ISRAEL'S PROSPECTS FOR ECONOMIC INDEPENDENCE

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PREFACE

The purpose of the present study is to evaluate Israel's prospects for economic independence. For our purposes this means an evaluation of Israel's ability to reduce substantially its heavy dependence on foreign aid. This dependence, as the study will show, results from the country's pursuit of a number of ambitious social, economic and military objectives, the materialisation of which is beyond the country's limited national economic capabilities. Israel has had therefore to rely continuously on a large import surplus, that is a large deficit on current account. This import surplus has been financed through several sources, the most important of which are unilateral transfers from world Jewry, capital movements and German Reparations.

In view of the special nature of Israel's relations with the sources of its aid and its conflict with the Arab world it becomes difficult to discuss the country's prospects for economic independence without becoming involved in issues that reach beyond the range of economics.

However, since this study is concerned with economic considerations alone, the writer will attempt to make those assumptions that would keep the analysis within economic frontiers.

Within the limitations of the available sources of information, the appraisal of economic independence will take into account the development of the components of the balance of payments, including imports and exports, the performance of the economy, and the prospects for independence in the light of the relevant factors.

The study is divided into five chapters. The first is an analytical description of the Palestinian base of the present Israeli economy. The second chapter centers around some of the more important characteristics of this economy. In the third chapter an analysis is made of the economy's more important achievements in the period 1950-1960, thus paving the way to an analysis in the fourth chapter of the nature and magnitude of the costs incurred in the attainment of these achievements.

In the light of the information and analysis provided in the first four chapters, an attempt is made in the concluding chapter to make appropriate evaluations of the future expectation of the continuation of the causes inherent in the structure of the Israeli economy and its system of allocating resources, that have been considered to be responsible for the country's dependence on foreign aid.

ACKNOWLEDGEMENTS

The greatest obstacle facing an Arab in preparing a study of the Israeli economy is the deficiency in relevant statistical data. The present author, however, was not very much impeded by this obstacle because of the kind gesture of Dr. Yusif A. Sayigh of making available to him his private collection of Israeli economic publications.

Dr. Sayigh's help, however, did not stop at the provision of the necessary data. He was kind enough to lend his expert and patient guidance for the analysis of the information he made available.

The author wishes to pay his sincere gratitude to Dr. Sayigh for his great help in making the study at hand a possibility.

ABSTRACT

In its fifteen years of existence as an independent state, Israel has been able to accomplish a number of remarkable achievements very much in line with its society's ambitious objectives.

Among the more significant of these achievements is the development that took place in the various branches of the national economy, especially in agriculture and industry. It was thanks to this development that the cushioning of a tremendous population explosion and the great rise in per capita income within the framework of a welfare state were made possible.

Naturally, development of this magnitude has required immense investment activity, the financing of which has been well beyond the domestic capital resources. This was primarily because the country has invariably used a very large portion of its gross national product for consumption expend-

iture, thus leaving little for savings and domestic investment.

The situation being such, it has been imperative to find the necessary funds in foreign sources. Zionist institutions, friendly governments, and Zionist sympathizers have been very generous in their donations, loans, and grants-in-aid.

Israel's economic development has thus been achieved mainly through foreign aid. But it has not been without disturbing consequences, foremost among which have been inflation and an excessive rise in foreign obligations.

The imminent coming to a close of German Reparations, which have constituted the most important single share of foreign aid, and the maturation of much of the country's foreign obligations, together with other developments have animated the concern of official circles with the country's prospects for economic independence. This concern is no doubt well founded.

Our analysis of the period 1950-1960, which is the period for which adequate information is available to us, has shown that Israel's dependence on foreign aid is attributable to structural disequilibrium in the national economy. Indeed, there is every indication that the country's dependence on foreign aid will continue in the foreseeable future, as long as the Israeli society continues to press for a quick and concurrent attainment of various ambitious social, economic, and military goals, requiring intense investment activity, while at the same time continuing to consume a rather large part of the gross national product.

TABLE OF CONTENTS

Page

LIST OF TABLES

LIST OF TABLES (Continued)

CHAPTER I

INTRODUCTION TO THE PALESTINIAN BASE OF THE ISRAELI ECONOMY

Any thorough attempt to study the economy of Israel must begin by an analysis of the base from which this economy sprang, since it did not come into existence at the time of the establishment of the state in 1948, but had its roots in Mandatory Palestine. In other words, if we are to be able to draw a clear picture of the organization and performance of the present Israeli economy, we must first begin by analyzing the economy of the Jewish community of Palestine in the years preceding 1948, because Israel's economy is in many ways a continuation of the economy of the Jewish community of Palestine. This chapter is primarily designed to familiarise the reader with the Palestinian base of the present Israeli economy.

The Jewish community of Palestine consisted mainly of Jewish immigrants who came to the country from the four corners of the world where they had lived as citizens of their original countries. Most came to Palestine mainly as an escape from persecution or in an effort to pave the way for the establishment of a Jewish national home in Palestine in accordance with Zionist principles.

Prior to Britain's occupation of Palestine, Jewish immigration was only a trickle because the Ottoman rulers of Palestine did not look with favour on the idea of establishing a Jewish state in a country which they governed in the name of a Moslem Caliph.

The Mandatory permitted the advent of about 368 thousand Jewish immigrants from 1920 to November 1945.[1] This it did in accordance with the Balfour Declaration[2] which it had made public in November 1917, and in execution of Article 2 of the Mandate Charter which stipulated that:

> "The Mandatory shall be responsible for placing the country under such political, administrative and economic conditions as will secure the establishment of the Jewish

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[1]Government of Palestine, <u>A Survey of Palestine</u>, vol. I & II, 1945 and 1946, p. 185. (Please note that the main part of this Chapter, is based, unless otherwise stated, on Chapters VII, VIII and XVII of this source and hence, it will be referred to only in cases of direct quotation).

[2]The Balfour Declaration is the common name given to the British Government's declaration of policy made two days after the occupation of Beersheba on October 31, 1917, by British forces waging war against the rule of Constantinople. This declaration, made to express the British Government's views concerning Zionist aspirations, came in a letter addressed by the British Secretary of State for Foreign Affairs, Lord Balfour, to Lord Rothschild.

> national home as laid down in the preamble, and the development of self-governing institutions, and also for safeguarding the civil and religious rights of all the inhabitants of Palestine, irrespective of race and religion."

and in accordance with Article 6 of the same charter, which called upon the Mandatory Administration to "....facilitate Jewish immigration under suitable conditions...." and to encourage in cooperation with the Jewish Agency, the ".... close settlement by Jews on the land, including State lands and waste lands not required for public purposes."

The Jewish immigrants came either on their own or were brought by the various Zionist institutions established for that purpose. The most important of these institutions were the "funds" and "trusts" established by the Zionist Organization with contributions from World Jewry. These institutions were responsible to the Zionist Organization and later on in 1920 to the Jewish Agency which replaced it in that function in

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The declaration in the letter read as follows:

> "His Majesty's Government view with favour the establishment in Palestine of a National Home for the Jewish people, and will use their best endeavours to facilitate the achievement of this object, it being clearly understood that nothing shall be done which may prejudice the civil and religious rights of existing non-Jewish communities in Palestine, or the rights and political status enjoyed by the Jews in any other country."

accordance with Article 4 of the Mandate Charter.

World Jewry entrusted its contributions to the Zionist Organization, and later on to the Jewish Agency, because these authorities were established to act as the representative of the Jewish people of the world and the custodian of its acquired properties in Palestine.

The subsidiary Zionist institutions were many and any attempt to go into their system of organization and their relationships to one another and to the Mother Organization, would only cause us to digress away from the purpose of this chapter. Hence, we shall only attempt to discuss some of the functions of the more important of those institutions.

1. <u>The Jewish National Fund (Keren Kayemeth Leisrael Ltd.</u>)

This Fund was established in 1901 to "acquire land to be held in perpetuity as the inalienable property of the Jewish people and to lease it for agricultural and urban development".[1] By the end of 1944 it had acquired 758,200 dunums of land (about 48 per cent of total area in Jewish possession) at the cost of LP 6 million, which includes expenditures on drainage and irrigation.

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[1] *Ibid.*, p. 377.

2. The Palestine Foundation Fund (Keren Hayesod)

Established in 1920 to act as the financial instrument of the Jewish Agency in its effort to build the Jewish national home, the Keren Hayesod was entrusted with the task, inter alia, of providing the necessary credit to develop the land acquired by the Jewish National Fund. The credit would be made available for the establishment of new agricultural settlements utilizing Keren Kayemeth lands, and for the expansion of existing settlements.

By the end of 1945 the Keren Hayesod had spent about LP 5.75 million, of which LP 1.32 million were invested in cooperative settlements (Moshavim) and LP 2.10 million in communal settlements (Kibbutzim). The remaining LP 2.3 million was invested in agricultural training and research and in the development of irrigation schemes and citriculture.

3. The Jewish Colonization Trust Ltd. and the Anglo Palestine Bank

The Jewish Colonization Trust was established in 1899 to act as the first Zionist banking institution. It was entrusted by the Mother Zionist Organization with the accounts of its various affiliates. In 1903 the Trust established the Anglo Palestine Bank as a subsidiary branch and in view of its rapid development the Trust handed over its activity to this energetic bank and retained for itself the position of a holding company for the various financial institutions of the Zionist Organization.

Working side by side with the above institutions was the Palestine Jewish Colonization Association (P.I.C.A.), established in 1883 by the famous Zionist philanthropist Baron Edmund de Rothschild. The Baron and his Colonization Association spent about LP 15 million by the end of 1945 on Jewish agricultural colonization in an effort to "...create a class of farmers who, as owners of their farmsteads, would constitute a peasant class rooted and attached to the soil."[1] Thus the PICA would extend to a Jewish farmer or a Jewish would-be farmer, a loan for about 50 years at 1 to 3 per cent rate of interest per annum to pay for only a small proportion of the initial investment undertaken by the PICA in either purchasing the land or draining already purchased land. By the end of 1945 two thirds of the 450,000 dunums acquired by this colonization association had been transferred to independent settlers who were, unlike settlers on

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[1] Ibid., p. 374.

Keren Kayemeth land, free to dispose of their land, but who continued to live on it serviced by a number of producer and consumer cooperatives.

Besides the above mentioned institutions that were mainly concerned with the settlement of Jews on the land, were a number of other Zionist bodies concerned with the social, cultural, medical and educational conditions of the Jewish community. For example, the Hadassah Medical Organization established in 1918 and the Women's International Zionist Organization (W.I.Z.O.), established in 1921, cared for the development of Zionist health services, while the Hebrew University established in 1925 cared for the cultural and educational aspect of the Jewish community. The Emergency Funds and Youth Aliya sponsored the transportation of Jewish child immigrants from Europe and cared for these immigrants. A summary of the income, expenditure and investments of the Zionist institutions hitherto mentioned is given in Table I below. This table readily reveals that each institution devoted the major share of its investments to the activity for which it had been intended when established. Thus we see that the Keren Hayesod and the Keren Kayemeth channeled the major part of their income to agricultural settlements, while the Hadassah did go to the field of social and health services.

TABLE I

SUMMARY OF INCOME, EXPENDITURE AND INVESTMENTS OF THE JEWISH NATIONAL FUNDS AND INSTITUTIONS IN PALESTINE DURING THE PERIOD, OCTOBER 1917-SEPTEMBER 1944
(In £P)

	Keren Hayesod 1921-1944	Keren Kayemeth 1918-1944	Hadassah 1918-1944	Wizo 1921-1944	Hebrew University 1925-1944	Emergency Funds (incl. Youth Aliya) 1929-1944	Total	% 1917-1944
INCOME:								
Receipts from contributions	12,315,830	9,153,681	2,658,333	583,313	1,710,978	2,701,110	29,892,961	83.9
Receipts from services, collections of debts, grants, etc.	3,613,678	382,633	841,433	223,688	189,369	353,139	5,740,084	16.1
Total	15,929,508	9,636,314	3,499,766	762,001	1,900,347	3,054,249	35,633,045	100.0
Percentage	44.7	27.1	9.8	2.1	5.3	8.6	100.0	
EXPENDITURE AND INVESTMENTS								
a) Immigration and settlement								
1. Immigration and training	2,710,524	-	-	-	-	69,593	2,854,335	8.0
2. Agricultural Settlement	4,388,179	8,786,222	-	272,692	-	731,687	14,301,999	40.0
3. Public works, labour and housing	1,605,439	19,385	-	59,122	-	192,640	1,816,813	5.1
4. Urban settlement, trade, industry & investments	1,240,099	870,147	-	5,321	-	165,985	2,389,657	6.7
Total	9,944,241	9,675,754	-	337,135	-	1,059,905	21,362,804	59.8
b) Public services and national organizations								
5. Education and culture	1,898,671	-	612,210	264,292	1,830,483	1,664,366	6,631,098	18.5
6. Health and social works	179,302	-	3,203,298	226,647	-	54,024	3,668,316	10.3
7. National organization, security & emergency	2,404,766	108,326	-	5,555	-	302,311	2,898,374	8.1
8. General administration, interest, etc.	837,859	27,642	-	56,127	56,292	109,674	1,192,412	3.3
Total	5,320,598	135,968	3,815,508	552,621	1,886,775	2,130,375	14,390,200	40.2
Total expenditure and direct investments	15,264,839	9,811,722	3,815,508	889,756	1,886,775	3,190,280	35,753,004	100.0
9. Add. amounts transferred to other institutions (incl. in this table)	+ 948,770	+622,172	-	+39,950	+ 6,991	+100,964	+1,807,960	
10. Deduct amounts received from other institutions (incl. in this table)	- 627,172	- 64,844	-343,657	-164,046	- 54,082	-421,782	-1,807,960	
Grand Total	15,586,437	10,369,050	3,471,851	765,660	1,839,684	2,869,462	35,753,004	

Source: Government of Palestine, A Survey of Palestine, Vol. II, 1946, p. 914.

Our analysis of the Zionist institutions seeking to promote Jewish activity in Palestine, would in no way be complete without recording the enormous efforts of the Histadrut (General Federation of Jewish Labour) which went to enlarge and coordinate Jewish economic activity in Palestine.

The Histadrut was established in 1920, and undertook the dual role of safeguarding the Jewish worker in employment opportunities created by others, together with the founding of economic enterprises owned by the Histadrut through its holding company 'Hevrat Oudim'. In its capacity as owner of construction, industrial, agricultural and financial enterprises, etc., the Histadrut was able to play an important role in absorbing large numbers of Jewish immigrants in accordance with its objective of paving the way for a socialist society in which the 'Labor Sector' plays a leading economic role.[1]

On January 1, 1945, the Histadrut had 143,000 adults and 8,500 youths as full-fledged members constituting about 75 per cent of all Jewish wage and salary earners.

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[1]Nathan Robert, <u>et.al</u>., <u>Palestine: Problem and Promise</u>, 1946, pp. 290-92.

The Hevrat Ovdim, the Histadrut's holding company, controlled a number of transport cooperatives such as Egged, Hamaavir and Hamakasher; one hundred collective communal settlements and 53 small holders' settlements; the Tnuva agricultural producers' marketing cooperative; the Hamashbir Hamerkazi consumers' cooperative; the Yakhin citrus grove development company; the Nir company for financing the settlement of agricultural workers; the Workers' Sick Fund (Kupath Holim); the Workers' Bank; the Hassneh workers' life insurance company and last but certainly not least the Solel-Boneh Ltd., the largest contract construction enterprise, and a holder of a number of large industries.

The majority of the Histadrut's members were also members of the most influential Zionist party, the socialist Mapai. Together, the Mapai and the Histadrut, aided by other socialist minded parties and groups, built a socialist framework around the Jewish community in Palestine. They were successful because many of the immigrants constituted fertile ground for socialist ideology, coming as they did from Eastern European countries where capitalism had offered only its evils and little of its privileges. The immigrants came to build a national home in which the worker would be free from persecution and exploitation. The teachings of the Zionist socialist parties offered them comfort while the Histadrut provided them with protection and benefits.

Working within this organizational framework, the Jewish community of Palestine, backed by the whole of Zionism, concentrated all efforts on building an economy that could absorb as large a number of immigrants as could be brought in to the country by the influence and pressure of the various Zionist organs. These efforts were guided by the basic principles of Zionism which centered around the objective of ultimately gathering in Palestine a Jewish majority settled on the land and ready for statehood.

Settlement on the land was the order of the day as far as Zionist strategy was concerned, because such settlement served a variety of means and ends. The Zionist Movement sought a way by which it could re-establish a link with the past history of ancient Israel. It needed to embody the sacred attachment of a Zionist to his 'promised land'. It has to prove concretely his love for the land and his readiness to defend it with life if needs be. It had to create a system by which Jewish possessions could be protected and Jewish political goals reached. It had to create room and occupation for large numbers of immigrants.

In view of all this, Zionist strategy decided that agricultural settlements would answer most of the requirements, and issuing from this conviction came the efforts of the various colonization institutions to develop agricultural establishments and agriculture itself. Thus land was bought or leased from the Mandate or from Arab owners, and enormous funds and efforts were sunk into the land in careful preparation for the day when the community would become a state.

By the end of 1944 (and with little change by 1948), the Jewish community was in possession of 1,731,300 dunums of land of which the Jewish National Fund owned 758,000 dunums or about 48 per cent, while the remainder was owned by the PICA and private individuals. During the same year 716,850 dunums were cultivated, of which 414,000 dunums were cultivated by 210 cooperative and communal settlements comprising a total population of about 63,000 persons. Table II below gives a comprehensive idea of the number and type of agricultural settlements, their population and area cultivated in 1944.

The major part of Jewish agricultural land was situated in the more fertile areas of Palestine such as the Valley of Jezreel and the Vale of Sharon. The

TABLE II

NUMBER AND POPULATION OF AND AREA CULTIVATED BY AGRICULTURAL SETTLEMENTS IN 1944

Type of Settlement or Place	Number	Population	Cultivated Area (In dunums)
Individual	44	76,000	299,000*
Cooperative	99	29,500	179,000
Communal	111	33,500	235,000
Schools and Farms	5	4,000	4,000
TOTAL	259	143,000	717,000

* Including citrus.

Source: Government of Palestine, A Survey of Palestine, vol. I & II, 1945 and 1946, p. 378.

farms utilised modern equipment and were mainly run on a mixed farming basis. Technical and financial advice came from the specialised Zionist units created for that purpose. Table III below gives us an idea of the share of Jewish farming in the country's agricultural activity. The table records the area utilised and the main crops in the season 1944/45, but does not make allowance for livestock and poultry which in 1944 respectively supplied 28 per cent and 13 per cent of income derived by the Jewish community from agriculture.

TABLE III

TOTAL AND JEWISH AREA IN DUNUMS OF LAND UNDER, AND PRODUCTION FROM, MAIN GROUPS OF CROPS IN THE SEASON 1944/45

	Palestine Total		Jewish Cultivation	
	Dunums	Tons	Dunums	Tons
Grains	4,367,629	209,955	215,191	16,579
Vegetables	279,940	244,834	40,207	55,730
Fodder	143,543	197,352	119,573	176,525
Fruits (excluding citrus)	392,926	94,718	37,217	21,398
Olives	600,133	79,469	7,587	1,182
Melons	125,979	142,827	5,675	7,193

Source: Government of Palestine, A Survey of Palestine, vol. I & II, 1945 and 1946, p. 323.

The table also does not include citriculture; it is important to note here that the Jewish community operated in 1944 some 120,000 dunums of the total 300,000 dunums devoted to citriculture.

It is apparent from what has been said that agriculture played a vital role in the socio-economic life of the Jewish community in Palestine. However, the fact that this community and its various organizations devoted a substantial part of their efforts to the development of agriculture, did not necessarily mean that agriculture was the most important economic sector as far as the industrial origin of national product was concerned.

In 1936, agriculture absorbed 18.7 per cent of the community's labor force, which was the largest group employed in any one single branch of activity, but agriculture generated only about 9.5 per cent of the community's national income for that year. In that same year, industry absorbed as much as 17.5 per cent of the community's labour and generated 19.6 per cent of its income. Yet more significant was the commerce, finance and transport sector which generated about 39.3 per cent of the community's income for 1936 and employed as many workers as did the agricultural sector in that year.[1] This sectorial distribution of income and employment held its ground in 1944 as is shown in the information contained in Table IV below.

The structure revealed in Table IV is somewhat similar to that characterizing 1936, except that in 1944 industry and handicrafts employed 26.9 per cent

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[1]Robert Nathan, et.al., Palestine: Problem and Promise, 1946, p. 150.

TABLE IV

NATIONAL INCOME OF PALESTINE, 1944, DISTINGUISHING SHARE OF JEWISH COMMUNITY

	Number engaged in 000's		Percent of total Jewish labour	Income LP million		Percent of total Jewish income
	Palest. total	Jews		Palest. total	Jews	
Total	545	245	100.0	123.0	73.4	100.0
Agriculture	176	24	9.8	29.5	9.1	12.4
Industry and handicrafts	79	66	26.9	28.2	24.9	33.9
Housing	-	-	-	6.1	3.2	4.4
Building and construction	29	9	3.7	5.6	2.7	3.7
Transport and communications	27	12	4.9	8.3	4.8	6.5
Commerce, finance, hotels, restaurants and cafes	72	43	17.6	22.8	15.9	21.6
Government and local authorities	44	12	4.9	7.5	2.7	3.7
Other	118	79	32.2	15.0	10.1	13.8

Source: Jewish Agency for Palestine, Statistical Handbook of Jewish Palestine, 1947, p. 404.

of the total number of Jews engaged instead of 17.5 per cent, and generated 33.9 per cent of the community's income instead of 19.6. Commerce, finance, hotels, restaurants and cafes had meanwhile moved into second position generating 21.6 per cent of the total income and employing 17.6 per cent of the total number employed. Agriculture held its position as third most important branch from the point of view of the income produced but lost its position of leadership in employment, falling to third position.

The above findings also compare very favourably with the estimates of P.J. Loftus for the national income of Palestine and the distribution of labour force amongst the various economic branches in 1945. His findings were almost identical with the above quoted figures for 1944 from the point of view of the industrial origin of income and employment as far as the Jewish community was concerned.[1]

A detailed analysis of the three most important branches of the community's economy would seem imperative at this point, but on account of the inavailability of

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[1] P.J. Loftus, National Income of Palestine, 1948, pp. 25-27.

adequate information concerning the commerce and finance branch, analysis of this branch is not possible. Having detailed the characteristics of Jewish agriculture in an earlier part of this chapter it only remains for us to concern ourselves with a brief examination of developments in Jewish industry.

During the period of the Mandate, Jewish industry was able to boast a number of important achievements. The number of establishments increased from 1,850 in 1921-22 to as many as 6,116 by 1943. During the same period the number of gainfully employed persons in industry soared from 4,750 to 52,000. Capital investment increased from LP 600,000 in 1921-22 to about LP 16 million in 1943. The real spectacular increase was in the value of annual output which during the period under study increased from LP 500,000 to about LP 38 million.[1]

The rapid development of Jewish industry in Palestine was made possible by the enormous funds that were made available for investment in industry, mainly through the extension of credit on easy terms by the Zionist credit institutions, and through the import of private Jewish capital by the large numbers of Jewish

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[1]Nathan, op.cit., p. 222.

entrepreneurs who came to the country in the late twenties and early thirties and who continued to come in escape from Nazi Europe. Of great help for Jewish industry were the war conditions that afforded a protective barrier against foreign competition in the local market and that resulted in heavy expenditures by Allied forces in the area. These favourable conditions permitted Jewish industry to expand and draw on a somewhat large reserve of industrial workers and other skilled workers who had had previous experience in industry and other occupations in their countries of origin before their immigration into Palestine.

The rapid development of Jewish industry, however, did not change the basic characteristics of this industry. That is, it remained primarily concerned with the production of consumption goods such as foodstuffs and clothing. New industries, such as metal works and machinery, chemicals and diamonds, however, were gradually coming into the forefront.[1]

Meanwhile, the Histadrut was becoming more and more powerful and more and more demanding. It kept on insisting and getting wage increases for its members

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[1] A Survey of Palestine, op.cit., pp. 500-502.

and providing them with its various social insurance facilities and privileges. By the end of 1945 the average income of the Jewish earner was about LP 141 in comparison with LP 44 in 1936. These figures, however, are at current prices and should we choose to divide these figures by the pre-war cost-of-living index we would find that the increase was only 23 per cent in nine years, which is not an insignificant increase.[1]

Jewish efforts were able by the end of the Mandate to found a flourishing industry and a carefully planned agriculture backed by funds from World Jewry. The Jewish Agency very capably and efficiently assumed the responsibilities of internal government for the Jewish community. But, despite all the efforts of Zionism, it had failed by the end of 1948 to make the Jewish community a majority in Palestine. This community remained a minority (albeit large) of 33 per cent of the total population and in possession of only 6 per cent of the country's total land area. The White Paper of 1939 which placed limitations on immigration and land purchase, had been a severe blow to the prestige of the Zionist Movement and to the influence it had in

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[1] Yusif A. Sayigh, The Economy of Israel, (Cairo, 1963; in Arabic), Ch. III.

British and international governing circles. The mere continuance of the Mandate constituted a limitation to the economic and military strategy of Zionism. It became evident to all that the Zionist effort would continue to be somewhat limited in effect as long as the Mandate continued. Realising all this, the Zionists speeded their efforts towards independence through a wide variety of means that we cannot discuss here, and ended up on May 15, 1948 with the establishment of the state of Israel and the de facto termination of the Mandate.

An important point, worth mentioning before the termination of this chapter is that concerning the capital imports of the Jewish community in Palestine. These totalled some LP 162 million from 1922-46, and included LP 109 million in immigrants' properties other than personal effects, LP 46 million in receipts of Zionist institutions in Palestine (see Table I), and LP 9 million from the Zionist philanthropist Baron Rothschild (part of whose donations were invested in Palestine prior to 1922).[1]

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[1] Polk William, <u>et.al.</u>, <u>Backdrop to Tragedy</u>, 1957, p. 334.

The Jewish community greatly relied on this capital inflow to build up the Jewish economy described in this chapter, and gave that economy a dependent characteristic similar in many respects to the Israeli economy which, as will be shown in subsequent chapters, relied heavily on capital imports.

CHAPTER II

SOME BASIC CHARACTERISTICS OF THE ISRAELI ECONOMY

The establishment of the state of Israel on May 15, 1948 gave Zionism about 20,662 square kilometers[1] of land over which to exercise full authority and in which to have a completely free hand. Within its de facto boundaries, Israel now can utilise any means it chooses for the achievement of its ends. The Jews are now the clear majority in their State; they own almost all of the land and the various sources of livelihood for the population. They are thus the sole masters of their national economy, free to produce what they choose and able to protect what they possess. No outside political authority stands now in the face of the Zionist

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[1]The United Nations Partition Plan for Palestine, had allotted 14,920 square kilometers of the total area of Palestine for the Jewish state. Israel, managed during the war with the Arabs to augment this area by a further 5,742 square kilometers which it occupied by force of arms, thus bringing the total area under Israeli control to 20,662 square kilometers.

all-out effort to achieve the economic, political, social and ideological goals of Israeli society.

Before going into the various economic objectives of Israeli society it is necessary to point out that this society was very much occupied from May 15, 1948 to July 20, 1949 in military endeavours to protect the new born state from the threat posed by the engaged Arab armies. Moreover, the fact that the last truce agreement was signed with Syria on July 20, 1949 did not lead this society to give up its efforts to continue to mobilize an important part of its potentialities for defense against an ever-present Arab threat to invade Israel. This threat has led to the placing of defence on an almost sacred pedestal in Israel.

Returning to the other objectives of Israeli society, we note that the country's Declaration of Independence and the 1950 Law of Return, stated very explicitly that the main non-military objective of Israel, was to gather in the country all of the 'exiles' or Diaspora Jews who were willing to come to Israel. According to Zionist views, this in fact had been the reason why Israel was established. It was the sacred right of any Jew irrespective of nationality and belief (except those who presented a threat to public security), to immigrate to Palestine, because Israel was established in the name of Jewry. Hence, the familiar exultation concerning the Israeli achievements in the fields of defence and immigration are noticeable in all Israeli publications.

But transporting hundreds of thousands of immigrants was not all there was to the idea of collecting the Jews of the world in Israel. There was need to carry out large settlement programs to house, feed and employ the masses of immigrants and to "...break down the geographical, cultural and linguistic barriers between the sections and endow them with a single language, a single culture, a single citizenship, a single loyalty, and new laws and statutes."[1]

Therefore, in 1948, the state of Israel had set out to achieve the goal of collecting hundreds of thousands of Jewish immigrants and their moulding into a single society, and their absorption into a rapidly growing economy without causing any disequilibrium in the national economy. Before discussing how successful Israel has been in realising its goals, that is before

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[1]Introductory essay by David Ben Gurion, entitled "Achievements and Tasks of Our Generation", in the Israel Government Yearbook, 1961-62, p. xxi.

analysing the economic achievements of Israel, it is necessary to try first to single out some of the basic characteristics of the Israeli economy.

A. Ownership Structure

By ownership structure, we mean here the relative share of each of the various types of ownership sectors in the control of the country's economic enterprises. In non-communist countries, it is customary to find two main types of ownership sectors, the private and the public, with a mixed sector in which these two jointly participate. In Israel, however, the third sector which is referred to as the "Labour Sector" and which includes the Histadrut and the cooperative and collective enterprises, is not a "mixed" sector but a distinct one with peculiarities all its own. Moreover, the public sector in Israel has the peculiarity of including not only the central government and the local authorities, but also the "national institutions" such as the Jewish Agency, the Jewish National Fund and the Foundation Fund. Thus the public sector enterprises are those in which the government or national institutions hold more than

50 per cent of total shares.[1]

The peculiarity of Israel's ownership structure, does not, however, end at the co-existence of three types of ownership groupings, two of which are untypical of the non-Communist world. There is the further peculiarity of the distribution among the three sectors of areas of activity and specialization.

A study of the country's national product in 1953 revealed that 53.9 per cent of the country's net domestic product originated in enterprises owned by the private sector, that is in proprietorships and companies owned by individuals. Of the remaining 46.1 per cent of net domestic product, the Labour sector (Histadrut and cooperative and collective enterprises) was responsible for about 46.8 per cent (21.6 per cent of total net domestic product),

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[1]Harold Lubell, "The Public and Private Sectors and Investment in Israel", <u>Middle Eastern Affairs</u>, April 1961, p. 98.

while the public sector was responsible for about 53.2 per cent (24.5 per cent of total net domestic product).

As is revealed in Table V below, the private sector though active in almost every economic branch, generated 31.1 per cent of its income in mining and manufacturing, where it also contributed 78.9 per cent of all value added in that branch. But the fact that the private sector generated the largest part of its income in that particular branch, did not prevent it from being the chief producer amongst the other two ownership sectors in other economic branches such as contract construction, public utilities, and every other branch except agriculture and government. It did not hold first position in agriculture and government which are the domain of the two other ownership sectors par excellence because agricultural activity is carried mainly in publicly owned land by settlements affiliated with the "Labour" sector, and government is a public sector by definition.

TABLE V

NET DOMESTIC PRODUCT (VALUE ADDED) BY TYPE OF ENTERPRISE AND ECONOMIC BRANCH, 1953

	Net domestic product originating in each branch (Mill. of IL)	Value added in million of IL*				Percent of total value added*				Percent of total value added in branch				
		Histadrut a	Cooperative & collective enterprises	Partnerships & companies owned by individuals	Public sector	Histadrut a	Cooperative & collective enterprises	Partnerships& companies owned by individuals	Public sector	Histadrut a	Cooperative & collective enterprises	Partnerships & companies owned by individuals	Public sector	Total
Agriculture	140	3.1	86.0	50.0	0.9	0.3	55.1	8.1	0.3	2.2	61.4	35.7	0.7	100.0
Mining & Manufacturing	242	30.0	16.9	190.9	4.1	33.1	10.8	31.1	1.5	12.4	7.0	78.9	1.7	100.0
Contract construction	76	14.0	-	55.0	7.0	15.5	-	9.0	2.5	18.4	-	72.4	9.2	100.0
Public utilities	25	-	-	18.0	7.0	-	-	2.9	2.5	-	-	72.0	28.0	100.0
Transportation and communications	86	5.0	20.0	40.0	21.0	5.5	12.8	6.5	7.5	5.8	23.3	46.5	24.4	100.0
Trade	122	10.0	4.0	106.0	2.0	11.0	2.6	17.2	0.7	8.2	3.3	86.9	1.6	100.0
Wholesale	(45)	9.0	-	35.0	1.0	9.9	-	5.7	0.4	20.0	-	77.8	2.2	100.0
Retail	(77)	1.0	4.0	71.0	1.0	1.1	2.6	11.6	0.4	1.3	5.2	92.2	1.3	100.0
Banking, finance and real estate	65	6.0	6.0	45.0	8.0	6.6	3.8	7.3	2.9	9.2	9.2	69.3	12.3	100.0
Other services and repair shops	134	-	23.0	110.0	1.0	-	14.7	17.9	0.4	-	17.2	82.1	0.7	100.0
SUB-TOTAL	890	68.5	155.8	614.9	50.7	75.6	99.7	100.0	18.2	7.7	17.5	69.1	5.7	100.0
Government and non-profit organizations	250	22.0	-	-	228.0	24.3	-	-	81.6	8.8	-	-	91.2b	100.0
TOTAL: ALL BRANCHES	1140	90.6	156.2	614.5	279.3	100.0	100.0	100.0	100.0	7.9	13.7	53.9	24.5	100.0

a) Enterprises controlled by Hevrat Ovdim; and administrative apparatus of the Histadrut.
b) Includes all non-profit organizations other than the Histadrut administrative apparatus.
* Author's computations, totals may not add up because of rounding.

Source: Harold Lubell, "The Public and Private Sectors and Investment in Israel", Middle Eastern Affairs, April 1961, p. 99.

In agriculture, the private sector ceded its leadership to the cooperative and collective enterprises which constitute part of the Labour section. (The Labour sector accounted for 61.4 per cent of total value added in agriculture). Cooperative and collective enterprises generated 55.1 per cent of its total income in agriculture, 14.7 per cent in services and repair shops and 12.8 per cent in transport and communication. The other part of the Labour sector, namely the Histadrut, accounted here for only a minor share of total value added, mainly because the Histadrut had spread its economic activities so widely as to include almost every economic branch. (Nevertheless the Histadrut generated the major part of its income - 33.1 per cent - in mining and manufacturing, where it controlled the heavier industries).

The government sector, naturally enough, generated 81.6 per cent of its income in government and non-profit organizations and was responsible for 91.2 per cent of total value added in that branch.

The picture just given pertains only to 1953, information for more recent years not being available. However, an equally revealing, though not identical method, of assessing the relative share of each sector for which information is available, carries the picture forward to 1958, as Table VI below shows.

Examining Table VI closely we find that the method of assessing the relative importance of sectors is not by stating the proportion of total value added in each sector as was done in Table V above, but by comparing the size of employment in the three ownership sectors. If we are to follow this approach as being indicative of the relative importance of the sectors in each of the economic branches and in the economy as a whole, we will find that the sectors in 1958 held more or less the same ground as in 1953, within certain margins of change.

Comparing Tables V and VI we find that a certain rough relationship continued to hold over the years between share in total employment and share in total value added. Thus, the private sector in 1958 employed 41.9 per cent of the total number of persons employed in the economy in that year. Against this the private sector was responsible for 53.9 per cent of total value added in the economy in 1953. Similarly the public sector which was responsible for 24.5 per cent of total value added in 1953, had 28.3 per cent of total employ-

TABLE VI

EMPLOYED PERSONS BY TYPE OF ENTERPRISE AND ECONOMIC BRANCH, 1958

	Thousands		Engaged in[a]			Percent of All Branches[a]			Percent of branch			
	Total Employment	Jewish wage & salary earners[a]	Histadrut & cooperative & collective enterp.	Partnerships & companies owned by ind.	Public sector	Histadrut, cooperative & coll.enterp.	Partnerships & companies owned by individuals	Public sector	Histadrut, cooperative & coll.enterprises	Partnerships & companies owned by individuals	Public sector	Total
Agriculture	115.1	32.8	15.0	15.4	2.3	12.4	9.1	2.0	46.0	47.0	7.0	100.0
Mining & manufacturing	141.8	93.8	18.3	68.6	6.8	15.2	40.6	6.9	19.5	73.2	7.3	100.0
Construction & public works	64.3	49.1	18.2	22.8	8.1	15.1	13.5	7.1	37.1	46.4	16.5	100.0
Public utilities	13.1	12.0	-	1.2	10.8	-	0.7	9.5	-	10.0	90.0	100.0
Transportation & communications	44.3	25.9	7.6	4.9	13.4	6.2	2.8	11.7	29.4	18.9	51.7	100.0
Trade, banking & finance	80.8	37.4	8.3	26.7	2.4	6.7	15.7	2.1	22.2	71.4	6.4	100.0
Other services (including govt.)	195.1	150.5	52.8	27.5	70.1	43.9	16.3	61.5	35.1	18.3	46.6	100.0
Not known	3.8	1.8	-	1.8	-	-	11.1	-	-	100.0	-	100.0
TOTAL	658.3	403.3	120.2	168.9	113.9	100.0	100.0	100.0	29.8	41.9	28.3	100.0

Other than in first column, all figures pertain to Jewish wage and salary earners and presumably exclude employer as well as all non-Jews.

a) Figures computed by author and may not add up to totals due to rounding.

Source: Harold Lubell, "The Public and Private Sectors and Investment in Israel", Middle Eastern Affairs, April 1961, p. 100.

ment in 1958. Finally, the Histadrut and cooperative and collective enterprises in 1958 employed 29.8 per cent of the total number of persons employed while in 1953 this sector accounted for 21.6 per cent of total value added in the national economy.

Not only did the three sectors in 1958 maintain their relative importance vis-a-vis total economic activity in the country, but they also maintained (within a certain margin) their individual spheres of predominance. Hence, the indication in Table VI that 40.6 per cent of the private sector's total number of employed persons were employed in mining and manufacturing. This figure also indicates that 73.2 per cent of the total number of persons employed in industry and mining were employed in enterprises owned by the private sector. Thus despite the passage of five years, the private sector continued to play the leading role in industry.

Similarly, the public sector maintained its undisputed control of the government branch, while the labour sector continued to dominate the agricultural branch.

B. The Framework of Economic Policy

In the first chapter of this study, it was pointed out that the Jewish Agency and the various Zionist institutions devoted specific attention to the acquisition of agricultural land and the development of agriculture and agricultural settlements. This phenomenon was explained by the determination of the Zionist public institutions to encourage immigration and the close settlement of Jewish immigrants on their "promised land", where they would resume their sacred attachment to the land and thereby "cleanse themselves of material attachments." It was further pointed out that agricultural colonization fulfilled a number of religious, military, political and economic ends.

Attention was also called to the involvement of the labour sector in the promotion of cooperative enterprises particularly in agriculture and marketing and to some extent in contract construction, industry and transportation. Also noted was the wide-scale activity of individual proprietors and private companies in most of the economic branches but particularly in industry and services.

Hence, there existed a three-way division of economic interest among the three sectors even before the establishment of the state in 1948. This division continued in practice after the establishment of the state, as was clearly shown in the preceding section of this chapter. This continuation came about mainly as a result of the government's economic policy that either encouraged the particular structure inherited from Mandate days or did not do much to alter it.

By economic policy, we mean here the framework of rules and regulations designed by the country's legislative authority and executed by its executive administration to guide the national economic efforts towards the attainment of society's objectives. The decisions of the legislature with regard to the means to be adopted for achieving the desired ends are of course influenced by the socio-economic beliefs held by the legislative representatives of the society under question.

In Israel, the legislative authority is the Knesset (Israeli parliament) and any major decisions regarding economic policy have to meet with the approval of the majority of Knesset members. Hence, in a way, the economic policy of Israel is decided upon in the Knesset, and to be able to understand this policy it is necessary that we familiarize ourselves with the opinions held by the majority group in that parliament. It remains to be said that the Knesset consists of the representatives of a large number of parties holding clear-cut social and political views.

Israel has had five Knesset elections since the establishment of the state and at every election one of the major issues was the country's economic policy. For five times, the Israeli voter was asked to state his opinion regarding what he considered was the most appropriate economic policy. (The ends of the policy can be listed as a pace of economic development rapid enough to absorb the largest possible number of immigrants in the shortest possible time with as high a general standard of living as possible.) In the five elections the majority of Israeli voters voted "socialist" and laid bare the intrinsic socialist nature of the Israeli society (see Appendix I).

Yet, despite Israel's socialist flavour we notice that the government's economic policy has not been as socialistic as might have been expected in a society whose socialist ideology was carefully nurtured for more than forty years. The first indication of the government's rather flexible socialist policy has been the ownership structure discussed previously. Another indication has been the absence of a system of comprehensive central planning and the rather modest development budget of the government and the restriction of government interference to those sectors where it controlled the major share of activity. The government's economic policy up till 1961 displayed more of a dual existence of private initiative and socialist practice than the predominance of the latter.

Up till 1961, the government seemed to have been more interested in the application of socialist ideology concerned with distribution rather than that of socialist ideology concerned with production and the ownership of means of production. The result of this has been that Israel boasts today one of the most advanced and progressive systems of social security, progressive taxation and social justice, and has little to show from the point of view of centrally planned and coordinated economic effort.

This failure to adopt socialist practice in the field of production, in accordance with the prevailing socialist sympathies of the leading political parties of the country, is not without cause. The leftist elements in Israel had the political strength to institute an economic policy far more socialistic in its content than that which was actually instituted, but refrained from doing so. Their moderation reflects their awareness of the special circumstances of the country. Israel, they cannot fail to remember, has a continuing pressing need for huge remittances from abroad, whether in the form of grants or loans. Almost without exception, the donors and creditors (whether individual Jews, Gentiles, banks, or governments) are "Western" - that is, belong to the capitalist world, and would naturally frown upon a far-reaching socialist policy. No doubt the government of Israel has therefore to be very cautious in instituting socialist practices that menace the inflow of foreign aid. And this caution is generally endorsed by the major political parties.

It has to be added that there also exist in Israel a right wing of no small power. This wing champions capitalism, and partly for that reason appeals to foreign contributors. But, what is more significant, this wing is highly combatant in political and international matters, and in view of the unsettled issues between Israel and the Arab States, it is appeased by the major (left-wing) parties. This state of affairs partly explains why Israel's governments or cabinets have been coalitions between the various political factions in the country. By making room for the right-wing in the government, the left-wing parties have assured themselves of the support of the opposition. On balance, the presence of the right wing in power has produced a rather flexible version of socialism in the country and has served to encourage the flow of foreign aid and private initiative into the country.[1]

Consideration for the circumstances just referred to produced the flexible socialist policy that we have encountered, but as the years went by and the economy's problems (such as inflation, economic instability, mal-investment and the ever increasing deficit on current account) remained unsolved, the socialist parties began to exert more pressure for a reformation of policy. This pressure culminated in 1961 in the decision that government should intervene more directly in economic affairs. Accordingly, the government on November 14, 1961, decided to adopt central economic planning to

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[1] The main part of this reasoning comes from the fourth chapter of Yusif A. Sayigh's The Economy of Israel.

stabilise and improve the functioning of the national economy and help the country start on the path of economic independence -- a path that had become one of the most closely held goals of the Israeli society. A Higher Planning Authority attached to the Ministry of Finance was established to coordinate and evaluate economic growth in the various branches of the national economy. This Authority was to draw up a five year plan that would be put into execution pending the approval of a committee of experts from the ministries concerned.

In its declaration of its 'New Economic Policy', on February 2, 1962, the government reaffirmed its decisions made in 1961, and made public its further decision to establish a general framework for the planning of the development of the various branches of the economy. The government's new policy envisaged the undertaking of "vigorous measures" to improve the country's balance of payments position and to rid it of the instability with which it had been plagued in the past. The vigorous measures declared by the government included the devaluation of the Israeli Lira, the abandonment of many protective import levies, economic planning by a central authority, proper manipulation of the "Law on Restraint of Trade", the linkage of the cost-of-living allowances system to increases in productivity and the refraining from undue and excessive expenditures by both the household and the government sectors.[1]

As can be surmised from the components of the New Policy, the government's decision did not mean that it would pose as a threat to private initiative. On the contrary, as the Minister of Finance, Mr. Levi Eshkol, announced in presenting the government's New Economic Policy, it was clear that the state would continue to encourage private initiative under the auspices of the government and the guidance of specially-created authorities.

C. The Relative Strength of the Economic Sectors

In this section we shall attempt to single out the economy's more important sectors, for the purpose of pointing out the fields of greater concentration. Thus we will try to determine the share of each economic sector in the generation of domestic product, in total

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[1]Document, "Israel's New Economic Policy", Middle Eastern Affairs, March, 1962, pp. 85-87.

employment, and in total investment. Due to the inavailability of relavent data for many years back, we shall restrict our analysis to the years 1958, 1959, and 1960.

Industry generated 23.9 per cent of gross domestic product in 1958, about 24.2 per cent in 1959 and 24.5 per cent in 1960. In all three years industry played second role only to the commerce and services branch which in 1958 was responsible for 26.8 per cent of total gross domestic product, 27.3 per cent in 1959 and 27.8 per cent in 1960. The public sector occupied third position in all three years, producing 11.3 per cent of the gross domestic product in 1958, some 15.5 per cent in 1959 and 15.7 per cent in 1960. The only other important branch was agriculture which accounted for 13.2 per cent, 12.5 per cent, and 11.5 per cent of gross domestic product for 1958, 1959, and 1960 respectively.[1]

From the point of view of employment by economic branch it was industry that maintained first position, employing 22.4 per cent of total persons employed in 1958, 22.6 per cent in 1959 and 23.2 per cent in 1960.

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[1]Bank of Israel, Annual Report, 1960, p. 18.

Public services occupied second position, employing 21.8 per cent in 1958 and 1959 and 22.0 per cent in 1960. Meanwhile, agriculture assumed third position with 17.6 per cent in 1958 and 1959 and 17.1 per cent in 1960. The fourth and only other important branch was commerce, finance and insurance which accounted for 12.4 per cent in 1958 and 12.2 per cent in 1959 and 1960.[1]

It appears therefore that there are four important economic sectors in Israel, whether considered from the point of view of their share in gross domestic product or in total employment. This characteristic holds true also for the four branches together when we consider domestic investment, except that here the ranking is somewhat altered. To begin with, investment in residential housing accounted for the largest share of total investment in the period 1955-1959 (33 per cent) and in 1960 (29 per cent). Moreover, agriculture attracted 19 per cent of total investment in contrast to industry's 14 per cent in the period 1955-1959, but lost the second position to the latter in 1960, attracting as it did only 17 per cent of total

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[1] *Ibid.*, p. 87.

investment in comparison to industry's 20 per cent. The share of commerce and services was 13 per cent from 1950 to 1959 and 15 per cent in 1960.[1]

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[1] Note that the percentages for industry exclude mining and electricity which received respectively 2 and 6 per cent in the period 1955-1959 and 1 and 3 per cent in 1960.

APPENDIX I

Political Parties in Israel*

Israel has a multitude of political parties ranging from the extreme right of the right wing to the Communist party in the extreme left.

The reason for the multiplicity of parties can be traced to the circumstances that prevailed in Palestine prior to the establishment of the state of Israel in 1948, and to the varied national and social backgrounds from which the Jews in Palestine had come. Thus a relatively small number of Sabras (Palestine-born Jews) could boast that their fathers had also been Sabras when the state was established; the majority of Palestinian Jews had come to Palestine as immigrants.

Jewish immigrants came into Palestine in waves (alliya) and each wave (Alliyot) was almost totally composed of immigrants from a particular country or close region of the world (for example the second Alliyot was almost totally composed of Eastern European Jews, while the fifth Alliyot came mainly from Nazi Germany). In their countries of origin the Jews had learned to adopt the socio-political and economic ideolo-

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*Please note that this Appendix is a liberal paraphrasing of the sources cited.

gies of their gentile neighbours, and continued to uphold these convictions when they immigrated into Palestine. Thus we see that the second Alliyot not only brought into Palestine Eastern European Jews but also sociolist-minded immigrants.

Once in Palestine, the immigrants from a particular country and hence with a particular ideology tended to group together in parties of a particular ideology, that continued to exist after the establishment of the state.

Thus in Israel today there are ten major and many more minor political parties, each upholding a particular ideology and cooperating - at times even merging - with other parties of similar convictions.

In the table below, the reader is given an idea of the relative importance of each of the parties as can be deduced from the five Knesset (Parliament) election results between 1949 and 1961.

Table VII points out the individual strength of each party measured in terms of the number of Knesset seats won in each election but does not afford a classification into parties of the left, the right and the center. Such a classification is provided below,

TABLE VII

FIVE KNESSET ELECTION RESULTS, MAIN PARTIES

CONCERNED

(Number of Seats Held)

	First Knesset 1949	Second Knesset 1951	Third Knesset 1955	Fourth Knesset 1959	Fifth Knesset 1961
Mapai	46	45	40	47	42
Herut	14	8	15	17	17
	7	23	13	8	
Liberals					17
	5	4	5	6	
National Religious					
Agudat Yisrael	16	3	6	6	4
Polaei Agudat Yisrael		2			2
Mapam	19	15	9	9	9
Ahdut Ha'avoda			10	7	8
Arab Parties (Affiliated to Mapai)	2	5	5	5	4
Other Parties	7	-	-	-	-

Source: Israel, Government Yearbook, 1961-62, p. 20.

Notes: a) Figures for the first to fourth Knesset refer to the General Zionist and Progressive Parties which merged in 1961 to form the Liberal Party.

b) In the first five Knessets, Hapoel Hamizrahi and Mizrahi (now united in the National Religious Party) presented a Religious Front list jointly with Agudat Yisrael and Polaei Agudat Yisrael.

c) In the second to fourth Knesset Agudat Yisrael and Polaei Agudat Yisrael presented a joint list.

d) In the first two Knessets Ahdut Ha'avoda was united with Mapam.

e) The other parties represented in the first Knesset were: Sephradim (4 seats), Fighters (1), Wizo (1), and Yemenites (1).

and includes the more important parties of each block, the measure of importance being once again the number of seats held by each party. This three way classification does not imply, of course, that the three blocks are of equal strength.

Parties of the Left

The main leftist parties in Israel are the Mapai, Mapam, Ahdut Ha'avodah and the communist.

The Mapai was founded in 1930 as a result of the merger of Ahdut Ha'avodah (Unity of Labor) and Hapoel Hatzair (Young Worker) under the leadership of Dr. Haim Arlosorov. These two factions had before 1930 laid the foundation of the movement to establish Jewish settlements of the Kibbutz and Mushav type. They were also responsible for the launching of the mammoth projects of the Histadrut, and were the motive force behind the successful cooperative movement of the Jews in Palestine. In 1940 the Ahdut Havodah faction deserted the Mapai and joined forces with the Polaei Zion and later on with the Mapam.[1]

The Mapai which refers to itself as a "moderate,

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[1]Hani al-Hindi and Muhsin Ibrahim, Israel, 1958, pp. 144-145 (In Arabic).

democratic, non-marxist socialist, Zionist party", is today the most powerful party in Israel and has been so ever since its formation. It claims that the Zionist resurrection in Israel and the need to create a working class that would lead the country, are things that cannot be obtained by borrowing ideological views formed under socio-political circumstances different from those that exist in Israel. The right thing, says Mapai, is to develop a sort of Israeli socialism and abide by its rules.[1] The Mapai has abided by its rules by establishing a large number of agricultural settlements, creating a widespread cooperative movement, organising enterprises such as the famous contracting company Solel-Boneh (Koor) and the Workers Bank (Davar), setting up the Kupath Holim (sick fund) and erecting public housing units. These schemes it realised through its control over the Histadrut (which is its main source of influence), government offices and the Jewish Agency.[2]

In the realm of economic ideology the Mapai advocates a "gradual democratic planning of the economy

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[1]Israel, Who's Who, 1952, p. 739.

[2]Oscar Kraines, Government and Politics in Israel, 1961, p. 63.

with step by step nationalization of natural resources, public services and public utilities. Pragmatic, compromising and flexible, however, the party feels that the Israeli economy should be based on harmonious, side by side development of constructive private enterprise and planned collectivist endeavor. To encourage private investment domestically and from abroad, Mapai has proposed and carried out many concessions to private enterprise. It has favored wage ceilings, taxes on cooperative settlements, hiring of immigrants to work on collective farms, and sale of a sizable amount of "abandoned" Arab land to private persons. It has, further, rejected any "soak-the-rich" program, since this would discourage private investment at a time when the economy depends on private financial aid and investment from abroad. It has urged a system of graduated taxation, premiums for productivity, and an index approach to cost of living allowances. Wage increases, Mapai insists, must depend on increased production; and increased output must be directed mainly to increasing exports or lowering prices of commodities for domestic consumption and only partly for raising wages.[1]

With regards to immigration the Mapai believes that the state should maintain an open door policy so that any Jew who wants to immigrate may do so with the help of the state and semi-public organisations whose duty is to help absorb him into the economy and protect his rights.[2]

The second most important socialist party in Israel is the Mapam (United Laborers of Israel), founded in 1948 upon the merger of Hashomer Hatzair (Young Guard) and Ahdut Ha'avoda, after a split in Mapai. It is a purely ideological party based on chalutzic zionism and revolutionary socialism and has a marxist element. It draws its strength from the collective and cooperative agricultural settlements, from industrial workers and intellectuals.[3]

The program of the Mapam advocates the establishment of a classless socialist society, based on political leadership by farmers in collectives. The party opposes the financial concessions made to private enterprise to encourage economic expansion, and does not favour foreign capital investment in Israel. It maintains that the

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[1]Alex Rubner, The Economy of Israel, 1959, pp. 44-45. (It must be noted that the economic policy actually put into effect by Mapai-dominated governments over the years 1948-62 has not always borne out the principles underlying Rubner's statement.)

[2]Hindi and Ibrahim, op.cit., p. 153.

[3]Ibid., p. 157.

economy can be placed on a sound basis if all industry was nationalized together with natural resources and if agriculture was completely collectivised. The Mapam adopts the policy of "tax-the-rich-and-protect-the-poor" through increased direct taxation of property owners, compulsory investments and excess profit taxes together with reduced indirect taxes and a ban on wage freezes. Like the Mapai, it believes in an open-door policy with regard to immigration.[1]

Left of the Mapai and right of the Mapam is a third labor party, the Ahdut Ha'avodah which ran its first election as an independent party in 1955. Prior to that date it had been a part of Mapai from the day of its establishment till 1948 when it joined Mapam. Ahdut Ha'avodah is the second most influential party in the Histadrut, and draws it strength from urban workers. It calls for a reduction in imports, especially consumer goods, the increase in exports and the raising of subsidies and export premiums. Moreover, the party strictly opposes any changes in the system of automatic cost-of-living allowances.[2]

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[1] Kraines, op.cit., pp. 68-69.

[2] Ibid., pp. 71-72.

Parties of the Right

The right wing in Israel includes a rather large number of parties ranging from moderate factions to extremists. Included in the right wing group are the religious parties which stand for the founding of legislation and public policy on the religious tenets of Judaism. Though they may differ amongst themselves regarding certain issues, these parties hold liberalist convictions and anti-solicitist attitudes as far as economic planning is concerned.

The only right wing party of significance in Israel is Herut or Freedom party. Herut is the strong and stubborn opponent of Mapai. This fanatic party came into existence after the establishment of the state when the terrorist Irgun-Zvei-Leumi (National Military Organisation) joined forces with other terrorist groups like the Stern group (followers of Abraham Stern) to found a political party. The Herut's emblem shows the boundaries of Israel extending over both banks of the Jordan River, emphasizing the desire to expand the territories of Israel. In line with this expansionist conviction, Herut advocates the rapid expansion in immigration programs so as to activate a military build-up for the acquisition of new Arab territories.[1]

The Herut is an anti-socialist party that dislikes Mapai's concept of a broad economic role by the state, and would greatly approve stripping the Histadrut (the main subject of its continuous attack), of all its enterprises and to hand these over to the trust of the private sector. The private sector, maintains Herut, could do a better job than the Histadrut, provided it was left to operate unhampered by restrictions in the form of high taxes and currency controls. The party maintains that such controls should be gradually decreased, which would act as an incentive to higher production levels that would enable the country to end its shameful dependence on foreign charity. Economic independence is a closely-held aim of Herut and the party advocates taking strict measures to economise the use of foreign exchange domestically and to boost production for export to meet toward the same aim.[2]

Parties of the Center

There are four parties in the center, but only

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[1]Hindi and Ibrahim, op.cit., p. 161.

[2]Krains, op.cit., pp. 80-81.

two are of significance; the General Zionist and the Progressive Zionist, and these two merged in 1961 to form the Liberal party.

The General Zionists are champions of capitalism or free enterprise in Israel, and draw their strength from the spheres of businessmen and professionals. As such the party opposes the promotion and subsidization of collectivism by the state, and is especially bitter against the Histadrut operating business enterprises and enjoying monopolistic powers. Although it calls for the promotion of a social insurance system and a policy of land development, it believes that the economic development of the country is best realised by the encouragement of private enterprise. The latter if left to operate in accordance with the profit motive and under a less vigorous tax system, would create enough opportunities to absorb the ever-increasing numbers of immigrants to whom the country should keep its doors wide open.[1]

The Progressive Zionist party was established in 1948 following a split in the ranks of the General

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[1] Israel, Who's Who, op.cit., p. 740.

Zionists. The former party claims to be a representative of all the factions in Israel since its members include farmers, civil servants, industrialists, labourers, university graduates and members of agricultural settlements. Advocating a liberal, though non-socialist, outlook toward labour and social welfare, it is in essence a party in favour of free enterprise.[1]

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[1] Hindi and Ibrahim, op.cit., p. 165.

CHAPTER III

ISRAEL'S ECONOMIC ACHIEVEMENTS

In the preceding chapters, attention was focused primarily on those aspects of the Israeli economy that were considered to be of value in helping the reader form a clear idea of the background and characteristics of the economy under study.

In the present chapter, an attempt will be made to discuss the economic achievements of Israel. Such a discussion is thought here to be of importance because it takes us out of the realm of description and into the realm of economic analysis, and this in turn brings us closer to the stage at which we can begin to discuss the main question of this study, namely the country's prospects for economic independence.

The method adopted for gauging Israel's economic achievements will mostly be the analysis of the growth of the country's gross national product (subsequently GNP), and the citing of some of the developments in industry and agriculture as illustrations of such growth.

Before that is done, however, an attempt will be made to review the population background against which Israel's achievements are outlined. The importance of population growth, to the examination of which the first section of this chapter is devoted, derives mainly, as will be shown, from its immigration content, so crucial to the standards, priorities and achievements of the country.

The period of coverage, which ought to extend over the whole period of Israel's exist3nce, that is from 1948 to 1962, will on the whole be limited to the period between the beginning of 1950 and the end of 1960, owing to the inadequacy or inavailability of earlier and more recent data.

The exclusion of 1948 and 1949 is further justified mainly because these two years were quite abnormal, characterised as they were by open war, mass immigration, and inflation.

It is necessary to point out here, and before going any further, that the assessment of Israel's economic achievements, by an analysis of the growth in GNP, would not exhaust all the different aspects of these achievements. A number of other indicators of growth such as the rise in the level of employment, the growth in educational and technical standards, etc., deserve examination but will not be covered, mainly because of the deficiency in relevant information.

A. Population

At the termination of the Mandate, Palestine's population counted some 2,115,000 persons of whom about 700,000 were Jews and 1,415,000 were Arabs and other non-Jews. By the end of 1960 Israel's Jewish population had increased by 273 per cent to 1,911,200 persons while the Arab and other non-Jew population had decreased by about 592 per cent to about 239,200 persons.

Of the 1,211,200 persons that represent the increase in the Jewish population, as much as 854,582 persons or 71 per cent were immigrants who came and remained in Israel during the thirteen year period. The bulk of net immigration (656,522 persons) took place in the four-year period from the end of 1948 to the end of 1951, while the balance of 198,060 persons came in nine annual waves which averaged about 22,000 immigrants per annum. The average for the period 1952-1960 falls short of the average annual natural rate of growth of population in the country, in contrast to the period 1948-1951 when the rate of growth through immigration exceeded by far the natural rate of growth.

In order to be able to draw a somewhat more comprehensive picture of population growth in Israel it is easier to refer to Table VIII below, which traces the year-by-year growth of population.

Table VIII points clearly to the extremely important role played by immigration in the process of population growth in Israel. Hence, an analysis of such growth should center mainly on an analysis of the immigration movement.

Just like the movement in Mandatory days, Jewish immigration to Israel took the form of successive waves (Aliya). The difference, however, from the point of view of the duration and numbers included in each immigration wave (Aliyot), is that whereas every post-1948 Aliyot extended over a shorter period than the average pre-1948 Aliyot it brought relatively more immigrants into the country. The fact that the post-1948 waves were more dense is of course quite understandable, since the country's doors were thrown wide open in the face of immigration after 1948 in contrast to the Mandatory period when the authorities imposed certain restrictions on Jewish immigration, as explained

TABLE VIII

POPULATION OF AND IMMIGRATION TO ISRAEL, 1948-1960

Year	Total population at end of yr.	Jews	Arabs and others	Total immigration	Total emigration	Net immigration
1948[x]	2,115,000	700,000	1,415,000			
1948	920,000	765,000	155,000	101,837	1,154	100,683
1949	1,173,900	1,013,900	160,000	239,954	7,407	232,547
1950	1,370,100	1,203,100	167,000	169,720	9,966	159,754
1951	1,577,800	1,404,400	173,400	174,014	10,476	163,538
1952	1,629,500	1,450,200	179,300	23,408	13,500	9,908
1953	1,669,400	1,483,600	185,800	10,388	13,000	2,612
1954	1,717,800	1,526,000	191,800	17,485	7,500	9,985
1955	1,789,100	1,590,500	198,600	36,327	6,400	29,927
1956	1,872,400	1,667,500	204,900	54,996	11,400	43,596
1957	1,976,000	1,762,700	213,300	71,100	11,400	59,700
1958	2,031,700	1,810,100	221,600	26,093	11,700	14,393
1959	2,088,700	1,858,800	229,900	23,045	9,750	13,295
1960	2,150,400	1,911,200	239,200	23,644	8,800	14,844

x May 1948.

Source: Yusif A. Sayigh, The Israeli Economy, 1963 (In Arabic).

in Chapter I.

The first Aliyot after the establishment of the state took place during the period May-August 1948, and was distinguished by the top priority given to young Jews from Europe brought to Israel to help bolster the position of the Israeli armed forces engaged in war with the Arab countries.

Mass immigration did not begin until September 1948 with the liquidation of the principal German, Austrian and Italian displaced persons' camps. These camps had been erected to harbour the survivors among the occupants of Nazi concentration camps liberated after the war, and were to serve as points of embarkation for Israel. Zionist institutions for immigration such as the "Mossad le'Aliya", which had specialised in illegal immigration to Palestine, were assigned the role of organizing the mass immigration to Israel, financed by Zionist and American funds.[1]

In the winter of 1948-49 the Jews who had been

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[1]Moshe Sicron, Immigration to Israel, 1948-1953, Falk Project For Economic Research In Israel, Jerusalem, 1957, pp. 33-34.

retained in Cyprus for attempted illegal immigration to Mandatory Palestine, were evacuated and transported en masse to Israel.[1]

A wave comprising a large part of the Jewish communities of Bulgaria, Yugoslavia and Turkey followed. Some 100,000 Polish Jews and 120,000 Rumanian Jews were transported to Israel in 1949 just before Poland restricted emigration and before Rumania put a complete halt to it. Emigration from Arab countries and particularly from Iraq, North African countries and from Iran resulted in the evacuation of a sizeable part of the Jewish communities of the latter two and almost all of Iraq's Jews by the end of 1950. Operation "Ezra and Nehemia" alone, brought 124,000 Iraqi Jews and 27,000 Irani Jews towards the end of 1951. Operation "Magic Carpet" airlifted almost the entire Jewish community of Yemen to Lydda by way of Aden.[2]

The sum total of these operations landed 627,519 Jews in Israel during the period May 1948 to the end of 1951. The significance of this figure emerges more

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[1] Ibid.

[2] Ibid.

clearly when we note that total Jewish immigration to Palestine from 1882 to mid-1948 was between 542 and 562 thousand immigrants only,[1] and that the total Jewish community of Palestine numbered some 700,000 in May 1948.

Mass immigration, resulting from the open door policy of Israel which, in accordance with the country's "Declaration of Indépendence" and the 1950 Law of Return, welcomed all those Jews of the world who chose to immigrate, was brought to an end with the close of 1951. The open door policy had created a number of serious problems for the government, the Zionist institutions concerned and the country as a whole. The immigrants were coming in numbers exceeding the absorptive capacity of the national economy and the vast organizational facilities of the authorities. The varying backgrounds of the immigrants created sociological problems and their state of poverty put a heavy burden on the institutions that were forced to provide them with homes and food, pending their allocation to new jobs. The immense funds spent on the construction of homes and transition camps (Maberot) for the new immigrants and the wages they received for

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1. _Ibid._, p. 34.

doing relief work, such as building roads, together with the money spent on the purchase of food for these immigrants, all served to create serious inflationary pressures in the economy. These mal-effects of the open door policy forced the Jewish Agency to reconsider this policy despite all the Zionist objections that immigration was the undisputable right of every Jew. The reconsideration brought about a number of restrictions that were imposed on the right of Jews to immigrate to Israel at the expense of the Zionist institutions concerned. The new restrictions established a case of priority that gave top treatment to young and healthy people prepared to spend two whole years in agricultural settlements working and living off the soil. Those immigrants who had relatives in Israel who could support them and immigrants coming on their own were excluded from all restrictions (unless they presented a threat to public health and security).[1]

B. National Accounts

The preceding section may have led the reader to form the opinion that the torrent of Jewish immigration must have created insurmountable economic problems.

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[1] *Ibid.*, p. 35.

There is no doubt that Israel's problems as a result of immigration were many, but the severity of these problems was somewhat reduced by a number of 'cushioning' factors among the most important of which was the immense Arab exodus from the country.

Net Jewish immigration brought 656,522 persons into the country by the end of 1951, while the forced Arab flight took out some three quarters of a million in a matter of months. Jewish immigration continued to be unrestricted up to the time when the number of Jewish immigrants had about made up for Arab flight.[1]

Unwittingly, the Arab exodus and the property which the Arabs abandoned in their flight,[2] greatly

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[1]U.N., Economic Survey Mission for the Middle East (The Clapp Mission), Part I, The Final Report and Appendices, 1949, p. 15.

[2]Estimates of the value of such abandoned property, made by various parties concerned, have varied from the minimum of LP 100 million made by the Palestine Reconciliation Commission, to the maximum of LP 2,000 million made by the Higher Arab Commission for Palestine. Yusif A. Sayigh's estimate is about LP 757 million. No estimate has been attempted by the Israelis.

facilitated the task of Israel, especially during the first few years after the establishment of the state. Indeed, one of the more remembered statements attributed to Chaim Wizeman is that which called the Arab exodus a "miraculous simplification of Israel's task".

Moving from this advantageous position (and relying mainly on foreign aid, as will be shown in the following chapter) Israel has managed to record a number of noteworthy achievements, to the examination of which the remaining part of this chapter will be devoted. Before entering into such an examination, however, it is only fair that the reader be brought into contact with some of the handicaps facing a person seeking to construct meaningful time series pertaining to the developments in Israel's national accounts.

The reader was forewarned at the beginning of this study that a number of difficulties have been met within the collection of the data. The most important of these difficulties that are relevant at this point are the disagreements among the various official and semi-official publications with regards to the actual figures of national income, GNP, capital formation, etc. The methods of estimating and classifying the necessary data were found to differ markedly from one source to another, and even when the methods were similar the results were often different. Thus it became necessary to rely on what could be considered as the most reliable sources and the sources that cover the greatest number of years and to use the same method, or nearly the same method, of estimation and classification.

Don Patinkin's estimates of Israel's national accounts for the period 1950-1958 are considered by many, and emerge from our own examination, as the most reliable for the period, and these estimates will be heavily used in our analysis. Supplementary information for the years 1959 and 1960 will be taken from the Bank of Israel Annual Report for 1960, which is again considered among the more reliable sources.[1]

According to Patinkin's estimates, Israel's GNP at current prices increased from IL 474.8 million in 1950 to IL 3,530 million by the end of 1958, while the country's national income at current factor cost increased from IL 352.9 million in 1950 to IL 2,728 million in

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[1]Don Patinkin, The Israel Economy: The First Decade, The Falk Project for Economic Research In Israel, Fourth Report, 1957 and 1958. The Bank of Israel, Annual Report 1960.

1958.[1]

The Bank of Israel reported that by the end of 1960 the country's GNP was valued at IL 4,396 million at current prices while the national income had reached IL 3,376 million.[2]

The implication of these data is that in a period of ten years Israel's GNP increased by more than nine and a quarter times, namely at a compound rate of growth of about 25 per cent per annum, and that the national income grew at the compound rate of about 26 per cent per annum.[3] The mere enormity of these rates of growth raises many a doubt as to their validity, but there is of course, as might very well be expected, an explanation for these abnormal rates.

It will be noted that the GNP and national income figures quoted from Patinkin and the Bank of Israel, are at current prices, and current prices tell exaggerated stories in countries gripped by inflation,

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[1]Patinkin, <u>op.cit</u>., pp. 45 and 62.

[2]Bank of Israel, <u>Annual Report, 1960</u>, p. 63.

[3]The formula adopted for the calculation of the compound rate of growth is:

$\log. (1 + i) = 1/n\ (\log. \text{Amount}/\text{Principal})$ where i = compound rate and n = number of years.

as in the case of Israel. The extent of this exaggeration can in a way be measured from the abnormal developments in the consumer price index during the period in question. This index records an increase from 100 in 1950 (base year) to 333.4 in 1960.[1]

Accordingly, if we are to be able to judge somewhat more accurately the achievements of Israel, we must view the growth in GNP at constant prices and not at current prices. To do that, we divide the GNP figure at 1960 prices by the 1960 consumer price index with 1950 as a base year (4396 ÷ 333.4) and arrive at the 1960 GNP at constant 1950 prices of IL 1,318.5 million. Thus it would be more revealing to state that Israel's GNP increased from IL 474.8 million in 1950 to IL 1,318.5 million in 1960. These new figures indicate a 277.7 per cent increase in GNP in ten years and not an increase of 925.9 per cent as indicated by the current prices figure. This means that the compound rate of growth falls from 25 per cent per annum to 11 per cent per annum as a result of deflating by the consumer price index for arriving at GNP at constant prices.

The reduction is evident, but it ought in fact

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[1] Ibid.

to be much greater because the consumer price index is higher than what it is reported to be. To begin with this index did not take into consideration the black market prices which ruled for many a consumer good in the country. Such a disregard for the prices of a widespread market and the inclusion of only controlled prices tends, of course, to under-estimate the full increase in the consumer price index. Furthermore, the government is reported as having manipulated prices by increasing the supply of certain consumers' goods entering into the consumer price index, just before the prices of those commodities are quoted for the index. Such a practice evidently artifically lowers the prices of the particular commodities concerned and tends to produce a deflated consumer price index.[1]

The reason for these artificial deflations of the consumer price index is assumed to be the desire to limit wage increases, since wage increases in Israel are linked to the cost-of-living index. This limitation is done in an effort to combat the inflationary pressures resulting partly from the continued demand for wage

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[1] Rubner, op.cit., Chapters VIII and IX; Patinkin, op.cit., pp. 44-46.

increases at every substantial increase in the cost-of-living index of the country.

From the above it becomes clear that the consumer price index is not a very reliable measure of the real increase of the cost of living in Israel, nor is it the best index with which to deflate GNP at current prices, but we have no alternative to using that index for deflating purposes and to depending on the reported increases in it, since it is the index used in Israel's studies, official and unofficial alike.

The further question as to the choice of a better index comes mainly as a result of the knowledge that both consumer and investment prices enter into the estimation of the GNP, and of the finding that during the period 1950-1960 the index of investment prices reported a much higher increase than that of the consumer price index. Thus the investment index grew from 100 in 1950 to 525.9 in 1960, whereas the consumer index grew from 100 to only 333.4 as mentioned earlier in this section.[1]

Hence, we can arrive at more accurate results for our purpose if we utilize both the investment and consumer price indexes. To do that for instance, we

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[1]Bank of Israel, <u>op.cit.</u>, p. 63.

should produce a weighted average of the two by multiplying the consumer price index in each year by its share in the general price index, or multiplying it by the share of consumer goods and services in the GNP, and doing the same for the index of investment prices, and then taking as the denominator the average of the two totals. Unfortunately, however, the available information is quite inadequate for producing such a weighted average. Hence the only alternative is to be satisfied with an unweighted average of the two indexes. Such an unweighted average is (333.4 + 525.9 ÷ 2) = 429.6 in 1960.

If we divide the 1960 GNP at 1960 prices, i.e. IL 4,396 million, by this average, we arrive of course at a much lower figure than if we utilised the consumer price index alone. The new 1960 GNP would thus be IL 1,023 million at constant 1950 prices. This new figure gives us an increase of 215.5 per cent in ten years vis-a-vis the 277.7 per cent arrived at by utilising the consumer price index alone. The new annual compound rate of growth would be only 8 per cent in comparison to the 11 per cent arrived at by utilising the other method.

Yet, whether it is 11 per cent or 8 per cent the fact remains that as far as we can judge, Israel's achievements have been quite significant. Few countries can claim to have achieved anywhere near that rate of growth and this undoubtedly further underlines Israel's achievements.

A question comes to mind here concerning the means by which Israel has been able to achieve these heights in economic development. There is necessarily more than one explanation, but we propose here to enter into a discussion of the process of capital formation in Israel as one of the major factors involved, Before doing that, however, it is advisable that we examine the degree of capital formation in some countries more familiar to us in this part of the world so that when we do come to Israel's investment activity we can judge it by comparing it with those countries.

A standard measure of the magnitude of investment activity in any country is the relation of gross domestic capital formation to GNP and it is this standard that we shall adopt here. Thus we will examine the ratios for Jordan, Lebanon, Morocco, Egypt and Turkey, which are the only Middle Eastern countries for which relevant data are available.

In the period 1959-1961, Jordan's GNP totalled about JD 301.8 million while its gross domestic capital formation constituted about JD 40.8 million. In other words, Jordan's ratio of gross domestic capital formation to GNP was about 13.5 per cent.[1] That of Turkey from 1956 to 1958 was about 8.2 per cent, while Lebanon's ratio for the same period was about 6.8 per cent.[2] The available figures for Egypt show a 10.2 per cent for the period 1950-1956, while those for Morocco average about 19.8 per cent for the period 1951-1956.[3]

Thus the ratio varied from as little as 6.8 per cent to as much as 19.8 per cent. The significance of these figures in comparison to Israel's standards emerges markedly when we note that Israel's ratio of gross domestic capital formation to GNP averaged about 26.5 per cent from 1950 to 1960.[4] The difference in ratios is evident.

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[1]Hashemite Kingdom of Jordan, The National Accounts, 1959-61, pp. 1-2.

[2]United Nations, Economic Developments of the Middle East, 1958-1959, pp. 43-44.

[3]United Nations, Economic Survey of Africa Since 1950, N.Y., 1959, pp. 205-206.

[4]Patinkin, op.cit., p. 48 and Bank of Israel, op.cit., p. 11.

Furthermore, in order that this difference may be placed in a broader context, a table is provided below to compare Israel's ratio of gross domestic capital formation to GNP with the ratios of 16 European and American countries.

Table IX places Israel as the country with the third highest investment activity amongst the countries listed, measured in terms of the ratio of gross domestic investment to GNP.[1]

Thus whether compared with countries of the Arab world or with American and European countries, Israel stands out prominently as one of the world's most investment-minded countries. The investments of Israel have helped it in achieving what it did achieve in the decade under study, but there is more to the story of capital formation in Israel than the achievements of this capital formation. The investments, naturally, had to be financed either by domestic savings or foreign aid, and we shall have occasion to go into such considerations in Chapter IV,

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[1]Patinkin claims that Norway's figures are inflated and those of Venezuela are unreliable. If this is the case then Israel might rank as the country with the highest ratio in Table IX.

TABLE IX

RATIO OF GROSS DOMESTIC INVESTMENT TO GNP IN ISRAEL AND SOME SELECTED COUNTRIES *

Country	Per Cent	Rank
Norway	28.2	1
Venezuela	27.7	2
Israel	26.8	3
Finland	25.0	4
Netherlands	23.9	5
West Germany	23.8	6
Austria	22.1	7
Union of South Africa	20.7	8
Argentina	20.2	9
Italy	20.2	10
France	18.9	11
USA	18.5	12
Ireland	14.8	13
UK	13.5	14
Panama	13.1	15
Puerto Rico	12.8	16
Colombia	11.1	17

* For Panama, Puerto Rico and Colombia, the unweighted average of 1950, 1952 and 1954, and for Venezuela for 1952 and 1954; for other countries the unweighted average of 1950, 1952 and 1955. For Israel the average for 1950-1958.

Source: Don Patinkin, "The Israel Economy: The First Decade", Falk Project for Economic Research in Israel, Fourth Report, 1957 and 1958, p. 50.

and in Israel's case foreign aid has played an unduly preponderant role. But before moving on to that chapter let us for a while discuss some of the developments in industry and agriculture that came about mainly as a result of the investments discussed above.

C. Industry

The first important development in Israeli industry after the establishment of the state came in 1950 when the government issued a law for the encouragement of capital investment. In accordance with this law, an Investment Center was created to lend expert advice in matters of industrial investment and to act as a liaison agency between the government and private investors. The Center was instructed to investigate proposals by private individuals or companies and recommend for the approval of the government those investment projects which it considered to be economical to the national economy. To arrive at its decisions, the Center was to consider the contribution of the proposed investment to the augmentation of the economy's absorptive and productive capacities, and the extent to which such an investment would improve the country's balance of trade situation, its demographic distribution and the greater utilisation of its natural resources.[1]

To encourage private domestic and foreign investments to be forthcoming to this Center, the government granted a number of privileges to foreign and national private capital. Thus a non-resident was entitled to repatriate annually, in the foreign currency in which he made the investment, 10 per cent of the capital initially invested, either as profit or as amortization or both, providing that the repatriated sums did not exceed the profits of that year. Investment in imported machinery and equipment was to be considered similar to an investment in foreign currency. Moreover, the government promised to reduce its taxes to a single tax of 28 per cent of profits, instead of the dual tax of 25 per cent of income and 28 per cent of profits. It also provided domestic industry with a sheltering umbrella of protective tarrifs and a complex system of subsidies. Moreover, in an attempt to direct investment activity towards development regions such as the Negev, the government promised to open credit to investors in such regions that might reach as much as 65 per cent of the approved

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[1] U.N., Economic Developments in the Middle East, 1945-54, p. 122.

capital.[1]

By the end of 1958 the Investment Center had approved 790 projects, 91 per cent of which were submitted by private concerns. Total investment by the end of 1957 was more than IL 1,250 millions. About 70 per cent of this total sum came from foreign sources.[2]

As a result of these investments and their direction, Israeli industry has known a number of significant changes. Industrial production quadrupled and the number of industrial employers increased from 45,000 to 140,000 between 1949 and 1958.[3] New establishments utilising up-to-date equipment have been created while existing firms have been expanded and modernised. New products such as motor vehicles, motor scooters, wireless sets, electrical appliances, plywood, paper, insulating boards, superphosphate, sulphuric acid and other chemicals, tyres, glass, etc., have been introduced. New industries have also been directed out of the concentration centers around Haifa and Tel-Aviv and into development areas such as the

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[1] Syrian Army, Israel, 1959, p. 494.

[2] Ibid.

[3] "Rebirth In An Antique Land," The Economist, May 16, 1959, p. 20.

Negev.[1] The Israeli industrial enterprise, however, has remained generally small or medium-sized with very few large firms, on account of the limited local market.[2]

In 1957, the preliminary outlines of a general plan of industrial development were framed. They envisaged the investment of some IL 358 million in the various industrial branches (outside mining and electric power), during the period 1958-61. The resulting value added was expected to be IL 340 million, including the output of industrial potential unexploited in 1957. The additional labour intended to be put to work on the basis of this plan was estimated at 45,300 persons.[3]

For the purpose of meeting its targets, the plan sought to encourage foreign investors to invest in Israeli industry and called upon the government to participate in investment and to offer long-term loans to domestic entrepreneurs. It also advocated the expansion of vocational training, the preparation of technicians,

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[1]Food and Agricultural Organization, The Economy and Agriculture of Israel, Jerusalem, 1959, pp. 50-51.

[2]*Ibid.*, p. 51.

[3]*Ibid.*, p. 87.

the establishment of research centers to raise the quality of manufactured products, and market research centers to improve marketing techniques and to advise on what commodities to produce in the country.[1]

The plan's most ambitious parts were those concerned with the raising of efficiency levels and the expansion in basic or heavy industries, particularly metallic industries (part of which concerned the establishment of a "Steel Town" at Acre), textiles, chemicals, foodstuffs and transportation items, priority being given to industries drawing upon local raw materials.[2]

However, there were many inefficient investments or misinvestments in certain branches and enterprises, despite the large sums and great efforts that have been invested in industry in Israel.[3]

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[1] Ibid., p. 88.

[2] Ibid., pp. 88-89.

[3] Alfred Sherman, "Israel's Economic Problems", The World Today, October, 1959, p. 396. "Specialist consultants, for example, questioned the advisability of investing IL 120 million (with a large foreign currency component) in a steel combine which was to mine low-grade ores and smelt them by electricity in order to make and roll billets for reinforcement rods. It was pointed out that the savings in foreign currency would be infinitisimal and the cost very high. But the project, sponsored by the trade-union-owned industrial combine, has been established with government capital and tariff protection for its

Having outlined some of the major developments in industry in Israel it remains for us to give the reader an idea of the type of goods that this industry has been known to specialise in in recent years, i.e. in 1958, 1959 and 1960. Accordingly, a table is provided below, covering these years and showing the gross industrial product by branch in constant 1958 prices.

From the table presented, it will be noticed that throughout the three year period 1958 through 1960, the clothing industry and the food, drinks and tobacco industry were by far the most important industries from the point of view of their share in the total value of gross industrial product. It will also be noticed (with some simple calculations) that these two industries were responsible together for 24.5 per cent of total gross industrial product in 1958, 24.8 per cent in 1959 and 23.8 per cent in 1960. Moreover, each of them produced

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products. Experts similarly advised against sinking government money in a copper-mining project near Eilat, but their advice was disregarded; the final investment was twice what had been estimated, at constant prices, and unless world prices of copper show large and unexpected increase the plant will not only fail to cover capital charges but is likely to show a continued deficit on current operation."

TABLE X

THE GROSS INDUSTRIAL PRODUCT, BY BRANCH 1958 TO 1960 (1958 PRICES)

	1958		1959			1960		
	Gross product (millions of IL)	Gross product as a percentage of gross output of branch	Gross Product (millions of IL)	Gross product as a percentage of gross output of branch	Percentage increase in gross product as compared with 1958	Gross product (millions of IL)	Gross product as a percentage of gross output of branch	Percentage increase in gross product as compared with 1959
Mining & quarrying	17.9	57.2	24.2	57.6	35.2	26.1	57.7	7.9
Food, drinks & tobacco	91.7	21.2	107.7	21.5	17.4	112.6	21.3	4.5
Textiles	58.1	35.1	64.3	33.3	10.7	80.5	35.2	25.2
Clothing	92.2	44.9	109.0	44.8	18.2	119.8	44.8	9.9
Wood and carpentry	65.0	46.6	77.2	46.5	18.8	83.3	46.6	7.9
Paper and cardboard	13.5	38.7	14.7	38.6	8.9	17.9	36.7	21.8
Printing and publishing	33.1	43.5	38.1	43.5	15.1	42.4	43.4	11.3
Leather and footwear	44.1	55.1	46.9	55.0	6.3	49.4	55.1	5.3
Rubber and plastics	22.5	43.9	26.1	44.5	16.0	31.1	44.5	19.2
Chemicals and oil	48.6	23.5	56.0	23.4	15.2	64.3	23.1	14.8
Non-metallic minerals	56.3	52.9	63.9	52.7	13.5	64.6	52.8	1.1
Diamonds	20.0	29.0	27.7	29.1	38.5	33.8	28.9	22.0
Basic metals	15.2	38.7	17.7	35.5	16.4	23.7	37.9	33.9
Metal goods	64.9	45.5	73.4	46.3	13.1	79.5	45.6	8.3
Machinery	26.2	47.4	30.7	47.2	17.2	34.9	47.3	13.7
Electrical equipment	24.4	46.0	28.6	46.1	17.2	34.9	46.2	22.0
Transport vehicles and repairs	40.6	45.5	46.8	45.4	15.3	52.4	46.0	12.0
Miscellaneous	16.9	53.8	19.4	53.7	14.8	24.0	53.9	23.7
TOTAL	751.1	37.3	872.3	37.2	16.1	975.1	37.2	11.8

Source: Bank of Israel, Annual Report, 1960, p. 148 (Table XI-2).

on the averag e more than 30 per cent in excess of the third and fourth largest producing industries, namely wood and carpentry, and metal goods.

The rate of growth from year to year varied between the various industries and within each industry. "The different relative rates of expansion in the main branches of industry reflect the changes that occured in industry's orientation towards exports. The branches dependent on the local market's demand for consumer goods, such as most of the food industry, a part of the clothing branch and the leather branch on the whole expanded more slowly. However, branches supplying the home market with durable consumer goods mainly purchased by the upper income groups continued to expand very fast. Branches producing chiefly for the building sector, such as mining and quarrying, the wood industry, the metal industry and the non-metallic minerals industries expanded only moderately. On the other hand, branches producing mainly for export, or which diverted their products to exports as an alternative to the local market, grew appreciably. The same applies to branches developed during recent years for the specific purpose of import substitution, such as paper, textile, basic metal and electrical equipment industries."[1]

The government has done a lot to encourage industry in general and production for exports and import substitution in particular. Exporters were granted premiums on their exports; furthermore, they were refunded the duties paid for the import of raw materials utilised for the manufacture of products destined for both export and domestic markets. The exporters were also offered cheaper input prices and often higher product prices in the home market. "In such cases, not only is the economy likely to pay an exceedingly high marginal price for the additional exports, but the very volume of exports becomes dependent upon domestic demand and the exporters' position in the home market. In so far as they enjoy with or without government assistance, the market position of cartels or monopolies, they are able to raise their prices at home and thus obtain compensation for their lower income from exports."[2]

Just in the way of familiarising the reader with the type of product which Israeli industry exports, a

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[1]Bank of Israel, <u>op.cit</u>., pp. 145-146.

[2]<u>Ibid</u>., p. 164.

table is provided below with information regarding direct industrial export by branch in 1958, 1959 and 1960.

TABLE XI

DIRECT INDUSTRIAL EXPORTS BY BRANCH, 1958 to 1960
(Thousands of IL. 1958 prices. IL 1.80=$)

	1958	1959	1960	Percentage Increase or Decrease (-) Over Preceding Year	
				1959	1960
Mining and quarrying	6,602	13,764	15,222	108.5	10.6
Food, drinks and tobacco	14,253	17,837	19,838	25.1	11.2
Textiles	6,005	9,933	21,376	63.7	117.4
Clothing	10,029	12,338	14,773	23.0	19.7
Wood and Carpentry	5,755	7,776	8,506	35.1	9.4
Paper and Cardboard	1,765	2,976	4,193	68.6	40.9
Printing and publishing	1,657	867	3,118	-47.7	259.6
Leather and footwear	1,105	622	895	-43.7	43.9
Rubber and plastics	11,429	13,834	17,333	21.0	25.3
Chemicals and oil	6,567	16,523	22,652	151.6	37.1
Non-metallic minerals	4,824	7,934	8,262	64.5	4.1
Diamonds	61,883	86,074	105,699	39.1	22.8
Basic metals	930	1,092	1,855	17.4	69.9
Metal goods	2,598	7,362	8,694	183.4	18.1
Machinery	1,140	1,736	3,677	52.3	111.8
Electrical Equipment	384	682	1,179	77.6	72.9
Transport vehicles & repairs	4,892	10,564	6,895	115.9	-34.7
Miscellaneous	4,593	10,253	13,488	123.2	31.6
Total	146,411	222,067	277,655	51.7	25.0

Source: Bank of Israel, <u>Annual Report</u>, 1960, p. 166 (Table XI-B).

D. Agriculture

As was shown in Chapter I, agriculture played less of an economic and more of an ideological and social role in the life of the Jewish community of Mandatory Palestine. The objective of agricultural policy then centered on the establishment of the Jewish community as a land-owning majority group in Palestine. Agricultural colonization was assigned the role of 're-establishing the sacred attachment of the Jews to their promised land'.

With the establishment of the state in 1948, agriculture continued to be held in high esteem from ideological and social points of view, but gradually economic considerations began to assume more significant attention until by February 1962 with the declaration of the New Economic Policy, economic logic emerged clearly as a guide for action.

The circumstances under which the state had come into existence necessitated a reconsideration of the goals of agricultural activity. The siege conditions thrown on the newly independent state, the exodus of Arab farmers who had thereto supplied the Jewish community with cheap foodstuffs, the mass immigration of Jews, among other things all pointed clearly to the need for replanning the goals of agricultural activity.[1]

Agriculture came to be looked upon after the establishment of the state not only as a means for providing work for immigrants but also as a means by which to meet the pressing needs of the population for basic foodstuffs. The new state had to feed itself in difficult times and Israeli farmers together with government and semi-public institutions were called upon to utilise more land and to step up agricultural produce to meet the pressing needs of the population. The authorities in charge of agriculture and immigration focused their attention on the diversion of the inflow of new immigrants to work on abandoned Arab properties and the tasks assigned to agriculture.

Accordingly, the area under field crops was increased from 106.6 thousand hectares in 1948/49 to 255.0 thousand hectares in 1950/51. The area under vegetables and potatoes was similarly increased from 6.9 thousand hectares to 15.7 thousand hectares while the area under fodder and other irrigated crops was increased from 6.5 thousand hectares to 11.8 thousand hectares in the same

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[1]F.A.O., op.cit., p. 22.

period.[1]

With the return to more normal times, that is with the coming to an end of hostilities and the subsiding of the immigration wave, the authorities began to think in terms of not only expanding agricultural output but also of improving the rate of yield and the quality of the produce. Here the task fell upon the shoulders of the government and the Jewish Agency who together owned about 90 per cent of the country's total area. There was the need to invest in irrigation projects, mechanization and agricultural research; to expand the utilisation of fertilisers, crop rotation and the use of new types of crops. Since a basic feature of agricultural settlements in Israel (see Appendix), was that they did not have any financial means of their own, they had to be helped in the task of improving their performance by the Agency and the government institutions. For that purpose, the sum of IL 1,109 million was invested by the government and the Agency (and partly by individuals) during the period

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[1] U.N., Economic Developments in the Middle East, 1945-54, p. 128.

1949-1957. This sum represents 20 per cent of total gross investment in the country during the period at 1957 values.[1]

The crops that received the greatest deal of attention in this period were those that could be used either to export to foreign markets such as citrus, or those that could be used as primary materials in local industry such as industrial crops.

The government's attention and contributions to agricultural development, however, did not stop at its collaboration with the Jewish Agency and its settlement authority, in investing in agricultural settlements and irrigation schemes etc. They extended to other fields of aid such as the encouragement of domestic agricultural produce in the face of foreign competition through both fiscal and monetary policy. Thus the method of encouraging local suppliers of foodstuffs, for example, centered on "protecting local production against competitive imports at world market prices, notably by limiting most imports to complementary quantities."[2] The government also encouraged

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[1]F.A.O., op.cit., p. 32.

[2]Ibid., p. 34.

Israeli agriculture by initiating a complex system of subsidies to inputs and outputs of agriculture, so that agriculture in Israel could clearly be shown as the pet sector of the government.[1]

The availability of abandoned Arab lands, the ease of confiscating the lands of those Arabs that remained in Israel, together with the large sums invested in agricultural development, made possible the expansion of total cultivated area from 1,650,000 dunums in 1948/49 to 4,055,000 dunums in 1959/60. Also during the period, irrigated area was increased from 300,000 dunums to 1,305,000 dunums. The expansion of agricultural produce was mainly the result of the additional area brought under irrigation, because the recurrence of drought greatly reduced the output of unirrigated land.[2]

The additional areas that were irrigated were mainly devoted to the rejuvenation of abandoned citrus groves, since citrus was the main export item of Israel.

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[1] Ibid., pp. 35-41.

[2] U.N., op.cit., p. 28 and Bank of Israel, op.cit., p. 131.

Thus we find that the irrigated area of citrus groves was increased from 164,000 dunums in 1953/54 to about 320,000 dunums in 1959/60.[1] This increase of almost 100 per cent proceeded in accordance with the country's general economic policy which aimed at exporting 14 million cases of citrus fruits in 1962 at the estimated value of $ 85 million or almost 45 per cent of the country's planned exports of $ 190 million for 1962.[2] These developments and aspirations are, however, somewhat misleading because during the closing years of the Mandate, the area under citrus groves was as much as 280,000 dunums and the export of citrus fruits in good years amounted to some 16 million cases. An evaluation of the developments in Israeli citriculture has to take the above in mind because it was mainly through the utilisation of abandoned Arab groves that Israel managed to increase substantially the area of its groves.

Another important development from the point of view of the area under irrigation, was the introduction and expansion of industrial crops such as cotton, sugar

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[1]Bank of Israel, op.cit., p. 131.

[2]United Arab Republic, Syrian Army, Israel, 1959, pp. 662-63.

cane, sugar beat and groundnuts. The irrigated area under this category of crop was increased by about four and a half times from 47,000 dunums in 1953/54 to about 191,000 dunums in 1959/60. The expansion in the cultivation of industrial crops was even more significant in unirrigated areas where the increase was from 122,000 dunums in 1953/54 to 727,000 dunums in 1959/60.[1]

A development, slightly in the opposite direction, was in the area devoted to the cultivation of vegetables, potatoes and melons. This area remained almost unchanged throughout the period, and in fact was subject to some decrease from 203,000 irrigated dunums and 75,000 unirrigated dunums in 1953/54 to 196,000 irrigated and 62,000 unirrigated dunums in 1959/60.[2]

A probable explanation for the above developments is that whereas the local market (and to some extent the export market) was saturated with vegetables and potatoes (and with milk, eggs, live fish and poultry), it was not so saturated with respect to industrial crops.[3] The latter, as their name signifies, were crops

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[1]Bank of Israel, op.cit., p. 131.

[2]Ibid.

[3]F.A.O., op.cit., p. 23.

that could be put to industrial use, and the process of putting them to such a use served not only to create a demand for additional manpower that was becoming more and more difficult to absorb in rural areas, but also pointed out the path for future developments. The processing of agricultural products was considered a solution to many of the problems of agriculture in Israel.

Another unsatisfied consumer need in Israel was the demand for mutton and beef.[1] Hence, the area of irrigated land devoted to grains and fodder was increased from 182,000 dunums in 1953/54 to 293,000 dunums in 1959/60.[2]

The acquisition of abandoned Arab agricultural lands and the large scale investments of the government and the National Fund, together with increases in productivity through technological advances and the accumulation of know-how by Israeli farmers, have together resulted in large surpluses in several agricultural products. This situation has brought Israeli agriculture

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[1] *Ibid.*

[2] Bank of Israel, *op.cit.*, p. 131.

to the stage where "its output capacity exceeds the demands for its products at prices covering production costs".[1] The home market cannot absorb any additional output without a fall in prices. A fall in prices can only be attained by a reduction in costs of production and such a reduction can best be achieved by reducing water costs that account for a substantial part of total costs. The cost of water, artificially low as it is because of government subsidies, will continue to be high as long as the country is using up all of its natural water resources. It can only be reduced if the Jordan River scheme is completed, and until that scheme is completed, expansion in agricultural output will probably continue to be economically unsound.

Unless the Jordan River scheme is completed and proven to be an important element in reducing water costs, Israeli agriculture will continue to struggle within the domain of diminishing returns. It cannot hope to fight its way out in the face of foreign competition in foreign markets unless it is able to

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[1] Ibid., p. 110.

reduce its prices and overcome its transportation and organizational difficulties.[1] With the consolidation of the European Market, Israel's main customer, and the raising of its tariff barriers, Israel's chances of expanding its agricultural exports are becoming increasingly more difficult.

[1] *Ibid.*, p. 111.

APPENDIX II

The Cooperative Agricultural Settlements of Israel*

Israel has three main types of agricultural co-operative settlements. These are: (1) the Kibbutz, or collective settlement; (2) the Moshav or cooperative smallholders settlement, and (3) the Moshav Shitufi, which is based upon a combination of the main features of the former two types. "Each individual settlement is registered as a cooperative society, and each bears the triple aspect of a producers' cooperative, a marketing cooperative, and a consumers' cooperative. In addition to conforming to the principles of nationally owned land[1] and cooperative trading, all the settlements are bound by their rules to care for their members on the basis of mutual aid, and to carry out their economic

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*Please note that in this Appendix paraphrasing is liberally used.

[1]In 1960 about 90% of Israel's land was owned by the government, the Jewish National Fund and the Development Authority. In the same year this total area was transformed, by a series of Land Laws, to the Israel Land Administrative Authority, which was instructed to administer it in accordance with the Jewish National Funds principle of leasing the land and not selling it to agricultural settlements. (Israel, Government Yearbook, 1961/62, p. 367).

activities on the basis of their own labour.[1]

It is claimed that the idea of agricultural settlements based on a cooperative way of living, has its roots in the Essene community which was a Jewish community living in ancient Palestine sometime around a century before Christ. The Essenes laid the foundations of a communist order based on agriculture and continued to live in their communes till the destruction of the Second Temple in 70 A.D.[2]

In more modern times the first record of any attempt made by the Jews to establish villages based on a collective ownership of land and a communal responsibility for the needs of community members, was that of the 'Bilu' immigrants of 1880, a few years after the establishment of the first Jewish colony 'Petach Tikva' in 1878. The attempt, however, ended in failure.[3]

The World Zionist Organization, which was established after the meeting of the First Zionist

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[1]Noah Malkosh, Cooperation In Israel, 1954, p. 23.

[2]H. Darin Drabkin, The Other Society, 1962, p. 22.

[3]Israel, Government Yearbook, 1962/63, pp. 67-68.

Congress, in accordance with the Basle Programme, established the Jewish National Fund and the Keren Hayesod. The purpose of these organizations was to carry out the Zionist policy of preparing a class of Jewish immigrants who would till and live on the soil of Palestine and hence acquire a love for the land. Thus, the Jewish National Fund would purchase land in Palestine from funds collected from World Jewry, and the Keren Hayesod would be responsible for the development of the land.[1]

Among those who answered the call to immigrate to Palestine and live on its soil, were a number of the believers in collective ideals and communal principles, such as the 'Hechaluz' or pioneer organization founded in New York at the beginning of this century.[2]

"The collective idea grew out of two sources: a world trend towards collective principles, and conditions among the Jewish masses in Diaspora, which proved a fruitful breeding ground for the idea."[3]

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[1]Alex Rubner, The Economy of Israel, 1959, pp. 101-102.

[2]Darin Drabkin, op.cit., p. 66.

[3]Ibid.

The labour movement in Europe, and with it, the disappointment with capitalism, was coming of age during the second half of the nineteenth and the beginning of the twentieth centuries - this was also the period when the majority of the pioneering Jewish immigrants came to Palestine. The disappointment with capitalism was greatest in Eastern Europe, which was much less economically and socially developed than Western Europe. The founders of Israel's Kibbutzim came mainly from the working classes of Eastern Europe and had suffered the 'evils of capitalism' in those countries. Hence it was no surprise that the pioneering immigrants who came to a new country were decided on building in Palestine a new society "free from exploitation, on the basis of equality and social justice."[1]

Not only hate for the 'evils of capitalism' but also the love for simplicity edged the pioneers on. Tolstoy's ideals of simple village life attracted many of the 'halutzim' leaders such as A.D. Gordon, and these in turn affected by their writings and speeches the immigrant masses.[2]

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[1] Ibid.

[2] Ibid.

The leaders of the immigrant waves, the young intellectual Jews of Europe, driven out by anti-Semitism, unwilling"to follow their fathers in the occupations which were reserved for the Jews, and unwilling to go back to the ghetto, where they felt stifled by tradition", immigrated to Palestine "prepared to accept the idea of the commune as the most suitable settlement method" for the colonization of the country in preparation for the achievement of the Zionist goal.[1]

Meanwhile, a number of Jewish philanthropists, the most prominent of whom was Baron Rothschild, began their efforts "to create a class of farmers who, as owners of their farmsteads, would constitute a peasant class rooted and attached to the soil." For that purpose, Baron Rothschild established the Palestine Jewish Colonization Association (P.I.C.A.). The P.I.C.A. would reclaim waste land and invest time and effort to offer Jewish would-be farmers with plots of land for which they would be required to pay a price that covers only a small proportion of the cost of the initial investment. Moreover the purchasing farmer would pay for his farm-

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[1] *Ibid.*, p. 68.

stead in instalments over a period of fifty years at 1-3 per cent rate of interest per annum.[1]

The first collective settlement (Kvutzah) to be founded in Palestine by Jewish immigrants, was Kvutzah Daganiah. Daghaniah was founded in 1909 on the bank of the Jordan River by a small number of immigrants from the second aliyot. Daghaniah was not only the first Kvutzah, but also the turning point in the trend of Jewish agriculture which still continues today. The people of Daghaniah, anxious to make their experiment a success to be copied by others, decided from the beginning that if they wanted theirs to be a profitable farm, they had to base it on mixed farming and not on grain growing. The success of the experiment urged the Jewish National Fund and the Keren Hayesod to duplicate it all over the country.[2]

During the 1920's the communes, in an effort to maintain mixed farming and to expand agricultural projects, had to accept the idea of taking on additional

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[1] Government of Palestine, <u>A Survey of Palestine</u>, Volume I, 1945, p. 374.

[2] United Nations Series on Community Organization and Development, <u>Israel</u>, 1954, pp. 13-14.

manpower. But since the basic principle of the commune was to create and preserve family ties and group solidarity so that each commune behaved as if it were one family doing all the work and reaping all the profit, it was out of the question to increase manpower by hiring outside labor. Hiring outside labor would mean defeating the purpose of collective cooperative work.[1] Therefore, the only alternative was to expand the numbers of the members of each commune. This expansion fitted in with defense requirements and with efforts to increase the number of immigrants. "Very gradually and with the greatest regard for the social cohesion of the group", and with the expansion in the number of members and the number of economic undertakings, the Kvutzah evolved into the more familiar form of the Kibbutz.[2]

In what follows we shall discuss briefly some of the main characteristics of each of the agricultural settlements mentioned earlier.

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[1] _Ibid._, pp. 6-7.

[2] _Ibid._, p. 14.

The Kibbutz

The Kibbutz (or Kvutzah, as the two terms have come to be used interchangeably), is located on, and utilizes, nationally-owned land, leased by the Kibbutz founding members from the Jewish National Fund. The lease which ordinarily is for a period of forty-nine years is renewable as long as the members of the Kibbutz keep to the basic principles of collective living. These principles are in accordance with socio-economic norms. Thus, the entire work of each Kibbutz is to be performed by its members, hired labor being out of the question. No Kibbutz member receives wages for the work he performs, and all his requirements such as food, clothing, etc., are provided by the Kibbutz, the distribution of such goods and services being not according to the amount and quality of work performed but according to the quantity of such goods and services available for distribution and according to the needs of individual members. The management of the Kibbutz is turned over to members elected by democratic vote and equal rights of men and women. Though each man and his wife are allotted private quarters, the children are housed in special quarters and are cared for by Kibbutz members, and food is served in a communal dining hall.[1]

Kibbutzim (plural) are not restricted in their activities to a certain type of economic activity. They may engage in mixed farming, fishing, handicrafts and even small scale processing industries. Kibbutzim vary widely in size, from groups of 50 people to large communities of 1500, or more.[2]

The Moshav

The Moshav is a sort of mixed farming village which consists of about 100 families on the average, with each family owning a small plot of land which on the average is about 7½ acres. Each family employs its adult members on the land and turns over its output to a Moshav owned cooperative, which markets the produce of the Moshav and determines the income of each family unit in accordance with the quantity and quality of the produce which the family unit remits to the central marketing office of the Moshav. In actual production, cooperation is limited to the common ownership of heavy equipment, which each family can rent. Unlike the Kibbutz

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[1] Ibid., pp. 14-15.

[2] Noah Malkosh, op.cit., p. 24.

a Moshav is entirely based on the family unit and 20 per cent of the average Moshav's population consists of non-members who perform the non-agricultural services of the community. In a Moshav the children can inherit the property of their parents if they continue to engage themselves in their occupation.[1]

The Moshavim (plural) have a central institution, the Moshav Movement, which guides the affiliated Moshavim in social, cultural, economic and organizational matters. "The Moshav Movement helps the individual Moshavim to plan their farming operations, to obtain credit, to establish enterprises owned in partnership by a number of Moshavim, to maintain high standards in education of the children, and to settle any differences between groups."[2] The Moshav Movement has succeeded in absorbing a substantial part of the country's new immigrants. This success is attributed to the "loose cooperative framework which makes the common venture possible without stifling the family orientation of the members with regard to economic life, and secures a fine balance

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[1] *Ibid.*, p. 29.

[2] *Ibid.*, p. 27.

between individual initiative and responsibility to the group."[1]

<u>The Moshav Shitufi</u>

The Moshavim Shitufiim are a cross breed between Kibbutzim and Moshavim. Like the latter, the Moshavim Shitufiim are based on the family group, with the mother looking after domestic duties and, like the former, the Moshavim Shitufiim are collectively owned and collectively run farms. Organizationally, these settlements are linked to the Moshav Movement.[2]

Of course, the above brief description of the types of agricultural settlements does not do justice to settlements. But, we shall have to be restricted to such a brief resume, because any greater consideration would lead us into a subject which is in need of a separate thesis to explain.

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[1] *Ibid.*, p. 28.

[2] *Ibid.*, p. 30.

CHAPTER IV

THE COST OF ISRAEL'S ECONOMIC ACHIEVEMENTS

The economic achievements of Israel, just like any other achievement, could be accomplished only through the incurring of certain costs. Just like the country's achievements that were not purely economic in nature, the costs incurred by Israel were also not only economic. They had their socio-political and military aspects as well.

However, since the study at hand is solely interested in economic considerations, no attempt shall be made in the present chapter to go into any of the non-economic features of the burden borne by Israel as a result of the quest for development.

To be able to analyse the economic costs incurred by Israel during the period under survey it is necessary to begin with an examination of the total resources at the disposal of the country and the uses to which these resources were put. Such an examination helps in determining the extent to which the country relied on foreign sources of finance to maintain its development efforts. Once that is done it becomes possible to measure the economic burden borne by the country as a result of its drive for development and as a consequence of the methods used to finance such development.

A. Total Resources and Their Uses

The total resources available to a country are the sum-total of what that country produces, i.e. its GNP, plus the balance on the country's trade account. These resources are put to three main uses. A part is used up as general expenditure on consumption by the public and private sectors, while another part is set aside to cover depreciation allowances. The third part is used to finance net domestic capital formation.

Israel's total available resources (subsequently t.a.r.) for the period 1950-1960 were to the value of some IL 29,792 million at current prices. Of this total, the GNP accounted for about IL 25,046 million or about 84.1 per cent. The balance of IL 4,746 million, by definition came from the import surplus on the country's current account during the same period.[1]

In order for this finding to be properly appreciated it is necessary to compare Israel's ratio of import surplus to t.a.r., with similar ratios of some selected countries. Comparing Israel's ratio with those of two Latin American countries, the U.S.A., four Western European countries and four Middle Eastern countries, the following findings were obtained.

During the period 1952-1956 Israel's import surplus was in the magnitude of 18.9 per cent of its t.a.r. During the same period Panama's import surplus was 6.0 per cent, while that of Argentina was 0.9 per cent. The U.S.A. had an export surplus for the same period which was about 0.5 per cent of its t.a.r. Similarly, West Germany had an export surplus of about 1.0 per cent just as did the United Kingdom, Italy had an import surplus of 2.0 per cent while France had a surplus of 0.79 per cent.[2]

During the period 1952-1958 Cyprus had an

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[1]Patinkin, op.cit., p. 45 and Bank of Israel, op.cit., p. 10.

[2]Patinkin, op.cit., p. 50.

import surplus that averaged about 6.7 per cent of its t.a.r. every year.[1] Turkey's import surplus for the years 1948, 1952, 1954 and 1956 accounted for about 2.5 per cent of its t.a.r. for those years.[2] This latter ratio fell to 1.0 per cent in the period 1956-1958.[3] Egypt's ratio for the years 1948, 1952, 1954 and 1956 was 0.5 per cent.[4]

The highest ratio which the present writer was able to find, and for that purpose the only ratio higher than that of Israel was Jordan's. This country's import surplus for the period 1959-1961 was as much as 27.1 per cent of its t.a.r.[5]

Through the above comparisons it becomes very clear that Israel's dependence on an import surplus is unusually great. The degree of this dependence becomes even greater when it is brought out that the

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[1] U.N., Yearbook of National Accounts Statistics, 1959, N.Y., 1960, p. 64.

[2] U.N., The Development of Manufacturing Industry in Egypt, Israel and Turkey, 1958, p. 20.

[3] U.N., Economic Developments in the Middle East, 1958-59, p. 45.

[4] U.N., The Development of Manufacturing Industry in Egypt, Israel and Turkey, op.cit., p. 20.

[5] Hashemite Kingdom of Jordan, National Accounts, 1959-1961, pp. 2-3.

import surplus of Israel is in reality more than what it is claimed to be. To begin with, a number of Israeli economists, as well as foreign students of the Israeli economy, believe that a not insignificant part of the government's imports of military equipment, financed by foreign aid, is purposely omitted from the country's balance of payments. This naturally reduces the recorded value of the import surplus and by definition increases the share of the GNP in the country's t.a.r.[1] A somewhat similar under-valuation of the country's trade deficit arises from the exclusion of the value of smuggled imports paid for in foreign currency.[2] Furthermore, one must always remember that in Israel imports that are actually recorded, are estimated at the official and overvalued rate of exchange for the IL, before they are entered into the balance of trade account.[3]

Even if these and other factors are not taken into consideration the fact remains that Israel has relied heavily on foreign aid, to the extent of about

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[1]Don Patinkin, op.cit., p. 56.

[2]Rubner, op.cit., pp. 44-46.

[3]Patinkin, op.cit., pp. 92-93.

$ 310 million per annum during the period 1950-1960. The immediate question that comes to mind here is why Israel had to rely so heavily on foreign aid. The answer is best arrived at by analysing the uses to which the country's resources have been put during the period under study.

In the period 1950-1960 Israel spent about 61.2 per cent of its t.a.r. or about IL 18,253 million on private consumption. In the same period it also spent about 17.1 per cent of t.a.r. on government consumption. Government and private consumption together with depreciation allowances used up IL 25,352 million or 85 per cent of the country's t.a.r. for the period. Remembering that the GNP was responsible for only 84.1 per cent of t.a.r., it becomes evident that what the country produced was not only insufficient to pay for consumption expenditures and depreciation allowances, but that the country also used up part of the foreign aid it was receiving for consumption purposes. Evidently also, this being the situation, the country had no way of financing even the smallest investment programs. Since Israel's investment programs were very ambitious and large it was impossible for the country to finance these programs without the help of foreign loans and grants.

It has been established that for the period 1950-1958 there existed a very high correlation (r=0.67) between the country's import surplus and its investment activity. This coefficient is calculated in real terms and not nominal terms and thus it does not make allowances for the effects of inflationary price movements. If such allowances are made the correlation becomes significantly higher and reaches 0.94.[1]

It is safe to conclude that Israel's insistence, not to cut down on its consumption, and its adoption of very ambitious goals that could only be realised with the investment of enormous funds, necessitated the incurring of a large import surplus or trade deficit. This trade deficit has not shown any signs of improvement but on the contrary there is every indication that it has been continuously growing from year to year. (See Table XII) Whether or not it will continue to grow in the foreseeable future, is a matter reserved to a lengthy discussion in the concluding chapter of this

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[1] *Ibid.*, p. 54.

TABLE XII

ISRAEL'S BALANCE OF PAYMENTS, 1950 - 1960
($ Millions)

	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960
A. IMPORT SURPLUS											
1. Imports of goods & services	327.6	426.1	393.2	365.2	373.2	426.6	534.5	557.2	572.1	603.6	693.0
a. Payments of dividends & interest	1.0[a]	1.0[a]	12.8	18.9	19.0	20.3	25.6	28.1	34.0	35.7	38.9
b. Other imports of goods & services	326.6	425.1	380.4	346.3	354.2	406.3	508.9	529.1	538.1	567.9	654.1
2. Less exports of goods & services	-45.8	-66.6	-86.4	-102.3	-135.2	-143.9	-177.9	-222.0	-238.7	-287.4	-352.0
3. Import surplus	281.8	359.5	306.8	262.9	238.0	282.7	356.6	335.2	333.4	316.2	341.4
B. FINANCING OF IMPORT SURPLUS											
1. Net receipts from unilateral transfers	89.6	136.8	191.1	172.8	260.6	210.4	240.5	245.4	251.0	251.0	299.5
a. U.S. grant-in-aid[b]	-	14.0	84.0	44.7	37.2	20.5	6.8	24.1	11.2	9.5	9.7
b. Technical assistance[b]	-	-	2.3	2.6	1.8	0.4	0.4	0.4	0.3	0.3	0.2
c. Reparations from Germany	-	-	-	40.9	82.3	87.5	79.3	77.9	69.7	66.4	79.7
d. Personal restitutions from Germany	-	-	-	-	6.1	18.8	25.7	45.0	65.4	70.7	97.8
e. Private cash remittances	19.6[c]	38.8[c]	6.9	8.1	14.8	24.3	25.5	21.2	25.3	21.8	28.3
f. UJA & other institutional cash remittances	70.0[d]	84.0[d]	46.2	47.3	87.2	43.1	87.6	55.7	60.8	73.6	75.2
g. Transfers in kind	e	e	51.7[f]	29.2[f]	31.2[f]	15.8	15.3	21.1	18.3	8.7	8.6
2. Net receipts from capital movements	106.4	115.6	116.4	75.3	1.0	76.4	100.4	78.6	68.6	54.7	45.8
a. Long and medium term capital	44.4	87.6	114.9	69.6	71.2	76.3	78.4	69.4	93.6	81.2	101.4
i. State of Israel bonds	-	50.4	46.3	36.1	29.2	32.2	47.4	44.7	33.7	35.3	29.1
ii. Export-Import Bank	44.4	27.7	27.5	4.4	1.8	-2.1	-2.1	-11.4	-6.5	-6.4	-4.6
iii. U.S. Government loans within framework of grant-in-aid	-	-	-	-	-	25.4	32.6	20.4	43.9	18.3	28.5
iv. Other government obligations		9.5	11.2	7.2	21.1	8.7	-5.8	1.3	-2.2	21.0	7.4
v. Private capital	..	..	29.9	21.9	19.0	12.1	6.3	14.4	24.7	13.0	41.0
b. Short term capital	62.0	28.0	1.5	5.7	-70.2	0.1	22.0	9.2	-25.0	-26.5	-55.6
3. Errors and omissions	85.8	107.1	-0.7	14.8	-23.6	-4.1	15.7	11.2	13.8	10.5	-3.9
4. Total financing of import surplus	281.8	359.5	306.8	262.9	238.0	282.7	356.6	335.2	333.4	316.2	341.4
C. EXCHANGE RATE[g]	0.357	0.357	0.856	1.206	1.543	1.800	1.800	1.800	1.800		

a. This estimate seems unreasonably low.
b. In 1952-54, U.S. and U.N. technical assistance both in item B1b 1955-58, U.S. technical assistance included in item B1a.
c. Includes personal gifts and transfers in kind.
d. Includes institutional gifts and transfers in kind.
e. Included in cash remittances (items B1e and B1f).
f. Includes cash transfers by immigrants.
g. For 1950-51 and 1955-58, defined as the official rate; for 1952-54, the weighted average of the multiple official rates in force during this period, modified by levies and subsidies.

Source: 1950-58, Falk Project, Fourth Report 1957 and 1958, 1959, p. 52.
1959 and 1960, Bank of Israel, Annual Report 1960, 1961, pp. 22-23.

study. However, the growth of the country's trade deficit raises an issue which concerns us here and that is how Israel has managed to finance its chronic deficit.

B. Financing the Trade Deficit

Israel's sources for financing its trade deficit can be divided into two major groupings. On the one hand, there are unrequited transfers and grants from foreign private and government sources and from the "National Institutions" (Zionist Organizations). On the other hand, there are capital movements which include long-, medium-, and short-term loans from foreign governments and from foreign public and private institutions. The figures under these two main groups of financing for the period 1950-1960 are presented in the table above which shows the extent of Israel's trade deficit for each year and the means by which this deficit was covered during the period.

A number of significant conclusions can be drawn from the data enclosed in Table XII above concerning the relative share of each of the categories of transfers and capital movements in closing the trade deficit in each of the years included.

Except for 1950 it is quite clear that the major part of foreign sources of financing Israel's trade deficit came from unilateral transfers which accounted on the average for about 72.1 per cent of the total of those sources. The share of unilateral transfers increased steadily from 1950 when they accounted for the minimum of about 38.0 per cent of total sources of finance to 1960 when they accounted for the maximum share of about 87.7 per cent. There is, however, as can be easily detected, one exception to this trend of steady increase, this is the year 1954 when unilateral transfers were more than what was actually needed to balance the import surplus. The explanation is that some of the net $ 260.6 million worth of unilateral transfers for 1954 were used to balance the deficit in the short-term capital item of the balance of payments which was in the value of some $ 70 million.

Short term capital movements played a negative role not only in 1954 but also for the period as a whole since this item showed a total credit of $ 128.5 million against a total debit of $ 177.3 million. Long-and medium-term loans played a more substantial role. They were dominated by the proceeds from the sale of State of Israel Development and Independence bonds bought mainly by the Jewish community of the United States of America. These proceeds netted some $ 38.4 million per annum, or $ 384.4 million for the period 1950-1960 as a whole.

Almost equally important and significant as the sale of Israel's bonds abroad was the Export-Import Bank loan which put at the disposal of Israel some $ 105.8 million, and the United States' government loans of about $ 169.1 dominated by the proceeds from the sale of surplus American wheat shipped to Israel. This points to the significance of the fact that all forms of aid hitherto mentioned under long- and medium-term loans, came from the United States and had either its government's support or its approval (the Export-Import Bank being an official U.S. institution).

Returning to the unilateral transfers category of aid, it should be borne in mind that this category includes grants and donations that Israel will not pay back to the rest of the world in the future as it will have to do for loans. The following points ought to be singled out in connection with unregistered unilateral transfers.

Of the \$ 2,348.7 million worth of grants and donations received by Israel, about \$ 730.7 million or 31.1 per cent came as cash remittances by Zionist institutions and by the United Jewish Appeal. These remittances played by far the most important single role with regards to Israel's capital imports.

In 1953 German Reparation Payments were started and these payments were expected to play an extremely important role in financing a significant part of Israel's large imports. Increasing steadily from about \$ 40.9 million in 1953 to about \$79.7 million in 1960 and at the average rate of about \$ 53.0 million, these payments constituted the second largest singular foreign financing item in Israel's annual balance of payments.

Payments by Western Germany to Israel, however, did not stop at Reparations but were supplemented beginning with 1954 by Personal Restitutions for Jewish persons whose properties in Germany were confiscated or damaged during the second world war, or who suffered physically under Nazism. Increasing from \$6.1 million or 2.3 per cent of total unilateral transfers in 1954, personal restitutions came to account for the largest single share of \$ 97.8 million or 26.5 per cent of total unilateral transfers in 1960.

Of the remaining \$705 million under [illegible] unilateral transfers, some \$ 434.5 million were in the form of private cash remittances and transfers in kind. Another \$262.7 million were donated by the government of the United States of America as grants-in-aid. The balance of over \$8 million came from technical assistance donations by the government of the United States and by the United Nations.

C. Features of the Economic Burden

The first section of the present chapter pointed out that Israel, during the period 1950-1960, was living beyond its national capabilities. It was only through its reliance on foreign aid that the country was able to achieve what it did achieve. The nature and magnitude of that aid was discussed in the second section of this chapter. We can now proceed to a discussion of the economic burden falling on Israel because of living beyond its national capabilities.

The economic burden has two main aspects. On the one hand, there are the country's commitments to the rest of the world, while on the other hand there are a set of economic costs ranging from the near-exhaustion of some natural resources to the influence of disequilibrating forces unleashed in the process of development - particularly inflation and the misallocation of resources it brings about.

The country's commitments to the rest of the world are in the nature of an economic cost because they represent a liability or a debt which Israel owes the rest of the world; a debt which has to be repaid.

The commitments are of course not of a uniform type since they represent liabilities in local as well as foreign currencies, and of differing maturation periods.

By the end of 1960 Israel's foreign exchange liabilities were in the value of some $708.1 million. Of these, long term loans accounted for about $ 541.8 million, while medium term loans were in the value of $ 64.7 million. The remaining $ 101.6 million were in the form of short term loans.[1]

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[1]Bank of Israel, op.cit., p. 39.

To cover part of its liabilities Israel built up a foreign exchange reserve that amounted to some \$ 270.4 million by the end of 1960. This means that the country owed the rest of the world about \$ 437.7 million in foreign exchange for which it had no foreign exchange cover.[1]

The local currency liabilities by the end of 1960 were in the value of some \$ 237.3 million. This puts Israel's gross commitments to the rest of the world in the neighbourhood of \$ 941 million, or a net total of \$ 675 million.

However, large as Israel's commitments to the rest of the world are, they remain only one aspect of the economic burden borne by the country. Two other important aspects of the economic burden which weighs down the national economy can be cited. These are the using up of the country's natural resources for the purpose of furthering economic development, and the economic dislocations resulting from the steps taken to insure that development.

To speak of the using up of some of the country's

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[1]*Ibid.*

natural resources as being a feature of the economic burden borne by the country implies that a rather large part of those resources has been used up, or that the further use of these resources will intensify the operation of the phenomena of diminishing returns. The best illustration of this point is in the agricultural sector. One of the more appropriate methods that can be used to determine the extent of the using up of Israel's natural resources in the sphere of agriculture is by determining the part of the country's cultivable land actually brought under cultivation and the part of the country's water resources used up for irrigation purposes.

In the crop year 1959/1960 (and with very little change thereafter) more than four million dunums of land were actually cultivated. This means that Israel has reached the limits of horizontal expansion in agriculture within the financial, technological and agricultural capabilities of the country.[1] Any further horizontal expansion, or even vertical expansion for that matter, will be predicated upon the possibility of increasing the volume of water that could be made available for

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[1]Yusif Sayigh, op.cit., Chapter VII.

irrigation. In that respect and given the water resources in existence, the future is not very promising, for these resources have been so thoroughly tapped that the government, in fear of the imminent salination of the subterranean water reserves, has passed a law rationing irrigation water and seriously regulating its distribution.[1]

The full utilisation of the country's natural water resources has not only threatened the country's reserves but has also led to a tremendous rise in water prices or costs, so that by 1958 these were estimated to be on the average about 15 per cent of the value of agricultural output.[2]

So costly has been the price of irrigation water in Israel that it has been estimated to be for fodder crops, in some parts of Israel about four times that in Southern California where it is already unusually high.[3] The cost in Israel should be looked upon to

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[1] Government Yearbook, 1962/63, p. 46.

[2] Alex Rubner, op.cit., p. 116.

[3] Ibid., pp. 116-117.

be even higher than recorded because the Makeroth Water Company, which is responsible for water control and distribution, quotes artificially-lowered prices so as to subsidise agricultural output (beyond the other subsidies it already enjoys).[1]

The meaning of all this is that unless Israel is able to tap hitherto unknown or untapped water there is little hope for expanding the cultivable area in the country. The hitherto untapped water sources are two. On the one hand there is sea water that could be distilled, while on the other hand there is the unutilised waters of the Jordan River and Lake Tiberias. The former alternative is still in its experimental stage and the second runs the great risk of involving Israel in a war with its objecting neighbours. Moreover, experts have many serious doubts concerning the prospects of the Jordan River Project from the economic and engineering points of view. Nevertheless Israel is going ahead with both alternatives and there is reason to believe that the first stage of the Jordan project will be completed by the end of 1963.[2]

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[1] _Ibid_.

[2] Yusif Sayigh, _op.cit._, Chapter VII.

The using up of a large part of the country's natural resources and/or the pushing of agricultural production into a very high cost range, and the ever-increasing indebtedness of the country to the rest of the world, may be important features of the economic burden borne by Israel but in truth they are more in the nature of the causes for that burden rather than its effects.[1]

What may be considered more as a result or consequence of the economic burden are the set of disequilibrating forces referred to earlier in this chapter such as the inflationary pressures and their consequences which came about as a result of the quest for development and the particular method adopted to finance that development. The inflationary pressures increased the burden through a sort of cumulative action, but it was the quest for development and the

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[1] In fact, they are intermediate causes. The primary set of causes is Israel's insistence on achieving all its military, economic, and social objectives together and speedily, without the country having the resources that would make the achievement possible. (See Chapter II for a discussion of the objectives of Israeli society).

steps taken to insure its materialisation that caused the inflation and the economic burden and not vice versa.

Inflation has often been referred to as a situation in which too much money is chasing too few goods. Such a situation in which the effective demand is greater than the available supply of goods and services leads to a rapid rise in the prices of those goods and services; this rise in turn increases the costs of production with producers trying in turn to shift the burden or part of it on to the consumer in the form of higher prices.

A fast-growing effective demand necessarily means a rapidly-expanding money supply; in Israel this expansion was so great as to increase the money supply from IL 93 million in mid-1948 to IL 1,001 million in mid-1961. This stupendous expansion did not proceed at a uniform rate throughout the period. There were two main periods of rapid expansion. The first extended from 1948 to 1951 while the second extended from 1953 to 1957. A third period of expansion seems to have started beginning 1960.[1]

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[1]The remaining part of this section is based on part of the seventh chapter of Dr. Sayigh's book referred to elsewhere.

The reasons given for such a rapid expansion in the money supply are manifold but amongst the more important causes the following can be cited. To begin with the country's commercial banks contributed greatly to the expansion of the money supply by adopting an easy money policy. This policy of extending credit to the public at very easy terms was made possible mainly because the government did not attempt to impose any of its potentially effective monetary weapons. The banks also used the foreign exchange received from foreign loans, but especially personal restitutions as legal cover on which to issue credit.

The government and the public institutions (the Jewish Agency and affiliates) contributed further to the expansion in the money supply by earmarking and spending large funds in the absorption of immigrants. Much of these expenditures were sunk in unproductive undertakings more in the nature of relief work. Housing and feeding the new immigrants contributed greatly to increasing the effective demand without adding to a commensurate extent to the gross national product of the country.

Last but not least, the upkeep of a very large (but largely unproductive) army contributed greatly to the widening of the gap between effective demand and available supply.

The expansion in the money supply might have had a lesser inflationary effect had the government and the people not possessed as large a propensity to consume as explained in earlier parts of this study.

All the above is of course from the money supply point of view only. There is naturally another side of the picture which includes the production and costs aspect. The costs of production and the rapid rise in prices have been discussed in detail in Chapter III of this study. As for production it is sufficient to say that it was unable despite its rapid rate of development (discussed in Chapter III also) to keep up with the increase in the purchasing power made available to the public.

Thus we have on one side an easy money policy and on another a rather large propensity to consume and by definition a low propensity to save. Together these two phenomena reduced markedly the chances of the country's productive capacity to catch up with effective demand.

What added to the intensity of inflation was the accepted and practiced doctrine of closely tying up the workers' wages with the cost of living index. Every time prices increased and pushed the cost of living index upward beyond a certain modest point, wages were automatically increased and this naturally led to higher costs and once again higher prices and so on and on in a spiral.

The linkage of wages to the cost-of-living index and the resulting rises in the initially-high costs of production caused the country's products to lose their competitive ability. With every disturbance in the relationship between Israeli and international prices to Israel's disadvantage the country's products lost more ground in the local and international markets. This led to the adoption of a large protective tariff system in the local market and a very costly and complex system for subsidising exports. It is this subsidy system that explains the otherwise contradictory phenomena of rising costs and expanding exports.[1]

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[1]See Patinkin, op.cit., p. 123 regarding subsidies and their significance for Israel's foreign trade.

In reflection of the deterioration of the value of the Israeli pound it is important to note that this currency was devalued several times so that its value at the last devaluation in February 1962 brought it to 8.2 per cent of its 1948 value. The Israeli pound began its life as officially equal to $ 4.0; now it is worth $ 0.33.

Not only did the Israeli pound lose its international value but it also lost the trust and confidence of Israeli citizens many of whom were unwilling to keep large sums in cash and showed a marked preference to hold their wealth in kind or in foreign currencies.[1] This contributed further still to increasing the velocity of circulation and thus added further to the pressure of inflation.

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[1]On this point as well as other measures taken by the public, such as the tying of financial obligations with goods, land, or gold, see Alex Rubner, The Economy of Israel, pp. 93-97.

CHAPTER V

CONCLUSIONS

We can, at this final stage in the study, sum up the more important findings of the preceding chapters and evaluate Israel's prospects for economic independence, this evaluation being the main concern of our thesis. The following are in brief the pertinent conclusions.

a) In the period under study, i.e. 1950-1960, Israel's population increased, mainly as a result of net immigration during the first few years after the establishment of the state, from 1.4 million in 1950 to 2.2 million in 1960. (In May 1948 the Jewish community of Palestine numbered some 700,000).

b) Israel's GNP at current prices increased from about IL 475 million in 1950 to about IL 4,396 million in 1960. However, as pointed out in Chapter III, current prices inflate the growth in GNP during a period of rising prices. Therefore to measure the real growth in the GNP it is necessary to measure this product at constant prices. This can be done by deflating the figures by the consumer price index. According to this method we found that the GNP increased from IL 475 million in 1950 to IL 1,319 million in 1960 at constant 1950 prices. Although the correction (from IL 4,396 million to IL 1,319 million) is quite substantial, yet due to some shortcomings of the consumer price index, as indicated in Chapter III, it is preferable to deflate by an average of the consumer price index and the price index of investment goods. Such a measure reveals that Israel's GNP grew from IL 475 million in 1950 to IL 1,023 million--a total growth for the period of 215 per cent.

c) Large as was the growth in Israel's GNP it was not sufficient to meet the increasing requirements for government and private consumption expenditures and for depreciation. Indeed Israel spent annually during the period 1952-1956 more on consumption and depreciation combined than the value of its GNP.

This was primarily because government and private consumption expenditures, which were initially very high, continued to grow at the same pace as the growth in GNP.

d) This being the situation and with the Israeli society insisting on a concurrent realisation of various socio-economic objectives that necessitated the adoption of highly intensive investment programs, Israel had no choice but to depend on foreign financial aid. This dependence reflected itself in an import surplus which closed the gap between the total domestic resources available to the economy and the total resources required. The following definition explains the place of the import surplus in the equation between availability and use of resources:

T.A.R. = GNP + Import Surplus = Public and private consumption expenditure + Depreciation + Net domestic capital formation

e) Despite the passage of eleven years between 1950 and the end of 1960 the country's import surplus continued to account for a large share of total available resources. Indeed, the ratio of the import surplus to t.a.r. remained constant, indicating that in absolute terms the import surplus grew at approximately the same rate as the growth in GNP which has already been shown as a very high rate. In numerical terms Israel's annual import surplus increased from \$ 281.8 million in 1950 to \$ 341.4 million in 1960.[1]

f) As a result of the continued pressure to achieve concurrently a number of socio-economic as well as military objectives, the economy was brought under a serious economic burden highlighted by the inadequacy of domestic savings and the dependence on foreign aid. The circumstances surrounding the inadequacy and dependence raised the doubt--despite the remarkable performance of the Israeli economy--whether Israel will be able in the foreseeable future to reduce the magnitude of its dependence on foreign aid sufficiently enough to set itself on the road leading to economic independence.

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[1]In 1961, Israel's import surplus was at the value of \$ 402.4 million, and in 1962 it was at the value of \$ 427.0 million. (Israel, Government Year-Book, 1962/63, p. 136).

The doubts as to the ability of Israel to achieve economic independence have, as will be shown below, grown appreciably over the years and have come to occupy the attention of many Israelis concerned with the future of the country. However, before we can move to evaluate the seriousness of such doubts or in other words to evaluate Israel's prospects for economic independence, which is our main interest in this thesis, it is advisable, first, to discuss briefly some of the implications of economic dependence.

Economic dependence may arise as a result of any one or more of a variety of causes that may be of a structural or non-structural nature. Moreover, a country running a trade deficit because of the structural disequilibrium of its economy, may use the foreign aid put at its disposal to either neutralise and even reverse the structural disequilibrium causing its dependence, or may use such aid for purposes that have nothing to do with redressing the trade deficit but rather to increasing it. An economically dependent country may use the aid to achieve a long term objective of economic development and in that case economic dependence may be looked upon as a necessary short term evil to achieve a long term good. In other words, economic dependence is not by necessity an evil that ought to be avoided.

To condemn a country's efforts to better its lot, simply because such efforts involve large financial costs, would be naive. Furthermore, quite often, societies passing through dangerous experiences touching upon their development and indeed their very existence, are forced to disregard economic considerations or to disobey economic logic for a while for the attainment of non-economic goals which they consider as being worth much more than what is warranted by economic considerations alone.[1]

Conversely, economic independence may be maintained at a very low level of economic performance in a stagnant society and may well be an evil to avoid. A situation can easily be imagined where foreign exchange earnings are in equilibrium with payments,

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[1]Yusif Sayigh, op.cit., Chapter VII.

and continue to be so in the absence of large capital imports for use in development. It is obvious that independence in this case is not a desirable state of affairs. Likewise a state of dependence arising mainly because of a reckless import policy involving the acquisition of luxury consumption goods is an evil to be avoided: indeed, the worst evil of all.

More specifically in the case of Israel, an economist cannot pass judgement on whether or not the country should discontinue its dependence on foreign aid, by simply taking into consideration the economic burden of dependence. Accordingly, we shall not discuss whether Israel should or should not attempt to achieve economic independence, but will examine whether Israeli society wants to achieve that goal and if so examine its prospects of success.

In Israel, the tendency seems to be one that considers economic independence a necessity and its attainment a nationally-desirable goal. Thus we find that proposals which claim to contribute to the attainment of economic independence are in great demand in the country.

Concern with economic independence may not have been a very important issue during the early years of statehood because then the chief concern was with the maintenance of the newly-acquired political independence at any social, economic or military cost. Once the country's political independence was secured, due consideration was given to the attainment of certain socio-economic goals. At that time economic dependence was looked upon as a necessary step on the path towards social welfare. An all-out effort was then in process to achieve the socio-economic goals of the Israeli society.

Gradually, however, the country began to feel the weight of the burden it had imposed on itself in its drive to achieve its goals. Economic dependence was the most significant aspect of that burden, and concern with the shortcomings of dependence began to grow appreciably. Specially relevant to this increasing concern, and to the concern with the achieving of independence, were the coming to close of German Reparations,[1]

[1] German Reparations constituted the second largest category of foreign aid to Israel during the period 1953-1960, averaging annually about $ 53 million. Additional German aid came in the form of personal restitutions which totalled $ 529.5 million from 1954-1960.

the maturation of some foreign loans,[1] the development and consolidation of the European Common Market,[2] and the continued inability of exports to narrow the increasing gap between exports and imports.

As these and similar considerations were raised by influential public figures, Israeli public opinion was gradually put into a state of mind that considered every effort leading to the achievement of economic independence a highly necessary endeavour. Hardly anybody made a speech in Israel "proposing anything whatever remotely connected with economic matters, without claiming that what he is proposing would contribute to the achievement of economic independence."[3]

The best expression of official concern with economic independence came in February 1962. This was

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[1]By the end of 1960 Israel's commitments to the rest of the world were $ 941 million gross, or $ 675 million net.

[2]In 1961, about 29 per cent of Israel's total exports went to countries of the European Common Market. Almost all of Israel's agricultural exports and most of its industrial exports go to this market. The Market is Israel's largest trading partner.

[3]Abba P. Lerner, loc.cit., p. 3.

in the new Economic Policy stated by the Minister of Finance, Levi Eshkol (now Prime Minister), declaring that one of its main objectives was the attainment of such a state of independence.[1]

In announcing its new policy the government emphasized that the need to assign priority consideration for the attainment of economic independence arose of the following influences:

a) The accelerated consolidation of the European Common Market, which is Israel's biggest trading partner.

b) The coming to a close of German Reparations, which constituted a substantial share of total foreign aid to Israel.

c) The maturation of much of the obligation from the sale of Independence and Development Bonds.

d) The marked continued inability of national products to stand up to foreign competition and of exports to pay for imports.

e) In the light of the above, the need within the coming years for more than $ 350 million per annum

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[1]Document, Middle Eastern Affairs, March 1962, p. 89.

to finance the import surplus.[1]

The government considered this need as necessitating the adoption of "vigorous measures" such as, the devaluation of the Israeli pound, the abolition of most levies on imports, the stabilization of prices, the linkage of wage increases to increases in productivity and the construction of a comprehensive central plan that would organise and coordinate economic activity in the country.[2]

If economic independence is as seriously sought in Israel as we have tried to indicate, it remains for us to evaluate the prospects of achieving such an objective. The evaluation requires an examination of the causes behind Israel's dependence on foreign aid, and subsequently an appraisal of the strength of the factors that are expected to make for independence. In this appraisal, the relationship between Israel's past performance and its circumstances throw light on the country's future prospects.

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[1] Ibid., pp. 85-86.

[2] Ibid., pp. 85-88.

Israel's dependence on foreign aid can be attributed to a number of causes. The primary set of cases is the country's insistence on achieving all its military, economic and social objectives quickly and concurrently, without the country having the adequate domestic savings necessary to finance the investment programs involved in these objectives.

Israel's investment programs have been very ambitious and its savings inadequate to finance these programs. As a result therefore the country has had to depend on foreign aid. If the country wants to reduce its need for foreign aid, it has to adopt one or more of three main alternatives. It can reduce its investment activity, it can find means by which to increase domestic savings, or it can try to reduce the import surplus by increasing exports or decreasing imports or by effecting a combination of both measures.

The important question to ask here is why Israel has been unable to finance its growing investment activity from its own sources, i.e. from savings out of its GNP, considering that GNP has been rising remarkably.

To begin with, it will be remembered that Israel's gross domestic capital formation bears a very high ratio to GNP: 26.5 per cent for the period 1950-1960. Such a high ratio of GNP going to finance investment activity places Israel in the rank of one of the most highly investment-oriented countries in the world.[1] The enormity of Israel's investment effort--its ambitions remaining the same--partly explains the inability of the country to finance such an effort. The other part of the explanation arises from the rather weak propensity to save of the government and people of Israel.

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[1]See Table IX, and the discussion on page 75 of this study.

The fact that government and private expenditure on consumption alone accounted for as much as 93.1 per cent of GNP during the period 1950-1960, is by itself an explanation why the country has been unable to finance its investment activity from domestic savings. But the real issue is why so large a portion of GNP should go to consumption expenditures. Here the answer is not obvious, and some elaboration is called for.

Once again the problem must be tackled from the point of view of the factors affecting both private and public consumption expenditures. But since no sufficient explanation has been offered by students of the Israeli economy for the high propensity to consume in the private sector, save that the socio-economic ideology of the country encourages such a pattern of behaviour, we shall have to restrict our analysis to the public sector.

Like the private sector, the public sector has shown the tendency to consume not only a rather large part of its annual income but also all of the marginal additions to this income, year in and year out, and to the extent of dissaving. But unlike the behaviour of private individuals, the behaviour of the public sector has some concrete explanations. There are two such main explanations.

In the first place, it has been claimed that a substantial part of government consumption expenditures has been directed towards immigrant settlement and rehabilitation and for welfare and relief transfers. In the second place, the defense burden answers for the larger part of the remaining expenditures.[1]

It is very difficult to estimate the extent of "dissavings generated by the necessity of resettling and rehabilitating the new immigrants", therefore any such estimate attempted by us would be purely arbitrary and would not be very revealing. Nevertheless, the fact remains that the new immigrants constituted a serious drain on government resources during the period of waiting for absorption into the national economy. They had to be housed, fed and often paid for doing relief work.[2] By merely glancing back at

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[1] Don Patinkin, op.cit., p. 101.

[2] Ibid., pp. 101-102.

Table VIII which indicates the great numbers of immigrants arriving in Israel, it is possible to conclude that the government did indeed direct a substantial part of its expenditures to the benefit of the new immigrants.

The thing to note, however, is that immigration reached a peak at the end of 1951 after which it came to a relative standstill for three years. However, when it did pick up in 1955 it did not gather sufficient momentum to compare favourably with the years prior to 1951 (See Table VIII). The meaning of this is that the increase in government expenditures should have fallen accordingly. But it has failed to. Government expenditures not only did not fall as a result of the fall in immigration but even continued to increase. It would therefore be very unrealistic to expect that government expenditures will be reduced in the future. Not only would the expectation be unrealistic, but its time horizon would have to be very long. This is so because there is no way of telling when the Soviet Union or its satellites may permit their Jewish communities to emigrate to Israel.[1] If they do, then the government's expenditures as a whole will be increased by the renewed prominence of the important expenditure item of immigrant resettlement and rehabilitation. Thus, not much long-term hope can be safely pinned on the chance of reducing government expenditures as a result of the fall off in immigration.

Let us now examine the other major item of government expenditure, namely defence. It is important to note, however, that Israel's estimates of these expenditures, if taken at their face value, might be somewhat misleading.

As published by the government, Israel's defence budget represents only about 29 per cent of total government expenditures. This means that, relatively speaking, defence expenditures are less than those of France which are about 37 per cent of government's total expenditures, and much

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[1]Another heavy concentration of Jews is in Morocco, However, the chances of a massive exodus from Morocco are slim, owing to Arab solidarity on the issue of immigration to Israel.

less than the defence expenditures of the United States that represent about 51 per cent of total government expenditures.[1] It also means that the share of the Israeli defence budget is relatively smaller than the share of the Syrian defence budget which was about 44 per cent during the period 1950/51 - 1960/61, and much smaller than the share of the Jordanian expenditures on defence, which during the period 1951/52 - 1959/60 represented as much as 56 per cent of total government expenditures for the period.[2]

It should be borne in mind, however, that Israel's published defence expenditures are undervalued for a variety of reasons. Not only does the government attempt to keep secret, for security and strategic purposes, an important share of its defence purchases but it also does not emphasize the fact that on account of the nature of Israel's military organization a rather substantial part of what should appear as military expenditures appear elsewhere. Thus, for example,

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[1] _Ibid_., p. 57.

[2] Syria, _Statistical Abstract, 1960_, p. 302, and, Jordan, _Statistical Yearbook_ (issues of 1958 and 1960).

each Kibbutz is not only an agricultural unit but also a military stronghold equipped with military installations and populated by men and women trained in modern warfare and mobilization techniques, able to take part in active fighting in coordination with other Kibbutzim. This "citizen army" is the backbone of the Israeli military machine, and the Kibbutzim are a chain of defense fortresses, combining commercial endeavour with defence.[1]

Israel's mobilization system is another example of concealment of the real financial burden of the country's military effort. Each time the auxiliary forces are called up in partial or complete mobilization, the country's laws require that part (one third) of the expenses incurred to pay the auxiliaries' wages be shouldered by their peace-time employers. Moreover, most auxiliaries are called upon to report for training for periodic short durations, without pay.[2]

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[1] M.R.D. Foot, Men in Uniform (Weindenfield and Nicolson, London, 1961), pp. 76-80.

[2] Ibid., pp. 80-81.

Whatever may be the real weight of Israel's defence expenditures, the fact remains that an important part of the government's expenditures is attributed to military purposes, and we should now concern ourselves with the prospects of reducing such expenditures in the foreseeable future.

Evidently, any reduction in Israel's military expenditures is by necessity dependent on the possibilities of bringing to an end the state of war and the hostilities between Israel and the Arab world. Because of the inherent nature of the conflict it is very improbable that any arrangements for peace can be worked out one way or another, and Arabs and Israelis will most probably continue to face each other as mortal enemies. There is indeed, every indication that the arms race between Israel and its neighbours is gaining in momentum.

Modern arms have a high rate of obsolescence and the upkeep and servicing of such arms is a highly technical and expensive necessity. Thus if Israel is to be able to keep up the superiority it has had, or at least to keep a sort of balance of power in the area, it must continue to shoulder the huge expenses involved. Moreover, Israel has to face the extremely expensive consequences of the U.A.R.'s picking up of the challenge posed by Israel when the latter introduced missiles into the picture. This being the situation it is indeed very unlikely that Israel's military expenditures will be reduced tangibly in the future.

The above analysis brings us to the conclusion that given the prevailing circumstances, there is not much hope for increasing savings in the country by depending on either a reduction in private or in public consumption expenditures in the near future. If this is so, then the only alternatives to reducing the import surplus of the country (other than through a sudden and substantial increase in efficiency and productivity beyond realistic expectations) are those of reducing the intensity of investment activity in the country or the improvement in the prevailing system of allocating resources.[1]

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[1]Of course there are a number of other alternatives, such as the termination of the Arab blockade, the discovery of some rare natural resources in commercial quantities, the success of the Jordan River Project, some sort of technical or organizational breakthrough etc., but these are not matters of the immediate future and their discussion would be out of place here.

Studying the probable effects of a reduction in investment activity or the more efficient re-allocating of resources is a very complex matter because it involves many variables. It is not at all easy to treat the problem of reducing investment activity "as if it were one of simple arithmetic: as if any decrease in investment would automatically reflect itself in a reduction in the import surplus. This would, of course, be true in the completely hypothetical case in which the import component of investment goods were 100 per cent". But since this is far from being the case in Israel then the problem becomes far more complicated.[1]

If a reduction in the import surplus is to take place as a result of a reduction in investment activity, a number of variables must be assumed to behave in a certain manner. To begin with, the GNP must continue to grow at more or less the same rate despite the falling off in investment. In view of the very high average propensity to consume (private and public)

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[1]Don Patinkin, op.cit., p. 136. This quotation ought to be explained. Although the import surplus has generally been as large as investment, this does not mean that a) there are no domestic savings, or b) that the import surplus consists entirely of capital goods for investment. What instead is meant is the equality in size of the import surplus and investment.

there is very little flexibility in manipulating the size of investment. With marginal propensity to consume high and continuing to remain high, the only chance for GNP to keep its rate of growth would be through a sensational drop in the capital/output ratio due to a sensational rise in productivity, or through a much more efficient re-allocation of resources than exists at present.[1]

Neither of these alternative measures is capable of being put into effect in a short period of time, or of being far-reaching enough to bring about the desired increase in GNP along with a substantial drop in the import surplus.

There are indeed here the elements of an impasse. The economic logic of the situation indicates that there is no escape from a reduction in consumption and/or investment if the import surplus is to be reduced substantially, with the assumption of a reasonable expectation of improvement in labour and capital productivity,

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[1]An efficient reallocation of resources is necessary to insure that "the domestic resources released from investment activity are redirected to other activities in which one way or another they help produce import substitutes or exports." (Don Patinkin, op.cit., p. 136).

and the assumption of development in the trade position of Israel remaining along the same path that it has been taking in recent years. This leaves one possibility to explore: effecting a reduction in the country's import surplus through augmenting exports or curtailing imports or a combination of both.

If we look back at Table XII we notice that Israel's exports increased by some 665 per cent from 1950 to 1960, at an average compound rate of growth of some 23 per cent per annum. Simultaneously, imports increased, with substantial annual fluctuations, by only 111 per cent during the same period, or at an average compound rate of growth of some 8 per cent per annum. Such developments appear as significant achievements for the Israeli economy. However, despite the very rapid rate of growth in the country's export trade, this rate was not sufficient to enable the country to proceed on the path of economic independence.

To elaborate, it will be noticed from the information provided in Table XII, that despite the relatively more rapid rate of growth of exports than of imports, the import surplus remained a substantially large one, during the period under study, growing with intermittent fluctuations from about $ 282 million in 1950 to about $ 341 million in 1960.[1] This phenomenon is explained by the great difference between the absolute values of exports and imports in the base year, 1950. Thus, whereas the total value of exports of goods and services in 1950 was $ 45.8 million, the total value of goods and services imported during the same year was $ 327.6 million.

To be able to evaluate the future prospects of imports and exports it is necessary to break them down into visible and invisible imports and exports, and to further classify the visible or merchandise imports and exports into commodity groups. Such classification will enable us to appraise from the nature of the goods and services imported and exported by the country, and from past trends of growth, the country's prospects for reducing its import surplus.

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[1] In 1961 and 1962 the country's import surplus was $ 402 million and $ 427 million respectively as we have already indicated.

From the services or invisible trade side of the picture, the following important points can be singled out.[1] From 1950 to 1960 Israel's receipts from services rendered to the rest of the world amounted to about 35.4 per cent of its total proceeds from exports during the period. The annual share rose steadily from 22.1 per cent in 1950 to about 40.4 per cent in 1960, i.e. from $ 10 million to $ 142 million. The most important part of the increment came from increases in earnings from transportation and insurance. In the meantime, Israel's payments to the rest of the world for services rendered to Israel, increased from $ 35 million in 1950 to $ 197.8 million, i.e. from 10.7 per cent of total imports to about 28.5 per cent, constituting an average of about 23.6 per cent of total imports of goods and services during the period 1950-1960. Here again transportation and insurance

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[1]The information pertaining to services is derived from three sources, For the period 1950-1956 the information is from the I.M.F., Balance of Payments Yearbook, 1955-56. The 1957-58 issue of this same source provides the information for the years 1957 and 1958. For the years 1959 and 1960 the information is from the Bank of Israel, Annual Report, 1960, pp.22-23.

payments constituted the most important single share of total payments for services, increasing from $ 4.5 million in 1950 to $ 67.0 million in 1960. Alongside the growth in transportation and insurance payments, came the growth in capital servicing and government expenditure abroad. Payments for capital servicing increased steadily from $ 6.3 million in 1950 to $ 46.6 million in 1960. Government expenditures for services increased from $ 13.0 million to $ 57.9 million.

The pertinent conclusion we can draw from the above is that despite the rapid increase in receipts for services rendered by Israel to the rest of the world during the period under study, the country's net payments did not decrease but on the contrary increased from $ 25.5 million to $ 55.6 million. This of course was due to the large growth in payments made by Israel to the rest of the world for services rendered during the period, and for past loans.

Israel is building up its merchant marine and its airline company El-Al, to reduce its net payments for transportation costs. It is also improving its tourist trade. But the road in both cases is a long one, and it still has to find a way to reduce government expenditures abroad. In addition there is little chance of reducing capital servicing payments due both to growing interest payments on accumulated debt and to maturity of past debts to foreign countries.

The visible or merchandise trade side of the picture offers a further variety of interesting developments.

During the period 1951-60, about 20 per cent of the value of the country's total commodity imports consisted of foodstuffs. Of this share, about 60 per cent, or 12 per cent of all commodity imports, consisted of cereals and their preparations.[1] The prospects of reducing this almost constant part of imports in future years depend on agricultural expansion and climatic conditions. Since, as we have indicated in

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[1]The information pertaining to merchandise trade for the period 1951-60 is taken, unless otherwise stated, from the 1955, 1958, and 1961 issues of the U.N. Yearbook of International Trade Statistics.

this study, future agricultural expansion in Israel is dependent on the completion of the Jordan River scheme, we can safely assume that the country will continue to be in need of substantial imports of foodstuffs, especially since Israel has one of the most rapidly increasing populations in the world.

Imports of mineral fuels, lubricants and related materials accounted for about 10 per cent of total commodity imports during the period 1951-60. Since no important oil discoveries have been made in Israel, we can assume that the country will continue to need fuel imports representing at least 10 per cent of its future commodity imports as it has done in the past. This share might very well increase in future years to keep pace with the country's rapidly growing industrial activity.

Very similar to the case of fuel imports is that of raw material imports. Of the large variety of raw material imports we can cite three major items that during the period 1951-60 accounted for 17 per cent of all commodity imports. Wood and timber imports accounted for 3.4 per cent of total imports during the period. Iron and steel imports accounted for 8.6 per cent while rought diamond imports accounted for 9.4 per cent.

Because of the limitations in Israel's timber resources it is very likely that wood and timber imports will continue to hold their share, if not to increase with the development in the carpentry and furniture industry in the country. We can expect the same development to occur with regards to iron and steel imports, for despite the decline in construction activity and the development of the Steel Town at Acre, iron and steel imports have continued to hold their important position among commodity imports. As for diamond imports, these will very probably continue to increase as they have done in the past because cut and polished diamonds are the most important single item on Israel's export list; and since the country has no diamond mines, rough diamond imports will continue to grow with the growth in the diamond cutting and polishing industry in the country.

In several parts of this study reference was made to the intensive investment activity in the country.

If Israel is to continue its past trend, then it will continue to need heavy imports of investment goods. Of the investment goods imported into the country during the period 1951-60, imports of electrical, building, metal working and industrial machinery, together with road motor vehicles, tractors and spare parts accounted for 17 per cent of total commodity imports.

We have thus accounted for 64 per cent or about two thirds of the country's commodity imports and we have seen that such imports will most probably continue to be in demand in the foreseeable future, more so if Israel continues its investment activity and population growth. It is difficult to account for the remaining 36 per cent, mainly because they constitute a large variety of items, none of which account for a substantial part of total imports, save probably for certain raw materials not mentioned above. Reference is made here to items such as wool and cotton yarn which Israel does not produce in sufficient quantities to meet the requirements of its growing textile and clothing industry.

Turning to the export side of the picture, our analysis becomes relatively more simple. This is because two export items alone, citrus and diamonds, netted 61 per cent of commodity export proceeds during the period 1951-60. Citrus fruits and juices accounted for 37 per cent, while cut and polished diamonds accounted for the remaining 24 per cent.

The substantially large share of these two commodities simplifies the evaluation of the future prospects of the country's commodity exports, because any future developments in exports are necessarily dependent to a large degree on developments in citrus and diamond exports. But before venturing into an analysis of any such developments something should be said about the country's exports in general and the markets for such exports.

It is important to remind the reader of the reference made in Chapter III to the important role played by government subsidies in encouraging exports. Direct and indirect subsidies of all sorts have been given to Israeli exporters in the hope of artificially reducing costs and thus augmenting the prospects of their products on the world market. We re-emphasize the role of subsidies at this stage to point out that at least part of the country's export increment, "was made possible only because the economy paid a high marginal price for the additional foreign currency earned. Indeed, in certain cases this price was so high as to be beyond the range which can be profitable to the economy."[1]

The need for subsidising exports in Israel arises from a number of basic problems which beset Israeli industry and which cause the production costs of Israeli products to be too high to enable these goods to stand up to foreign competing goods. In brief, the problems of Israeli industry centers around production at less than full capacity because Israeli firms, like their Palestinian Jewish predecessors, were founded with a much larger market in mind. Wages are very high and because of their linkage to the cost of living index they tend to always push up

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[1]Bank of Israel, op.cit., p. 163.

costs in a country where the cost-price spiral is sensitive and high. Israel is distant from its important markets both for raw materials and fuels and for finished products, and has thus to incur extra transportation costs in both directions. The problem of inefficiency is an ever present one, especially since an important part of Israel's labor force consists of men and women who come from a pre-industrial background or whose literacy is minimal.

Israel's New Economic Policy of 1962 aims at taking 'vigorous measures' to combat these and the other problems facing the Israeli economy. But unless this New Economic Policy of 1962 proves to be more successful than its predecessor of 1952, Israel's chances of moving towards economic independence will not be very promising.

The markets for Israeli exports have been mainly three. The United Kingdom imported 22.2 per cent of Israel's total commodity exports during the period 1950 to 1960. The U.S.A. imported another 18.1 per cent, while the countries of the European Common

Market accounted for another 16.4 per cent. But, whereas the share of the United Kingdom fell steadily from an all-time high of 32.6 per cent in 1950 to an all-time low of 16.7 per cent in 1960, and while the share of the U.S.A. fell also steadily from an all-time high of 25.4 per cent in 1951 to an all-time low of 13.6 per cent in 1960, the share of the European Common Market increased steadily from an all-time low of 9.0 per cent in 1950 to an all-time high of 29.8 per cent in 1960.[1] The significance of this development is that Israel has become over the years more and more dependent on the European Common Market as an outlet for its exports, and since this market is rapidly consolidating and lifting its tarrif barriers an important export market for Israel is seriously threatened. Indeed, the Israeli Minister of Foreign Affairs, was quoted as having said in a statement to the press, that the failure of Israel to join the Common Market could mean a "fatal blow" to Israel.[2]

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[1] U.N., Yearbook of International Trade Statistics, op.cit.

[2] Al-Nahar (Beirut Arabic daily), February 28, 1964.

A relatively new market for Israeli exports is the non-Arab states of Africa, to which Israeli officials and sympathisers have looked with great enthusiasm especially after the opening of the gulf of Aqaba to Israeli navigation in 1956. But there is reason to believe that this market has not developed to the full extent of Israeli aspirations. To be precise Israeli exports to its more important trade partners in Africa, namely Ethiopia, Kenya, South Africa, Nigeria, and Ghana, increased by only about $ 5 million after the opening of the Gulf of Aqaba, from $ 2 million in 1957 to $ 7 million in 1960, i.e. from 1.4 per cent of total commodity exports in 1950 to 3.4 per cent of total commodity exports in 1960. Needless to say, the low per capita income of those countries restricts Israel's hope to find there a new and large market for any citrus exports that have to be diverted away from the European Common Market. The same can be said for diamond exports. Israel is also up against the Arab blockade which is beginning to attempt influencing Israel's markets in Africa.

Returning to our analysis of citrus fruits and diamonds and their prospects, we find once again a not too promising future. To begin with, citrus fruit exports, subsidised as they are, are meeting with severe competition from deciduous fruits and Spanish citrus fruits, with the result that prices have fallen, bringing foreign exchange earnings down with them. Heavy transportation costs, high irrigation costs and marketing difficulties side with foreign competition to threaten the prospects of Israeli citrus exports. Reflecting the burden of these difficulties is the noted stagnation in foreign exchange earnings of citrus exports and even a decline in such earnings from \$ 48 million in 1957 to \$ 47 million in 1960.[1] The number of cases exported in 1960 was 8.4 million, which does not compare favourably with exports of up to 16 million cases from Mandatory Palestine in good years.

In contrast to citrus exports, the proceeds

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[1] U.N., Economic Developments in the Middle East, 1959/61, pp. 154-159.

from exports of cut and polished diamonds have been continuously increasing. In a matter of five years, from 1956-1960, they more than doubled, increasing from $ 25 million to $ 61 million, and they maintained a steady share of about 24 per cent of a rapidly increasing volume of commodity exports.[1] But the increases in foreign exchange earnings from diamond exports should be contrasted with increases in imports of rough diamonds. This is because exports of cut and polished diamonds have a rather low local value added, requiring as they do an input of 100 per cent imported diamonds that amounts on the average to about two thirds of gross value of the finished product.[2] Thus any future increases in diamond exports must by necessity be accompanied by increases in imports of highly expensive rough diamonds.

Exports of textiles, clothing and other industrial exports have meanwhile been increasing fairly rapidly but here again the future prospects

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[1] Ibid.

[2] Bank of Israel, Annual Report, 1960, p. 165.

are first and foremost dependent on the country's ability to overcome the competitiveness of other countries' textiles.

To sum up: a number of significant developments took place in Israel's foreign trade activity over the years 1950-1960. These developments influence substantially the country's future prospects for economic independence.

Probably the most important development was the huge growth in exports. Though the annual rate of growth in recent years compared with the earlier years of the period has somewhat fallen, exports have grown several fold. The most significant expansion has been in the branch of invisible exports. A somewhat slower, but a nevertheless quite significant, expansion took place in industrial exports. Agricultural exports have recently been growing at an extremely modest rate. On balance, it can legitimately be expected that the overall growth in exports, and particularly in invisible and industrial exports, will continue in future years.

However, despite the expansion in exports, the import surplus has always been on the increase in absolute terms. This is primarily because together with the expansion in exports there has been a rapid expansion in imports. Although the rate of growth of the former was substantially greater than that of the latter, exports were unable to catch up with the volume of imports because the country's imports started off from a much higher base than its exports.

In conclusion, the logic of the situation seems therefore to indicate that Israel will not be able for several years to come to reduce its import surplus to the limit set by its New Economic Policy.

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