1. In accordance with its terms of reference the Committee conducted the consultation with Israel on the restrictions applied by it for balance-of-payments reasons. The Committee had before it: (a) a basic document for the consultation (BOP/6/Rev.1) and a list of products to be liberalized on 1 June 1962, supplied by the Israeli authorities (issued as document L/1767) and (b) material provided by the International Monetary Fund as noted in paragraph 2 below. In conducting the consultation the Committee followed the "Plan" recommended by the CONTRACTING PARTIES. The discussion was completed on 8 May 1962. The present report summarizes the main points of discussion during the consultation.

Consultation with the International Monetary Fund

2. Pursuant to the provisions of Article XV of the General Agreement the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Israel. In accordance with the agreed procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Israel. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision relating to the last consultation with Israel under Article XIV of the Fund Agreement and the background material prepared in connexion with that consultation.

"With respect to Part I of the Plan for Consultations, relating to balance-of-payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, the Fund calls the attention of the CONTRACTING PARTIES to the Executive Board decision of March 21, 1962, taken at the conclusion of its recent consultation with Israel and particularly to paragraph 5 which reads as follows:

'During the past two years Israel has further relaxed restrictions on imports and on invisible transactions. Discrimination on imports and bilateralism have been reduced but remain substantial. The Fund urges Israel to reduce its reliance on discrimination and bilateralism.'

"With respect to Part II of the Plan for Consultation, relating to alternative measures to restore equilibrium, the Fund draws attention to the decision taken at the conclusion of its last consultation with Israel. The Fund has no additional alternative measures to suggest at this time."
Opening statement by the representative of Israel

3. In his opening statement the representative of Israel outlined the progress made since the last consultation in simplifying and considerably relaxing import controls. This progress reflected the improvement in Israel's foreign exchange reserves and was evidence of the Government's desire to liberalize trade to the greatest possible extent. In drawing up the new programme of import liberalization and in implementing its import policy, the Government had taken due account of the recommendations or suggestions by members of the Committee made at the time of the last consultation. An outline of major measures taken under Israel's new economic and trade policy had been made available to contracting parties in February in document L/1727. Most of the measures announced at that time had already been implemented or would be put into effect in the near future. Additional measures of import liberalization were at present under consideration by the Government. This progress, as outlined in the paragraph below, had been made despite the fact that when imports reached a new peak, the balance on current account had deteriorated and net indebtedness had continued to increase.

4. Under the economic policy adopted by the Government of Israel on 9 February, the Israeli pound had been revalued and a uniform rate of exchange of 163 per US dollar had been established. This rate applied to all exports and imports. The premium system for the export of goods and services and subsidies for capital transfers were abolished. Subsequently, a Free Imports Order was promulgated. It contained some 400 items, imports of which would be freed from all licensing restrictions on 1 June 1962. Imports of the goods included in this list had amounted to $120 million in 1961, or between 20 and 25 per cent of total imports. This was the first time that Israel had published a list of products which were completely free from quantitative restrictions, licensing procedures and the requirement to import minimum quantities.

5. During the last consultation the Israeli representative had estimated that 50 per cent of imports were effectively liberalized, i.e. under the Automatic Approval System; this figure now stood at 80 per cent, comprising between 20 and 25 per cent which would be subject to the Free Imports Order and the balance subject to Automatic Approval. It was the intention of his Government to augment the Free Imports Order and to include additional commodities (with an annual import value of approximately $180 million in 1961) in the expectation that by the end of 1962 50 per cent of all imports into Israel, representing an import value of approximately $300 million, would be freed from all licensing requirements. The speed at which the remaining restrictions would be removed would depend on the development of the balance of payments which in turn depended largely on the trade relationship between Israel and the European Economic Community. It was the declared policy of the Government of Israel, within the framework of the new programme, to eliminate progressively all quantitative restrictions on imports and to simplify administrative procedures with respect to foreign trade. It was envisaged, therefore, that all imports still being licensed...
under the Automatic Approval System would be included ultimately under the Free Imports Order. The long-term foreign trade policy of the Government of Israel provided for an improvement in the balance of payments not through restrictive measures on imports but rather through an overall expansion of foreign trade.

6. He stated that there had been a continuous increase in imports during the last three years, imports amounting to US$426 million in 1959, US$496 million in 1960 and US$568 million in 1961. While the value of imports had increased, the balance-of-payments position on current account had deteriorated. In 1959 the deficit on current account amounted to US$316 million, in 1960 to US$336 million and in 1961 to US$397 million. Net indebtedness had further increased from US$672 million in 1959 to US$675 million in 1960 and to an estimated figure of US$702 million in 1961. It was hoped that the new economic programme would result in a reduction in the trade deficit and a further increase in foreign exchange reserves. Nevertheless, taking the foregoing figures into account, it was apparent that the import restrictions maintained were necessary to safeguard the country's foreign exchange reserves, especially as it could be expected that the trade balance would continue for some years to come to show a considerable deficit due to the process of growth and expansion of Israel's economy. It was estimated that by 1965 imports would reach US$650 million and exports US$400 million, but this estimate was subject to revision in the light of the effects of the recent exchange reform on foreign trade.

7. The representative of Israel further stated that, since the last consultation the importance of bilateral trade-and-payments arrangements in Israel's foreign trade had been constantly reduced both in relative and in absolute figures. It was estimated that in 1962 total imports under bilateral agreements would amount to about US$25 million; this represented between 4 and 5 per cent of total imports. It was the intention of the Government of Israel to continue its efforts to terminate bilateral trade arrangements except with State-trading countries.

8. Referring to imports under State trading in Israel, the representative of Israel explained that so far it had been necessary, for reasons of security, to maintain some degree of State trading in order to ensure adequate supplies and essential stocks of certain foodstuffs. Items under State trading were wheat, oilseeds, sugar, fats and oils and certain other foodstuffs; however, State trading in some of these products would be discontinued with effect from 1 June 1962.

9. Commenting on the reference in the IMF Executive Board decision to remaining discrimination in Israel's system of controls, the representative of Israel stated, the explanation was, that a certain portion of Israel's imports was tied to bound resources, i.e., funds which carried the obligation to import from the country supplying these funds. Examples were international development loans tied to sources of supply and imports under the reparations agreement with the Federal Republic of Germany. Deliveries under the latter would be terminated in 1963.
10. The Committee thanked the representative of Israel for his concise and clear statement. The Committee noted that there had been a favourable development of Israel’s foreign exchange reserves since the time of the last consultation. They welcomed the fact that there had been a major reform of the Israeli foreign exchange system, and considerable relaxation and simplification of controls affecting imports. The Committee expressed the hope that the favourable development of Israel’s foreign exchange reserves would continue and would be translated, to the greatest extent possible, into further elimination of import restrictions.

11. Members of the Committee observed that Israel’s foreign exchange reserves, at present amounting to approximately US$350 million, were the equivalent of the value of approximately six months’ imports and that, according to some estimates, Israel’s exports in 1962 might be expected to increase by US$10-15 million, while imports might decrease by as much as US$20-30 million as a result of increasing import substitution. With an estimated surplus on capital account for 1962 of US$20 million, total foreign exchange reserves could be expected to show a further significant increase in 1962. They expressed the view that on the basis of the already favourable ratio of reserves to imports, and in view of the likelihood of this favourable development continuing, Israel might be expected to make even more rapid progress in the elimination of restrictions than currently envisaged.

12. The representative of Israel explained that the favourable development of the reserve position during the past year had indeed been one of the pillars on which the new economic policy was based. Notwithstanding the considerable improvement in foreign exchange reserves, there were a number of factors preventing his Government from proceeding with import liberalization at a rate faster than currently envisaged. For example, it was too soon to assess the full effect on trade, and thus on the balance of payments, of devaluation and of other measures taken in that connexion, such as the elimination of import levies, on many categories of products and also import duty reductions. There was also some uncertainty regarding the future development of Israel’s exports to member countries of the European Economic Community, particularly of agricultural products. A representative of one of the member States of the EEC stated that in his view there was no cause for such anxiety. He pointed out that in view of the provisions of Article XXIV of the General Agreement the tariff system resulting from the Treaty of Rome did not constitute discrimination. The representative of Israel, while wanting to share the optimistic view expressed by the delegate of the EEC, pointed out that the development would depend on the policy ultimately adopted by the EEC. He added that this was especially the case in regard to the common agricultural policy of the EEC. In fact, the determining factor would be the readiness to share the benefit of the expected growth in demand within the EEC market with outside producing countries or, alternatively, to reserve the market exclusively for inside producers. The outcome might have an important influence on Israel’s balance-of-payments positions and consequently its ability to accelerate the implementation of its policy of trade liberalization.
13. The representative of Israel further explained that, on the basis of total estimated import outlays (imports of goods and services) of US$800 million in 1962, reserves were only the equivalent of roughly five months' imports. While the Government hoped that the country's foreign reserve position would further improve, and had in fact based its liberalization programme on that assumption, any estimate of the level of exchange reserves expected to be at hand by the end of the year could at present be only conjecture on account of the factors cited above. An additional factor influencing the level of import demand and export prospects was the internal price level, still not firmly established after devaluation in February 1962.

14. The representative of Israel further stated that another important factor to be taken into consideration was that a large part of the increase in reserves arose from new long-term indebtedness, incurred in relation to large development projects all of which required large-scale imports of capital equipment and raw materials. Moreover, in the case of Israel there was the continuing need to provide for large numbers of immigrants and their successful integration in the economy. Quite apart from considerations of financial prudence, it had to be recognized that a more rapid removal of restrictions, after many years of controlled imports, might have undesirable economic and social repercussions which might endanger the implementation of the new economic development programme and possibly even the Government's programme of import liberalization. While the level of import liberalization achieved to date might appear modest at first sight, the rate at which import controls had been relaxed or removed had been very rapid, as a comparison between the present import régime and the régime prevailing in 1958/59 would show.

15. In the discussion of the rôle of private foreign investment in Israel's balance of payments, the representative of Israel stated that private capital imports had become increasingly important in recent years for financing economic development. It was his Government's hope that the recent exchange reform and the measures of trade liberalization would give an added incentive for private foreign capital to be invested in Israel's rapidly growing industries.

Alternative measures to restore equilibrium

16. The Committee welcomed the stated intention by the Israeli authorities to rely increasingly on monetary and fiscal measures for controlling the level of import demand. It was noted in this connexion that for the first time the Government budget showed a small surplus. The rapid credit expansion during 1960 and during the first half of 1961 had apparently been checked and additional measures had been taken to reduce the effect of devaluation on the money supply. Members of the Committee noted, however, that the cost-of-living index in 1961 had shown larger increases than in either 1959 or 1960.
and that prices continued to show an upward tendency which had been reinforced by devaluation. They enquired whether the link between wages and salaries on the one hand and the cost of living on the other would be maintained under the new economic policy, thus causing the danger of wage-price inflation. The representative of Israel explained that the Government did not find it possible to eliminate the link between wages and the cost-of-living index which had been a feature of the official wage policy for more than twenty years, i.e., antedating independence. It was recognized however, that this linking involved some danger of a wage-price spiral being set in motion, and the maintenance of wages linked to the cost-of-living index did not mean that the Government would not take fiscal and monetary measures to avoid an undesirable expansion of the money supply.

17. One member of the Committee recalled that at the last consultation it had been noted that domestic savings accounted for less than one half of gross domestic investment and that the Government was trying to encourage a shift towards financing a larger share of total productive investment from domestic savings. He enquired to what extent the Government had succeeded in stimulating savings and in increasing the share of domestic savings in productive investment. The representative of Israel explained that, as pointed out at the last consultation, a lasting increase in the savings rate could only be brought about on a voluntary basis. Inflationary tendencies in the economy and anticipation of devaluation had been factors unfavourable to the growth of savings and their flow into productive investment. Domestic saving, as a proportion of gross domestic investment, was still small and had not grown as rapidly as the Government had hoped. The representative of Israel further explained that, as a result of the recent measures adopted by the Government, a more favourable savings and investment climate had been created. Certain changes in the public's saving-mindedness were already noticeable although it was too soon to assess the full impact of the new measures on the savings rate. In addition to regular savings, restitution payments to citizens of Israel could be regarded as constituting a form of delayed savings. Receipts under this heading had been increasing in recent years and to a large extent funds thus derived had not gone into current consumption.
System and method of the restrictions

18. In reply to a number of questions by members of the Committee regarding the present system of controls, the representative of Israel confirmed that following the statement of intention made in announcing the new economic and trade policy in February 1962, the Government had abolished all subsidies on capital transfers, as well as the export premium system. Import duties and restrictions on most types of machinery and on many raw materials had been abolished, and duties and levies on imports of a wide range of other products, except luxury goods, had either been abolished or considerably reduced. Further progress had been made in simplifying foreign trade procedures, including the abolition of import permits for 400 items, included in the Free Imports Orders referred to in the opening statement; imports of these items would be entirely free from administrative control.

19. In the discussion of the operation of the Automatic Approval System, the representative of Israel explained that licences were issued automatically without any attempt by the licensing authority to place a ceiling on imports. The requirement that importers must undertake to import specified minimum quantities of goods for which licences were sought was designed to assure that imports would not be effected in excessively small quantities, thus requiring unnecessarily high outlays for transportation. The requirement was also designed to prevent an unwarranted increase of persons engaging in import trade. Minimum import limits were sufficiently low, amounting to US$5,000 for most of the commodities affected, to ensure that this requirement did not prevent interested persons from setting up in the import trade. The granting of a licence application was subject, however, to the licensing authority being satisfied that there was no gross deviation of declared import prices from normal market prices for this type of product. This latter requirement had been introduced to prevent exchange manipulations through over-invoicing and similar practices. The representative of Israel stated that this requirement had become of very limited importance, however, and was becoming even less important following the exchange reform. To his knowledge no licence had been refused in the past year or two on account of such practices. He explained that the experts of the different licensing authorities, on the basis of their knowledge of the market, were in a position to determine whether prices quoted were normal and reasonable. In no case was advice on such measures sought from industry or traders handling competitive or related products.

20. Another factor taken into consideration in issuing licences, was the availability of like products from bound sources of supply. In the interest of making the best use of the country's freely disposable foreign exchange reserves, an attempt was made to indicate to importers availabilities from tied sources and, where necessary, to issue licences in accordance with the need to assure the full utilization of import facilities under bound sources of supply. He further explained that, although it would be too soon to eliminate this requirement, in practice it was becoming less and less important. Deliveries under the reparation agreement with the Federal Republic of Germany were scheduled to be terminated in 1963 and the overwhelming proportion of deliveries under this...
agreement had already been made. Moreover, as the list of products included under the Free Imports Order was scheduled to increase significantly, the number of items subject to any form of administrative discretion and guidance would be further reduced.

21. Members of the Committee welcomed the statement that administrative interference with imports under the Automatic Approval System was decreasing. They considered, however, that licences were not issued automatically, in the pure sense of the term, and urged Israel to endeavour to remove, as quickly as possible, all restrictions on products falling under this category and, in the meantime, to reduce discrimination.

22. In reply to questions concerning the policy for imports under bilateral agreements the representative of Israel stated that no special attempt was made by the licensing authorities to guide importers to import from bilateral agreement countries. There was no need to interfere with importers regarding their decision as to sources of supply for products exchanged with Israel's bilateral trading partners. The value of trade under bilateral agreements was less than 5 per cent of total imports. The relatively small proportion of total trade conducted under bilateral agreements, divided between several countries and between various commodities, meant that for any given product imports under bilateral agreements could satisfy only a small or insignificant part of total import demand. He explained that bilateral agreements were in force with Brazil, Bulgaria, Ghana, Greece, Hungary, Poland, Portugal, Rumania, Turkey, Uruguay and Yugoslavia. The agreements with Brazil and Ghana provided for multilateral payments and the latter agreement was dormant. The agreement with Uruguay was of a modest nature and applied only to a limited number of products. Members of the Committee welcomed the intention of Israel to reduce further its reliance on bilateral trade and payment arrangements and urged that rapid progress be made in that direction.

23. Members of the Committee enquired about prospects for products subject to individual licensing being moved to the Automatic Approval category and eventually being included under the Free Imports Order. The representative of Israel explained that products under Individual Licensing, representing about 20 per cent of imports, were produced in Israel and that a somewhat longer period of adaptation might be required before they could face the full impact of competition from imports. It was the Government's intention, however, to subject these products to gradually increasing competition from imports, as expressed in the statement made by the Minister of Finance in February 1962 when announcing Israel's new economic and trade policy. Members of the Committee enquired whether in addition to the Free Imports Order, the Automatic Approval System and the Individual Licensing system, there would continue to be a list of products, imports of which were, in effect, prohibited. The representative of Israel said that it was intended that the three categories referred to above should cover all classes of goods. The prohibited list was currently under examination with a view to moving the items on it into the Individual Licensing category. It was not intended to use quantitative restrictions to protect domestic production.
Effects of restrictions

24. Members of the Committee noted with satisfaction that under the new economic policy protection to domestic industries would gradually be reduced. They expressed the hope that whatever import substitution was envisaged should not depend on the protection of local industries through measures other than the tariff. They noted that in the past imports of certain products which were available in sufficient quantities from domestic production had not been licensed, or had been licensed only sparingly, and enquired whether it was the intention of the Israeli authorities to continue to restrict such imports. The representative of Israel explained that the Government intended within the broad lines of the policy announced recently to subject domestic products to increasing import competition. He reminded the Committee that the first list of products covered by the Free Imports Order constituted already the first step in the implementation of this policy.

General

25. Members of the Committee thanked the representatives of Israel for the co-operative manner in which they had engaged in the consultation. They welcomed the considerable progress made since the last consultation in relaxing and simplifying controls and procedures affecting imports. They noted the measures taken by the Israeli authorities to ensure further rapid growth of the economy while at the same time trying to avoid inflation. Members of the Committee also welcomed the statement by the Israeli authorities that domestic industries and agriculture would be subjected to increasing import competition and that to this end all quantitative restrictions were ultimately to be abolished. The Committee noted, however, that in the sector of imports remaining subject to licensing control, there was a degree of administrative discretion and also that there continued to be an element of discrimination in the administration of Israel's import controls. The Committee expressed the hope that Israel, taking account of the favourable development of its foreign exchange reserves, would find it possible to accelerate the relaxation of remaining import restrictions and, in the meantime, continue to reduce discriminatory practices.

26. The representative of Israel thanked the Committee for the sympathetic attitude it had adopted throughout the consultation and for the many helpful suggestions and recommendations made during the course of the discussions. He would not fail to convey to his Government the views expressed by the members of the Committee.
International Monetary Fund Executive Board Decision Taken
on 21 March 1962 at the Conclusion of the Consultation
between the Fund and Israel

1. The Government of Israel has consulted the Fund under Article XIV, Section 4, of the Fund Agreement concerning the further retention of its transitional arrangements.

2. During the period 1958 to 1960, the real gross national product continued to increase. Immigration slowed down and the economy approached conditions of full employment. Wage increases did not exceed the rise in productivity, and price increases were moderate. The rates of increase in the volume of credit and money supply were lower in 1958 and 1959 than in earlier years, but in 1960 they slowed a renewed increase. In 1961, the increase in the real gross national product was again substantial. Full employment prevailed and there was pressure on resources, reflected in some shortages of skilled labour in construction and certain industries. Both prices and wages increased considerably. As a result of accelerated credit expansion and a large inflow of foreign exchange, originating mainly from restitution payments, the money supply rose rapidly in the first half of 1961, but the increase came to a halt in the second half of the year.

3. Exports have risen substantially in recent years, but in 1960 and 1961, the increase in imports was larger than the increase in exports. At the same time, the inflow of capital increased, and despite some deterioration in the balance of payments on goods and services account, there was a substantial increase in foreign exchange reserves. Israel's policy remains to reduce the current account balance-of-payments deficit through a combination of expanded exports, particularly of industrial products, intensified import substitution by the utilization of domestic resources, and restraints on consumption.

4. The Fund welcomes the reform of the exchange rate structure. This measure should strengthen the balance of payments and facilitate the desired growth of the economy. The Fund appreciates the recognition by the Israeli authorities that appropriate fiscal and credit policies are needed to achieve the full benefits of the exchange reform, and urges the vigorous pursuit of policies designed to strengthen confidence in the national currency.

5. During the past two years Israel has further relaxed restrictions on imports and on invisible transactions. Discrimination on imports and bilateralism have been reduced but remain substantial. The Fund urges Israel to reduce its reliance on discrimination and bilateralism.

6. In concluding the 1961 consultations, the Fund has no other comments to make on the transitional arrangements maintained by Israel.