

CHAPTER XIII

THE MONEY SUPPLY, CREDIT AND THE BANKING SYSTEM

1. MAJOR TRENDS IN THE DEVELOPMENT OF THE MONETARY SYSTEM

THE VOLUME of bank credit extended to the Government and to the public¹ was considerably expanded in 1958. The foreign currency reserves held by the banking system likewise increased. As a result, the value of the public's financial assets rose significantly. This applies particularly to time deposits and other deposits not forming part of the money supply. The latter—defined as demand deposits and cash in the hands of the public—increased to a lesser extent.

The average money supply in 1958 exceeded the 1957 average by 15.2 per cent, thus increasing more slowly than during the 1954–1957 period, when the expansion proceeded at a rate of about 20 per cent per annum.

While the increase in the money supply was relatively small in 1958, the deposits of the public other than demand deposits expanded considerably. This applies particularly to deposits held under saving schemes, on which a higher rate of interest and reduced income tax rates are allowed. Such deposits may be withdrawn at one month's notice; however, premature withdrawal forfeits the right to the higher interest otherwise payable. The turnover velocity of these deposits was very low; however, since they may be withdrawn at a month's notice, the public seems to consider them as being little less liquid than the money supply.

A significant increase also occurred in time deposits for fixed periods, which are not regarded as liquid, since they cannot be prematurely withdrawn, or—had they been deposited against obligations—unless these obligations had been met. Foreign currency deposits earmarked for payments abroad—also considered liquid—likewise expanded.

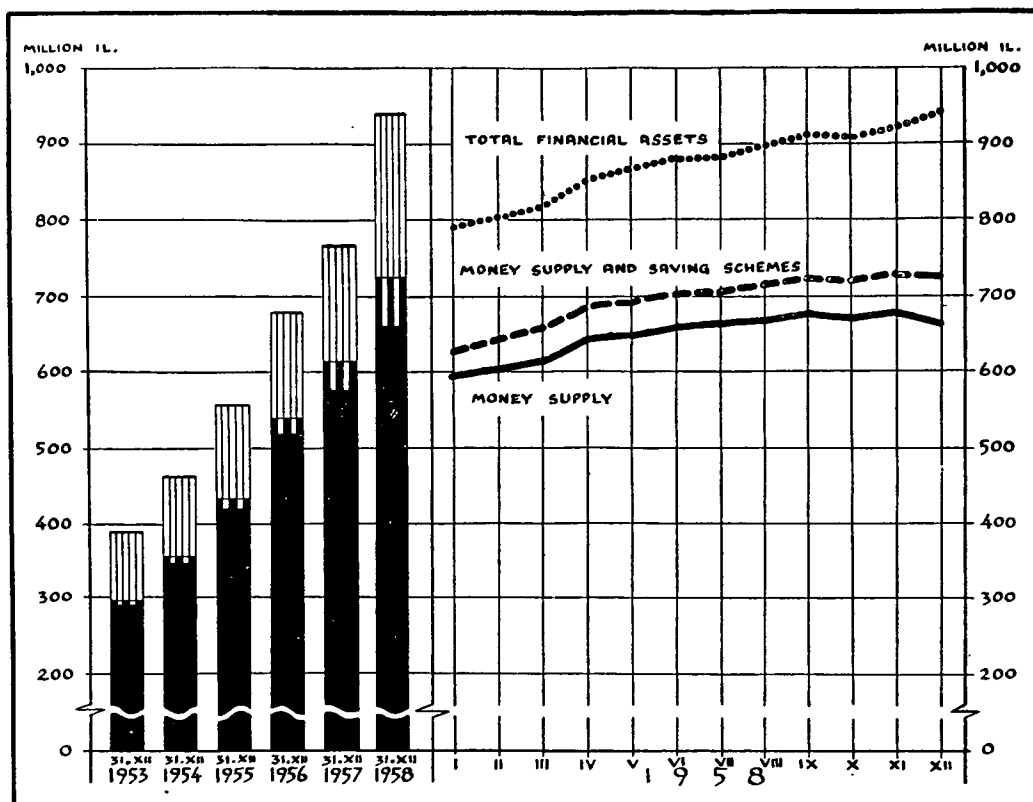
The rate at which the money supply expands may serve as an indicator of the rise in the monetary demand of the public; in fact, the latter increased by 15 per cent. It should be noted, however, that the real national product and the real import surplus expanded by 8 per cent only. This gap resulted in the generation of inflationary pressures by the excess demand. Prices consequently

¹ The term "public" as used in this chapter refers to the entire economy, apart from the Government sector. It includes, therefore, individuals, companies, the local authorities, the National Institutions, financial institutions other than banks and Government corporations, and certain non-residents holding deposits in Israel banks.

rose by 2 to 3 per cent,—a comparatively small increase, due to the drop in import prices and certain other factors (see Chapter I—"Main Economic Developments in 1958", and Chapter VI—"Prices").

DIAGRAM XIII-1

The Financial Assets of the Public, 1953-1958
(millions of IL.)



(a) *Factors increasing the money supply and other deposits*

Credit to the public was expanded by IL.60 million and credit to the Government by a similar sum. This was the main cause of the increase in the financial assets¹ of the public, a subsidiary cause being a IL. 22 million rise in average foreign currency reserves.²

¹ The financial assets of the public comprise cash and all deposits of the public in banking institutions. This term thus covers the less liquid deposits, as well as the money supply (which consists of cash and demand deposits).

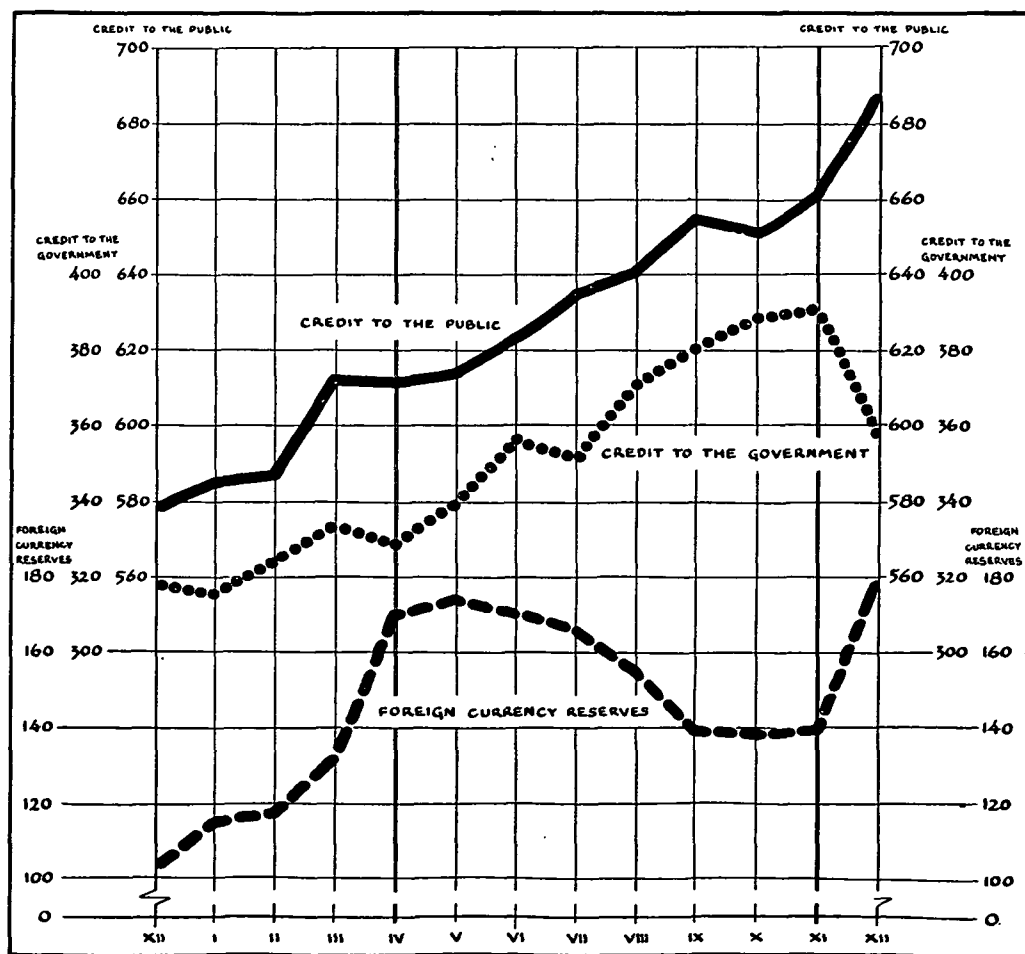
² The figures on the money supply and credit cited here and elsewhere in this chapter are annual averages in all cases when they are related to other data and other developments covering the whole year,—e.g., the national output, the balance of payments, prices, etc.

The accumulation of foreign exchange reserves at the Bank of Israel and the credits granted by the latter to Government and public not only expand the volume of the public's financial assets directly, but also increase it indirectly—by adding to the liquid assets of the banking system, thus providing a basis for the expansion of bank credit.

The weight of each of the factors in the expansion of the money supply varied during the year: In the months January–April 1958, the public's financial assets grew chiefly through the IL.67 million rise in foreign exchange reserves. Most of these reserves were transferred to the Bank of Israel, thus expanding consider-

DIAGRAM XIII-2

Foreign Currency Reserves and Credit Granted to Government and Public, 1958
(millions of IL.)



ably the liquid assets of the banking system. During these months, the volume of credit extended by the Bank of Israel to the Government, grew likewise, albeit by only IL. 7 million, while Government's liabilities to the banking institutions increased by IL. 5 million. Consequently, the liquidity of the banking system became excessive and the Bank of Israel restricted rediscounts by IL. 25 million in order to reduce it, at the same time enabling banking institutions to extend credit from their own resources.

Between May and November, the amount of foreign currency held by the banking system declined by IL. 30 million. At the same time, the Government's debt to the banking system rose by IL. 62 million, of which its indebtedness to the Bank of Israel represented IL. 39 million. The amount of re-discounts granted by the Bank of Israel remained stable and there was no marked change in the amount of liquid assets held by the banking institutions.

In December 1958, the foreign exchange reserves in the Bank of Israel increased, as a result of transfers by the Government. The Government's debt was thus reduced.

An additional factor augmenting the liquidity of the banking system in 1958 was that the public's deposits expanded more rapidly than its cash holdings.

The expansion of the foreign exchange reserves in the Bank of Israel during the first half of the year, and the larger volume of credit granted to the Government in the second half, greatly expanded the liquid assets held by the banking institutions—the more so since there was only a slight rise in the public's cash withdrawals from the banks. Consequently, a considerable expansion of credit to the public ensued.

(b) The expansion of credit and its control

New liquidity regulations came into effect at the beginning of 1958, fixing a minimum liquidity ratio of 58 per cent on demand deposits and deposits for terms not exceeding 18 months. The Governor of the Bank of Israel was, however, authorized to issue orders lowering the liquidity ratio, by exempting certain loans from the liquidity regulations, up to a limit therein determined. Such an order came into effect simultaneously with the new liquidity regulations and fixed this limit at 20 per cent of the value of deposits subject to the liquidity regulations.

The Bank of Israel grants exemptions for loans considered to rate a high priority from the aspect of economic development—and first and foremost, to enterprises producing for export or for the replacement of vital imports. Insofar as the Governor takes full advantage of his prerogative to approve such exemptions, the minimum liquidity ratio required of the banks falls to 38 per cent.

The liquidity regulations refer only to demand deposits and to deposits for periods not exceeding 18 months. Deposits within the framework of saving schemes are covered by special regulations, stipulating that 60 per cent of them must be invested in securities approved for this purpose by the Ministry of

Finance and the Bank of Israel, or deposited in non-liquid form with the Bank of Israel. The banks are allowed to use the remaining 40 per cent of these funds for the expansion of credit, but as regards 25 per cent the purpose must be approved by the Ministry of Finance and the Bank of Israel. No approval is required for the remaining 15 per cent.

Apart from the liquidity regulations, the volume of credit was also controlled in 1958 through a provision limiting the granting of credit by individual banking institutions to the volume they had extended in 1953, plus the increases authorized thereafter. However, insofar as the banks' liquidity exceeded the legal requirements, they were exempted by the Bank of Israel from the volume restriction. The latter has thus virtually ceased to be used for the quantitative control of credit, becoming rather an instrument for its qualitative control.

In 1958, the Bank of Israel facilitated a considerable expansion of credit, chiefly by exempting loans to agriculture and industry from the liquidity and volume restrictions. Credit to the public was expanded rapidly, in particular during the second half of the year, with the seasonal increase in the credit requirements of agriculture. As a result, the liquidity ratio of the banking institutions during the last months of the year declined to the legal minimum of 38 per cent.

The total amount of bank credit granted to the public from the resources of the banking institutions between January and December 1958 was IL. 89 million. During the same period, however, the Bank of Israel contracted re-discounts by IL. 24 million, the net expansion of bank credit to the public thus amounting to IL. 65 million.

(c) The demand for additional credit

Though the volume of credit was considerably expanded, complaints were once again voiced about the shortage of credit, particularly by the industrial sector. Indeed, such a shortage was felt more keenly in 1958, the demand for credit being stimulated by new factors (besides those discussed in earlier Annual Reports, and particularly in the 1956 Report).

At the legally determined rate of interest, the demand for bank credit exceeds the amounts which the Bank of Israel can permit without generating an acute inflation. Excessive credit expansion cannot alleviate the credit shortage, as it is likely to be followed by a rise in prices which would stimulate the demand for credit further.

The numerous complaints about the credit shortage in 1958, despite the sizable increase in the value of loans granted and the relatively stable price level, were due to several factors which gained importance during the year: Competition between producers and merchants grew keener, but it was reflected by the larger volume of credit sales or by extending the period for which the credit was granted, rather than by price reductions.

Another factor increasing the demand for credit in 1958 was the maturing of

investments, some of which had been made without any reserve of turnover capital being provided for the current financing of production. Only some of the numerous requests for working capital submitted by new enterprises to banking institutions are granted, since the latter use most of the credit they are permitted to extend within the framework of the liquidity and volume ordinances for the benefit of their older clients. Hence, a high proportion of the new concerns' applications for working capital is directed to the Bank of Israel, in the form of requests for re-discounts or exemptions from the liquidity regulations. Under the prevailing conditions, the Bank could not permit an expansion of credit that would satisfy all demands.

(d) *The rate of interest*

The debitory rate of interest in banking institutions remained virtually unchanged in 1958, reaching the maximum level permitted by the 1957 Order implementing the Interest Law, under which interest on credits to agriculture and industry must not exceed 10 per cent per annum, while the maximum rate on credits to other branches is 11 per cent. Interest on credits exempted by the Bank of Israel from the liquidity and volume restrictions was limited to 9 per cent. The maximum rate on loans linked to the dollar exchange rate or to the consumer price index is fixed by law at $6\frac{1}{2}$ per cent.

The Bank of Israel charges 6 per cent per annum on bills rediscounted in local currency. To this, the banking institution may add a further $2\frac{1}{2}$ per cent. Re-discounts in foreign currency, which are only granted to finance imports for exports and exports on credit, are effected at the rate of 3 per cent, banking institutions being allowed to charge an additional 2 per cent.

The creditary rate of interest rose somewhat, due to competition among banking institutions trying to attract time deposits—and particularly participation in their saving schemes. Higher rates, and the larger proportion of deposits bearing relatively high interest, raised the average creditary interest rate from 2.4 per cent in 1957 to 2.8 per cent in 1958. Average interest rates on savings deposits and time deposits rose from 3.8 per cent in 1957 to 4.5 per cent in 1958.

2. THE INCREASE IN THE FINANCIAL ASSETS OF THE PUBLIC

The average money supply totalled IL.646 million in 1958,—IL.84 million (or 15.2 percent) more than in the preceding year. During 1957 the money supply had expanded by 19.4 per cent, while in 1955 and 1956 the annual rate of expansion had been 20 per cent. The rate of expansion thus decreased during the year under review.

The money supply—defined as cash held by the public plus demand deposits—comprises assets of the highest liquidity, whereas time deposits are regarded as being less liquid.

The distinction between the degree of liquidity of the various financial assets is based on certain assumptions as to the public's intentions. The main assumption is that the public generally prefers to hold funds destined for expenditure within a short time in the form of cash or demand deposits, on which normally no interest is paid. On the other hand, amounts earmarked for spending at a later date are generally held in the form of less liquid, interest-bearing assets.

The last few years have witnessed a considerable expansion of certain liquid types of financial assets held by the banking system, which are by definition excluded from the money supply. In 1956, various banks introduced saving schemes. The rate of interest on monies deposited within the framework of these schemes is staggered according to the period of saving—up to a maximum of 6 per cent, and benefits from income tax allowances. Such deposits may be withdrawn at 30 days notice, in which case the depositor forfeits the interest payable on them. (For further details, see Chapter XVI—"Personal Saving"). By the end of 1958, the total of funds accumulated under saving schemes had reached IL.53 million, half of this amount being saved during the year under review.

It may be assumed that a considerable proportion of deposits in saving accounts reflects the transfer of balances previously kept in the form of demand deposits. It would seem that the public regards the deposits within the framework of saving schemes as being relatively liquid, though the turnover velocity of these deposits during the year was low—less than one—as against 18 in demand deposits.

Other assets of relatively high liquidity are time deposits for periods not exceeding 3 months.

Together with amounts deposited under saving schemes and time deposits for periods not exceeding 3 months, the average money supply in 1958 was 17.4 per cent above the level of 1957. During 1957, the increase was 21 per cent. During both years, these rates of expansion were thus higher than those for the money supply only. However, in 1958 the expansion was smaller than in 1957.

A breakdown of the increase in the financial assets of the public during 1958 is given in Table XIII-1.

The non-liquid assets held by the public¹ include certain deposits in local and foreign currency. Four types of local currency deposits may be distinguished:

(a) Deposits for periods not exceeding 3 months: These include not only the deposits of individuals, but also considerable amounts deposited by institutions—and in particular by provident funds, insurance funds and insurance companies. Between January and July, these deposits expanded from IL. 61.9 million to IL. 77.7 million. However, later in the year, the deposits of provident funds were transferred in the banks' statistics to the item "deposits earmarked for loans". By the end of 1958, therefore, the amount of deposits for periods exceeding 3 months had receded to IL. 67.9 million. The above-mentioned

¹ Only assets constituting a liability of the banking system are discussed here.

TABLE XIII-1

The Financial Assets of the Public, 1953-1958
(millions of IL.)

(End of period)

Period	Cash held by public	Demand deposits	Total money supply (1)+(2)	Deposits under saving schemes	Time deposits for periods not exceeding 3 months	Total (3)+(4)+(5)	Non-liquid assets	Total financial assets of public (6)+(7)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1953 ^a	128.0	162.1	290.1	—	4.8	294.9	94.7	389.6
1954	146.6	201.9	348.5	—	6.9	355.4	109.8	465.2
1955	172.5	247.2	419.7	0.7	11.8	432.2	120.7	552.9
1956	228.3	289.0	517.3	11.4	10.3	539.0	131.4	670.4
1957	230.9	345.3	576.2	26.5	9.8	612.5	155.4	767.9
1958	251.4	408.5	659.9	52.8	11.7	724.4	215.5	939.9
1958 January	236.8	355.4	592.2	27.8	8.2	628.2	160.7	788.9
February	239.8	361.2	601.0	29.4	8.7	639.1	161.8	800.9
March	245.1	368.1	613.2	30.6	10.0	653.8	161.7	815.5
April	245.3	394.8	640.1	31.7	10.3	682.1	166.3	848.3
May	246.0	400.2	646.2	32.9	10.7	689.8	174.9	864.7
June	248.4	408.4	656.8	34.9	10.0	701.7	177.1	878.8
July	254.4	403.9	658.3	35.9	9.5	703.7	178.4	882.1
August	254.8	411.6	666.4	37.3	9.1	712.8	184.4	897.2
September	259.9	412.1	672.0	38.6	10.8	721.4	188.2	909.6
October	256.5	412.2	668.7	40.0	11.7	720.4	187.9	908.3
November	259.6	413.7	673.3	41.6	12.8	727.7	192.3	920.0
December	251.4	408.5	659.9	52.8	11.7	724.4	215.5	939.9

^a Some of the figures for 1953 are estimates, owing to the different classification methods then in use.

transfer in the banks' statistics was due to a purely technical re-classification, and has no economic significance.

(b) Deposits earmarked for loans: These deposits represent amounts deposited by private institutions for the granting of loans to certain clients (or the participation of the above institutions in loans granted to certain clients by the banks)—and are non-liquid, the depositor being unable to withdraw his money until the loan granted from it has been fully repaid. These operations do not affect the volume of liquid assets held by the banking institutions or the public, reflecting merely the transfer of such assets from the depositor to the borrower. As already pointed out, the deposits of provident funds, previously included with time deposits, were transferred to this item. Deposits earmarked for loans rose from IL.35.3 million at the end of 1957 to IL.47 million at the end of 1958.

(c) Deposits against liabilities: These represent amounts deposited against guarantees given by the banking institutions to their clients, and are also non-liquid, as they may be withdrawn only at the end of the period covered by the guarantee. However, unlike deposits earmarked for loans (which, as already stated, represent only a transfer of liquid assets from depositor to borrower), this type of deposit reduces the volume of liquid assets held by the public. Deposits against documentary credits are likewise included in this item. Deposits against liabilities declined during the year from IL.14.8 million to IL.11.1 million.

TABLE XIII-2

Non-liquid Assets of the Public in Banking Institutions, 1953-1958
(millions of IL.)

(End of period)

Period	Local currency deposits				Foreign currency deposits	Total
	time deposits for periods exceeding 3 months	deposits earmarked for loans and the public's participation in loans	deposits against liabili- ties	deposits linked to the dollar exchange rate (PAZAK)		
1953 *	34.7	31.0	14.0	—	15.0	94.7
1954	38.1	27.2	11.8	—	32.7	109.8
1955	51.2	28.4	11.9	—	29.2	120.7
1956	52.5	32.8	13.4	2.3	30.4	131.4
1957	61.9	35.3	14.8	5.6	37.8	155.4
1958	67.9	47.0	11.1	14.9	74.6	215.5
1958 January	66.2	34.4	15.4	6.1	38.6	160.7
February	67.6	31.9	15.6	6.7	40.0	161.8
March	67.3	31.0	15.5	7.3	40.6	161.7
April	68.1	30.8	15.4	8.1	43.9	166.3
May	71.1	29.3	13.4	8.4	52.7	174.9
June	76.2	26.8	13.3	9.2	51.6	177.1
July	77.7	26.5	12.7	9.8	51.7	178.4
August	75.3	32.6	12.5	10.6	53.4	184.4
September	66.4	41.6	13.2	11.2	55.8	188.2
October	57.3	51.2	12.3	12.2	54.9	187.9
November	59.2	49.6	11.8	13.4	58.3	192.3
December	67.9	47.0	11.1	14.9	74.6	215.5

* See note * to Table XIII-1.

(d) Time deposits linked to the dollar exchange rate (PAZAK): These represent foreign currency transfers from abroad (mainly personal restitution payments from West Germany) deposited for a fixed period. The account

holders, however, may draw on such funds only with the approval of the exchange authorities. Deposits of this type may, therefore, be considered as linked local currency deposits, though in the banks' statistics they appear under "foreign currency deposits". The banks re-deposit these funds with the Bank of Israel, which grants loans to the Treasury against part of them. Since restitution payments were considerably expanded during the year under review, the volume of these deposits grew from IL.5.6 million at the end of 1957 to IL.14.9 million at the end of 1958.

The total increase in non-liquid, local currency deposits between the end of 1957 and the end of 1958 was IL.23.3 million.

Foreign currency deposits are mainly of two types:

(a) Deposits of residents earmarked, with the approval of the Controller of Foreign Exchange, for payments abroad: These are partly held by exporters for the financing of raw material imports (PAMAZ accounts) and partly by residents transferring foreign currency. The funds in these deposits also largely originate from restitution payments, 20 per cent of which may be spent abroad by the recipient and need not be converted into local currency (TAMAM accounts).

(b) Deposits of non-residents (PATACH accounts): These are funds not intended for use in the country, which benefit from a special arrangement made in 1958, whereby a higher rate of interest is allowed to non-residents maintaining foreign currency accounts in Israel (6 per cent on time deposits for a one-year period).

The foreign currency deposits held by residents and non-residents have a very slight impact on the liquidity of the public, since they are not usually spent in the country. The volume of these deposits was doubled during the year, expanding from IL. 37.8 million at the end of 1957 to IL.74.6 million at the end of 1958—i.e., by IL.36.8 million.

The total value of the various non-liquid deposits in local and foreign currency reached IL.60.1 million at the end of 1958, 38.7 per cent more than at the end of 1957. However, much of the expansion took place in December 1958, so the average annual increase was lower in the year under review than in the preceding year.

The average volume of all types of non-liquid assets expanded by IL.34 million—an increase of 23.5 per cent over 1957. This exceeds the rise in the money supply and other liquid assets, mainly because of the relatively large increase in foreign currency deposits.

The average nominal value of the public's financial assets was 19 per cent—or IL.136.8 million—higher than in 1957. The largest increase occurred in saving scheme deposits and in foreign currency deposits for fixed periods. The smallest increase was recorded in the amount of cash held by the public: The proportion of cash in the money supply declined from an average of 41.1 per cent in 1957 to 38.7 per cent in 1958. This downward trend has been in evi-

dence for a number of years and may be attributed to higher creditory interest rates and to the fact that certain elements in the population, previously not in the habit of depositing money in banks, have now begun to do so. The resulting structural change in the financial assets of the public is shown in Table XIII-3.

TABLE XIII-3
The Financial Assets of the Public, 1957-1958
(average percentages)

	1957	1958	Percentage increase from 1957 to 1958
Cash	31.4	28.7	14.1
Demand deposits	44.9	45.4	48.3
Money supply	76.3	74.1	62.4
Saving schemes and time deposits for less than 3 months	3.9	5.3	12.7
Total	80.2	79.4	75.1
Non-liquid deposits	19.8	20.6	24.9
Total financial assets			
Percentages	100.0	100.0	100.0
Millions of IL.	734.3	871.1	136.8

The expansion of the money supply and other financial assets of the public was not uniform throughout the year—the increase being steepest during the first six months. Tables XIII-1 and XIII-2 show monthly developments and the factors causing them.

3. FACTORS DIRECTLY RESPONSIBLE FOR THE INCREASE IN THE FINANCIAL ASSETS OF THE PUBLIC

The major factor increasing the financial assets of the public was the expansion of credit. The amount of bank credit granted to the Government in 1958 was, on the average, approximately IL.60 million higher than in 1957, while credit to the public was expanded by a similar sum. The IL.22 million increase in foreign currency balances and the additional IL.7 million invested by the banking system in non-governmental securities constituted subsidiary factors tending to increase the financial assets of the public. On the other hand, the latter were contracted by the IL.6 million decline in balances in transit.

TABLE
Consolidated Balance Sheet c
(million)

(End of period)							
Assets and liabilities	1953 ^a	1954	1955	1956	1957	1958	1958 Jan.
<i>Credit to the public</i>							
Bank of Israel	—	—	15.7	35.1	51.6	27.6	43.3
Banking institutions	204.5	231.4	240.1	264.1	306.4	395.6	321.3
Total (1)	204.5	231.4	255.8	299.2	358.0	423.2	364.6
<i>Investment in non-governmental securities</i>	5.5	7.8	9.0	14.4	17.3	27.5	18.3
Total (2)	210.0	239.2	264.8	313.6	375.3	450.7	382.9
<i>Credit to the Government</i>							
Bank of Israel	133.5	133.5	171.1	236.7	271.3	289.0	272.7
Banking institutions	37.9	19.3	28.8	26.5	45.7	67.2	42.4
Total (3)	171.4	152.8	199.9	263.2	317.0	356.2	315.1
<i>Net balances of foreign exchange</i>							
Bank of Israel	8.0	53.5	83.5	92.4	82.8	162.1	93.8
Banking institutions	15.0	31.9	21.7	27.7	19.7	17.3	21.1
Total (4)	23.0	85.4	105.2	120.1	102.5	179.4	114.9
<i>Balances in transit</i>	16.0	20.5	23.4	18.5	17.1	6.7	19.3
<i>Less: Deposits in saving schemes and time deposits for periods not exceeding 3 months</i>	4.8	6.9	12.5	21.7	36.3	64.5	36.0
<i>Non-liquid assets</i>							
In local currency	79.7	77.1	91.5	101.0	117.6	140.9	122.1
In foreign currency	15.0	32.7	29.2	30.4	37.8	74.6	38.6
Total (5)	99.5	116.7	133.2	153.1	191.7	280.0	196.7
Other accounts (net) ^b (6)	30.8	32.7	40.4	45.0	44.0	53.1	43.3
<i>The money supply</i>							
(1) + (2) + (3) + (4) - (5) + (6)	290.1	348.5	419.7	517.3	576.2	659.9	592.2

^a See note * to Table XIII-1.

^b Including own capital and investments in real estate.

1958										
<i>Feb.</i>	<i>Mar.</i>	<i>Apr.</i>	<i>May</i>	<i>June</i>	<i>July</i>	<i>Aug.</i>	<i>Sept.</i>	<i>Oct.</i>	<i>Nov.</i>	<i>Dec.</i>
34.2	33.7	27.2	21.7	21.6	22.3	21.6	22.6	20.9	22.2	27.6
323.7	333.1	336.7	343.7	351.8	360.8	369.0	380.8	380.3	386.6	395.6
357.9	366.8	363.9	365.4	373.4	383.1	390.6	403.4	401.2	408.8	423.2
23.3	21.4	21.3	23.6	22.5	23.8	22.4	22.6	22.2	23.1	27.5
381.2	388.2	385.2	389.0	395.9	406.9	413.0	426.0	423.4	431.9	450.7
270.8	279.6	277.7	278.2	289.4	289.2	303.8	315.8	323.1	316.5	289.0
52.5	53.9	50.6	61.7	66.2	61.8	66.7	64.5	64.8	73.8	67.2
323.3	333.5	328.3	339.9	355.6	351.0	370.5	380.3	387.9	390.3	356.2
107.5	124.1	157.9	173.2	167.0	157.9	145.8	127.5	126.0	131.7	162.1
9.2	7.8	11.7	0.3	2.9	7.4	8.6	11.6	11.7	7.3	17.3
116.7	131.9	169.6	173.5	169.9	165.3	154.4	139.1	137.7	139.0	179.4
22.1	12.5	14.8	13.0	8.1	10.7	10.2	14.4	12.3	12.4	6.7
38.1	40.6	42.0	43.6	44.9	45.4	46.4	49.4	51.7	54.4	64.5
121.8	121.1	122.4	122.2	125.5	126.7	131.0	132.4	133.0	134.0	140.9
40.0	40.6	43.9	52.7	51.6	51.7	53.4	55.8	54.9	58.3	74.6
199.9	202.3	208.3	218.5	222.0	223.8	230.8	237.6	239.6	246.7	280.0
42.4	50.6	49.5	50.7	50.7	51.8	50.9	50.2	53.0	53.6	53.1
601.0	613.2	640.1	646.2	656.8	658.3	666.4	672.0	668.7	673.3	659.9

TABLE XIII-5
Changes in the Financial Assets of the Public, 1956-1958
(millions of IL.)

	Increase or decrease (-) from end of year to end of year				Increase or decrease (-) from annual average to annual average			
	millions of IL.		percentages		millions of IL.		percentages	
	from 1956 to 1957	from 1957 to 1958	from 1956 to 1957	from 1957 to 1958	from 1956 to 1957	from 1957 to 1958	from 1956 to 1957	from 1957 to 1958
<i>Financial assets</i>								
Cash	2.6	20.5	1.1	8.9	26.9	19.3	13.2	8.4
Demand deposits	56.3	63.2	19.5	18.3	64.0	66.0	24.1	20.0
Money supply	58.9	83.7	11.4	14.5	90.9	85.3	19.4	15.2
Deposits under saving schemes and deposits for periods not ex- ceeding 3 months	14.6	28.2	67.3	77.7	11.3	17.4	63.8	6.00
<i>Total</i>	73.5	111.9	13.6	18.3	102.2	102.7	21.0	17.4
Non-liquid deposits	24.0	60.1	18.3	38.7	23.4	34.1	19.3	23.5
Total financial assets	97.5	172.0	14.5	22.2	125.6	136.8	20.6	18.6
Other accounts (net)	-1.0	9.1	—	—	1.2	5.4	—	—
<i>Total</i>	96.5	181.1	13.5	22.3	126.8	142.2	19.4	18.3
<i>Factors affecting the volume of financial assets</i>								
Expansion of credit to the public	58.8	65.2	19.7	18.2	44.1	59.0	15.7	18.2
Investment in non-gov- ernmental securities	2.9	10.2	20.1	59.0	3.5	6.9	28.5	43.7
<i>Total</i>	61.7	75.4	19.7	20.1	47.6	65.9	16.3	19.4
Expansion of credit to the Government	53.8	39.2	20.4	12.4	79.0	60.8	37.1	20.8
Foreign currency reserves	-17.6	76.9	-14.7	75.0	- 0.1	21.8	- 0.1	17.0
Balances in transit	- 1.4	-10.4	- 7.6	-60.8	0.3	- 6.3	1.6	-32.6
<i>Total</i>	96.5	181.1	13.5	22.3	126.8	142.2	19.4	18.3

The share of the various factors in the expansion of the public's financial assets underwent some changes during 1958. Between January and April, this expansion was mainly caused by the growth of foreign exchange reserves, while there was only a moderate increase in bank credit granted to Government and public. Between May and November, foreign currency deposits held by the banking system declined steeply, but credit was expanded to the Government and to the public at an accelerated rate. In December, bank credit to the public continued to expand and foreign currency reserves resumed their upward trend, mainly because the Government began to sell foreign exchange to the Bank of Israel, thus considerably reducing its indebtedness to the banking system.

4. FOREIGN EXCHANGE BALANCES

The average net foreign exchange balances held by the banking system were by IL.22 million larger in 1958 than in 1957. This increase was subject to the

TABLE XIII-6

Net Balances of Foreign Exchange held with the Banking System, 1953-1958
(millions of IL.)

(End of period)

Period	With the Bank of Israel	With banking institutions			Total (1)+(4)
		assets	liabilities	net assets (2)-(3)	
	(1)	(2)	(3)	(4)	(5)
1953 ^a	8.0 ^b	29.0	14.0	15.0	23.0
1954	53.5	72.6	40.7	31.9	85.4
1955	83.5	54.8	33.1	21.7	105.2
1956	92.4	48.5	20.8	27.7	120.1
1957	82.8	54.6	34.9	19.7	102.5
1958	162.1	64.5	47.2	17.3	179.4
1958 January	93.8	54.0	32.9	21.1	114.9
February	107.5	53.0	43.8	9.2	116.7
March	124.1	52.7	44.9	7.8	131.9
April	157.9	52.4	40.7	11.7	169.6
May	173.2	47.7	47.4	0.3	173.5
June	167.0	47.7	44.8	2.9	169.9
July	157.9	50.3	42.9	7.4	165.3
August	145.8	51.1	42.5	8.6	154.4
September	127.5	54.1	42.5	11.6	139.1
October	126.0	52.2	40.5	11.7	137.7
November	131.7	56.0	48.7	7.3	139.0
December	162.1	64.5	47.2	17.3	179.4

^a See note ^a to Table XIII-1.

^b Foreign exchange balances held with the Issue Department of the Bank Leumi le-Israel B.M.

usual seasonal fluctuations. Between January and April, there was a significant rise of IL.67 million, since receipts from exports, donations and the Development Loan reach their peak during these months, while foreign currency expenditures are not subject to serious seasonal fluctuations. From May to November, foreign exchange balances declined by IL.30 million, income from exports and unrequited receipts being relatively limited in this period. In December, however, foreign exchange reserves resumed their upward trend—rising by an additional IL.40 million as a result of loans obtained by the Government abroad.

5. CREDIT TO THE GOVERNMENT

The average net indebtedness of the Government to the banking system rose by IL.60.8 million during 1958, the rate of increase being slower than in 1957, when the average level of credit granted to the Government by the banking system rose by IL.79 million. (The breakdown is given in Table XIII-7). The 1958 increase was spread over the whole year, except for the month of December, when the Government reduced its debts by IL.34 million by redeeming some of its foreign currency liabilities. Consequently, the increase in the Government debt between the end of 1957 and the end of 1958 (IL.39.2 million) was smaller than the difference between its average indebtedness in 1957 and 1958 (IL.60.8 millions).

Of the aforementioned IL.39.2 million increase, the Government's larger debt to the Bank of Israel represented IL. 17.7 million, while its commitments to the banking institutions rose by IL.21.5 million.

The balance of current loans obtained by the Government from the Bank of Israel increased by IL.25.6 million during the year. However, the Government repaid IL.2.2 million on account of the Security Advance, while its net indebtedness to the Bank of Israel was further reduced by IL.4.8 million through the increase in the Bank's capital, which is deducted when calculating the net amount of credit granted. The portfolio of Government bonds held by the Bank declined by IL.0.8 million.

In addition to receiving loans from the Bank of Israel, the Government obtained considerable credit from the banking institutions against loans from abroad. In certain cases, the Treasury took such loans for the purpose of converting them into local currency. These transactions were executed through local banks in two stages, the Israel banks first receiving foreign loans, and later granting credits against them to the Treasury. The amounts concerned must, therefore, be treated as loans to the Treasury from the banking institutions. They increased by IL.17.3 million during 1958.

The portfolio of Government securities held by the banking system rose in the year under review by IL.9.8 million, chiefly because banks are now required to invest in Government or Government-guaranteed securities 60 per cent of the amounts deposited under approved saving schemes. On the other hand, the

IL5.6 million increase in the Government's deposits with the banking institutions reduced the net volume of credit received by it.

TABLE XIII-7
Government Indebtedness to the Banking System, 1953-1958
(millions of IL.)

(End of period)

Period	Bank of Israel				Banking institutions				Total
	current credit (net)	long-term credit & securities	less: capital accounts	total	current credit (net)	long-term credit & securities	less: deposits (net)	total Government indebtedness	
1953 ^a	—	133.5 ^b	—	133.5 ^b	12.0	33.8	7.9	37.9	171.4
1954	10.4	122.6	-0.5	133.5	9.5	25.4	15.6	19.3	152.8
1955	32.5	138.5	-0.1	171.1	17.1	22.6	10.9	28.8	199.9
1956	89.3	155.7	8.3	236.7	12.5	32.4	18.4	26.5	263.2
1957	68.6	217.8	15.1	271.3	28.5	32.7	15.5	45.7	317.0
1958	94.2	214.8	19.9	289.0	45.8	42.5	21.1	67.2	356.2
1958 January	72.0	217.8	17.0	272.7	26.8	32.0	16.4	42.4	315.1
February	69.1	218.4	16.7	270.8	35.7	32.1	15.3	52.5	323.3
March	77.9	218.3	16.6	279.6	36.1	32.6	14.8	53.9	333.5
April	74.8	218.2	15.3	277.7	32.7	33.0	15.1	50.6	328.3
May	78.0	217.4	17.3	278.2	41.3	34.8	14.4	61.7	339.9
June	87.9	216.8	15.3	289.4	40.9	40.0	14.7	66.2	355.6
July	87.6	216.8	15.2	289.2	38.1	40.5	16.8	61.8	351.0
August	103.9	216.8	16.9	303.8	41.4	40.4	15.2	66.7	370.5
September	117.9	214.7	16.8	315.8	39.9	42.1	17.5	64.5	380.3
October	128.4	214.7	20.0	323.1	40.6	40.3	16.1	64.8	387.9
November	124.9	214.6	23.1	316.5	50.3	40.4	16.9	73.8	390.3
December	94.2	214.8	19.9	289.0	45.8	42.5	21.1	67.2	356.2

^a See note ^a to Table XIII-1.

^b Treasury bills and land bills held with the Issue Department of the Bank Leumi le-Israel B.M.

General Note:

1. Re obligations to the Bank of Israel:

Current credit (net)=(advances to the Government in local and foreign currency+deposits with banking institutions earmarked for loans to the Government)—(Government deposits in local and foreign currency+deposits of Government institutions+deposits of international financial institutions+deposits of other institutions).

Long-term credit and securities=treasury bills+land bills+Government bonds and promissory notes held as cover for currency in circulation.

Capital accounts=(paid up capital+reserve fund+other liability accounts)—(Government promissory notes for the redemption of the Bank's capital+other assets accounts).

2. Re obligations to banking institutions:

Current credit (net)=(loans to the Government—loans to the Government from deposits of the Bank of Israel+advances to purchasers of Government bonds)—(Government demand deposits+Government deposits representing the proceeds of bond sales).

Long-term credit and securities=the 3% Government Loan+other Government bonds.

Deposits (net)=(Government time deposits+deposits earmarked for special purposes+Government deposits earmarked for loans within the framework of the Development Budget)—loans from Government deposits.

Some Government obligations to the banking system appear in the Government's credit and debit account, while others constitute budgetary items. On deducting from the Government's debt the items appearing on the revenue side of the budget—i.e., securities held by the banking system and the capital account of the Bank of Israel—we obtain a figure reflecting current bank credit, which does not appear in the budget, but in the credit and debit account. In 1958, this totalled IL.37.3 million¹.

The expansion of credit to the Government accounted for 62 per cent of the increase in the money supply during 1957, but for only 43 per cent during 1958.

6. CREDIT TO THE PUBLIC

(a) *Bank credit and the liquidity of banking institutions*

The average level of bank credit extended to the public in local and foreign currency was IL.59 million—or 18 per cent—higher in 1958 than in 1957. The rate of expansion was thus somewhat faster than between 1956 and 1957, when it averaged 15.7 per cent.

The expansion was accelerated during the second half of 1958: In the January-April period, bank credit granted to the public increased by only IL.5.9 million, or IL. 1.5 million per month, but the expansion between May and December totalled IL.59.3 million—a rate of more than IL.7 million per month—due to the higher seasonal demand for credit from the agricultural sector.

The net increment of bank credit extended to the public between the end of 1957 and the end of 1958 was IL.65.2 million: Whereas the value of bills rediscounted by the Bank of Israel declined by IL.24 million, additional credit granted to the public by the banking institutions totalled IL.89.2 million.

The credit expansion was largely effected through loans to agriculture and industry approved by the Bank of Israel, which helped to finance the considerably increased output of these sectors, especially as regards commodities intended for export and for the replacement of imports. The technical aspects of this credit expansion are described below.

New liquidity regulations came into force at the beginning of 1958², prescribing a minimum liquidity rate of 58 per cent on local currency demand deposits and time deposits for periods not exceeding 18 months.³ Liquid assets are defined to comprise cash, balances held with the Bank of Israel, net balances held with other banks and Treasury bills.

The regulations authorize the Governor of the Bank of Israel to permit banking institutions to deduct loans approved for this purpose by the Bank of Israel

¹ A full discussion of the financial activities of the Government is given in Chapter XV—"The Financial Activities of the Public Sector".

² For a description of these regulations, see Annual Report for 1957.

³ Excluding deposits within the framework of saving schemes, which will be discussed later.

from the amount of liquid assets they are legally required to hold, up to a limit of 20 per cent of the value of deposits against which such assets must be held.

When this concession is fully exploited, the effective liquidity rate required of banking institutions falls to 38 per cent.

TABLE XIII-8

Credit granted to the Public through the Banking System, 1953-1958

(millions of IL.)

(End of period)

Period	From the resources of the Bank of Israel	From the resources of banking institutions	Total bank credit (1)+(2)	Against govern- ment deposits	From govern- ment deposits earmarked for loans	Total credit to the public (3)+(4) +(5)
	(1)	(2)	(3)	(4)	(5)	(6)
1953 ^a	—	204.5	204.5	7.0	47.7	259.2
1954	—	231.4	231.4	22.8	69.3	323.5
1955	15.7	240.1	255.8	38.6	104.3	398.7
1956	35.1	264.1	299.2	46.8	134.1	480.1
1957	51.6	306.4	358.0	60.1	160.6	578.7
1958	27.6	395.6	423.2	64.8	199.2	687.2
1958 January	43.3	321.3	364.6	63.4	157.2	585.2
February	34.2	323.7	357.9	64.8	164.9	587.6
March	33.7	333.1	366.8	75.8	169.6	612.2
April	27.2	336.7	363.9	76.6	170.8	611.3
May	21.7	343.7	365.4	72.2	176.3	613.9
June	21.6	351.8	373.4	70.3	178.8	622.5
July	22.3	360.8	383.1	70.8	180.4	634.3
August	21.6	369.0	390.6	67.8	182.4	640.8
September	22.6	380.8	403.4	63.9	186.9	654.2
October	20.9	380.3	401.2	62.2	187.4	650.8
November	22.2	386.6	408.8	60.5	192.1	661.4
December	27.6	395.6	423.2	64.8	199.2	687.2

^a See note ^a to Table XIII-1.

Banking institutions are still subject to credit restrictions, fixing the volume of credit they may grant at its 1953 level, with the addition of some increases authorized between 1954 and 1957. However, when the liquidity ratio of a bank exceeds the legal requirement, the Bank of Israel permits credit to be expanded beyond this limit.

The Bank likewise exempts from the liquidity and volume regulations loans granted for high priority economic purposes and particularly for the production of import substitutes and exports. But these exemptions raise the average liquidity ratio of the banking institutions, including liquidity exemptions, above the 58

per cent level, thus enabling a further expansion of credit within the regular framework of the liquidity regulations.

The regular liquidity provisions do not cover deposits accumulated under approved saving schemes. Such deposits are subject to special arrangements, the banking institutions being required to invest 60 per cent of them in securities approved for this purpose by the Ministry of Finance and the Bank of Israel, or to deposit them with the Bank of Israel (such deposits being excluded from the definition of liquid assets). The remaining 40 per cent may be used to expand credit—25 per cent for purposes approved by the Ministry of Finance and the Bank of Israel, and 15 per cent at the banks' discretion.

In 1958, virtually all banks attained their legally fixed credit level and a large proportion of the credit expansion was effected through the exemptions approved by the Bank of Israel. Of the IL.380 million worth of new credits granted by the banks during 1958, no less than IL.105 million were authorized by exemptions from the liquidity or volume regulations, or both.

The liquidity laws enable banking institutions to expand credit in proportion to the amount of their liquid assets up to a liquidity ratio of 38 per cent providing they conform to the qualitative credit policy. The value of liquid assets held by the banking system rose in 1958 by approximately IL.25 million; a further IL.26 million worth of credit were granted according to exemptions from the liquidity rules. The depositing of IL.26 million within the framework of saving schemes enabled the banks to extend yet another IL.11 million.

During the first two months of the year, the Bank of Israel restricted re-discounts by not renewing bills already redeemed and selling bills not yet due for payment to the banking institutions. This was done in order to reduce the excessive liquidity of the banking institutions. The outstanding balance of Bank of Israel re-discounts declined from IL.51.6 million at the end of 1957 to a minimum of IL.21.6 million in May and June 1958, remained virtually unchanged until November and rose by IL.5 million in December. The decline affected only bills re-discounted in local currency. The balance of bills re-discounted in foreign currency—financing imports for exports, or documentary credits to customers for Israel goods abroad—showed no significant changes.

The liquid assets held by the banking institutions were increased chiefly by the accumulation of foreign exchange reserves in the Bank of Israel—which rose by IL.79.3 million over the year. On the other hand, credit granted to the Government by the Bank of Israel and the rediscounting of bills for the public contracted by IL.6.3 million, thus reducing the volume of the banking institutions' liquid assets by an equivalent amount. The activities of the Bank of Israel were, therefore, responsible for a IL.73 million increase in the volume of liquid assets held by the banking institutions, which—however—was reduced by the additional IL.20.5 million of cash taken out by the public. As a result of all these factors, the sum total of cash held by the banking institutions and their deposits with the Bank of Israel rose by IL.52.5 million, of which IL.36.0 million

TABLE XIII-9
Liquid Assets Held by Banking Institutions, 1955-1958
 (millions of IL.)

Period	Credits by the Bank of Israel		Net balances of foreign exchange in the Bank of Israel	Net balances with banking institutions	Total (1)+(2)+ (3)+(4)	Less			Liquid assets (5)-(8)
	to the public	to the Government				cash held by the public	deposits of banking institutions with the Bank of Israel not subject to liquidity regulations ^a	total (6)+(7)	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	
1955	15.7	171.1	83.5	26.1	296.4	172.5	5.1	177.6	118.8
1956	35.1	236.7	92.4	17.9	382.1	228.3	17.9	246.2	135.9
1957	51.6	271.3	82.8	19.3	425.0	230.9	32.8	263.7	161.3
1958	27.6	289.0	162.1	8.2	486.9	251.4	49.3	300.7	186.2
1958 January	43.3	272.2	93.8	16.0	425.8	236.8	34.7	271.5	154.2
February	34.2	270.8	107.5	18.6	431.1	239.8	32.9	272.7	158.4
March	33.7	279.6	124.1	18.4	455.8	245.1	40.9	286.0	169.8
April	27.2	277.7	157.9	16.7	479.5	245.3	43.1	288.4	191.1
May	21.7	278.2	173.2	14.3	487.4	246.0	44.6	290.6	196.7
June	21.6	289.4	167.0	16.0	494.0	248.4	42.2	290.6	203.4
July	22.3	289.2	157.9	15.0	484.4	254.4	42.0	296.4	188.0
August	21.6	303.8	145.8	16.2	487.4	254.8	42.1	296.9	190.5
September	22.6	315.8	127.5	17.7	483.6	259.9	42.8	302.7	181.0
October	20.9	323.1	126.0	15.1	485.1	256.5	42.3	298.8	186.2
November	22.2	316.5	131.7	15.5	485.9	259.6	43.6	303.2	182.7
December	27.6	289.0	162.1	8.2	486.9	251.4	49.3	300.7	186.2

* Deposits under saving schemes and in connection with documentary credits and foreign exchange deposits.

were in the form of liquid assets. Other deposits with the Bank of Israel, totalling IL.16.5million, represent the increase in the obligatory holdings of banking institutions in the Bank of Israel in connection with saving schemes and documentary credits, and are not considered liquid. Net balances with other banks declined by IL.11.1 million during the year. The volume of liquid assets held by the banking institutions expanded by IL.24.9 million.

Of the total increase in liquid assets, IL.35.2 million were liquid balances at the Bank of Israel. The latter may be broken down into obligatory deposits which the banking institutions are required to hold, to the extent of 15 per cent of their local currency deposits subject to the liquidity regulations (IL.13.2 million), and balances in excess of these amounts (IL.22 million).

The liquidity ratio of the banking institutions, which had been 40.9 per cent at the end of 1957, rose during the first half of 1958 due to the considerable increase in foreign exchange reserves and the relatively limited expansion of

TABLE XIII-10

The Liquidity of the Banking Institutions, in Local Currency, 1955-1958
(millions of IL.)

(End of period)

Period	Liquid balances with the Bank of Israel			Cash held by bank- ing insti- tutions	Net balances with bank- ing insti- tutions	Total liquid assets (3) + (4) + (5)	Deposits subject to liquidity regula- tions	Effective liquidity ratio $\frac{(6)}{(7)} \times 100$
	obliga- tory depo- sits ^a	excess depo- sits	total (1) + (2)					
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1955	43.1	38.6	81.7	11.1	26.1	118.9	300.2	39.6
1956	47.1	59.4	106.5	11.6	17.9	136.0	332.3	40.9
1957	57.8	72.3	130.1	11.9	19.3	161.3	394.2	40.9
1958	71.0	94.3	165.3	12.7	8.2	186.2	479.0	38.9
1958 January	57.8	68.7	126.5	11.7	16.0	154.2	399.2	38.6
February	59.1	68.8	127.9	11.9	18.6	158.4	408.0	38.8
March	59.9	78.5	138.4	13.0	18.4	169.8	415.9	40.8
April	61.2	100.5	161.7	12.7	16.7	191.1	445.1	42.9
May	62.4	107.6	170.0	12.4	14.3	196.7	450.2	43.7
June	66.8	108.1	174.9	12.5	16.0	203.4	460.6	44.2
July	67.5	92.4	159.9	13.1	15.0	188.0	461.0	40.8
August	69.1	92.1	161.2	13.1	16.2	190.5	471.7	40.4
September	69.2	79.4	148.6	14.7	17.7	181.0	474.7	38.1
October	70.8	87.2	158.0	13.1	15.1	186.2	473.5	39.3
November	71.2	82.2	153.4	13.8	15.5	182.7	474.2	38.5
December	71.0	94.3	165.3	12.7	8.2	186.2	479.0	38.9

^a Obligatory balances of banking institutions with the Bank of Israel, equalling 15 per cent of the value of their deposits subject to the liquidity regulations two months before the specified period.

credit—reaching a maximum of 44.2 per cent in June. Thereafter, foreign currency reserves declined, while the credit expansion proceeded at an accelerated pace, and by the end of December 1958 the liquidity ratio had fallen to 38.9 per cent (see Table XIII-10).

(b) Credit to the public from Government deposits

The volume of short-term credit granted against Government deposits to persons owing taxes and to importers within the framework of the German Reparations and the U.S. Grant-in-aid expanded by IL.4.7 million during 1958, as compared with an increase of IL.13.3 million during 1957. Between January and April 1958, credits to importers considerably expanded, but from May onwards a decline ensued. Balances of credit granted for payment of income tax and customs duty fluctuated only mildly.

Credit granted by banking institutions from the Government's Development Budget deposits was expanded by IL.38.6 million in 1958, as against IL.26.5 million in 1957. These two types of credit are in fact granted to the public by the Government, but the banking institutions accept the risks involved and collect the principal and interest. As such credit is fully covered by non-liquid Government deposits, these deposits and loans do not directly affect either the money supply or the liquidity of the banking institutions.

(c) Destination of credit

The excessive demand for credit necessitates recourse to a policy of qualitative control, which enables the channelling of the limited credit funds available to purposes constituting economic priorities. The major considerations underlying the allocation of credit are the promotion of exports and the production of substitutes for imports, as well as the creation of productive employment in development areas.

The Bank of Israel and the Ministry of Agriculture have evolved criteria for the granting of credit to agriculture, which are based on the working capital requirements of high priority crops. The Bank of Israel grants exemptions from the liquidity and credit volume restrictions to the banking institutions according to the crop areas approved by the Ministry of Agriculture. In addition, the Bank approves loans to agricultural branches not covered by general agreements of this kind in accordance with the general considerations underlying credit expansion.

Industrial enterprises submit requests for loans directly to the banking institutions. Some funds are allocated to industry on the basis of general considerations, while other loans are granted for specific purposes by the Bank of Israel or from funds administered jointly by the banking institutions and the Government.

Within the framework of the qualitative credit controls, arrangements have

been made for the financing of export orders. This is done through an export fund, in which the Government and the banking institutions participate to the extent of 50 per cent each. Loans from this fund, which totalled IL. 21.4 million at the end of 1958, are approved by the Ministry of Commerce

TABLE XIII-11
Bank Credit, by Source and Destination, 1958*

Destination	Bank credit			Total (1) + (2) + (3)	Credit against Govern- ment deposits	Total bank credit (4) + (5)
	controlled by the Bank of Israel		uncon- trolled			
	from the resources of the Bank of Israel	from the resources of the banking institu- tions	from the resources of the banking institu- tions			
	(1)	(2)	(3)	(4)	(5)	(6)
<i>millions of IL.</i>						
Agriculture	4.5	60.9	43.7	109.1	6.4	115.5
Industry	5.7	17.4	75.7	98.8	31.7	130.5
Building	—	5.3	18.9	24.2	4.0	28.2
Commerce	0.2	1.9	44.5	46.6	7.4	54.0
Public utilities	14.2	4.5	1.9	20.6	0.8	21.4
Local authorities	—	1.9	4.8	6.7	0.3	7.0
Credit and financing institutions	—	—	7.3	7.3	0.2	7.5
National institutions	2.8	11.2	0.8	14.8	—	14.8
Services	0.2	2.2	16.8	19.2	6.7	25.9
Miscellaneous	—	0.3	60.6	60.9	7.2	68.1
<i>Total</i>	27.6	105.6	275.0	408.2	64.7	472.9
<i>percentages</i>						
Agriculture	16.3	57.6	15.9	26.8	9.9	24.4
Industry	20.6	16.5	27.6	24.3	49.0	27.6
Building	—	5.0	6.9	5.9	6.2	6.0
Commerce	0.7	1.8	16.2	11.4	11.4	11.4
Public utilities	51.5	4.3	0.7	5.0	1.2	4.5
Local authorities	—	1.8	1.7	1.6	0.5	1.5
Credit and financing institutions	—	—	2.6	1.8	0.3	1.6
National institutions	10.2	10.6	0.3	3.6	—	3.1
Services	0.7	2.1	6.1	4.7	10.4	5.5
Miscellaneous	—	0.3	22.0	14.9	11.1	14.4
<i>Total</i>	100.0	100.0	100.0	100.0	100.0	100.0

* Excluding the Israel Bank of Agriculture.

and Industry to finance the production of goods already ordered abroad. The balance of loans granted from this fund rose from IL.5.8 million at the end of 1957 to IL.16 million at the end of 1958.

The Bank of Israel finances imports for exports and the bills of its clients abroad by means of re-discounts in foreign currency. The outstanding balance of bills re-discounted in foreign currency by the Bank declined from IL.8.8 million at the end of 1957 to IL.5.7 million at the end of 1958. The value of other bills discounted in foreign currency fell during the same period from IL.12.7 million to IL.12.2 million. The Bank of Israel and the export fund thus supply a considerable portion of the credit required to meet export orders.

TABLE XIII-12
Bank Credit, by Source and Destination, 1954-1958*

<i>Destination</i>	<i>1954</i>	<i>1955</i>	<i>1956</i>	<i>1957</i>	<i>1958</i>
<i>millions of IL.</i>					
Agriculture	54.2	68.8	85.3	102.3	115.5
Industry	57.3	77.2	92.8	107.9	130.5
Building	31.8	19.8	21.4	27.4	28.2
Commerce	37.0	37.5	36.7	44.0	54.0
Public utilities	8.2	4.4	13.3	27.3	21.4
Local authorities	4.4	3.3	4.5	6.0	7.0
Credit and financing institutions	6.9	5.6	10.5	9.3	7.5
National institutions	3.5	3.0	3.1	11.0	14.8
Services	10.4	13.7	16.1	17.1	25.9
Miscellaneous	30.0	44.9	44.9	52.9	68.1
<i>Total</i>	243.7	278.2	328.6	405.2	472.9
<i>percentages</i>					
Agriculture	22.2	24.7	26.0	25.2	24.4
Industry	23.5	27.7	28.2	26.6	27.6
Building	13.0	7.1	6.5	6.8	6.0
Commerce	15.2	13.5	11.2	10.9	11.4
Public utilities	3.4	1.6	4.0	6.7	4.5
Local authorities	1.8	1.2	1.4	1.5	1.5
Credit and financing institutions	2.8	2.0	3.2	2.3	1.6
National institutions	1.4	1.1	0.9	2.7	3.1
Services	4.3	4.9	4.9	4.2	5.5
Miscellaneous	12.4	16.2	13.7	13.1	14.4
<i>Total</i>	100.0	100.0	100.0	100.0	100.0

* Excluding the Israel Bank of Agriculture.

The Ministry of Commerce and Industry further disposes of a turnover capital fund¹, totalling IL.27.8 million, in which the Government participates to the extent of two-thirds and the banking institutions participate to the extent of one third. The policy of the Ministry of Commerce and Industry is to approve loans from this fund for the financing of one month's output. The outstanding balance of such loans reached IL. 19.5 million at the end of 1958, as against IL. 17.5 million at the end of 1957.

All requests for loans beyond the credit ceiling fixed for a certain banking institution, for exemptions from the liquidity requirements and for re-discounts must be submitted to the Bank of Israel. The latter gives or withholds its approval according to the economic priority of the purpose for which the credit is requested. In case of approval it is usually stipulated that the loans be granted by the banking institution itself if its liquidity situation permits this. By and large, the Bank of Israel re-discounts bills in local currency only when the banking institution with which the prospective borrower is connected has already used up its credit funds within the framework of the liquidity regulations and no other bank is able or willing to grant the loan, or when the amount required exceeds any that a commercial bank can grant from its own resources.

Table XIII-11 shows that the distribution of credit under Bank of Israel control among the various sectors of the economy differs considerably from that of unsupervised credit. Of the latter, the banking institutions granted 27.6 per cent to industry and only 15.9 per cent to agriculture, while commerce received a comparatively large share—16.2 per cent—and 22 per cent were given to miscellaneous branches. On the other hand, about three-quarters of the total amount of credit extended by the banking institutions under Bank of Israel control, exercised through liquidity and credit exemptions, went to industry and agriculture, while other sectors obtained smaller allocations. More than half the re-discounts were granted to public services—and especially to big Government corporations, such as the Reparations Corporation, "Mekoroth", the Palestine Electric Corporation and "El-Al". Most of the balance was channelled to agriculture and industry.

Since the proportion of controlled credit within total bank credit has been increasing, the distribution of the latter between the economic sectors underwent some changes between 1954 and 1958, the share of agriculture rising from 22.2 to 24.4 per cent and that of industry from 23.5 to 27.6 per cent (See Table XIII-12.)

The development of banking institutions

In 1958, the trend towards expansion characterizing Israel banking continued, 31 new branches of banking institutions being opened, of which 26 by the 3 largest banks (Bank Leumi le-Israel B.M., the Israel Discount Bank Ltd., and the Work-

¹ Now also incorporating the Employment Fund.

ers' Bank Ltd.) and 5 by other banks. However, the number of credit co-operatives decreased by 7 (8 offices), 4 being amalgamated with existing banks, while 2 ceased their banking activities, concentrating on other financial operations. One society was liquidated. The net increase in the number of offices during 1958 was thus 23, as against 21 in 1957. Of the 418 branch offices in existence at the end of 1958, 222—or 53 per cent—belonged to the three big banks.

TABLE XIII-13

Banking Institutions and their Branches, 1955-1958

(End of period)

	1955	1956	1957	1958
The 3 big banks				
Main offices	3	3	3	3
Branches	104	114	193	219
<i>Total</i>	107	117	196	222
Other banks				
Main offices	22	24	24	24
Branches	52	61	67	72
<i>Total</i>	74	85	91	96
Credit co-operative societies				
Main offices	94	93	59	52
Branches	74	79	49	48
<i>Total</i>	168	172	108	100
All banking institutions				
Main offices	119	120	86	79
Branches	230	254	309	339
<i>Total</i>	349	374	395	418

Table XIII-14 shows the respective shares of the three largest banks, the other banks and the credit cooperatives within selected balance sheet items. It should be noted that in the period 1955 to 1958 no change occurred in the larger banks' share of any important balance sheet items. At the end of 1958, the percentage of cash and deposits controlled by these 3 banks, as well as their share of balances with the Bank of Israel, exceeded the proportion of total credit granted by them. The same situation prevailed at the end of 1957.

TABLE XIII-14
*Cash and Balances with the Bank of Israel, Credit and Deposits,
 by Type of Banking Institution, 1955-1958*
 (percentages)

	<i>The 3 big banks and their affiliates</i>	<i>Other banks</i>	<i>Credit co-opera- tives</i>	<i>Total</i>
Cash and balances with the				
Banks of Israel				
1955	56	27	17	100
1956	65	22	13	100
1957	67	24	9	100
1958	66	25	9	100
Loans to the public from the resources of the banking institutions				
1955	51	26	23	100
1956	51	27	22	100
1957	60	23	17	100
1958	60	25	15	100
Demand deposits				
1955	54	25	21	100
1956	55	24	21	100
1957	61	24	15	100
1958	62	24	14	100
Other deposits				
1955	52	25	23	100
1956	61	18	21	100
1957	66	21	13	100
1958	68	21	11	100

The structure of the assets and liabilities of the banking institutions

The total value of the assets and liabilities of the banking institutions rose during 1958 by IL.225 million—i.e., by 20 per cent. In comparison with the preceding year, the most striking development was that there was no change in contingent liabilities, while other assets and liabilities increased by over 25 per cent.

As a result of improved clearing arrangements¹, and particularly the acceleration of clearing on the last day of the year, balances held with other banking institutions declined by IL.15 million in 1958, while balances held for other banking institutions fell by IL.4 million. In consequence, the contingent item

¹ See Chapter XVIII—"The Activities of the Bank of Israel".

TABLE XIII-15

*Assets and Liabilities of the Banking Institutions, 1957-1958**(millions of IL.)*

<i>Assets and liabilities</i>	<i>Millions of IL.</i>		<i>Percentages</i>		<i>Increase or decrease (-) from 1957 to 1958</i>	
	<i>1957</i>	<i>1958</i>	<i>1957</i>	<i>1958</i>	<i>millions of IL.</i>	<i>percent-ages</i>
<i>Assets</i>						
Cash and balances with the Bank of Israel	174.8	227.5	20.1	20.8	52.7	30.1
Loans to the public	306.4	395.6	35.2	36.2	89.2	29.1
Loans to the Government	29.7	46.9	3.4	4.3	17.2	57.9
Loans to the public from Government deposits	220.7	264.0	25.4	24.1	43.3	19.6
Foreign exchange	54.6	64.5	6.3	5.9	9.9	18.1
Securities	50.0	70.0	5.8	6.4	20.0	40.0
Immovable assets	13.8	17.1	1.6	1.6	3.3	23.9
Net balances with banking institutions	19.3	8.2	2.2	0.7	-11.1	-57.5
<i>Total</i>	869.3	1,093.8	100.0	100.0	224.5	25.8
<i>Liabilities</i>						
Demand deposits	345.3	408.5	39.7	37.3	63.2	18.3
Other liquid deposits*	36.3	64.5	4.2	5.9	28.2	77.7
Non-liquid deposits	155.4	215.5	17.9	19.7	60.1	38.7
Foreign exchange commitments	34.9	47.2	4.0	4.3	12.3	35.2
Government deposits	237.3	286.1	27.3	26.2	48.8	20.6
Capital	39.9	47.8	4.6	4.4	7.9	19.8
Other accounts (net)	20.2	24.2	2.3	2.2	4.0	19.8
<i>Total</i>	869.3	1,093.8	100.0	100.0	224.5	25.8
<i>Contingent liabilities and guarantees</i>						
Balances held by and for banking institutions	29.9	25.9			- 4.0	-13.4
Clients' guarantees	195.1	195.0			- 0.1	—
Other accounts	62.1	67.2			5.1	8.2
<i>Total</i>	287.1	288.1			1.0	0.3
<i>Grand total</i>	1,156.4	1,381.9			225.5	19.5

* Deposits within the framework of saving schemes and time deposits for periods not exceeding 3 months.

“Balances held by and for banking institutions” contracted by IL.4 million, and the item “Net balances of banking institutions”, which represents balances in transit, declined by IL.11 million.

There was a relatively big increase in loans to the Government and investments in securities,—chiefly Government bonds or Government-guaranteed debentures, as banking institutions must invest in such securities 60 per cent of the deposits accumulated within the framework of approved saving schemes and a certain portion of the deposits of provident funds¹.

The largest increase on the liabilities side took place in liquid deposits other than demand deposits,—i.e., deposits under saving schemes, which received particular encouragement during the year, and time deposits for periods not exceeding 3 months. Time deposits for longer periods were likewise expanded, while the increase in demand deposits was relatively limited.

The foreign commitments of the banking institutions increased to a greater extent than the foreign currency deposits and foreign securities held by them, mainly owing to the fact that the banks incurred debts abroad in order to grant loans to the Government. Their foreign exchange position consequently deteriorated. On the other hand, the increase in cash and balances held with the Bank of Israel somewhat exceeded the overall increase in deposits, the ratio between these two items being somewhat improved.

The profitability of banking institutions

The profits of the banking institutions (before deduction of income tax and company profits tax) rose from IL.4 million in 1957 to IL.5.4 million in 1958. The ratio between profit and own capital rose from 14 to 17.2 per cent. This improvement, however, was wholly confined to banks, the profits of credit co-operative societies remaining unaffected. The profits of banks rose from IL.3.2 million to IL.4.6 million and the ratio of profit to own capital from 15.6 to 20.1 per cent. The ratio between profits and the total income of all banking institutions increased from 6.4 per cent in 1957 to 7 per cent in 1958. In the case of banks only, the rise was from 6 to 6.9 per cent.

During the year, the average annual rate of interest on loans extended by the banking institutions declined from 8.6 per cent to 8.4 per cent, while the rate of interest allowed on deposits rose from 2.4 to 2.8 per cent. The smaller differential between these two rates reduced the profit of banking institutions on each pound lent, but the expansion of the volume of credit compensated for this and their total profits rose² (see Table XIII-16).

¹ See Chapter XVI—“Personal Saving”.

² A detailed analysis of the profits of banking institutions will be published shortly in one of Bulletins of the Bank of Israel.

TABLE XIII-16
Income and Expenditure of Banking Institutions, 1957-1958
 (thousands of IL.)

<i>Item</i>	<i>Thousands of IL.</i>		<i>Percentages</i>		<i>Increase from 1957 to 1958</i>	
	<i>1957</i>	<i>1958</i>	<i>1957</i>	<i>1958</i>	<i>millions of IL.</i>	<i>percent-ages</i>
<i>Income</i>						
Interest and commission on loans and bills discounted	41,555	50,606	66.7	65.6	9,051	21.8
Commissions for services rendered	12,842	15,168	20.6	19.7	2,326	18.1
Other income	7,885	11,336	12.7	14.7	3,451	43.8
<i>Total income</i>	62,282	77,110	100.0	100.0	14,828	23.8
<i>Expenditure</i>						
Wages, salaries and social benefits	28,513	32,876	45.8	42.6	4,363	15.3
Interest on deposits	16,043	22,689	25.8	29.4	6,646	41.4
Other expenditure	13,738	16,143	22.0	21.0	2,425	17.5
<i>Total expenditure</i>	58,294	71,708	93.6	93.0	13,414	23.0
<i>Profits^a</i>	3,988	5,402	6.4	7.0	1,414	35.5
<i>Paid-up Capital</i>	28,516	31,401			2,885	10.1
<i>Profit as percentage of capital</i>	14.0	17.2				

^a Before deduction of income tax and company profits tax.