CHAPTER V

DOMESTIC INVESTMENT

1. Main Developments

Gross domestic capital formation continued downward in 1967 at an even faster rate than in the previous year, the real decline amounting to nearly 26 percent. Compared with the peak year, 1964, the level was approximately IL 1,200 million lower (at 1966 prices). At current prices, gross capital formation totalled IL 1,863 million in 1967, as against IL 2,504 million in 1966 and some IL 3,000 million in both 1965 and 1964.

Fixed investment shrank by some 20 percent in real terms during the year, while raw material and finished goods inventories were reduced by about IL 66 million. The decrease in gross capital formation occurred principally in residential construction, the figure here being one-third less than in the previous year and only about half of that in 1965. Nondwelling investment fell by 14 percent, following a decline of some 20 percent in 1966.

This striking change in capital formation over the last two years had a twofold effect. First, it tended to reduce both domestic demand and the national product during this period. Investment in 1967 accounted for only about 14 percent of total domestic demand, compared with some 19 percent in 1966 and an average of 25 percent during the years 1960–65. Second, this decline led to a much more sluggish growth of the capital stock in all sectors of the economy, particularly industry. The gross stock of capital asssets, which reflects the economy's productive capacity, expanded by only 5 percent in 1967, compared with 7 percent in 1966 and an average annual rate of some 11 percent during 1960–65. The gross industrial capital stock increased even less in 1967—by a mere 2 percent.

A turning point in investment activity was apparently reached in mid-1967. The figure for the year as a whole thus reflects two contrasting movements: a decline, which had begun in 1965 and gained momentum during the first half of 1967, reaching its nadir in the middle of the year; and an upswing from the third quarter onward, reflecting in the main the recovery from the low level of the war period (see Table V–1 and Diagram V–1). Fixed capital formation in the second quarter, which includes the war and the preceding period of tension, contracted by about 51 percent from the average quarterly level of 1966. All categories of investment reached their lowest point in this period —residential and other construction, machinery, equipment, and vehicles. The

Table V–1

GROSS DOMESTIC INVESTMENT, QUARTERLY, 1964–67

(Index: quarterly average for 1966=100)

	Quarter	Total gross domestic investment	Domestic investment excl. ships and aircraft	Dwellings	Non-residential construction	Machinery, equipment, motor vehicles[a] and inventories
1964	I	124	113	111	106	122
	II	120	117	114	112	126
	III	124	121	119	119	125
	IV	123	120	122	122	117
1965	I	126	121	134	122	108
	II	124	119	127	112	120
	III	119	120	120	125	114
	IV	116	118	118	115	122
1966	I	121	118	113	116	124
	II	97	100	107	98	96
	III	97	96	94	98	95
	IV	86	86	87	88	85
1967	I	79	73	73	96	51
	II	51	48	49	69	25
	III	85	85	75	94	86
	IV	80	87	73	97	90

[a] Excluding ships and aircraft.
SOURCE: Central Bureau of Statistics.

moderate expansion during the third and fourth quarters brought up the level of fixed investment (other than in ships and aircraft) to that at the end of 1966.

The changing trend of gross capital formation should be viewed in the light of the rapid and steady expansion during the years 1956–64, when real investment grew at an overall annual rate of some 12 percent, reaching a record 25 percent in 1964. An accumulation of unutilized assets became discernible at the end of 1964 and the beginning of 1965; nevertheless, construction activity was stepped up because of anxiety lest the Government impose building curbs. Together with the faster increase in the supply of capital assets, various factors operated in the last two years to dampen investment demand:

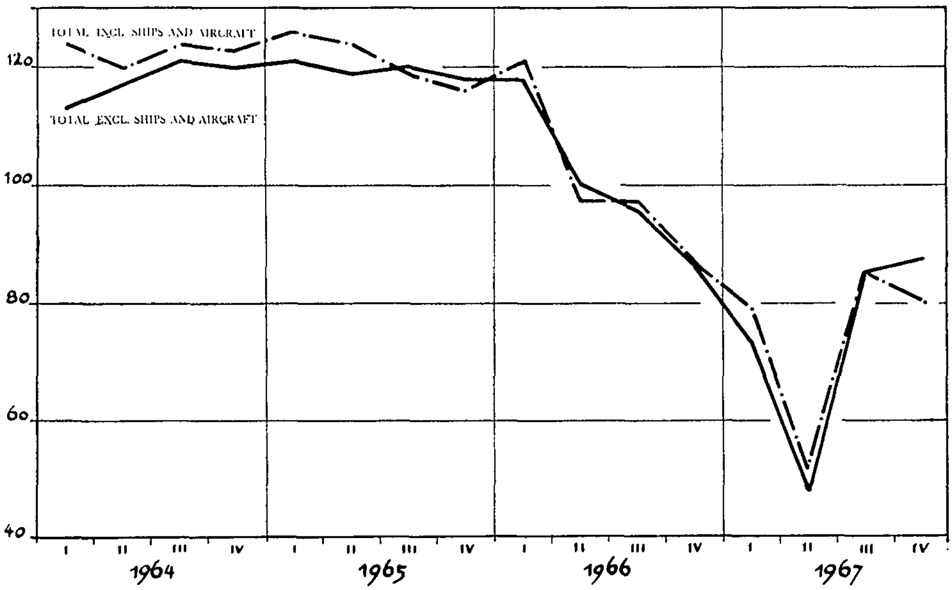
1. The contraction of immigration[1] reduced, both directly and indirectly,

[1] Net immigration in 1967 came to about 4,000, compared with approximately 8,000 in 1966, 20,000 in 1965, and 50,000 per annum during 1961–64.

Diagram V-1

GROSS DOMESTIC INVESTMENT, QUARTERLY, 1964–67

(quantity index: quarterly average 1966=100)



the demand for housing, various public buildings, and capital assets for supplying the additional demand generated by immigrants.

2. The smaller volume of private transfers from abroad for investment purposes depressed the demand for investment in housing and in other economic sectors. In 1967 total lump-sum personal restitution payments from Germany[1] were about 45 percent less than in 1964, since which they have declined continuously. Private capital transfers from abroad for nondwelling investment purposes plummeted by nearly 73 percent in 1967 to stand at only 14 percent of their 1964 level.

These factors too helped to create a surplus of various types of buildings—such as homes, industrial structures, commercial premises, and offices—which lasted until 1967.

Added to these constraining factors in 1966 was the Government's economic retrenchment policy, which sought to reduce investments mainly by trimming the development budget and deferring or preventing the launching of big projects. In 1967, particularly the second half, the Government began to reverse its policies: the development budget was increased and the execution of projects

[1] Total restitution received less current pensions. The amount of nonrecurrent restitution income invested in dwellings was estimated in savings surveys at about IL 200 million in 1964 and IL 120 million in 1967.

speeded up with a view to halting the recession and the idleness of productive factors. Capital formation in the public sector was 5 percent larger in 1967 than the year before. Moreover, the sector financed a much larger volume of private investment.

Private investment, on the other hand, continued downward in 1967. This trend was apparently due mainly to the drop in aggregate domestic demand, and to the belief, which persisted until the middle of the year, that the recession would continue and that profitability was unlikely to improve. Presumably the decline in profitability in 1966, and perhaps also the slower growth of output[1] in the private sector, strongly colored the outlook of investors.

Government measures to stimulate private investment mainly took the form of an amended Law for the Encouragement of Capital Investments and an increase in direct lending to the private sector. Under the amended law, an investor in an approved enterprise is now entitled to receive a grant amounting up to a third of the value of his investment (in machinery and equipment) in a development area, as well as to obtain development loans at a low interest rate.[2] The Government in fact subsidizes fixed investments to a not insignificant extent, thereby diminishing the risks from the investor's point of view. However, the grant may also result in investments which are more capital-intensive than is worthwhile for the economy as a whole. This apparently cannot be avoided if, under existing circumstances, the objectives of the law are to be achieved—namely, an increase in investment and the channelling of investment to development areas and to export branches. The amendments were approved in the first quarter of 1967 and applied retroactively from July 1, 1966, but presumably their contribution to investment activity will actually begin to be felt only after a fairly extended period, even if the war had not intervened.

The downtrend in investment, which marked 1966 and carried over into the early months of 1967, gained momentum during the period of prewar tension and hostilities. With the general call-up in May and June, all activities not connected with the security effort were shelved. Investment is one of the first to be affected by a climate of uncertainty and political instability. Thus, there were stoppages in the erection of buildings and in other construction jobs, as well as in the production and import of machinery and equipment.

[1] The decline in construction output in recent years resulted in the reduction of building equipment outlay by about three-quarters in 1966–67 as compared with 1962–65.

[2] To receive "approved enterprise" status, the concern must be sited in a development area and/or earmark over half of its output for export. In addition to the direct grant and loans mentioned above, an approved enterprise is exempt from indirect taxes on capital assets, and is entitled to an accelerated depreciation allowance for tax purposes, to Government participation in the cost of training workers, and to various other benefits such as exemption from income tax for the first five years in which it is liable to tax.

Table V-2

GROSS AND NET INVESTMENT, 1961–67

(IL million)

	1961	1962	1963	1964	1965	1966	1967[a]	Percent increase or decrease (–) as against preceding year					
								1962	1963	1964	1965	1966	1967
At current prices													
Gross fixed nondwelling investment	968	1,225	1,455	1,892	1,952	1,613	1,401[a]	30	16	30	3	–17	–13
Gross investment in dwellings	472	687	726	866	974	781	528	46	6	19	12	–20	–32
Change in inventories	92	125	103	182	86	110	–66	36	–18	77	–53	28	—
Total gross investment	1,532	2,067	2,284	2,940	3,012	2,504	1,863	35	10	29	2	–17	–26
Less: Depreciation	438	631	765	878	1,022	1,144	1,240	44	21	15	16	12	8
Net investment	1,094	1,436	1,519	2,062	1,990	1,360	623	31	6	36	–3	–32	–54
At 1966 prices													
Gross fixed nondwelling investment	1,420	1,472	1,604	1,998	1,981	1,613	1,389	4	9	25	–1	–19	–14
Less: Depreciation	472	550	631	701	790	871	939	17	15	11	13	10	8
Net fixed nondwelling investment	948	922	973	1,297	1,191	742	450	–3	6	33	–8	–38	–39
Gross investment in dwellings	657	828	819	909	974	781	528	26	–1	11	7	–20	–32
Less: Depreciation	170	187	207	227	250	273	290	10	11	10	10	9	6
Net investment in dwellings	487	641	612	682	724	508	238	32	–5	11	6	–30	–53
Total gross fixed investment	2,077	2,300	2,423	2,907	2,955	2,394	1,917	11	5	20	2	–19	–20
Change in inventories	108	137	107	185	84	110	–62	27	–22	73	–55	31	—
Total gross investment	2,185	2,437	2,530	3,092	3,039	2,504	1,855	12	4	22	–2	–18	–26
Less: Depreciation	642	737	838	928	1,040	1,144	1,229	15	14	11	12	10	7
Total net investment	1,543	1,700	1,692	2,164	1,999	1,360	626	10	—	28	–8	–32	–54

[a] Excluding investments in East Jerusalem, which totalled approximately IL 5 million in 1967.
SOURCE: Central Bureau of Statistics and Bank of Israel.

After the war, both direct[1] and indirect investment demand revived, owing chiefly to the greater security needs and to expectations of a rise in overall domestic demand. Factors working in this direction were Ministry of Defense orders placed with local industry in order to replenish stocks, meet new requirements, and substitute for imports; the increase in the country's population due to the unification of Jerusalem; the expansion of trade with the administered areas; and expectations of a growth of tourism. It also became necessary to replace various types of vehicles (buses and trucks) and equipment which were damaged or became worn out during the war. The revival of economic activity during this period, however, had only a slight effect on actual investments in 1967, owing to the time-lag between the planning of an investment and its implementation. Together with the abnormal demand of the postwar period, the second half of 1967 saw the initial results of the Government's countercyclical policy with regard to investment, aimed primarily at providing more jobs. As a result, there was a sizable increase in capital outlay on roads and highways, construction connected with the repair of war damage, other types of Government construction, afforestation, land reclamation, and posts and telecommunications.

Net capital formation[2] declined to IL 630 million in 1967—i.e. about one-third of gross capital formation during the year and approximately half the net investment of 1966. This reflects both the sharp drop in gross investment and the rise in estimated depreciation, which is a function of the economy's capital stock and its composition. In 1967 net industrial capital formation was, for the first time, of a negative magnitude. In other words, the potential productive capacity of this sector apparently decreased during the year. Gross industrial investment contracted by some 30 percent in both 1966 and 1967. On the other hand, the 1967 depreciation estimate for the industrial sector exceeded gross investment by 26 percent.

Since 1965 the expansion of the country's capital stock[3]—which reflects the current productive capacity of the economy—has been slowing down. The deceleration was particularly conspicuous in industry and agriculture, where the

[1] Direct investment in East Jerusalem during the second half of 1967 totalled some IL 5 million. The war was also directly responsible for investment in land reclamation in the Ayalon Valley, in road and highway construction, in the rebuilding of damaged property, etc. Investment in the administered areas is not considered part of domestic capital formation in Israel.

[2] Investment net of depreciation measures the change in the potential productive capacity of the country's capital assets until the end of their economic life-span.

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

growth rate came to only 2–3 percent in 1967, in contrast to an average of 6 and 10 percent p.a. respectively during 1960–65.

The smaller percentage increase in the real capital stock was accompanied by a decline in employment of some 5 percent in 1967. Consequently, capital stock per gainfully employed still increased, and more rapidly than in previous years—by 12 percent as against an average of about 7 percent p.a. during 1960–65 (see Table V–14).

The reduction of employment and national product due to the contraction of investment can be primarily attributed to the high domestic output component of construction outlay. On the other hand, about two-thirds of the expenditure on machinery and equipment represents direct import. Rough indicators show that since 1962 the proportion of equipment undergoing some form of processing in Israel has been on the rise. The higher relative price of imported equipment due to the devaluation of November 1967 should encourage the continuation of this trend.

Gross national saving declined even more sharply in 1967 than did investment, so that the capital inflow accounted for a higher proportion of total capital formation than in previous years. In 1967 gross national saving financed only some 32 percent of investment, as against 49 percent approximately in 1965 and 1966.

2. Investment, by Type of Investor[1]

The decline in fixed nondwelling investment in 1967 occurred entirely in the private sector, the capital outlays of the public sector and public sector companies increasing by 5 percent. This brought up the weight of the public sector from about 46 percent of total fixed nondwelling capital formation in 1966 to approximately 56 percent during the year reviewed (see Tables V–3 and V–4). During the years 1962–65 its share ranged from 44 to 49 percent. The striking increase in 1967 reflects both the larger weight of industries wholly under public ownership, such as electric power and minerals, and the increased share of public investments in every other economic sector except industry.

Almost all direct investments of the Government, its companies, the local authorities, and the National Institutions are infrastructural in nature, designed to improve transportation and communications and to expand various public services. A policy of advancing the implementation of development projects was introduced at the end of 1966, but was actually applied only in 1967—primarily in the second half of the year. These projects included the paving of roads, land reclamation and conservation, afforestation, the extension of the telephone network, and the erection of public buildings. Some of these projects absorbed

[1] The reference is to the sectors purchasing the capital assets, i.e. the final owner. See also the notes to Table V–3.

Table V-3

GROSS FIXED INVESTMENT, BY TYPE OF INVESTOR AND INITIATING SECTOR, 1962–67

(IL million, at 1966 prices)

	1962	1963	1964	1965	1966	1967	Percent increase or decrease (–) as against preceding year				
							1963	1964	1965	1966	1967
Nondwelling investment, by investing sector											
Government, local authorities, and National Institutions	212	259	302	356	298	322	22	17	18	–16	8
Government enterprises[a]	105	117	191	214	181	164	11	63	12	–15	–9
Public sector companies[b]	405	341	430	297	256	288	–16	26	–31	–14	13
Total public sector investment	722	717	923	867	735	774	–1	29	–6	–15	5
Nonprofit institutions	84	116	134	131	160	127	38	16	–2	22	–21
Private business enterprises[c]	666	771	941	983	718	488	16	22	4	–27	–32
Total private sector investment	750	887	1,075	1,114	878	615	18	21	4	–21	–30
Total nondwelling investment	1,472	1,604	1,998	1,981	1,613	1,389	9	25	–1	–19	–14
Investment in dwellings, by initiating sector											
Public	390	310	338	353	263	153	–21	9	4	–25	–42
Private	438	509	571	621	518	375	16	12	9	–17	–38

[a] The trading enterprises of the public sector, including the Post Office, Israel Railways, air and sea ports, and local authority enterprises.
[b] Companies in whose management the public sector has the decisive voice. Excluding investment in industrial companies of the defense establishment.
[c] Calculated as a residual.
SOURCE: 1962–65—Central Bureau of Statistics, after adjusting for differences in definitions; 1966–67—Bank of Israel estimates.

many relief workers in 1967, whose numbers averaged four times more than in 1966.

Public sector companies invest chiefly in mining and quarrying, electric power, water projects, shipping, and civil aviation. Here there were two striking changes in 1967: capital outlay in mining and quarrying expanded considerably with the execution of the second stage of the Dead Sea Works expansion program; on the other hand, investment in shipping and civil aviation fell off, owing chiefly to the sale of the s.s. Shalom.

Nonprofit institution investment is made entirely in the services sector, for the most part in health services, higher education, and research institutions. To a large extent, it is apparently determined by the scale of the institutions' transfers from abroad. Transfers from the public sector are utilized for financing their current expenditure.

The weight of private investments is particularly large in industry, construction, commerce, hotels, farming, commercial vehicles, and in 1967 also in ships. The decisive consideration guiding private businesses in their investment decisions is the prospect of future profits. This, in turn, depends partly on past and present profitability, as well as on the general trend of economic activity as reflected by output and sales. The sharp contraction of private investment in the last two years (by some 20 percent in 1966 and another 30 percent in 1967) is consistent with the sharp drop in profitability in 1966 and the standstill in the national product in the last two years. Since 1965 private capital transfers from abroad for investment purposes have fallen steadily. The year reviewed saw an upswing in profitability[1]—the return per unit of capital recovered from its steep drop in 1966 to regain the preceding year's level. With the increase in demand and the national product toward the end of the year, private investment also began to revive. Expectations that profitability would continue to improve were also awakened during the year by the relative stability of prices and wages, which, together with the rise in productivity, brought down unit production costs, after these had risen appreciably in previous years.

Most dwelling investments pass into the final ownership of households. But here greater significance attaches to a classification by initiating sector.[2] According to this classification, the weight of the private sector in dwelling investment increased in 1967, in contradistinction to the trend in nondwelling investment. The proportion of residential construction initiated by public bodies declined from 34 percent in 1966 to 29 percent. In preceding years the share of the public sector was greater still: in 1962, for instance, almost half of all such construction was initiated by the Ministry of Housing. The precipitate drop of

[1] See Chapter II, "Resources, Uses, and Incomes", Table II–10.

[2] Defined here as the sector responsible for the planning (determination of site, standard, and area) and supervision of construction. As a rule, it also finances a large percentage of the total cost. Most of the housing projects put up by the public sector are sponsored by the Ministry of Housing.

Table V–4

GROSS FIXED INVESTMENT, BY TYPE OF INVESTOR AND INITIATING SECTOR, 1962–67

(percentages)

	1962	1963	1964	1965	1966	1967
Nondwelling investment, by investing sector						
Government, local authorities, and National Institutions	14	16	15	18	19	23
Government enterprises	7	8	10	11	11	12
Public sector companies	28	21	21	15	16	21
Total public sector investment	49	45	46	44	46	56
Nonprofit institutions	6	7	7	6	10	9
Private business enterprises	45	48	47	50	44	35
Total private sector investment	51	55	54	56	54	44
Total nondwelling investment	100	100	100	100	100	100
Investment in dwellings, by initiating sector						
Public	47	38	37	36	34	29
Private	53	62	63	64	66	71
Total	100	100	100	100	100	100
Total public sector investment	48	42	43	41	42	48
Total private sector investment	52	58	57	59	58	52
Total fixed investment	100	100	100	100	100	100

Source: Table V–3.

nearly 42 percent in 1967[1] was due chiefly to the accumulation of a stock of unsold dwelling units as from 1964/65 because of smaller immigration. About half of all publicly initiated construction has been earmarked in recent years for immigrant absorption. The decline in the public sector's investment in housing in 1967 was actually even greater than indicated above, since it purchased a large number of units from the private sector.

Adding up all private investment in the economy, including privately-initiated residential construction, shows a decrease of more than IL 400 million in the year reviewed. The public sector was responsible for only IL 70 million of the

[1] In contrast to total public sector investment in housing, the data on residential building starts show a rise of 11 percent in publicly sponsored housing, whereas the figure for private building fell by 35 percent (see Chapter XIII, "Construction and Housing").

Table V-5

SHARE OF FIXED NONDWELLING INVESTMENT FINANCED BY PUBLIC SECTOR,[a] 1962–67

(percentages)

	1962	1963	1964	1965	1966	1967
Agriculture	23	24	24	23	22	26
Irrigation	100	100	100	100	100	100
Industry and construction[b]	10	8	13	7	8	2
Electric power	100	100	100	100	100	100
Mining and quarrying	100	100	100	100	100	100
Transportation and communications	63	46	56	56	66	78
Commerce and services	42	45	42	40	33	50
Total	49	45	46	44	46	56

[a] Including the Government, local authorities, National Institutions, Government enterprises, and public sector companies.
[b] Excluding investment in industrial companies of the defense establishment.

overall decline in capital expenditure, and this entirely because of the smaller investment in publicly-initiated housing projects.

3. Investment, by Economic Sector

The most striking change in the sectorial distribution of gross domestic capital formation in 1967 was the decline in the weight of housing from some 33 percent in previous years to 28 percent. Most of the increase in the nondwelling investment occurred in agriculture, irrigation, mining and quarrying, and the services. The relative share of electric power and the transportation and communications sector held steady, while that of industry continued downward (see Table V–8). This falling trend in industry (including construction equipment) has been in evidence for several years. Its weight averaged some 15 percent during 1960–63, dropping to 11 percent in 1966 and 10 percent in 1967. The private sector accounts for the preponderant share of industrial and construction investments, and these are affected by the factors mentioned above as explaining the general decline in the proportion of private capital formation.

The decline in investment demand in the last three years also occurred chiefly in industry and construction, total capital spending here dropping 48 percent (at constant prices) from the record level of 1964.[1] The decline affected industry, mining and quarrying, and construction machinery and equipment.

Real investment in transportation, exclusive of communications, also fell

[1] See also Chapter XII, "Industry", section 4.

Table V-6

REAL CHANGES IN GROSS FIXED NONDWELLING INVESTMENT, BY ECONOMIC SECTOR, 1961-67

(percent increase or decrease (–) as against preceding year)

	Agri-culture[a]	Irri-gation	Industry and con-struction	Mining and quarry-ing	Electric power	Trans-portation[b]	Commerce, services, and com-munications	Total	Total, excl. ships and aircraft
1961	-6	13	17	78	—	54	13	19	16
1962	-6	39	-3	85	46	-19	8	4	12
1963	-12	5	15	11	-22	17	16	9	11
1964	10	-37	12	4	-4	75	32	25	17
1965	-12	-13	1	-41	71	-12	11	-1	4
1966	-9	3	-34	-25	-18	-30	-6	-19	-17
1967	9	-12	-29	11	-14	-17	-13	-14	-14

[a] Including capital assets from farm output.
[b] Excluding posts and communications.
SOURCE: Table V-7, part B.

between 1964 and 1967 by a substantial 49 percent approximately. The amount expended on roads went up 33 percent during this period to reach IL 104 million (at 1966 prices). On the other hand, purchases of commercial vehicles were down approximately 55 percent, and investment in ships and aircraft by some 75 percent. The latter type of investment generally displays sharp fluctuations from year to year, it being largely a matter of chance that a big ship will be acquired or sold in a certain year. But while the magnitude of the decrease is of little significance, there can be no doubt that the downward trend over these three years was connected with the low profitability of shipping, and in particular with the big losses incurred by the passenger branch[1] (see Table V-9).

Investment in agriculture and irrigation has shrunk by approximately 15 percent since 1964. The decrease in the irrigation item reflects the completion of most of the work on the National Water Carrier. As to agriculture, investment expanded by 9 percent during the year, but if the change in the livestock inventory is discounted, the figure was the same as in 1966.[2] The weight of unemployment relief projects in agricultural investment increased in 1967 as a result of Government steps to regulate employment. The downward trend in agricultural investment has persisted for the past ten years. Its main cause is apparently the rapid expansion of farm supply, coupled with a relatively slow growth

[1] The sale of the s.s. Shalom at the end of 1967 for approximately IL 45 million, as well as the sale of the passenger ships Zion and Israel in 1966, suggest the source of the smaller investment here.

[2] The estimate probably has an upward bias. See also Chapter XI, "Agriculture", section 5.

Table

GROSS DOMESTIC NONDWELLING INVESTMENT,

(IL

	1962	1963	1964	1965		
				Buildings	Equipment	Farm output
						At current
Agriculture	137	130	152	29	46	69
Irrigation	111	124	82	59	16	
Industry and construction	275	337	387	123	281	
Mining and quarrying	65	76	82	32	18	
Electricity	76	64	63	37	75	
Transportation[a]	237	283	517	171	294	
Ships and aircraft	*66*	*50*	*175*		*92*	
Motor vehicles	*102*	*140*	*181*		*184*	
Other items	*69*	*93*	*161*	*171*	*18*	
Commerce, services, and posts[b]	354	441	609	458	244	
Total	1,255	1,455	1,892	909	974	69
						At 1966
Agriculture	179	157	173	29	47	76
Irrigation	129	136	86	59	16	
Industry and construction	318	365	408	123	288	
Mining and quarrying	76	84	87	32	19	
Electricity	89	69	66	36	77	
Transportation[a]	262	306	537	173	297	
Ships and aircraft	*66*	*50*	*175*		*92*	
Motor vehicles	*112*	*150*	*190*		*186*	
Other items	*84*	*106*	*172*	*173*	*19*	
Commerce, services, and posts[b]	419	487	641	459	250	
Total	1,472	1,604	1,998	911	994	76

[a] Excluding posts and communications.
[b] Investment in posts is generally listed under transportation, but because of statistical difficulties encountered this year in separating Post Office equipment from that for services,

V–7

BY ECONOMIC SECTOR AND TYPE OF ASSET, 1962–67

million)

	1966				1967			
Total	Buildings	Equipment	Farm output	Total	Buildings	Equipment	Farm output	Total
prices								
144	31	47	61	139	34	44	79	157
75	63	14		77	51	17		68
404	71	201		272	40	155		195
50	20	18		38	34	8		42
112	39	54		93	33	48		81
465	124	206		330	138	138		276
92		*47*		*47*		*46*		*46*
184		*137*		*137*		*85*		*85*
189	*124*	*22*		*146*	*138*	*7*		*145*
702	425	239		664	349	233		582
1,952	773	779	61	1,613	679	643	79	1,401
prices								
152	31	47	61	139	34	43	75	152
75	63	14		77	51	17		68
411	71	201		272	41	153		194
51	20	18		38	34	8		42
113	39	54		93	32	48		80
470	124	206		330	139	135		274
92		*47*		*47*		*45*		*45*
186		*137*		*137*		*83*		*83*
192	*124*	*22*		*146*	*139*	*7*		*146*
709	425	239		664	349	230		579
1,981	773	779	61	1,613	680	634	75	1,389

it was necessary to combine these two items.
SOURCE: Central Bureau of Statistics.

Table V-8

GROSS AND NET DOMESTIC INVESTMENT, BY ECONOMIC SECTOR, 1961–67

(percentages)

	Agriculture	Irrigation	Industry and construction	Mining and quarrying	Electricity	Transportation[a]	Commerce, services, posts	Total non-dwelling investment	Dwellings	Total domestic investment
Gross investment										
1961–63	8	5	15	3	3	13	19	66	34	100
1964	6	3	14	3	2	19	22	69	31	100
1965	5	2	14	2	4	16	24	67	33	100
1966	6	3	11	1	4	14	28	67	33	100
1967	8	4	10	2	4	14	30	72	28	100
Net investment										
1961–63	5	6	13		2	13	23	62	38	100
1964	3	3	12		1	20	27	66	34	100
1965	1	2	10		3	16	30	62	38	100
1966	1	3	1		3	11	40	59	41	100
1967	2	4	–9		3	9	57	66	34	100
Ratio of depreciation to total investment										
1961–63	57	23	50		57	34	18	37	24	33
1964	67	41	52		74	25	17	35	25	32
1965	81	49	60		45	36	19	40	26	35
1966	94	49	94		60	60	24	54	35	48
1967	89	59	126		75	78	32	67	55	64

NOTE: In the series on net investment, the mining and quarrying sector was combined with industry and construction because of difficulties in calculating separate depreciation estimates.

[a] Excluding investment in communications and posts, which is classified with commerce and services.

of demand.[1] At the same time, the relative profitability of branches accounting for the bulk of farm investments, such as orchards, may have declined. The capital outlays made necessary by the expansion of export crops in recent years (such as the erection of hothouses) do not alter the general picture because of the small weight of such expenditure (the amount spent on hothouses came to only IL 11 million in the last three years—see Table V–10).

Table V–9

GROSS INVESTMENT IN TRANSPORTATION,[a] 1960–67

(IL million, at 1966 prices)

	1960	1961	1962	1963	1964	1965	1966	1967
Railway	3	6	4	5	12	17	17	13
Ports	11	13	25	31	67	60	40	12
Roads[b]	26	38	42	59	78	96	75	104
Other investment	7	13	13	11	15	19	14	17
Subtotal	47	70	84	106	172	192	146	146
Motor vehicles	*55*	*86*	*112*	*150*	*190*	*186*	*137*	*83*
Passenger cars and commercial vehicles	*43*	*73*	*16*	*130*	*166*	*162*	*114*	*71*
Buses	*12*	*13*	*96*	*20*	*24*	*24*	*23*	*12*
Ships	108	131	16	50	173	94	28	31
Aircraft	—	36	50	—	2	–2	19	14
Total	210	323	262	306	537	470	330	274

[a] Excluding posts and communications (see note[b] to Table V–7).
[b] Including local authority investment in traffic equipment, sidewalks, etc.
[c] Airports, oil and gas pipelines, storage, etc.
SOURCE: Central Bureau of Statistics.

Investment in the commerce and services sector, including posts and communications, has fallen off by 10 percent since 1964. Expenditure on Post Office services did not contract during this period, so that the decline in commerce and services was even sharper, most of it taking place in 1967. The smaller amount expended on business premises and personal services accounted for the greater part of the decrease.

The only sector where investment expanded between 1964 and 1967 was electric power generation. However, the 21 percent increase here was due to the abnormally low level of capital expenditure in 1964. Compared with 1966, the figure fell by some 14 percent in the year reviewed, after having averaged approximately IL 100 million per annum (at 1966 prices) in 1965

[1] See also Chapter XI, "Agriculture", section 1.

Table V-10

GROSS INVESTMENT IN AGRICULTURE, 1960–67

(IL million, at 1966 prices)

	Orchards	Land reclamation, afforestation, drainage, etc.	Farm buildings and local irrigation networks	Machinery and equipment	Livestock	Total
1960	48	49	55	43	7	202
1961	47	37	43	50	13	190
1962	48	38	37	44	12	179
1963	46	36	39	36	—	157
1964	45	40	36	49	3	173
1965	41	33	29	47	2	152
1966	32	28	31	47	1	139
1967	25	37	34	43	13	152

SOURCE: Central Bureau of Statistics.

and 1966. Investment in this sector depends on both the continued extension of the national grid and the launching of special large-scale projects, such as the erection of new power stations.

4. PRICES

Investment prices edged up only 1 percent, the same rate as in 1966. This rise resulted from the higher cost of imported machinery and equipment, which in turn was due mainly to the devaluation in November.

Construction prices have apparently remained stable since 1965, despite the marked easing of demand for such investments.[1] According to the index of construction input prices, materials cost somewhat more in 1967, but this was apparently offset by a decrease of about 1 percent in wages. It should be pointed out, however, that this index does not reflect actual payroll expenditure but only official wage rates. Presumably the fall in wages was really greater, since all bonuses over and above the official wage tariff still being paid in 1966 were abolished in the year reviewed. Contractors' profits are not reflected by this index.

5. CAPITAL STOCK

The composition of the incremental gross capital stock in 1967 conformed to the long-run sectorial pattern. The most conspicuous change has been the declining weight of the capital stock in agriculture, and in recent years in

[1] See also Chapter XIII, "Construction and Housing", section 5.

Table V–11

GROSS FIXED INVESTMENT, BY TYPE OF ASSET, 1962–67

(IL million, at 1966 prices)

	1962	1963	1964	1965	1966	1967	Percent increase or decrease (–) as against preceding year				
							1963	1964	1965	1966	1967
Dwellings	828	819	909	974	781	528	–1	11	7	–20	–32
Nonresidential buildings	265	329	402	472	410	308	24	22	17	–13	–25
Other construction work	389	435	459	439	363	372	12	6	–4	–17	2
Total new construction	1,482	1,583	1,770	1,885	1,554	1,208	7	12	6	–18	–22
Assets from farm output	98	82	98	76	61	75	–16	20	–22	–20	23
Machinery and equipment	542	558	674	716	595	506	3	21	6	–17	–15
Motor vehicles	112	150	190	186	137	83	34	27	–2	–26	–39
Ships and aircraft	66	50	175	92	47	45	–24	250	–47	–49	–4
Total fixed investment	2,300	2,423	2,907	2,955	2,394	1,917	5	20	2	–19	–20

Source: Central Bureau of Statistics.

Table V–12

GROSS CAPITAL STOCK, BY ECONOMIC SECTOR, 1967

(IL million, at 1966 prices)

	Capital stock at end of 1966	Gross investment in 1967	Discards in 1967	Incremental capital stock in 1967	Capital stock at end of 1967	Weight in total capital stock (%)		Change in weight, 1959–67 (%)	Weight in incremental capital stock in 1967 (%)
						End-1959	End-1967		
Agriculture	3,307	152	63	89	3,396	22	16	–6	9
Irrigation	1,546	68	5	63	1,609	9	8	–1	7
Industry and construction[a]	4,699	236	158	78	4,777	26	23	–3	8
Electric power	1,210	80	20	60	1,270	7	6	–1	6
Transportation and communications	4,269	404[b]	124	280	4,549	18	22	+4	29
Commerce and services	4,682	449	49	400	5,082	18	25	+7	41
Total nondwelling capital stock	19,713	1,389	419	970	20,683	100	100	—	100
Dwellings	11,686	528	13	515	12,201				
Total stock of fixed assets	31,399	1,917	432	1,485	32,884				

[a] Including industry, construction, mining and quarrying.

[b] Including estimated investment in posts. The magnitude of the error in the sector's capital stock likely to result from this rough estimation is fairly small.

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

industry as well. This reflects the steep drop in the share of these sectors in total gross investment during the years 1960–67, and the relatively high proportion of discards in these sectors.[1] During 1960–67 the weight of the agricultural capital stock moved down from 22 percent of the total to 16 percent, while industry showed a decline from 26 to 23 percent (see Table V–12). On the other hand, the relative weight of infrastructural assets—such as roads, posts and communications, ports, and various public buildings—increased.

The value of assets scrapped amounted to 40 percent of gross capital formation in agriculture and nearly two-thirds of that in industry. As a result of the high proportion of discards and the relatively small volume of investment, these two sectors together accounted for only 17 percent of the total incremental non-dwelling capital stock. The high rate of discards in agriculture and industry in recent years can be ascribed mainly to the obsolesence of machinery and equipment purchased in the mid-1950's, when over 50 percent of all equipment expenditure was made by these two sectors. Discards in other sectors amounted to 30 percent of the 1967 investment, compared with approximately 25 percent the year before.

The real increase of some 5 percent in gross capital stock consists of a growth of 7–9 percent in transportation and communications, commerce, and the services, and about 2 percent in agriculture and industry. The long-run significance of this slow growth rate lies in the diminished possibility of expanding the national product in the future. At the same time, it should be noted that the sluggish growth of output during the recession increased the percentage of unexploited production capacity in the economy. The unutilized capital stock apparently decreased toward the end of 1967, due to the greater exploitation of available production capacity in the second half of the year, which resulted in the re-employment of at least part of the equipment idle in 1966.[2] This development was the outcome of the intensive use made of all types of heavy equipment and road vehicles during the war, as well as of the general revival of demand in the second half of 1967.

In recent years stress has been laid on the need to step up industrial exports while expanding production for the domestic market only moderately. However, during this period the number of gainfully employed in industry decreased, while the sector's capital stock expanded only very slightly. Even if we assume that all of this increase was in export production, it was insufficient to assure a sizable expansion of such capacity. In the short run, output can be expanded

[1] The value of discards, which represents assets withdrawn from use because of obsolesence, is based on the estimated economic life of various types of assets. The estimate for any given year is of limited significance and indicates orders of magnitude only. For additional reservations and explanations concerning this term and others used here, see A. L. Gaathon, *Capital Stock, Employment and Output in Israel, 1950–1959,* Bank of Israel, 1961, Ch. 1.

[2] The percentage increase in the national product in the last quarter of 1967 far outstripped that in the capital stock and the labor input.

Table V-13

GROWTH OF REAL CAPITAL STOCK, BY ECONOMIC SECTOR, 1960–67

(percentages)

	Agriculture	Agriculture and irrigation	Industry and construction	Electric power	Transportation and communications	Commerce and services	Total non-dwelling capital stock	Dwellings	Total fixed assets
1960	8	8	11	7	11	17	11	8	10
1961	7	8	12	7	17	17	12	9	11
1962	7	8	14	10	12	15	12	11	12
1963	5	7	12	7	12	16	11	10	10
1964	5	5	9	6	21	16	12	10	11
1965	4	4	5	10	16	15	9	9	9
1966	3	3	2	8	9	12	7	7	7
1967	3	3	2	5	7	9	5	4	5

SOURCE: See source to Table V-12.

Table V–14

GROWTH OF REAL CAPITAL STOCK PER GAINFULLY EMPLOYED,[a] BY ECONOMIC SECTOR, 1961–67

(percentages)

	Agriculture and irrigation	Industry, water, electricity	Transportation and communications	Commerce and services	Total non-dwelling capital stock[b]	Dwelling stock per capita
1961	7	3	8	12	6	3
1962	9	2	12	11	6	7
1963	11	6	6	8	7	6
1964	6	6	4	10	6	6
1965	6	7	17	11	8	5
1966	9	11	17	11	10	8
1967	11	13	–1	17	12	5

[a] Data on capital stock relate to the beginning of the year, while the number of gainfully employed is an annual average.

even without taking on additional hands or enlarging the capital stock, by a greater utilization of existing production capacity and introducing technological improvements. But the extent to which this can be done is inherently limited, especially if account is taken of the situation in 1967, when at least part of the capacity idle in 1966[1] was utilized. Thus a marked slowdown in the growth of industrial capital stock may hamper the rapid expansion of industrial output and exports in the years ahead.

6. Investment in Inventories

Investment in raw material and other inventories was considerably smaller in 1967,[2] with all sectors contributing to the decrease. For the first time, there was actually a disinvestment, totalling – IL 66 million at current prices, as compared with a growth of IL 110 million in 1966 and an average of IL 100 million per annum during 1960–65.

The most striking decline was in Ministry of Commerce and Industry food stocks—a disinvestment of – IL 35 million at current prices, as contrasted with

[1] See Chapter XII, "Industry".

[2] Investment in inventories is estimated as the physical change in stocks between the beginning and the end of the year, valued at the average prices prevailing during the year. The estimate is thus not identical with the inventory changes reported by the concerns. The difference between the two stems from price changes during the year.

a positive investment of IL 27 million in 1966. There were two main reasons for this development:

(a) The smaller import of meat from Eastern Europe.

(b) The additional consumption of essential items (mainly flour and sugar) originating in the administered areas.

Besides the running-down of Government stocks, private inventory investment also fell off. Industrial stocks shrank by approximately 3 percent,[1] following a 7 percent accumulation in 1966, and there was a similar decline in wholesalers' stocks.

In building materials, there was a negative investment of about – IL 10 million, which must be ascribed to the sharp cutback in construction work.

7. Public Financing of Investment

The weight of the public sector in total investment financing[2] rose considerably in 1967, reaching about two-thirds of the aggregate figure, as compared with 48 percent in 1966 and an average of 40 percent per annum during 1961–66.

The big increase in the year reviewed was the resultant of a sharp contraction of total domestic investment on the one hand and a 17 percent rise in public financing on the other. The incremental public sector financing was in the form of increased Government loans and grants for investment purposes, while local authority investments declined and the volume of Jewish Agency financing remained unchanged. All sectors benefited from the increase in public financing, with rises being particularly strong in industry, mining and quarrying, and housing. The incremental public financing consisted of a growth of 44 percent in Government lending to public sector companies and of 17 percent to private businesses and households. It should be stressed that this development does not necessarily reflect a greater predominance by the public sector in the channelling of investment funds. In recent years a considerable proportion of such financing has been provided by financial institutions, which mobilize capital from various sources (e.g. through the sale of bonds to social insurance funds or by borrowing from abroad). The Government exerts considerable influence over these institutions, as regards both their sources of capital and its allocation—and not necessarily through the funds it directly places at their disposal. In

[1] The estimate is very shaky. It is based on a preliminary survey covering a small number of enterprises, and past experience has shown that there is strong response bias in the reports submitted by firms just after the end of the year.

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

Table V–15

SHARE OF GROSS INVESTMENT FINANCED BY THE PUBLIC SECTOR, 1960–67

(percentages)

	1960	1961	1962	1963	1964	1965	1966	1967
Agriculture and irrigation	84	81	75	87	93	92	89	97
Industry and construction	39	36	24	29	11	7	11	49
Mining and quarrying	50	10	11	21	13	24	55	100[a]
Electric power	5	8	26	23	30	38	23	19
Transportation and communications	77	56	48	45	38	54	70	77
Commerce and services	57	42	44	46	47	43	53	67
Housing	38	29	36	30	36	33	36	63
Total	54	43	41	41	39	40	48	68

[a] Government loans granted to enterprises in this sector in 1967 exceeded their investments for the year. Apparently some of the funds were used for debt redemption and current outlays.

SOURCE: Investments—Central Bureau of Statistics; public financing—Bank of Israel estimates.

other words, the extent of Government influence on investment financing is greater than the amount of funds it directly supplies.

8. Gross Investment, by District

In the past several years the proportion of the country's population living in development areas[1] has moved up—from 33 percent in 1963 to 35 percent at the beginning of 1967. However, the share of these areas in the population increment is still below 50 percent: during the years 1963 to 1966 the total number of inhabitants increased by 326,000, of whom 46 percent were in development areas.

During the years 1963–66 about 40 percent of the total fixed investment[2] was made in the development areas, and the remaining 60 percent in the central area.[3] There is a marked disparity between the geographical distribution of dwelling and nondwelling investment: whereas per capita dwelling investment has been lower in the development areas than in the central area, per capita nondwelling investment has been somewhat larger in the development areas. About half of the total nondwelling fixed investment was made in development areas during the period discussed.

The development areas accounted for only 32 percent of incremental dwelling investment. This reflects the big difference in housing standards between

[1] Development areas are defined here as the Jerusalem, Northern, and Southern Districts.

[2] Excluding motor vehicles, ships, and aircraft.

[3] The Tel Aviv, Haifa, and Central Districts.

Table V-16

GROSS FIXED INVESTMENT, BY DISTRICT,[a] 1963–66

(percentages)

District	Total fixed investment[a]				Of which: Dwellings			
	1963	1964	1965	1966	1963	1964	1965	1966
Jerusalem	7	7	8	9	9	7	8	9
Northern	17	14	14	15	10	12	11	14
Southern	18	19	17	16	13	13	13	11
Total, development areas	42	40	39	40	32	32	32	34
Haifa	15	15	17	17	13	15	13	12
Central	16	18	18	17	19	20	20	21
Tel Aviv	27	27	26	26	36	33	35	33
Total, central area	58	60	61	60	68	68	68	66
Grand total	100	100	100	100	100	100	100	100

[a] Excluding motor vehicles, ships, and aircraft.
SOURCE: Economic Planning Authority, Central Bureau of Statistics, Ministry of Agriculture, and Bank of Israel.

development areas and the central districts—a difference expressed in the average area of residential construction per capita and in building standards. There is a striking disparity in this respect between the Tel Aviv and Southern Districts. Each accounted for 22 percent of the population growth in 1963–66, but whereas 34 percent of all housing investment in these years was made in the Tel Aviv District, only 13 percent was made in the Southern District.

The predominant share of the Tel Aviv District is noticeable in other investments as well. During the years 1963–66 it accounted for about 27 percent of the country's total fixed capital formation—mainly in housing, industry, and the services.

Most of the investments in the Northern and Southern Districts in recent years have been of an infrastructural nature—in the Northern District, in irrigation and agriculture; in the Southern District, in Ashdod Port and in mines and quarries. The decrease in the Northern District's weight within total investment is explained by the completion of the National Water Carrier and the steady downtrend in farm investments, most of which are made in the North. The smaller share of the Southern District is ascribable to the completion of most of the construction work at Ashdod and its harbor, as well as to the smaller capital outlay in the mining and quarrying industry. It should be noted that in recent years the majority of nonmining investments in the Southern District have been concentrated in Ashdod.