

CHAPTER XX

THE SECURITIES MARKET

1. GENERAL TRENDS

NET LOCAL INVESTMENT in new securities increased in 1962 by IL 46 million over the previous year and totalled IL 224 million.¹ This was equivalent to 14 per cent of the total gross capital formation in the economy—the same rate as in 1961 but 8 per cent more than in 1960.

The currency devaluation strongly affected security prices and the structure of the market as a whole. It increased the par value of dollar-linked loans by two-thirds, or approximately IL 230 million. The new issue of dollar-linked bonds was discontinued, and the balance of dollar-linked loans began to diminish because of the gradual repayment of existing loans. It took some time until the market fully acknowledged the new situation. Immediately after the devaluation, dollar-linked bonds were traded at about one third above pre-devaluation prices, but later on and until the end of the year, their prices advanced steadily.

Index-linked loans continued to be issued as before, but for private (as distinct from institutional) investors they were less attractive than dollar-linked bonds had been prior to the devaluation. The new issue of all types of linked bonds slowed down, therefore, particularly in the second half of the year. The net issue amount hardly increased at all in 1962 and totalled IL 119 million.

This contrasts with a sevenfold increase in the net issue of non-linked short-term loans, the balance of which rose in 1962 from IL 30 million to IL 100 million. Contrary to past experience, a large portion of the increment was taken up by private investors in 1962. It seems that in many portfolios this security

¹ Total of new domestic issues, less capital repayments; does not include: (a) securities issued without prospectus (bonus shares, shares created through conversion of bonds, etc.); (b) unquoted securities (private issues etc.); and (c) securities earmarked for foreign investors. The sum presented here is therefore the net amount of new capital raised during the year in cash from the local public against market securities. Most of these are quoted on the Stock Exchange, but also included are a number of bond issues floated by financial institutions and traded outside the Stock Exchange.

This year, for the first time, the net annual issue of Government short-term loans is also included, because of its relative importance in 1962, both in comparison with the total of Government issues and with the total of new issues during the year. The figures for 1961 were adjusted accordingly. It should be borne in mind, however, that this loan differs significantly from other securities dealt with here: this is a short-term paper, while the others are instruments of long-term capital movements.

Table XX-1
THE SECURITIES MARKET, 1960-62
(Indicators)

	1960	1961	1962 End of February	1962
Net domestic issues				
Proceeds ^a (IL million)	61	177 ^b		224
Percentage of gross capital formation	6	14		14
Number of issuing bodies	25	27		24
Securities listed on Tel Aviv Stock Exchange (end of year; IL million)				
Par value	444	627		897
Market value	493	710		1,052
Indices of security prices (end of year; average 1960=100)				
Dollar-linked loans	100.5	107.6	141.0	162.6
Index-linked bonds	103.8	113.3	119.7	128.7
Ordinary shares	128.9	112.3	127.8	145.3

^a See note 1, page 436.

^b Revised figure.

became a substitute for value-linked bonds, and possibly also for commercial paper. Business firms, too, for the first time maintained positions of the Short-Term Loan, a symptom of the increased liquidity prevailing after the devaluation and a by-product of the diminishing interest rates on non-bank credit.

The impact of the devaluation was strongly felt in the share market as well. High liquidity and a shift in the composition of assets of many investors after the devaluation created a bullish demand for shares. This was underpinned by the belief that after the devaluation equity prices must rise to reflect the increased value, in terms of Israel pounds, of company assets; profits were also expected to improve, in line with prices and incomes. Whether these calculations were right or wrong, the fact remains that the slackness in the share market, which had been felt since April 1961, ended with the devaluation. The boom was furthered by foreign purchases, which had been postponed until the devaluation reduced the cost of Israel securities in terms of foreign currency.

But the one-time boost in February was followed by a lull on the share market and even a decline in equity prices, which—though much less severe—coincided with the slump on foreign stock markets. In previous years the Tel Aviv Stock Exchange usually failed to react to fluctuations in foreign markets, but this time events abroad had a cautioning influence here, because it was felt that they might be detrimental to foreign investment in Israel securities, the anticipation of which had been among the factors stimulating the boom. From August until

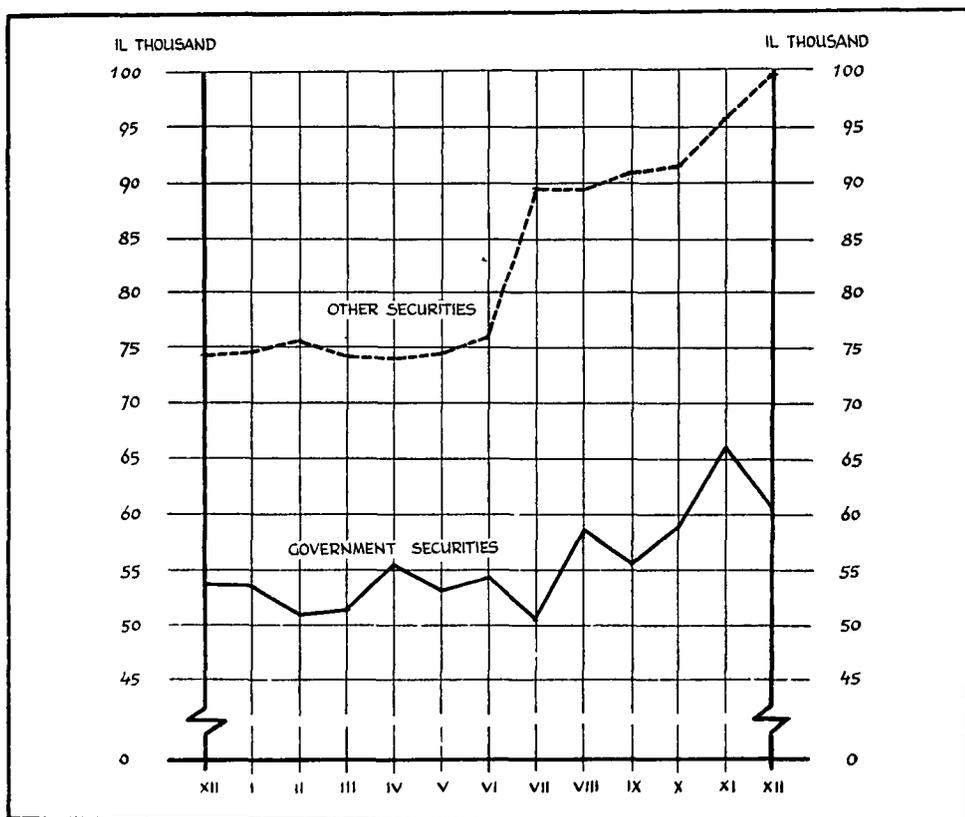
the end of the year, share prices advanced again, on increasing volumes. New issues were successfully floated, but in 1962 totalled a mere IL 34 million, as against IL 50 million in 1961.

Considering the rise of incomes and the fact that a fairly large portion of the new portfolio investments were institutional, the performance of the new issue market as a whole was, in actual fact, relatively modest. Devaluation gains apart, the total resources of savings institutions and their investment portfolios increased more or less in step with the incomes of their clientele. Private investment, in the narrow sense of the word, would therefore seem to have increased only slightly—a surprising conclusion in view of the growing importance of the stock market: the volume of Stock Exchange transactions, for example, increased in 1962 by 40 per cent over the previous year and the number of security holders almost certainly grew too.

The following observations may go some way to explain this apparent contradiction: (a) The bond market expanded in 1962 quite suddenly and consider-

Diagram XX-1

INVESTMENTS OF BANKING INSTITUTIONS IN ISRAEL SECURITIES,
BY MONTHS, 1962



ably, merely as a result of linkage differentials, i.e. independently of new issues. Furthermore, in the previous year there had been a particularly large increase in the purchase of dollar-linked bonds, because of special circumstances: the provident funds increased their acquisitions as a result of the revised regulations concerning their "approved" investments, while private investors did so because of growing expectations of devaluation; in 1962 these particular factors were absent. (b) The repayment of housing mortgages ahead of their maturities, in accordance with special arrangements made after the devaluation, claimed about IL 65 million of the public's liquid resources, possibly at the expense of stock exchange investment. (c) On the equity market, the rate of new issues failed to keep up with demand. This is indicated by the trend of share prices and numerous oversubscriptions.

The banks in 1962 apparently intensified their activities as principals in the securities market. The combined portfolio of banking institutions in non-Government securities increased by one-third, from IL 75 million to IL 99 million, linkage differentials aside. No relevant statistics are available, but it is quite likely that in respect of these non-Government securities the banks also increased their equity holdings. Most of the increase took place in the months May–July (see Diagram XX-1), when the market slackened somewhat—a suitable time for banking institutions to increase their investment portfolios.

2. THE STOCK EXCHANGE LIST

(a) *At par values*

The increase, at par value, of Israel securities listed on the Tel Aviv Stock Exchange totalled IL 270 million in 1962, including linkage differentials in the amount of IL 183 million¹ (see Table XX-2). Without such differentials, the increase would have been only about half of that recorded in 1961.

This comparison, however, is of limited significance, since the short-term loans are not included in the Stock Exchange list; they are traded on the Tel Aviv Stock Exchange without being formally listed, and as already mentioned, there was an especially large increase in 1962 in the net issue of these loans. The net amount of capital raised in 1962 against securities traded on the Stock Exchange, including short-term loans and excluding linkage differentials, totalled IL 157 million, as against IL 193 million in 1961.²

¹ Total linkage differentials came to approximately IL 230 million, but they were partly absorbed in the redemption of principal during the year.

² There is no identity between these figures and the sum of new issues in either of the two years. The difference stems mainly from three factors: (a) Changes in the Stock Exchange list are at par value, while new issues are recorded on the basis of issue prices. (b) The issue of a new security and its listing on the Stock Exchange do not coincide: listing generally lags behind issue, and the amount involved differs from year to year. (c) Not all the securities newly *listed* are newly *issued* securities.

Table XX-2
SECURITIES LISTED ON THE TEL AVIV STOCK EXCHANGE,
AT PAR VALUE, 1960-62

(End of year)

	IL million			Per cent		
	1960	1961	1962	1960	1961	1962
Government loans						
Dollar-linked	110	120	185	24.8	19.1	20.6
Index-linked	38	43	74	8.6	6.9	8.3
"Mixed" link	4	10	13	0.9	1.6	1.4
Non-linked	65	71	64	14.6	11.3	7.2
Total	217	244	336	48.9	38.9	37.5
Government-guaranteed loans						
Dollar-linked	47	54	57	10.6	8.6	6.4
Index-linked	19	15	13	4.2	2.4	1.4
Total	66	69	70	14.8	11.0	7.8
Other securities						
Ordinary shares	44	114	145	9.9	18.2	16.2
Preference shares	18	24	51	4.0	3.8	5.7
Dollar-linked loans		104	157		16.6	17.5
Index-linked loans	96	8	56	21.6	1.3	6.2
"Mixed" link loans		62	80		9.8	8.9
Others	3	2	2	0.7	0.3	0.2
Total	161	314	491	36.2	50.0	54.7
Total Israel securities	444	627	897	100.0	100.0	100.0
Foreign securities	...	46	111			
Grand total	...	673	1,023			

The outstanding balance of value-linked loans increased by IL 219 million and totalled IL 635 million at the end of 1962 (see Table XX-3); their percentage share of all securities listed on the Stock Exchange advanced from 66 to 71 per cent. In 1961 the absolute increase in the balance of linked loans amounted to only IL 122 million and their percentage share of all listed securities declined. But the increase that year represented "new" capital, whereas in 1962 it stemmed mainly from the revaluation of the existing balance; the increase over and above the revaluation amounted to a mere IL 36 million.

The total of all loans listed on the Stock Exchange advanced from IL 489 million to IL 701 million, and their relative share of all listed securities remained constant, at 78 per cent. If we add to this the short-term loans and subtract the revaluation differentials on loans linked to the exchange rate, we find that for the

Table XX-3

VALUE-LINKED LOANS LISTED ON THE STOCK EXCHANGE, AT PAR VALUE,
1961-62

(at end of year)

Type	IL million		Per cent of total securities listed on the Stock Exchange	
	1961	1962	1961	1962
Dollar-linked ^a	314	457	50.0	50.9
Index-linked ^a	102	178	16.3	19.9
Total	416	635	66.3	70.8

^a Including proportionate part of "mixed"-linked loans.

first time in years there was a sharp relative decrease in linked loans—from 80 to 73 per cent of total loan capital (see Table XX-4).

This finds its reflection also in the added relative importance of Government loans on the market. Their percentage of all loan capital listed on the Stock Exchange, which had been on the decline for several years, continued to drop in 1962—from 50 per cent to less than 48 per cent. However, in 1962, as in the preceding year, a number of loans were floated by financial institutions, the proceeds of which were deposited with the Government and held at the disposal of these institutions for use in accordance with Government directives.¹ Formally speaking, these are not Government loans, but in a way they amount to the same.

Table XX-4

ALL LOAN CAPITAL TRADED ON THE STOCK EXCHANGE, 1961-62^a

(at end of year)

	IL million (par value)		Per cent	
	1961	1962	1961	1962
Bonds listed on Stock Exchange, not adjusted for linkage differentials	489	518	94.2	83.8
Plus: Short-term loans	30	100	5.8	16.2
All loan capital traded on the Exchange	519	618	100.0	100.0
Of which: Value-linked loans	416	452	80.2	73.1

^a 1962 figures are not adjusted for linkage differentials.

¹ See Chapter XVII, "Financial Institutions".

Table XX-5
**GOVERNMENT LOANS TRADED ON STOCK EXCHANGE,
 AT PAR VALUE, 1961-62**

(at end of year)

	IL million		Per cent of loan capital traded on the Stock Exchange	
	1961	1962	1961	1962
Long-term	244	336	47.0	41.9
Short-term	30	100	5.8	12.5
Total	274	436	52.8	54.4

Moreover, if the Government short-term loans are added to the Government loans listed on the Stock Exchange, we find that the public debt increased both absolutely and relative to all the loans dealt in on the Stock Exchange (see Table XX-5).

In the state of high liquidity which marked the economy in 1962, the Short-Term Loan was a suitable instrument for the Government to use for mopping up means of payment from the public and easing the pressure of demand, provided that the proceeds from the Loan were not used to finance Government expenditure.

The weight of equity capital in the sum total of listed securities remained practically constant in 1962. The total par value of listed equities advanced from IL 138 million to IL 196 million, and their percentage of the Stock Exchange list remained approximately 22 per cent.

(b) *At market value*

At the end of 1962, the total value of the Stock Exchange list at market prices was IL 1,050 million (see Table XX-6). The increase during the year amounted to IL 342 million—half again as much as in 1961 and three times as much as in 1960.

Particularly striking was the increase in the total value of share capital: from IL 209 million at the end of 1961 to IL 345 million at the end of 1962, when equities accounted for 33 per cent of the total Stock Exchange list. The corresponding figure for the end of 1959 was less than 10 per cent!

The value of loan capital listed on the Stock Exchange rose from IL 501 million to IL 707 million, at market prices, but its relative share dropped from 71 to 67 per cent. It should again be noted that the short-term loans are not included in the Stock Exchange list; if they were, the decline would have been less: from 72 to 70 per cent.

The difference between the annual change in the Stock Exchange list at par

Table XX-6

SECURITIES LISTED ON TEL AVIV STOCK EXCHANGE, AT MARKET VALUE,
1960-62

	IL million			Per cent						
	1960	1961	1962	1960	1961	1962				
A. Value at end of year										
Bonds	363	501	707	74	71	67				
Shares	130	209	345	26	29	33				
All securities	493	710	1,052	100	100	100				
	Bonds		Shares			All securities				
	1960	1961	1962	1960	1961	1962	1960	1961	1962	
B. Annual changes (IL million)										
Due to net addition (at par) of new securities		41	107	41	76	58	82	183	} 342	
Due to premiums and price fluctuations		-14	31	54	3	78	40	34		
Total		27	138	206	95	79	136	122	217	342

value and that in its value at market prices stems not only from price fluctuations but also from the fact that newly issued shares added to the Stock Exchange list are for the most part floated at a premium. This premium, of course, is not included in the par values of the securities listed on the Stock Exchange, but is included in their issue value. The latter constitutes, as it were, the starting point for the formation of market prices of such securities, from the moment they are traded on the Stock Exchange.¹ Bonds, on the other hand, are nearly all issued at or very near their par value, and any difference between the change in the bond list at par values and the change at market prices stems, as a rule, from Stock Exchange fluctuations. The year 1962, however, differed in this respect, since the currency devaluation at once increased the par value of dollar-linked loans by two-thirds, while their market value increased to a lesser extent.

In 1962 the total market value of equities listed on the Stock Exchange increased by IL 136 million (see Table XX-6). More than half of this amount (IL 78 million) was accounted for by premiums and the rise of share prices. In 1961 the increase stemmed almost exclusively from the nominal addition of new securities, as the drop in share prices offset most of the premiums. As regards

¹ For example, a new share, issued at a premium of 30 per cent of its par value, is traded at a price of 130. Assuming this to be the only change in the Stock Exchange list, then a difference will be noted between the change in the list at par values and the change in the list at market prices, without fluctuations having taken place in the prices themselves.

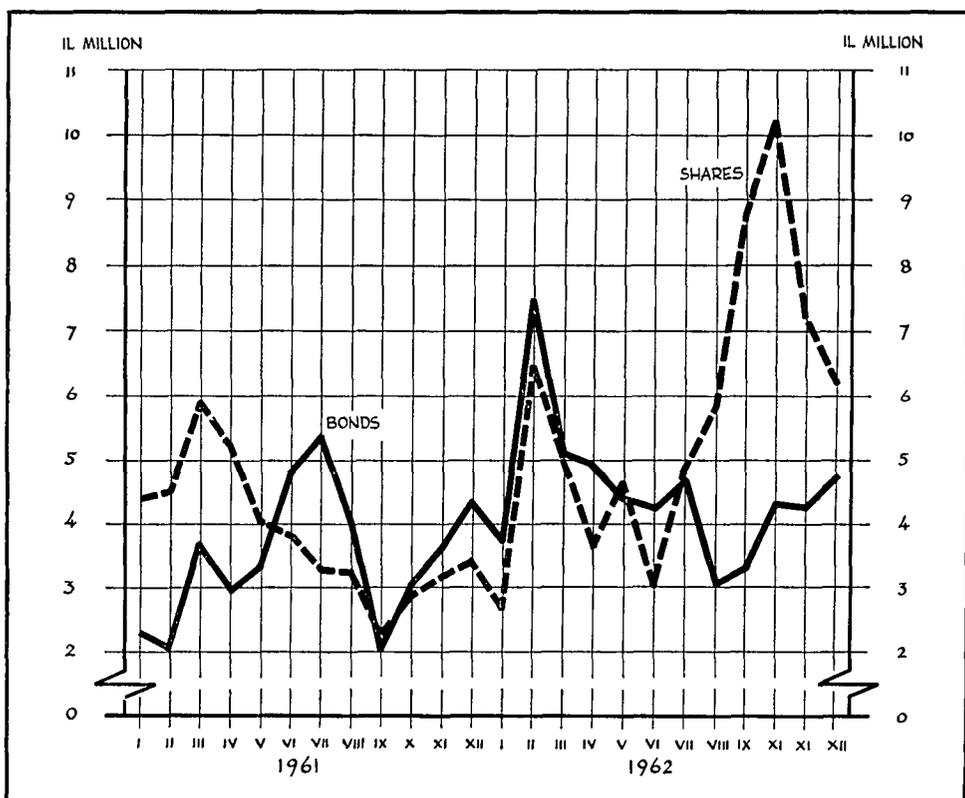
bonds, linkage differentials in 1962 create a statistical difficulty, because they gave rise both to an addition to the nominal value and to a boost in prices. But prices, as already mentioned, rose to a lesser extent than par values. The face value of those dollar-linked loans which had not been redeemed before the end of 1962 increased by about IL 183 million, and their market value by approximately IL 150 million. On the other hand, there was an increase of about IL 40 million in the value of the other loans, as a result of the rise in their prices.

3. TRADE ON THE STOCK EXCHANGE

The volume of Stock Exchange transactions in 1962 totalled IL 123 million,¹ i.e. IL 35 million more than in 1961. Trading was slack at the beginning of the

Diagram XX-2

VOLUME OF TRANSACTIONS ON TEL AVIV STOCK EXCHANGE, BY MONTHS, 1961-62



¹ At market prices; excluding the proceeds from new issues, the matching of buying and selling orders received by individual banks and brokers, and their own-account transactions outside the Stock Exchange.

year, as it had been during the second half of 1961. In February the Stock Exchange volume increased temporarily (see Diagram XX-2 and Table XX-7). After that, the trade in bonds ranged from IL 3 million to IL 5 million per month. Trading in shares underwent sharper fluctuations: it ranged from IL 3 million to IL 6 million per month throughout most of the year, and in the months September to November increased noticeably—up to IL 10 million in November. An upward movement of share prices usually went together with an increase in volume.

During most of the year, shares were traded more extensively than bonds. Exceptions were the months January to April, and June. In the first and last of these months, this was due to a certain slackness in the equity market rather than a particularly large volume in bonds. In February, following the currency devaluation, the volume expanded in both markets. The increased activity in equities

Table XX-7
VOLUME OF TRANSACTIONS ON TEL AVIV STOCK EXCHANGE,
MONTHLY, 1960-62
(IL thousand)

	Bonds			Shares		
	1960	1961	1962	1960	1961	1962
January	3,047	2,281	3,721	1,060	4,906	2,666
February	2,628	2,080	7,420	983	4,521	6,504
March	2,813	3,516	5,108	1,707	5,947	5,075
First quarter	8,488	7,877	16,249	3,750	15,374	14,245
April	2,878	2,937	4,917	1,778	5,225	3,584
May	2,891	3,306	4,427	2,633	4,063	4,651
June	3,026	4,796	4,261	3,718	3,779	2,985
Second quarter	8,795	11,039	13,605	8,129	13,067	11,220
July	3,162	5,413	4,675	3,074	3,227	4,766
August	2,466	4,049	3,016	3,894	3,261	5,811
September	2,353	2,075	3,300	4,259	2,171	8,731
Third quarter	7,981	11,537	10,991	11,227	8,659	19,308
October	2,577	3,011	4,323	6,220	2,849	10,216
November	2,460	3,567	4,305	4,379	3,168	7,181
December	3,159	4,332	4,709	4,541	3,388	6,215
Fourth quarter	8,196	10,910	13,337	15,140	9,405	23,612
Total	33,460	41,363	54,182	38,246	46,505	68,385

SOURCE: Tel Aviv Stock Exchange Ltd.

from September onward seems to indicate a growing interest by the investing public. (This is borne out by developments in the first quarter of 1963.)

The second half of the year saw a reform of dealing arrangements on the Tel Aviv Stock Exchange. This concerned the most active shares on the Exchange. Whereas formerly all trading had been multilateral¹ and a single price was made per Stock Exchange session for any given security, the opportunity was now given to members of the Exchange, on top of this, to carry out bilateral transactions, with prices fluctuating during the day.

Another noteworthy event in 1962 was the setting up of additional mutual funds (unit trusts) and the reorganization of existing ones in accordance with the 1961 law. At the end of 1962 there were four such funds, with total assets of IL 19 million. The expectation set upon them, from the point of view of the securities market, is that capital may possibly be attracted through them, which otherwise would not have been invested in securities. Moreover, thanks to the maneuverability of the funds, they should be able in some circumstances to serve as a regulating factor in the market and check price fluctuations which are out of line with the general trend. To encourage savings and to attract them into the securities market through the funds, tax concessions are granted on income from mutual fund certificates.

4. FIXED-INTEREST SECURITIES

(a) *Dollar-linked bonds*

During the years preceding the currency devaluation the bond market developed rapidly, though sporadically. Dollar-linked bonds always aroused the most interest, but their prices and the rate of new issues fluctuated, depending on changes in legislation as well as economic and monetary forecasts.² At times there was a strong interaction between the bond market and the equity market, with a boom in one of them often being accompanied by a recession in the other.

One of the side effects of the currency devaluation of 1962 was a sharp turn in the dollar-linked bond market. It also revealed the basic shortcomings of the dollar clause in domestic transactions. During most of 1961, the dollar-linked bonds were priced above their par values. On the eve of the devaluation their redemption yield was, on the average, lower than their coupon rate, and much lower than the yield obtaining with regard to other bonds. The acceptance of a small current income must, of course, be understood as the price paid by the holders of dollar-linked bonds for the prospects of linkage differentials. But after the devaluation, when the forecast of additional linkage differentials in the short

¹ The old system can best be described as a form of clearing: all dealers, having matched their own buying and selling orders for each security, announce the balance of their orders to the official dealer, who calculates the price at which a maximum of deals can be carried out. He then assigns purchases and sales to the dealers on the floor.

² A summary of these changes up to 1961 appeared in the 1961 Annual Report, pp. 398 ff.

run was actually nil, there was no longer any willingness to pay this price, and in order to bring the yield from dollar-linked bonds into line with that from non-linked loans, market prices of the former necessarily established themselves below the adjusted par value.¹

The average price of dollar-linked bonds after the devaluation was about 36 per cent above their issue price.² It is by this rise that the capital profit accruing to bond owners following the devaluation must be judged. This profit did not have the same meaning for all who held dollar-linked bonds on the day of devaluation, for two reasons:

1. The longer the lapse of time since the original investment, the lower the annual value of the gain, in nominal terms.

2. The nominal gain was partly offset by the loss in purchasing power sustained by the initial investment. The earlier the investment was made, the bigger the loss.

The real gain (allowing for the loss in purchasing power, as measured by the cost-of-living index) ranged between 3 per cent—in cases where the investment was made, say, in February 1956—and 36 per cent—where the investment was made immediately prior to the devaluation. Expressed in terms of compound annual profit, the range of this real profit was between 0.5 per cent and 26 per cent—as regards investments made between February 1956 and February 1961 (see Table XX-8).

Table XX-8

REAL CAPITAL GAIN ON INVESTMENT IN DOLLAR-LINKED BONDS, AT END OF FEBRUARY 1962^a

Date of purchase ^b	Real capital gain at end of February 1962 (Per cent of capital invested)	Annual compound interest equivalent
1962	36.5	—
1961	25.8	25.8
1960	19.8	9.5
1959	19.3	6.1
1958	15.5	3.7
1957	11.2	2.1
1956	2.6	0.4

^a Assumptions and method of calculation are described in Bank of Israel Bulletin No. 18, March 1963, pp. 43 ff.

^b February of each year; in 1962—before February 9.

¹ The original face value of the dollar-linked bonds plus the linkage differentials of IL 66.67 per IL 100 old face value.

² On the basis of the index of dollar-linked bond prices at the end of February 1962 (see Table XX-7, column 2).

The gains reaped from the dollar link were therefore shared unevenly by bondholders, depending on the dates of their investments, with the earlier investor gaining least. On the other hand, the devaluation losses incurred on dollar-linked liabilities were unevenly spread among debtors, with the earlier borrower gaining most. This distortion was a systematic fault of dollar linkage as such. Intended to ensure the repayment (and collection) of debts at their real value, the dollar clause actually introduced into lending and borrowing transactions two unforeseeable factors—the date and rate of the devaluation. Hence the imbalance in the division of devaluation gains, which in all likelihood was not intended by those who had conceived the linkage clause. Hence, too, the flurry of investments in dollar-linked bonds prior to the currency devaluation, which seems to have been prompted much more by the anticipation of capital gains than the desire to ensure a fixed real income.

Devaluation changed all this quite radically. The new issue of dollar-linked loans was discontinued altogether. As regards existing dollar-linked bonds, the dollar clause lost its significance for the time being: once the linkage differential had actually been determined, dollar-linked bonds became very much like non-linked bonds. Indeed, numerous holders sold them after the devaluation in order to realize their gains, as may be gathered from the increased volume of transactions in, and the relatively low prices of, dollar-linked bonds immediately after the devaluation. Nevertheless, transactions in dollar-linked loans during the first weeks after the devaluation amounted to only a very small percentage of the outstanding capital. Furthermore, the constant rise in prices of dollar-linked bonds from the end of February till the end of the year (see Table XX-7) points to a growing demand for them. There are several reasons for this development. First, at the price level of the end of February the redemption yield net of income tax from these bonds ranged from 10 to 13 per cent approximately.¹ This rate of income from Government paper or the bonds of financial institutions made such securities attractive to investors for whom income was the decisive factor. Secondly, for the same reason there was also room to expect a rise in prices and some capital gains, and therefore dollar-linked bonds at the then prevailing prices also attracted investors who were mainly out for profit. Thirdly, it is quite likely that some investors assumed the possibility of a further devaluation before maturity² and, hence, further linkage differentials.

Thus, between the end of February and the end of December the prices of dollar-linked bonds rose by 14 per cent, and their yield diminished accordingly, depending on their due dates.³ On the basis of market prices at the end of the

¹ At the end of February dollar-linked bond prices were already slightly above the level of the first few days after devaluation.

² The maturity of most series is not later than 1975, but there are a few series running till 1980 and even 2002.

³ Yields were lower the longer the bonds, because of the greater chances of additional linkage gains.

year, net redemption yields from these bonds ranged between 4 and 7 per cent approximately.

(b) *Index-linked bonds*

Developments in the index-linked bond market were different from what might have been expected—namely, that the devaluation and the anticipation of price increases would enhance the demand for such bonds. To be sure, immediately after the devaluation the prices of these bonds rose by about 4 per cent, and stood slightly above their par values (adjusted for accrued linkage differentials—see Table XX-9, column 5). Subsequently, prices fluctuated more or less in accordance with the cost-of-living index, but in the second half of the year they slipped back again to under the adjusted par values.

Table XX-9
INDICES OF LINKED-BOND PRICES, 1962

	Dollar-linked bonds			Index-linked bonds	
	Jan. 1962 = 100 ^a	Par value unadjusted for linkage differentials = 100 (at IL 1.80/\$1)	Par value adjusted for linkage differentials = 100 (at IL 3/\$1)	Jan. 1962 = 100	Par value adjusted for linkage differentials = 100
	(1)	(2)	(3)	(4)	(5)
January	100	101.8	—	100	96.7
February	134.5	136.5	81.9	104.3	100.4
March	137.0	138.3	83.0	106.0	101.8
April	141.9	143.0	85.8	108.8	101.7
May	142.2	143.8	86.3	109.6	101.1
June	145.1	147.3	88.4	109.7	101.9
July	150.2	150.9	90.55	109.0	103.0
August	151.7	153.0	91.8	108.1	101.5
September	152.4	152.2	91.35	107.1	99.25
October	153.4	152.8	91.7	108.8	97.7
November	153.8	153.4	92.1	110.8	98.1
December	155.1	154.3	92.6	112.1	98.1

^a Based on the index of the Central Bureau of Statistics, where average price 1960=100.

There are several possible explanations. First, the rise in the prices of index-linked bonds generally does not exceed the range of the rise in the index itself, for in contrast to dollar-linked bonds, they do not hold out the chance for a sudden and substantial lump-sum gain. This follows both from the nature of the cost-of-living clause—the index, unlike the exchange rate, rises gradually—and from the fact that it is almost always possible to subscribe for this kind of bond

at par value from new issues—a possibility which usually puts a “ceiling” on the prices of existing bonds.¹ Furthermore, past experience has shown that prices of index-linked bonds frequently lag behind the index. For these reasons, index-linked bonds must be excluded from the investments popular with short- and medium-term investors or investors who seek mainly capital gains. Therefore, not everyone who had held dollar-linked bonds up to the devaluation switched to index-linked bonds afterwards. And finally, the development of consumer prices in 1962—the cost-of-living index in the months May to August was actually below the level of April—was sufficient to cast doubt on the worthwhileness of the index link from the point of view of lenders.

As in former years, most of the purchases of index-linked bonds were accounted for by institutional investors. In order to encourage private purchases, an attempt was made to provide a greater variety of issues. In 1962 some series of index-linked bonds were issued with a shorter period to maturity than usual—five years as against eight or ten years for earlier series. Also, investors were offered the option between linking principal *and* interest to the cost-of-living index and linking the principal alone. Bonds of the first kind carry 5 per cent (plus linkage), and of the second kind—6 per cent (plus linkage of the principal). This implied a slight drop in the coupon rate of index-linked bonds, which in earlier series had been 6 per cent.

(c) *Short-term loans*

After the devaluation the demand for short-term loans increased, as has been noted. For many investors, both institutional and private, they apparently became a substitute for dollar-linked bonds, and perhaps also for those linked to the index.

For a considerable time up till February 9, when expectations of a currency devaluation had been growing, the anticipated linkage gains from dollar-linked bonds exceeded the yield obtaining on short-term loans. Dollar-linked bonds for this reason served as an outlet not only for long- and medium-range investments, but also for short-term speculation. After the devaluation, when chances of linkage gains were no longer foreseeable, at least in the short run, short-term loans became relatively more attractive for short- and medium-term investment in view of the combination of yield and liquidity which they offered.

The net income from the Government Short-Term Loan is 8.5 per cent per annum.² The grossed-up net income may come to more than twice this rate, depending on the marginal tax rate payable by the holder. The loan is highly

¹ At the ceiling, it will be worthwhile buying a new bond, at issue price, no less than an old bond at market price.

² Stemming from interest and the discount at which the loan is issued. The nominal interest is subject to income tax at a maximum rate of 25 per cent. The discount is tantamount to a capital gain, and as such is not taxed, as far as private investors, as distinct from dealers, are concerned.

liquid, not only because of the shortness of maturity but also because of the fact that the banks are actually ready (though in no way bound) to purchase this loan in the market at a price calculated to reflect the principal and income accrued since issue—that is to say, at a mathematical and not a market price—which protects sellers against losses.

(d) *New issues*

1. *Government loans*

The amount and composition of Government borrowing in the securities market in 1962 reflected the changes in the pattern of Stock Exchange investments. While gross issue figures of long-term Government loans were about equal in 1961 and 1962, the net amount dropped from IL 15 million to IL 5 million (see Table XX-11). During half of the year, capital repayments exceeded new issues. On the other hand, the net new issue of short-term loans increased seven-fold, from IL 10 million to IL 70 million.

Table XX-10
DOMESTIC ISSUES OF NEW SECURITIES, 1961-62
(IL million)

	Gross		Net	
	1961 ^a	1962	1961 ^a	1962
Long-term loans				
Government	35.0	34.4	14.8	5.3
Other	131.6	145.6	101.8	114.0
Total	166.6	180.0	116.6	119.3
Short-term Government loans (net)	10.0	70.1	10.0	70.1
Total loan capital	176.6	250.1	126.6	189.4
Shares listed on the Stock Exchange, at issue prices	51.0	34.2	51.0	34.2
Grand total	227.6	284.3	177.6	223.6

^a Revised figures.

As a result of new issues in the amount of IL 75 million and revaluation differentials on dollar-linked loans in the amount of IL 85 million, the Government's internal debt¹ grew in 1962 by IL 160 million, or 57 per cent (see Table XX-12 and Diagram XX-3). The most important change in the composition of

¹ Funded debt in the guise of market securities.

Table XX-11
ISSUE OF GOVERNMENT LOANS, 1961-62
(IL million)

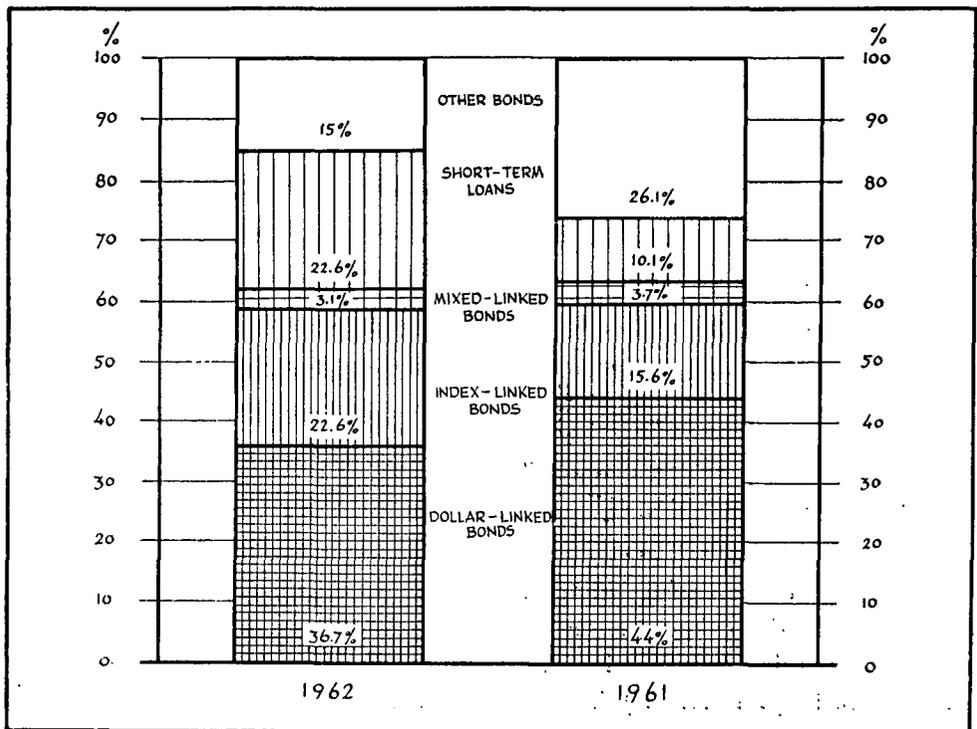
	1961		1962	
	Gross	Net	Gross	Net
Long-term	35.0	14.8	34.4	5.3
Short-term	74.1	10.0	177.4	70.1
Total	109.1	24.8	211.8	75.4

the debt was that short-term loans accounted for 23 per cent of the debt at the end of 1962, as against 11 per cent at the end of 1961.

The balance of linked Government loans grew from IL 178 million at the end of 1961 to IL 276 million at the end of 1962. Most of the increase stemmed

Diagram XX-3

GOVERNMENT BONDS: DEBT OUTSTANDING, BY TYPE OF SECURITY, 1961-62^a
(Percentages)



^a At end of year. Domestic issues only.

Table XX-12

GOVERNMENT FUNDED DOMESTIC DEBT, CLASSIFIED, 1961-62

Description	Balance at end of year			
	1961		1962	
	IL million	%	IL million	%
Linked				
Dollar-linked, interest-bearing	108.1	38.5	162.1	36.7
Dollar-linked, prize-bearing	15.3	5.5	25.5	5.8
Index-linked, interest-bearing	43.9	15.6	74.3	16.8
"Mixed" link, interest-bearing	10.3	3.7	13.8	3.1
Total	177.7	63.3	275.7	62.4
Non-linked				
Interest-bearing, issued to financial institutions	19.6	7.0	14.6	3.3
Other, interest-bearing	17.5	6.2	15.5	3.5
Prize-bearing	36.3	12.9	36.2	8.2
Short-term, interest-bearing	29.8	10.6	99.9	22.6
Total	103.2	36.7	166.2	37.6
Grand total	280.8	100.0	442.0	100.0

NOTE: Discrepancies are due to rounding.

from linkage differentials.¹ The proportion of linked loans within the Government debt remained almost constant—at slightly less than two-thirds.

The balance of non-linked loans, apart from the Short-Term Loan, diminished by IL 7 million and totalled IL 66 million at the end of 1962.

2. Non-Government bonds

The gross issue of non-Government bonds amounted to IL 146 million in 1962, as against IL 132 million in 1961. The net issue, after deduction of repayments, totalled IL 114 million.

As in the past, most of the issuing bodies were financial institutions: investment companies and investment and mortgage banks. Part of the capital raised was in fact earmarked for the Government and deposited with it, to be re-lent in accordance with its directives by these institutions.² Another part was earmarked, by agreement between the Histadrut and the Government, to finance investments of companies affiliated to Hevrat Ovdim, the holding company of the General Federation of Labor (Histadrut). This agreement applies above all to securities purchased by the provident funds as "authorized investments".

¹ Linkage differentials in February 1962 totalled IL 85.5 million.

² See Chapter XVII, "Financial Institutions".

5. EQUITIES

(a) *General*

The share market in 1962 went through four distinct phases:

1. In the first six weeks of the year, the slackness which had been felt in the second half of 1961 continued. Against the background of the general anticipation of devaluation, heavy purchases of dollar-linked bonds continued to be made at the expense of the demand for shares.

2. Immediately after the devaluation there was a steep rise in share prices (see Diagram XX-4 and Table XX-13). The reshuffle of many investment portfolios implied an influx of funds into the share market. This was connected with the realization of profits on the dollar-linked bond market and the public's increased liquidity in general after the devaluation. In addition, there were purchases on foreign account, which may also have contributed to the boom. The price level of ordinary shares rose by 16 per cent in February, and the Stock Exchange volume was 2.4 times as much as in January.

Diagram XX-4

ORDINARY SHARES: STOCK EXCHANGE VOLUME AND INDEX OF SHARE PRICES, BY MONTHS, 1961-62

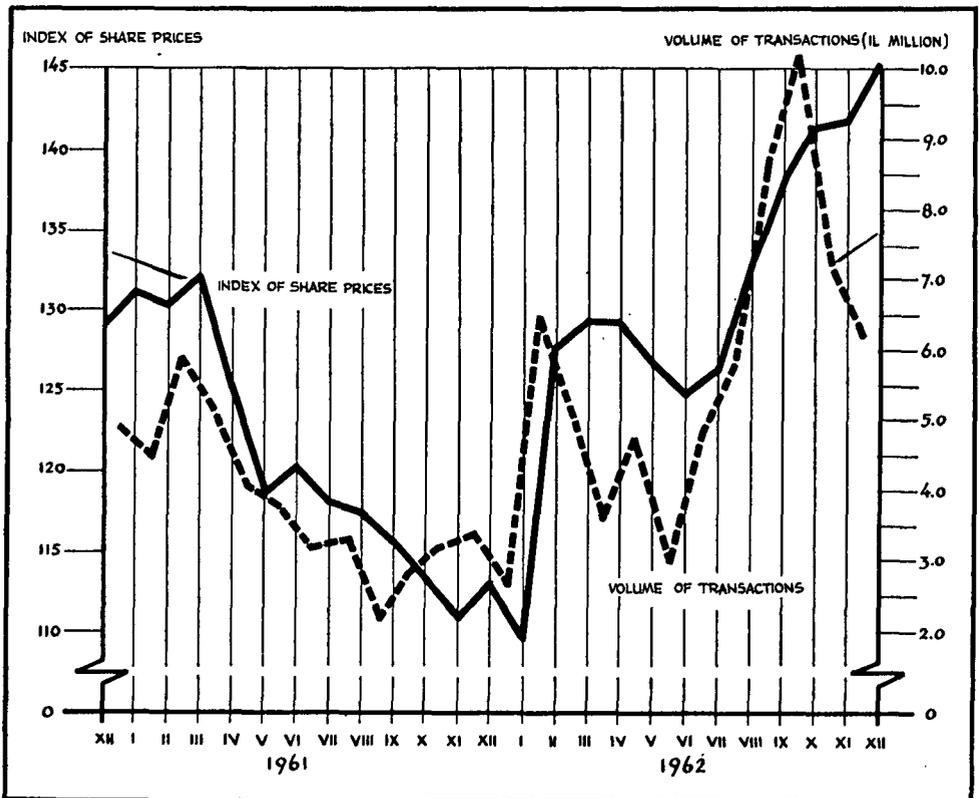


Table XX-13

INDEX OF ORDINARY SHARE PRICES, 1961-62

End of month	1961		1962	
	Average 1960 = 100	January 1961 = 100	Average 1960 = 100	January 1962 = 100
January	131.0	100.0	109.8	100.0
February	130.3	99.5	127.8	116.4
March	132.2	100.9	129.5	117.9
April	125.1	95.5	129.4	117.8
May	118.8	90.7	126.8	115.5
June	120.4	91.9	124.9	113.7
July	118.2	90.2	126.5	115.2
August	117.6	89.8	133.1	121.2
September	115.8	88.4	138.2	125.9
October	113.4	86.6	141.5	128.9
November	111.0	84.7	141.8	129.1
December	112.3	85.7	145.3	132.3

SOURCE: Central Bureau of Statistics.

3. In March and April the market calmed down and the volume shrank again (see Diagram XX-4). In May and June prices fell slightly—partly, at least, because of the official endeavors to freeze prices, which it was felt might adversely affect company profits. In May the volume of transactions increased as share prices continued to decline—an indication of some pressure from sales. The sharp break during these months on foreign stock markets apparently also had its effect, although, as already mentioned, the drop in Israel was by no means comparable.

4. In the second half of the year, a new boom set in. The index of ordinary share prices advanced by 16 per cent, and the volume reached record heights. Apart from minor fluctuations, the boom receded for only two days in October, when the Cuban crisis cast its shadow over the market, but the general trend was not affected thereby. Most of the new equity issues were floated, as already mentioned, in the latter half of the year (close to IL 30 million).

In December 1962, the Central Bureau of Statistics began to publish a daily index of share prices. This index is simpler than the monthly index (Table XX-13); it is not weighted and it includes only one class of shares for each company. On the other hand, it is more comprehensive, as it includes, apart from shares formally listed on the Stock Exchange, those shares which are traded on the floor without being listed. Moreover, unlike the monthly index, it is broken down into groups of shares by economic branches. Table XX-14 shows how share prices advanced in 1962 in the various groups.

Table XX-14

DAILY INDEX OF SHARE PRICES, END 1962

(End 1961 = 100)

	Index
All shares	127.0
Land and development	164.7
Finance and insurance	154.0
Investment companies	143.9
Commercial and industrial	111.1
Oil	96.8

(b) New issues

Activity in the new issues market slowed down somewhat in 1962. Total issues (including rights issues and offers for sale) on the local market aggregated IL 41 million, at issue prices, as against IL 60 million in 1961. Of this sum, IL 34 million represented shares listed on the Stock Exchange, and IL 7 million unlisted shares. Foreign investors purchased new Israel shares to the sum of approximately IL 21 million—about IL 7 million less than in the preceding year.

There were no industrial shares among the new issues of 1962. 58 per cent of the issue amount (IL 19.8 million) was accounted for by 11 financial institutions, and 36 per cent (IL 12.4 million) by three land and development companies. The remainder—IL 2 million—represented the shares of one commercial company. Appeal to the public for the raising of share capital was, in 1962, not yet as widespread among limited companies as might have been expected in view of the favorable market. Loan capital and various types of credit largely continued to play the role which should be reserved for share capital.

6. FOREIGN SECURITIES

Foreign securities¹ held by Israel residents at the end of 1962 amounted to \$ 25.7 million at original purchase prices, as against \$ 20.3 million at the end of 1961. The annual increase in 1962 was smaller than in 1961, when it amounted to \$ 7.7 million. As with other foreign currency assets, the increased rate of conversion into local currency was reflected here as well in 1962.

The exchange premium, which up to the currency devaluation applied to transactions in foreign securities, disappeared in 1962.

¹ Including the securities of foreign affiliates of Israel companies.