax and compulsory loan receipts edged down from 55.7 percent in 1970 to 54.4 percent; excluding the compulsory loans, their share dropped from 51.7 percent to 48.6 percent. The weight of import taxes went up noticeably, from 20.2 percent in 1970 to 26.3 percent; this was due to an 80 percent jump in such revenues following the revision of

13. The reference is to compulsory loans levied on wages and income: namely the Absorption Loan, the Compulsory Savings Loan, and the Compulsory Defense Loan. In this chapter the compulsory loans are classified under Government receipts on financial account, and the proceeds are itemized in section 5 below Nevertheless, there is good reason to discuss these loans together with direct taxes.

Table VII–5

GOVERNMENT TAX REVENUE, 1970-71

(IL million)

	1970	1971	Increase or decrease (–)	
			IL m.	%[a]
Direct taxes				
Income tax	2,232	2,713	481	21.5
National Insurance	825	1,243	418	50.6
Total	**3,057**	**3,956**	**899**	**29.4**
Indirect taxes				
Customs duties and import surcharge	890	1,665	775	87.1
Purchase tax	666	895	229	34.4
Fuel tax	252	358	106	42.2
Property taxes	233	258	25	10.7
Tobacco excise	134	162	28	21.3
Cement excise	60	57	–3	–5.0
Excise on beverages	29	32	3	11.1
Revenue stamp tax	123	157	34	27.0
Defense stamp tax	101	143	42	42.2
Vehicle license fees	65	76	11	16.1
Foreign travel tax	51	70	19	37.4
Licenses, fees, misc. service charges, and other taxes	131	122	–9	–6.9
Surtax on stocks	–	28	28	–
Current surplus of the Post Office and ports	117	160	43	36.8
Total	**2,852**	**4,183**	**1,331**	**46.7**
Grand total	**5,909**	**8,139**	**2,230**	**37.7**

NOTE: The definitions of direct and indirect taxes in this table are based on conventional national accounting procedures and differ somewhat from those used by the Accountant General. This table excludes compulsory payments which in the national accounts are defined as transfers – namely, the inheritance tax, land betterment tax, fines, and certain fees and licenses (e.g. drivers licenses and passport fees). On the other hand, this table includes the net profit of the Post Office and the ports (deficits of Israel Railways are included with subsidies).

[a] Calculated from unrounded figures.

SOURCE: State Revenue Administration, Accountant General, and National Insurance Institute.

rates, the imposition of an import surcharge in August 1970, and the devaluation in August 1971.

The downtrend in the weight of taxes on domestic production, evident for the past several years, carried over through the year reviewed, when the level reached 17.1 percent as against 18.7 percent in 1970. However, the proportion of such taxes in GNP did not change over the past three years. Nevertheless, it should not be inferred from this that their elasticity in relation to GNP is unitary, but rather that the increases in their rates in the past few years happened to result in collections rising proportionately to the growth of GNP.

Table VII–6

GOVERNMENT TAX REVENUE, BY MAIN CATEGORY, 1969-71

(IL million)

	1969	1970	1971	Increase from 1970 to 1971	
				IL m.	%
Taxes on income	2,237	3,057	3,956	899	29.4
Taxes on expenditure					
Imports	1,007	1,191	2,137	946	79.4
Local production	964	1,105	1,395	290	26.2
Taxes on property	208	253	293	40	15.8
Fees and licenses	190	303	358	55	18.2
Total	**4,606**	**5,909**	**8,139**	**2,230**	**37.7**
		Percentages			
Taxes on income	48.6	51.7	48.6		
Taxes on expenditure					
Imports	21.9	20.2	26.3		
Local production	20.9	18.7	17.1		
Taxes on property	4.5	4.3	3.6		
Fees and licenses	4.1	5.1	4.4		
Total	**100.0**	**100.0**	**100.0**		

NOTE: Taxes on income consist of income tax and National Insurance contributions. Taxes on imports consist of general customs duties and purchase tax on imports, surtax, and foreign travel tax. Taxes on local production consist of purchase tax, excises, the current surplus of the Post Office and ports, entertainment tax, defense stamp tax on production, and various other levies. Taxes on property consist of the property tax and land registration fees. Fees and licenses include *inter alia* the revenue stamp tax and defense stamp tax.

SOURCE: Taxes on income – State Revenue Administration and National Insurance Institute; taxes on expenditure – Central Bureau of Statistics.

2. *Direct taxes*

Receipts from income tax and compulsory loans went up in 1971 by 35.5 percent to reach IL 3,754 million. Excluding compulsory loans, the level reached IL 2,713 million – a 21.5 percent gain.[14] This rate lagged somewhat behind that for national income (23.3 percent) and gross private income from economic activity (23.4 percent). The elasticity of income tax revenue in relation to national income is greater than unity;[15] and the fact that the two moved up at similar rates in 1971, even though the average tax rates increased somewhat during the year (as will be detailed below), may be explained by the following two factors: (1) part of the incremental national income was tax-exempt or

14. These figures are from preliminary reports of the Accountant General and the State Revenue Administration. Final data on income tax collections in 1971, received shortly before the *Annual Report* went to press, are approximately IL 30 million higher than the figures cited here.
15. This finding is from an econometric model of the Israeli economy prepared by the Bank of Israel Research Department.

Table VII–7

GOVERNMENT REVENUE FROM INCOME TAX AND COMPULSORY LOANS, 1970-71

(IL million)

	1970	1971	Percent increase or decrease (–) in 1971	Percentage distribution	
				1970	1971
Income tax[a]					
Self-employed	445	524	17.7	19.8	19.2
Companies	549	636	15.8	24.4	23.4
Wage and salary earners	1,053	1,296	23.1	46.9	47.7
Thereof: Directors of companies listed as salaried employees and members of cooperatives	88	121	37.5	3.9	4.4
Deductions at source[b]	200	264	32.0	8.9	9.7
Thereof: From suppliers of goods and services	43	87	102.3	1.9	3.2
Total	**2,247**	**2,720**	**21.1**	**100.0**	**100.0**
Compulsory Defense Loan[c]					
Self-employed	27	46	70.4	10.9	10.3
Companies	53	89	67.9	21.5	19.8
Wage and salary earners	167	313	87.4	67.6	69.9
Total	**247**	**448**	**81.4**	**100.0**	**100.0**
Compulsory Savings Loan					
Collections from employers	173	400	131.2	62.7	68.3
Collections from employees	103	186	80.6	37.3	31.7
Total	**276**	**586**	**112.3**	**100.0**	**100.0**
Total income tax and compulsory loans	**2,770**	**3,754**	**35.5**		

[a] Net collections (i.e. after tax rebates); including Absorption Loan receipts, totalling IL 15 million in 1970 and IL 7 million in 1971.
[b] At-source deductions on interest and dividend payments, insurance commissions, authors' fees, and payments to suppliers and contractors for goods and services.
[c] Excluding the Defense Loan issues for banking institutions.
SOURCE: Income and Property Tax Commission, Ministry of Finance.

subject to relatively low rates; (2) the lag of income tax collections behind the growth of national income was apparently greater in 1971.

In 1970 a number of taxes had been raised. In April the defense levy was upped from 10 to 15 percent of the total tax assessed, the tax prepayment rates for companies and self-employed were increased, in June income tax began to be deducted at source from payments to subcontractors and Government suppliers, and in August company tax rates were raised. These measures were only partly reflected in the data for 1970, their full impact being felt in 1971, when they contributed to the rise in the average rate of income tax.

Company tax receipts added up to IL 636 million – a gain of 15.8 percent, compared with 34.9 percent in 1970. Receipts from the self-employed[16] totalled IL 517 million – an increase of 16.2 percent, as against 19 percent in 1970. Besides these sums, IL 87 million (IL 43 million in 1970) was withheld at source from payments to Government subcontractors and suppliers.

It should be noted here that the scope of the Law for the Encouragement of Capital Investments and the Law for the Encouragement of Industry was broadened in 1971. This increased the number of companies eligible for concessions and partial or full exemption from the tax – a fact which helps explain why income tax revenue trailed behind the growth of national income.

Income tax collected from employees (including company directors listed as salaried employees and members of cooperatives) was up 23.1 percent to stand at IL 1,296 million. The number of employees in the economy (excluding workers from the administered areas)[17] rose 4.5 percent and average earnings per employee by 15.3 percent. The average earnings subject to income tax went up less, since the cost-of-living allowance increment paid in 1971 was tax-free. In addition, the year reviewed probably saw a further erosion of the tax base – that is, there was a rise in the portion of the employee's incremental income that was either tax-free or subject to a relatively low tax.

As a result of the developments described above, the share of wage and salary earners in total income tax receipts inched up from 46.9 percent in 1970 to 47.7 percent, while the share of other taxpayers declined correspondingly.

The reference here is to taxes on income derived by employees from pay and fringe benefits, excluding taxes on property income and capital gains (such collections are included in Table VII-7 under "deductions at source"). On the other hand, company directors listed as salaried employees and members of cooperatives are also included under "wage and salary earners". The earnings of directors do not differ essentially from those of the self-employed, and part of the income of cooperative members is entrepreneurial income. But even excluding this group of employed, the share of wage and salary earners in total income tax receipts rose between 1970 and 1971. If compulsory loans are added, however, their share remained unchanged at 47.8 percent of total income tax and compulsory loan receipts.

These changes in the share of employees and nonemployees in total income tax collections do not correspond to the changes in the share of these two groups in total gross private income from economic activity. The share of wage-income in total gross private income from economic activity edged down from 68.4 percent in 1970 to 67.5 percent. This would seem to point to an increase in the average amount of income tax paid by employees as compared with nonemployees. However, the data available are not

16. Excluding company directors listed as salaried employees.
17. The contribution of workers from the administered areas employed in Israel to income tax collections is very slight, and therefore changes in income tax receipts are to be attributed to Israeli employees only.

sufficiently precise to permit the drawing of definite conclusions: the identity of employees in the tax collection data and that of recipients of wage income in the data on the distribution of private income from economic activity are not statistically clear. Nor do we know the extent to which the tax base eroded between the two years; that is, the degree to which the weight of what is defined as income from wages and salaries changed, and hence what portion of the incremental private income from economic activity not defined as wages and salaries was nevertheless received by employees.

National Insurance collections rose by IL 1,243 million, or 50.6 percent, after soaring 77.3 percent in the previous year.

In April 1970 there was a big hike in National Insurance contribution rates, new schemes were introduced, and the ceiling on employees' income subject to National Insurance was raised. These changes were only partly reflected in the data for 1970 but found full expression in 1971. In April 1971 unemployment insurance rates and those for reservists compensation benefits were raised by one percent of the employees' monthly wage or salary (up to a ceiling of IL 1,500). Half of the increase was borne by the employer, who was entitled to collect the remainder from his employee. With these changes, National Insurance contributions per employee (excluding the work injury benefit item) reached 14.9 percent of the employee's monthly wage or salary up to the IL 1,500 ceiling. The employer pays 11.1 percent and is entitled to collect the remaining 3.8 percent from his employee. Rates for the self-employed remain unchanged at 9.4 percent (including 0.8 percent for work injury benefits).

Along with these increases in National Insurance contribution rates, a number of concessions were introduced for low-income self-employed and for insured not working.

3. *Indirect taxes*

Indirect tax revenue in 1971 totalled IL 4,183 million, a gain of 46.7 percent as against the previous year's 20.4 percent. In contrast to 1970, when indirect tax rates were raised substantially, there were almost no changes in rates in 1971, with the exception of the July increase in the fuel tax. Nevertheless, on an annual average tax rates increased significantly in 1971 because the revisions of the previous year – in particular, the import surcharge introduced in August 1970 – found full expression in 1971. The devaluation of the Israeli pound was another contributory factor, being reflected both in the growth of revenue from customs duties and purchase tax on imports and in a larger revenue from purchase taxes on domestic goods that became dearer after the devaluation.

Of the IL 1,331 million incremental indirect tax revenue in 1971, two-thirds (about IL 900 million) derived from the following increases in rates:

(a) The various indirect tax hikes during 1970 produced some IL 600 million additional revenue in 1971. Of this, IL 505 million came from customs duties and the import surcharge, IL 70 million from purchase tax, and the balance from the tobacco excise and foreign travel tax.

(b) The August 1971 devaluation augmented revenues by IL 130 million, of which IL 75 million constituted customs duties, IL 20 million purchase tax, IL 28 million the inventory surtax, and IL 7 million the tobacco excise and foreign travel tax.

(c) The revision of the fuel tax in July 1971 added IL 70 million to tax receipts.

(d) A levy on defense imports was planned for fiscal 1971/72, but collection (IL 106 million in 1971) was begun only with the devaluation in August.

These changes in tax rates accounted for about 40 percent of the incremental revenue from taxes on domestic production and about 80 percent of that from import taxes. Excluding the influence of these changes, indirect tax revenue was up approximately 15 percent as a result of the expansion of economic activity, private consumption, and imports.

Following are the principal changes in indirect tax receipts.

Customs revenue shot up 87.1 percent to IL 1,665 million. Most of the increase stemmed from the revision of the tariff (including the defense import levy). Another factor was the larger volume of imports, chiefly of consumer goods – which went up 11 percent after edging down 1 percent in 1970 (this includes a 17 percent rise in consumer durables in 1971, as contrasted with a decline of 19 percent in the previous year).

Changes in the import product mix and the growth of private consumption – especially of durables – affected purchase tax receipts, which increased 34.4 percent to total IL 895 million. Of this sum, IL 375 million was collected on imports and IL 520 million on domestic production.

Revenue from the fuel tax came to IL 358 million, up 42.2 percent from 1970. About two-thirds of the increment is explained by changes in the tax rates introduced at the end of July 1971, when the gasoline tax was raised and for the first time a tax was imposed on kerosene and heavy fuel oil. The balance is attributable to a larger fuel consumption and to the growing shift to the more heavily taxed, higher octane gasoline.

Property tax collections amounted to IL 258 million, 10.7 percent over the 1970 figure. Rates were not revised in 1971, the increment mainly reflecting the expansion of construction activity.

All the other indirect taxes also yielded a larger revenue in 1971, with the exception of the cement excise, which declined 5 percent owing to slacker sales of taxable cement.[18] A breakdown of indirect tax revenue appears in Table VII-5.

4. *Miscellaneous revenue*

These receipts, which consist of domestic transfers, income from property, interest and dividends, and sales proceeds, went up from IL 716 million in 1970 to IL 964 million. The biggest increase was in Government and National Institution income from economic activity, namely property income and interest and dividend receipts. The former shot up 82 percent to IL 215 million, including IL 101 million in Bank of Israel profits transferred to the Accountant General. Interest and dividends increased by 24.5 percent to IL 414 million (including IL 106 million in interest from Government business-type enterprises, such as the postal service, railway, and airports).

Transfers by households went up 29 percent to reach IL 296 million; this includes IL 108 million in transfers on capital account (in the main the Government's receipts

18. Cement sold to enterprises approved under the Law for the Encouragement of Capital Investments or for certain specified purposes is either free of excise duty or subject to a low rate.

from its enterprises on account of depreciation, as well as revenue from the land betterment tax and the inheritance tax) and IL 188 million in current transfers for services supplied by public health and educational institutions, as well as drivers license fees, fines, and donations.

(d) *Payments*

Total expenditure by the Government and National Institutions, as reflected in their "balance of payments" (see Table VII-4), totalled IL 15,572 million at current prices, compared with IL 12,602 million in 1970.

Expenditure on current account went up 25 percent to IL 12,034, and that on capital account by 29.5 percent to IL 640 million.

The growth of current purchases (including payrolls and defense expenditure) slowed noticeably, the increase amounting to 14 percent at current prices as contrasted with 39.5 percent in 1970. On the other hand, the uptrend in transfer payments and subsidies grew more pronounced – a rise of 47 percent as against 21 percent in 1970.

1. Purchases on current and capital account

Government and National Institution consumption[19] was up 14 percent to stand at IL 7,032 million at current prices, or IL 6,094 million at 1970 prices – a 1 percent decline in real terms.

A breakdown of consumption as between domestic and overseas purchases shows that the latter was down 5.4 percent at current prices, while domestic purchases were up 26.6 percent. The contraction of overseas purchases resulted, as mentioned above, from the cutback in defense imports. Domestic defense purchases were 26.5 percent greater than in 1970.

Payroll outlay, excluding Ministry of Defense enterprises, amounted to IL 1,221 million, up 28.9 percent from 1970. Of this increase, 24.7 percent was due to a higher average expenditure per employee, part of it reflecting the payment of wage differentials for previous years, and 3.4 percent to a growth in personnel.

Government and National Institution purchases on capital account[20] were, at IL 640 million, up 29.6 percent. Approximately two-thirds of this sum (IL 412 million) was invested in transport and communications (roads, postal services, the railway, and airports); here the rise amounted to 36 percent. There was also a heavier investment in other sectors: capital outlays on agriculture and irrigation, which had fallen off in 1970, rose to IL 78 million, and those on public buildings and services to IL 150 million.

19. Defined as current purchases less sales; excluding interest paid locally and abroad, overseas outlays of the National Institutions, and net participation in the budgets of the administered areas. The overseas expenditures mentioned here are treated in the national accounts not as consumption but as transfers to the rest of the world.

20. These purchases are not identical with the share of the Government and National Institutions in gross domestic investment, since they include purchases of existing assets and other expenditures which are not included under the head of domestic investment.

Table VII–8

PURCHASES OF THE GOVERNMENT AND NATIONAL INSTITUTIONS ON CURRENT AND CAPITAL ACCOUNT, 1970-71

(IL million)

	1970	1971	Increase or decrease (–) IL m.	%
Purchases on current account				
Wages and salaries of civilian employees	947	1,221	274	28.9
Defense	4,778	5,294	516	10.8
Other purchases	464	553	89	19.2
Total purchases on current account	**6,189**	**7,068**	**879**	**14.2**
Domestic	3,819	4,826	1,007	26.4
Foreign[a]	2,370	2,242	–128	–5.4
Purchases on capital account				
Agriculture and irrigation	56	78	22	39.3
Transportation and communications	303	412	109	36.0
Public buildings and services	135	150	15	11.1
Total purchases on capital account	**494**	**640**	**146**	**29.6**
Domestic	354	450	96	27.1
Foreign	140	190	50	35.7
Grand total	**6,683**	**7,708**	**1,025**	**15.3**
Domestic	4,173	5,276	1,103	26.4
Foreign	2,510	2,432	–78	–3.1

[a] Including defense purchases totalling IL 2,280 million in 1970 and IL 2,032 million (including defense import levy) in 1971.

2. *Subsidies and transfer payments*

Subsidies and transfers paid by the Government and the National Institutions came to IL 4,465 million, an increase of 47 percent. Subsidies rose 69 percent to IL 1,291 million. This item consists of direct price supports, participation in or rebates of expenditures of producers and other enterprises, outlays by Government departments to encourage production and exports, Government participation in funds administered jointly with producers with the object of promoting production and exports, the subsidization of imported foodstuffs, and the covering of deficits incurred by the Government business-type enterprises.

Most of the increase under this head was in export subsidies, which were up 82.5 percent to IL 765 million. This substantial rise is explained by the growth of exports and the larger incentives granted to exporters (these were upped in August 1970 and January 1971). Rebates of indirect taxes on exports were reduced upon the devaluation of the Israeli pound in August 1970.[21]

21. On the changes in incentives and in the effective exchange rate for industrial exports see Chapter III, "The Balance of Payments", Table III-12.

Table VII–9

TRANSFER PAYMENTS, GRANTS, AND SUBSIDIES BY THE GOVERNMENT AND NATIONAL INSTITUTIONS, 1970-71

(IL million)

	1970	1971	Increase or decrease (–) IL m.	%
Transfer payments and grants to households	965	1,370	405	42.0
From the National Insurance Institute				
Benefits	458	582	124	27.1
Other transfer payments[a]	84	164	80	95.2
Provident and pension payments	155	204	49	31.6
Transfer payments by the Government	122	134	12	9.8
Transfer payments by the National Institutions	146	286	140	95.9
Transfer payments to nonprofit institutions	354	501	147	41.5
Transfer payments on capital account to business	55	108	53	96.4
Subsidies	764	1,291	527	69.0
On locally produced goods and services	317	413	96	30.2
On imported goods	28	113	85	303.5
On exports	419	765	346	82.6
Domestic interest payments	501	674	173	34.5
Net transfer payments to local authorities	401	521	120	29.9
Total transfer payments and subsidies	3,040	4,465	1,425	46.9

[a] Government and National Institution transfers through the National Insurance Institute, such as supplementary old-age pensions, cost-of-living grants, and benefit payments to casualties of hostile action.

The subsidization of local production, including the covering of deficits of Government enterprises, rose by 30 percent to IL 413 million. The most striking increases were in agricultural factor subsidies (which had been trimmed in the two preceding years) and in transportation subsidies.

Import subsidies were, at IL 113 million, much larger than in 1970. These are granted mainly on essential foodstuffs (imported under the control of the Ministry of Commerce and Industry), and to a lesser extent on agricultural inputs (feed).

Transfer payments to households went up 42 percent to IL 1,370 million. Of this amount, IL 582 million represented National Insurance benefit payments, which were IL 124 million over the 1970 level. The growth of such benefits, excluding those under the "employees' children allowance" scheme, stemmed from a rise of 9.5 percent in the number of beneficiaries and of 18 percent in the average payment. The latter is attributable to the upward revision of benefit rates in most National Insurance schemes in September 1970 and January, April, and September 1971.

Provident and pension payments added up to IL 204 million. These consist of compensation payments to victims of Nazi persecution and war invalids and pensions paid to retired Government and National Institution employees.

Other transfer payments to households rose sharply in 1971. These consist of the

Government's participation in graded secondary school fees, expenditure on food in health, educational, and welfare institutions of the Government and National Institutions, participation in hospitalization fees, social benefits, nonstatutory old-age and survivors pensions paid through the National Insurance Institute, low-income supplements, benefit payments to victims of enemy action, relief allotments to needy families and others, as well as the cost of initial immigrant absorption (financial aid to new arrivals in the country, employment and housing assistance, etc.). Such transfers increased by approximately two-thirds to IL 584 million. Of this amount, IL 164 million was disbursed through the National Insurance Institute (as against IL 84 million in 1970) and consisted mainly of low-income grants, special old-age pensions, and social benefits, the rates of which were upped in 1971. The remaining transfers rose by 56 percent to IL 420 million; these were paid by the National Institutions and various Government departments. The most striking increases were in Jewish Agency transfers for educational purposes (chiefly scholarships), immigrant employment, and health services.

Allocations to nonprofit institutions rose 41.5 percent to IL 501 million, with most of the increment going to educational institutions.[22]

Transfer payments to business on capital account doubled in the year reviewed to stand at IL 108 million. The bulk of this sum – about IL 90 million – consisted of grants to industrial concerns under the Law for the Encouragement of Capital Investments, while the balance consisted of other grants.

Total interest outlays of the Government and the National Institutions (excluding that paid to the National Insurance Institute and the War Risks Insurance Fund) went up 31 percent to IL 1,074 million, of which IL 674 million represented domestic interest payments (up 34.5 percent).

Net Government transfers to local authorities were, at IL 521 million, up 30 percent. Ordinary and extraordinary budget grants also increased – chiefly because of the indemnification of local authorities for forgoing tax hikes – and totalled IL 191 million. The amount of Government tax revenue shared with the local authorities, which is determined by the amount of Government tax collections,[23] rose to IL 175 million following the growth of tax revenue. Another transfer item – participations of various Government departments in local authority expenditure (in the main those of the Ministries of Social Welfare, Education, and Religion on social services) and grants from the Government's development budget and from the Israel Educational Fund – increased to IL 155 million.

(e) *Financial transactions*

Net loan receipts of the Government and the National Institutions from foreign and domestic sources increased by 8.4 percent to reach IL 4,233 million, the bulk of which consisted of medium- and long-term loans. After rising steeply in 1970 to IL 1,810 million, net foreign loan receipts declined in the year reviewed to IL 1,744 million to account for 42.5 percent of total net loan receipts, as compared with 47 percent in 1970.

22. See Chapter VIII, "Nonprofit Institutions", section 1.
23. Details are presented in section 3(b).

1. Foreign loans

Long-term foreign loan receipts amounted to IL 2,479 million in 1971, while foreign debt repayment came to IL 903 million. Together with the short-term credit, net foreign borrowing totalled IL 1,744 million (at the rates of exchange prevailing when the transactions were executed), as against IL 1,810 million in 1970 (or $464 million and $517 million respectively). Most of the decline was in long-term credit, whereas short-term credit increased. Two factors contributed to the contraction of the former: (a) a decrease in U.S. Government loans (a substantial part of which was for covering Ministry of Defense procurement orders in that country) from $375 million in 1970 to $302 million; and (b) an increase in debt repayment from $184 million to $227 million. This decline was partly offset by the growth of Independence and Development Loan receipts from $231 million to $301 million, thanks partly to the better terms offered purchasers.

Net long-term foreign loan receipts of the National Institutions continued downward, in line with the trend evident since 1968. But it should be noted that, whereas the decline in 1968 and 1969 stemmed from the deliberate effort of the Institutions to reduce their foreign indebtedness after receiving a special loan from the Bank of Israel to repay various foreign liabilities, the decline in the last two years is explained by the difficulties encountered by the Institutions in obtaining long-term financing in the international market. Almost all of the increase in their liabilities was in short-term loans.

2. Domestic loans

Long- and medium-term domestic borrowing was on a much larger scale in the year reviewed. Long-term loans, excluding those from the banking system, were up from IL 1,052 million in 1970 to IL 1,771 million. Less repayments, receipts from this source were double those in 1970 – IL 1,384 million as against IL 697 million – with all categories sharing in the increase: compulsory loans, Government bonds, and proceeds of financial institution security issues deposited with the Treasury.

The increase in Government compulsory loan receipts consisted of the following items:

Compulsory Defense Loan receipts went up from L 247 million in 1970 to IL 448 million in 1971.[24] Collections on account of this loan, which began in April 1970, are at a flat rate of 7 percent of taxable income (applicable to employees, self-employed, and companies alike). Interest is at 5 percent, tax-free, and the principal is pegged to the cost-of-living index. The principal will be redeemed after 15 years in twelve equal monthly installments, while interest will be redeemed in three equal triennial installments, beginning in the seventh tax year.

The Compulsory Savings Loan brought in IL 586 million in 1971, as against IL 276 million the year before.[24]

Compulsory Defense Loan receipts went up from IL 247 million in 1970 to IL 448 and self-employed it is 4 percent of total income and for companies and cooperative societies, 2 percent; on top of this, during the first year employers purchased an amount

24. See Table VII-7 for a breakdown of the increment.

Table VII–10

CHANGES IN GOVERNMENT AND NATIONAL INSTITUTION LIABILITIES, 1970-71

(IL million)

	1970	1971			Change in net receipts in 1971
	Net receipts	Loans received	Loans repaid	Net receipts	
A. Foreign loans and credit					
1. Long and medium-term loans					
Independence and Development Loans[a]	475	1,137	443	694	219
U.S. Government loans[b]	1,185	1,099	208	891	−294
Loans from the West German Government	116	169	1	168	52
Loans to the National Institutions	−11	29	57	−28	−17
Other loans	25	45	194	−149	−174
Total	**1,790**	**2,479**	**903**	**1,576**	**−214**
2. Short-term credit (net)	20	168	–	168	148
Total foreign loans and credit	**1,810**	**2,647**	**903**	**1,744**	**−66**
B. Domestic loans and credit					
1. Long- and medium-term loans					
Compulsory Defense Loan	247	448	–	448	101
Other Defense Loans[c]	75	–	–	–	−75
Compulsory Savings Loan	276	586	–	586	310
Absorption Loan	−52	7	74	−67	−15
Bond issues[d]	−39	295	108	187	226
Proceeds of issues deposited with the Treasury and loans from financial institutions	190	435	205	230	40
Total	**697**	**1,771**	**387**	**1,384**	**687**
2. Net short-term credit	338	2	–	2	−336
Total domestic loans and credit	**1,035**	**1,773**	**387**	**1,386**	**351**
C. Net credit from the banking system					
1. Long- and medium-term loans					
From the Bank of Israel	1,170	650	–	650	−520
Bonds purchased by banking institutions	96	106	–	106	10
Total long- and medium-term loans	**1,266**	**756**	**–**	**756**	**−510**
2. Short-term credit					
Changes in deposits with and credit from Bank of Israel	−276	411	–	411	687

Table VII–10 (contd.)

CHANGES IN GOVERNMENT AND NATIONAL INSTITUTION LIABILITIES, 1970-71

(IL million)

	1970	1971			Change in net receipts in 1971
	Net receipts	Loans received	Loans repaid	Net receipts	
Changes in deposits with and credit from banking institutions	71	−64	–	−64	−135
Total short-term credit	**−205**	**347**	–	**347**	**552**
Total credit from banking system	**1,061**	**1,103**	–	**1,103**	**42**
D. Total loans and credit					
1. Long- and medium-term	3,753	5,006	1,290	3,716	−37
2. Short-term (net)	153	517	–	517	364
Grand total	**3,906**	**5,523**	**1,290**	**4,223**	**327**

[a] Before deducting distribution costs.
[b] Including Export-Import Bank loans.
[c] Excluding the Defense Loan issues for banking institutions.
[d] Excluding bonds purchased by the banking system.

equivalent to 4 percent of their gross wage and salary payments, the figure being increased by an additional 2 percentage points in April 1971. This loan also bears 5 percent interest, tax-free, with the principal linked to the cost-of-living index. It will be redeemed in three annual payments, beginning in the fifth tax year.

The growth of receipts from the above-mentioned compulsory loans is explained by several factors: (1) the fact that collections were made during the whole of 1971, whereas in 1970 they began only in the middle of the second quarter; (2) the revision of Compulsory Savings Loan rates; and (3) the increase in private income from economic activity.

Along with the larger revenue from the Compulsory Defense and Savings Loans in 1971, there was a heavier redemption of the Absorption Loan, net payments rising from IL 52 million in 1970 to IL 67 million.

Net sales of other Government and National Institution bonds rose appreciably, amounting to IL 187 million as against a net redemption of IL 39 million in 1970. Sales grossed IL 295 million, of which IL 223 million was in option-type Development Loan issues, IL 31 million in other long-term Government loans, and IL 41 million in Hollis bonds (traded in foreign currency and sold by the Jewish Agency to domestic investors).

Net financial institution loan receipts also rose, from IL 190 million in 1970 to IL 230 million. These consist of the proceeds of bond issues floated by various financial institutions and deposited with the Treasury, as well as proceeds from bond purchases by insurance companies, social insurance funds, and the State Lottery.

It should be noted that the market for new bond issues is controlled by the Government. Since it approves all domestic issues, it is in a position to regulate the volume of its own and other flotations, and is also able to divert the issue proceeds to finance the Government budget or various extrabudgetary projects. Consequently, changes in the volume of Government issues do not always reflect fluctuations in the demand for these bonds, and changes in the volume of proceeds deposited with the Treasury do not necessarily represent changes in the volume of new flotations.

Issues of noncompulsory loans were up strongly in 1971 – IL 1,490 million as contrasted with IL 880 million in 1970. As in 1970, about 45 percent of the proceeds were used for directly financing the Government budget. The Government therefore utilized half of the incremental 1971 bond proceeds to directly finance its budget and the balance to finance various projects through financial institutions.

Net nonbank short-term credit fell precipitately, from IL 338 million in 1970 to only IL 2 million. The appreciable 1970 increase had stemmed from the growth of the Government's debt to contractors and suppliers, and this shrank in the year reviewed.

The public sector's debt to the banking system rose by IL 1,103 million in 1971, compared with IL 1,061 million the year before. Most of the increase was in Bank of Israel loans; this totalled IL 1,061 million (as against IL 894 million in 1970) and consisted of IL 650 million in net long-term loans and IL 411 million in short-term credit. In 1970 the breakdown was different: long-term loans amounted to IL 1,170 million, while Government deposits and other net short-term transactions with the central bank increased by IL 276 million.

Credit from other banking institutions was down from IL 167 million in 1970 to IL 42 million; the latter sum consisted of a IL 106 million increase in banking institution purchases of Government securities and a IL 64 million decline in borrowed receipts. In 1971 the banks took up IL 101 million of the Defense Loan issue floated specifically for them and IL 80 million of the special Development Loan issue. Part of these issues were in turn sold by the banks to other sectors of the economy.

3. *Credit outflow*

In 1971 the Government and the National Institutions provided the other sectors of the economy (including the local authorities) with IL 1,630 million in long-term loans – 14.6 percent more than in 1970. These were given within the framework of the Government and National Institution budgets and do not include loans granted by financial institutions from their bond issue proceeds or other independent resources.

The distribution of these loans by sector of final destination shows that the largest component was that granted for housing, which went up by IL 101 million to IL 930 million.[25] Industrial credit was more than doubled, from IL 80 million in 1970 to IL 197 million, with most of the increment going to industrial finance institutions (this was financed through foreign borrowing).

25. Credit for financing housing is treated as credit to the public, even if part of the publicly sponsored housing has not yet been actually handed over to the buyers or to public housing companies but is being held temporarily by the Government.

Table VII–11

DEVELOPMENT BUDGET LOANS[a] GRANTED BY THE GOVERNMENT AND NATIONAL INSTITUTIONS, BY ECONOMIC SECTOR, 1970-71

(IL million)

	1970	1971	Increase or decrease (–)	
			IL m.	%
Housing[b]	829	930	101	12.2
Agriculture and irrigation	150	184	34	22.7
Mining, quarrying, electricity	72	42	–30	–41.7
Industry and crafts	80	197	117	46.3
Transportation and communications	94	54	–40	–42.6
Tourism	45	63	18	40.0
Services and misc.	98	92	10	10.2
Total[c]	1,367	1,572	205	15.0
To local authorities	56	58	2	3.6
Grand total	1,423	1,630	207	14.6

[a] Including participations in company share capital; excluding investments of the Government and National Institutions.

[b] The entire amount of financing provided for housing is treated as loans to the public, even if part of the public housing has not yet been actually handed over to the buyers or to the public housing companies but is being held temporarily by the Government.

[c] Excluding loans to local authorities.

Loans for agriculture and irrigation rose by 34 percent to total IL 184 million, of which IL 85 million was granted by the National Institutions to agricultural settlements.

Loan capital provided for mining, quarrying, oil pipelines, and electricity was down IL 30 million to IL 42 million; most of the decrease was in loans to the Israel Electric Corporation, which in 1971 obtained its financing directly through sales of the Insurance Companies Loan. This and similar developments in the financing of the various sectors of the economy point to the diminishing weight of direct loans from the Government budget in financing investment, and the corresponding increase in the role of the financial and banking institutions, social insurance funds, and insurance companies. A decline in direct Government lending to a particular sector does not necessarily mean that the public sector granted less financing, but rather that in most cases the direct source of financing has shifted from the development budget to financial institutions.

The sectoral distribution of Government and National Institution loans is presented in Table VII-11.[26]

Collections of Government and National Institution loans totalled IL 200 million (compared with IL 153 million in 1970); this includes IL 187 million on account of Government development budget loans. The Government's outstanding claims arising out

26. The sectoral distribution relates to the final destination of the loans. Most were given through financial intermediaries (see Chapter XVI for the destination and volume of credit channelled through the financial institutions).

of development budget operations added up to IL 6,370 million at the end of March 1971.[27] Of this sum, approximately IL 1,540 million represented investment in shares and bonds (including amounts originally granted as loans but later converted into share capital), while as regards a further IL 820 million no decision has yet been taken whether to treat it as a loan or equity investment. The balance of loans to be collected thus totalled IL 4,010 million at the end of March 1971. Loan collections (excluding the sale of shares) were equal in 1971 to 4.5 percent of total Government loans outstanding on March 31, 1971; this compares with 4 percent in the previous year. It should be noted in this connection that a sizable part of the balance consisted of loans on which only interest is collected or whose redemption date either has not been fixed or has been deferred.

3. THE LOCAL AUTHORITIES

(a) *Operations of the local authorities*[28]

Local authority operations continued to expand in 1971: both consumption and investments were up appreciably, accompanied by a steep rise in the demand surplus. Purchases and transfer payments, which in 1970 had increased by 13.3 percent, rose 26.6 percent this year, notwithstanding the continued freeze on municipal tax rates. This was made possible by the much larger volume of transfers from the Government and National Institutions and by a much heavier borrowing, mainly from the banking system. Tax receipts and other transfers from the public (including various service fees and the participation of property owners in the authorities' expenditure) were up 12.3 percent, compared with 7.4 percent in 1970. This increase, despite the freezing of municipal tax rates, reflects the expansion of those economic activities that affect the magnitude of municipal tax collections, notably developments in the real estate market and housing construction.

Net receipts (including net loans) from the Government and National Institutions were up 28.6 percent to account for 36.5 percent of the authorities' total revenue.

The authorities' expenditure outpaced the growth of their revenue, with the consequence that their demand surplus rose from IL 197 million in 1970 to IL 302 million. Most of the demand surplus increment was financed by way of bank credit, which was up IL 200 million after rising by IL 67 million in 1970. Loans and net credit from the other sectors added up to IL 66 million, as against IL 88 million in the previous year. Most of the decrease was in short-term credit (in the main from contractors and suppliers), whereas net long-term credit (the bulk of it from financial institutions and the State Lottery) was higher in the year reviewed. Net loans from the Government and the National Institutions increased from IL 32 million to IL 36 million. Direct Government loans to the authorities have been declining for a number of years, since the Government is

27. Excluding loans to the National Institutions, local authorities, and the Ports Authority, as well as the amount charged to the National Water Carrier, concerning which it has not yet been decided whether to treat it as a loan to the Mekorot Water Company. In this chapter expenditures on the National Water Carrier and port development have been treated as direct Government investment.

28. Municipalities, local, regional, and religious councils, and regional authorities. Also included are the municipal expenditures of kibbutzim and moshavim (cooperative agricultural settlements).

Table VII–12

DEMAND SURPLUS OF THE LOCAL AUTHORITIES AND ITS FINANCING, 1969-71

(IL million)

	1969	1970	1971	Increase or decrease (–) in 1971	
				IL m.	%
A. Expenditure	762	871	1,078	207	23.8
Consumption	554	640	797	157	24.5
Transfers to households and nonprofit institutions	134	147	184	37	25.1
Interest paid	74	84	97	13	15.5
B. Revenue	824	943	1,131	188	19.9
Taxes	303	313	351	38	12.1
Other domestic revenue	203	229	259	30	13.1
Net transfers from the Government and National Institutions	318	401	521	120	29.9
C. Saving (B – A)	62	72	53	–19	–26.4
D. Purchases on capital account (less sales)	255	259	355	96	37.1
E. Demand surplus (D – C)	**193**	**187**	**302**	**115**	**61.5**
Sources financing the demand surplus					
F. Credit (net)					
Government and National Institutions	42	32	36	4	12.5
Banking system	86	67	200	133	198.5
Other domestic sectors	65	88	66	–22	–25.0
Total	**193**	**187**	**302**	**115**	**61.5**

allocating the proceeds of banking and financial institution security issues to the financing of the authorities' investments, the balancing of their budgets, and consolidation of their loans.

(b) *The "balance of payments" of the local authorities*

The "balance of payments" of the local authorities for 1970/71 is presented in Table VII-13. The table distinguishes between transactions in goods and services, financial transactions, and transactions with the rest of the public sector.

1. Receipts

Tax revenue in 1971 was, at IL 351 million, up 12.1 percent. Municipal rates have hardly risen during the past four years: the "package deal" signed by the Government, General Federation of Labor (Histadrut), and Coordinating Bureau of Economic Organizations (representing the employers) precluded the hiking of municipal taxes in 1970 and 1971, with the Government compensating the authorities by way of larger grants-in-aid. The share of municipal taxes in total revenue (net of credits) is decreasing steadily, standing at 36 percent in 1969, 35 percent in 1970, and 31 percent in 1971.

General rates make up about 40 percent of total municipal tax receipts; the balance consists of collections of the business tax, property tax arrears, local levies by regional councils, and land registry and other fees.

Other compulsory levies (apart from taxes) in 1971 added up to IL 270 million. Approximately 45 percent of this sum represented the participation of property owners in development costs and various current outlays, while another 50 percent represented their participation in the costs of various services provided, including service charges in primary schools and tuition fees in other educational institutions.

The net participation[29] of the Government and the National Institutions in local authority budgets was stepped up by 28.6 percent, from IL 433 million in 1970 to IL 557 million. This participation consists of four items:

(a) General grant-in-aid, comprising the general grant, which is allocated to the local authorities through the Ministry of Interior according to the classification of the authorities;[30] extraordinary grants, provided by the Ministry of the Interior to supplement the authorities' revenue from independent sources and to ease their financial situation; and a sum equal to 21 percent of the Government's income from vehicle license fees and 5 percent of its purchase tax receipts.

Total transfers under this heading rose from IL 115 million in 1970 to IL 191 million. This striking increase resulted in part from the stepping up of extraordinary grants to compensate the authorities for forgoing tax hikes and for their bigger wage outlays (both due to the "package deal"), and also from the increase in Government revenues from the purchase tax and vehicle license fees.

(b) "Shared revenue" – comprising 21 percent of the Government's income from vehicle license fees (identical to the sum appearing under the general grant-in-aid) and about 4.4 percent of its total revenue from taxes and license fees – in return for relinquishing to the Government the collection of the municipal property tax. With the growth of Government tax revenue, these allocations went up from IL 141 million in 1970 to IL 175 million. The shared revenue was allocated to the authorities in proportion to their weight in municipal property tax collections before the Government assumed responsibility for collection and to the number of vehicles owned by their residents.

(c) The participation of the Government and National Institutions in the financing of the local authorities' current operations, mainly the participation of the Ministries of

29. Allocations, grants, and net loans extended, less interest paid to the Government by the local authorities and their participation in various Government outlays.

30. The general grant-in-aid is allocated to the local authorities according to various criteria: the number of inhabitants, the age structure of the population, per capita receipts from various taxes, and per capita expenditure on social welfare. The authorities have been classified into 10 groups according to these criteria, the size of the per capita grant varying according to the group.

Table VII–13

"BALANCE OF PAYMENTS" OF THE LOCAL AUTHORITIES, 1970-71

(IL million)

Receipts	1970	1971	Increase or decrease (–)	Payments	1970	1971	Increase or decrease (–)
			Transfers and transactions in goods and services				
Taxes	313	351	38	Purchases on current account	646	803	157
Misc. revenue	240	270	30	Purchases on capital account	264	360	96
				Interest paid	84	97	13
				Transfers	147	184	37
Total	**553**	**621**	**68**	**Total**	**1,141**	**1,444**	**303**
			Transactions in financial claims				
Long-term loans	143	166	23	Participation in share capital	5	5	–
Loans and credit from the banking system	67	200	133	Repayments on long-term loans	63	75	12
Short-term credit	13	–20	–33				
Total	**223**	**346**	**123**	**Total**	**68**	**80**	**12**
			Transactions with the rest of the public sector				
From the Government and National Institutions							
Net participations	401	521	120				
Net loans	32	36	4				
Total	**433**	**557**	**124**				
Total receipts	**1,209**	**1,524**	**315**	**Total payments**	**1,209**	**1,524**	**315**

Social Welfare, Education, and Religious Affairs in the financing of various social services. In 1971 these disbursements (less various local authority participations in Government expenditure, including interest paid to the Government) amounted to IL 114 million, compared with IL 98 million in 1970.

(d) Loans and grants from the Government development budget and from the Education Fund of the National Institutions for construction and other investment purposes. Net loan receipts rose from IL 32 million in 1970 to IL 36 million, while total grants received dropped from IL 47 million to IL 41 million.

Net credit from sources other than the Government and National Institutions went up from IL 155 million in 1970 to IL 266 million. The bulk of the sum was provided by banking and financial institutions and the remainder by the State Lottery, contractors, and suppliers. The additional net credit in 1971 came from the banking system, while the amount obtained from other sectors fell off.

The much larger volume of bank credit enabled the authorities to expand their demand surplus and in particular their investment spending.

2. Payments

Local authority expenditure, excluding debt repayment, increased by 26.6 percent in 1971 – double the previous year's 13.3 percent – to reach IL 1,444 million.

The authorities' consumption rose 24.5 percent to IL 797 million, of which IL 535 million was payroll outlay. This item was up 23 percent, following a growth of 2.5 percent in personnel and of 20 percent in average pay per employee.

Transfer payments amounted to IL 184 million, of which IL 43 million went to nonprofit institutions (education and health) and IL 140 million to households.

Local authority investment increased by 36.5 percent to IL 360 million. All component items shared in the growth, with the biggest increases being in education – which accounted for over half of the authorities' total investment – and transportation (roads, sidewalks, and traffic regulation) – which accounted for a quarter of the total figure.