1. In accordance with its terms of reference the Committee conducted the consultation with Israel. The Committee had before it: (a) a basic document BOP/40; (b) International Monetary Fund documents dated 9 October 1964; (c) the International Monetary Fund Executive Board Decision dated 30 October 1964, and (d) a list containing import items that are free of restrictions and a list of items under automatic licensing indicating those specially liberalized recently.

2. In conducting the consultation, the Committee followed the plan of discussion for consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement pages 97-98). The consultation was held on 11 November 1964. This report summarizes the main points discussed.

Consultation with the International Monetary Fund

3. 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 the 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 and background material from the last consultation with Israel under Article XIV of the Fund Agreement.

"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 invites the attention of the CONTRACTING PARTIES to the Executive Board decision of October 30, 1964 taken at the conclusion of its recent consultation with Israel, and particularly to paragraph 5 which reads as follows:
'Israel has further relaxed restrictions on imports. The Fund welcomes the intention to complete the process of formal liberalization of imports by the end of 1965 and urges Israel to reduce reliance on bilateral payments arrangements.'

"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 recent Article XIV consultation with Israel. The Fund has no additional alternative measures to suggest at this time."

Balance-of-payments position and prospects

4. In the opening explanatory statement, the full text of which is annexed to this report, the representative of Israel outlined the progress made in the liberalization of imports since 1963, the foreign exchange position of Israel, and the basic trend underlying Israel's foreign trade and their future policy.

5. The representative of Israel stated that during 1964, the policy of removing quantitative restrictions and administrative controls on imports had continued steadily, and Israel was in the process of reviewing all products at present under quantitative restrictions; this review was to be completed by October 1965. At present according to the import statistics, 80 per cent of imports were free from restrictions, or came under automatic licensing, and only 20 per cent remained subject to individual licensing. This 20 per cent amounted to $140 million in 1963, and out of this amount, only $48 million were in fact competitive with Israeli products.

6. During the first nine months of 1964 Israel experienced a serious increase in her trade deficit. Imports increased substantially during this period, and are expected to reach $810 million for the whole of 1964, reflecting an increase
of 21 per cent over 1963. It is estimated that exports for the whole of 1964 would reach $360 million as against $351 million in 1963. The relatively static position of exports for the year was only partly explained by the fact that in 1964 there had been a $22 million drop in income from citrus exports, as compared with 1963. The representative of Israel said that to a certain extent tariff measures adopted by Western European countries in their integration would also have a limiting effect on the export possibility. Thus on total, taking goods and services together, the deficit in the balance of trade for 1964 would be approximately $600 million, as compared with $407 million for 1963, and $455 million for 1962.

7. The foreign exchange reserves of Israel amounted to $600 million in December 1963, and increased by $34 million up to September 1964. It was estimated that the foreign exchange reserves would amount to $650 million in December 1964. Thus the increase in the amount of foreign exchange reserves of $50 million, as compared with the reserves in December 1963, represented only 50 per cent of annual import needs, or six months' supply in comparison with the foreign exchange reserves in December 1963, which represented 60 per cent of the imports of goods and services for that year, or seven months' supply. In considering these figures it is essential to remember that Israel is highly dependent on imports for both basic foods and essential raw material for industry, in addition to capital equipment for development. Furthermore, Israel's special trading position and security position necessitated maintenance of essential stocks of food and raw materials.

8. Israel's foreign debt increased more than the slight increase in the foreign exchange reserves in 1964 compared with 1963, and in September 1964 foreign debt amounted to one billion dollars. Israel's balance of payments in the past had been assisted by unilateral transfer payments of various kinds, including personal
restitution and reparations from Germany and the proceeds of the sales of Israel Independence and Development Bonds. It was expected that both of these sources would decrease and no comparable increase was expected from other sources. The net income from restitution and reparations payments was $169 million in 1963, while the estimated income for 1964/65 is $135 million, and for 1965/66, $115 million. Since 1963, repayments of Israel bonds have commenced, and it is expected that the net annual income from this source would drop by $20 million.

9. On the export side, Government assistance was given for market research, design of new products, rationalization of industry and manufacture and supply of those products in which Israel might have a competitive advantage. In addition, the Government aimed to supply port services and export insurance at terms similar to those applicable abroad. It was the earnest hope of the Israeli exporters that the first cut in a general 50 per cent reduction of tariffs on industrial products, and on some agricultural products, would be taken at an early date.

10. The rapid rise in imports was attributed to the high level of economic activity, arising out of development. With the rise in incomes and prices, development activity in industry, agriculture and housing, had reduced almost to zero reserves of manpower, and had created a rising demand for both investment and consumer goods. The Government of Israel, recognizing the inflationary situation, was taking measures to limit the demand and divert resources into essential investment and development. However, there was no intention to limit imports by quantitative restrictions or to abandon the policy of liberalization undertaken in 1962, as it was the Government's firm belief that this policy was essential to make Israel's production efficient by competition with foreign manufacturers and in this way to reduce prices in the home market and increase the export potential.

11. Members of the Committee thanked the representative of Israel for his clear and comprehensive statement. The Committee welcomed the liberalization measures taken by the Government of Israel, and expressed the opinion that in view of the steady inflow of capital, further liberalization was called for. In making clear the decision of Israel, the representative of Israel said that
the Government was following a policy of liberalization which it had adopted in 1962, and the decision to further liberalize imports was taken in expectation of better trade returns. In spite of the worsening of the overall balance-of-payments position in the last year, it was the intention of the Israeli Government to continue the liberalization programme. By October 1965 all restrictions would have been reviewed, and by then he foresaw a small number of products still remaining under licensing as a protection to infant industry. The members of the Committee hoped, and urged, that the remaining items would be very few and would be truly of a hard-core nature. They expressed the hope that as restrictions were removed they would not be replaced by other kinds of protectionism.

12. The representative of Israel stated that it was not his Government's intention to increase protection and that in fact a decision had been taken to reduce present tariff levels. He stated that there had been considerable internal discussion on the timing of such reductions. He indicated that any tariff reduction would be applicable to all contracting parties to the GATT. Although it was planned to commence in October 1965 a review of tariffs with a view to their reduction, the rate at which tariffs were to be reduced was to be decided at a later stage.

13. In reply to a question, the representative of Israel indicated that the earlier estimate of a decrease in the foreign exchange receipts was based on preliminary estimates of exports and imports. Exports had barely reached their target, but imports had increased by more than had been estimated which reflects the continuing liberalization policy followed by Israel.
Alternative measures to restore equilibrium

14. The representative of Israel stated that the Government of Israel was aware of the rise in incomes and of the consequent pressure on available resources. Israel was taking measures to check demand inflation by limiting Government expenditure and by limiting private expenditure by savings schemes and other measures designed to restrain personal incomes. According to the recent budget announcement no new Government building projects are to be undertaken, and Government departmental expenditure is to be severely limited. With regard to restraining personal income, the Government of Israel had adopted a method of improved efficiency in tax collection in preference to increasing direct taxation. The Government was not in a position to increase sales tax because in Israel the wage system was linked to the cost-of-living index, so that imposition or increase of sales tax would create a wage price spiral effect. All these measures were undertaken in the spirit of making a start towards curbing the inflationary movement. It was also hoped that liberalization of imports would help in this direction.

15. A member of the Committee referring to the recommendations of the Export Institute enquired whether the Government of Israel found it possible to follow the policy of linking wages to productivity. The representative of Israel stated that Israel had set up a joint body of the manufacturers association, trade union and the Government to determine the increase in production as a guide to wage negotiations. In 1964, however, wages had increased more than productivity but it was hoped that the new body would have a restraining effect.

System and method of restrictions

16. The Committee recalled that the International Monetary Fund Executive Board decision urged that Israel reduce reliance on bilateral payments arrangements. A member of the Committee asked whether the future liberalization of imports would have an effect on Israel's volume of trade conducted under the bilateral
arrangements. The representative of Israel indicated that total imports under bilateral arrangements amounted to 4 per cent in 1963, and he expected the same figure for 1964. He stated that bilateral arrangements offered a framework and a guide-line for trading only, as goods could not be imported into Israel at prices above prevailing international prices. Israel would be happy to reduce the number of bilateral arrangements if her exports could have easier access to other markets. He stated that there are two kinds of exports: (a) exports of manufactured goods, and (b) exports of development products. With respect to exports of development products, they had found markets in Eastern Europe and Africa. There were bilateral agreements with Eastern European countries, but it was not the Israeli Government which determined their trading arrangements; it was the partner countries who decided the methods of trade. He said that he was not sure what would be the effects of the new interest of Eastern European countries in importing fertilizer from Israel.

17. A member of the Committee, pointing to the granting of individual licences as mentioned in the basic document, noted that the authorities granting these licences are said to take into account the necessity to protect infant industries. Article XII and Article XVIII:(b) do not authorize quantitative restrictions to ensure economic protection, but to help overcome a difficult financial situation of the country. Therefore he was happy to note that Israel was abandoning this policy, was liberalizing imports, and would not be open to criticism in this sense.

18. Referring to the recent increase in the tariffs of motor vehicles, a member of the Committee enquired whether the Israeli authorities foresaw any substantial increases in tariffs of this nature in connexion with the liberalization of quantitative restrictions. The representative of Israel replied that the recent increase in the tariff rate on motor vehicles was an exceptional measure which was called for by a large increase in the number of imported cars, from 7,000 in 1961 to 13,000 in 1964, and confirmed that it was not the intention of his Government to increase tariff rates in this way. Furthermore, an increased internal tax had been imposed to avoid any increased protection to domestic assembly of automobiles.
19. The representative of Israel informed the Committee that the publication of a negative list at present would have little meaning since the review of restrictions was to be completed by October 1965. Although 80 per cent of the trade was liberalized, a large number of tariff items, and particularly sub-items, would at present have to appear in a negative list. It was his hope that after the review was completed the negative list would be published and its extent would be minimal.

General

20. The members of the Committee thanked the representative of Israel for the very frank and detailed manner in which he had answered the many questions put to him, and they felt the consultation had thrown much light on import control policy and systems in force in Israel. They welcomed the efforts Israel had made in liberalizing imports and expressed the hope that in the review of 1965 the Government of Israel would make every possible effort to carry forward this liberalization policy, and avoid use of other measures to restrict normal trade.

21. The Committee welcomed the recent fiscal measures taken by Israel and hoped that further liberalization of imports would also help in reducing the pressure on domestic resources.

22. The representative of Israel thanked members of the Committee for their understanding and co-operation in the course of consultation. He stated that in spite of the difficult period which Israel faced, Israel would take all possible measures to reduce restrictions and liberalize trade.