

## CHAPTER V

# CAPITAL IMPORTS AND THE FOREIGN DEBT

### I. MAIN DEVELOPMENTS

Long- and medium-term capital imports added up to \$ 2.3 billion in the year reviewed, compared with \$ 3.2 billion in 1973 and \$ 1.8 billion in 1972. If the exceptionally huge inflow in the postwar final quarter of 1973 is disregarded, the strongly rising trend begun in 1970 was sustained. But because of the still sharper increase in the balance of payments deficit on current account and soaring world prices, the sizable capital inflow did not have any significant economic impact.

For the first time in three years, capital imports failed to match the growth of the current deficit; that part not covered by this source amounted to \$ 1.1 billion, similar to the year's defense import bill and equal to one-third of the total current account deficit. The economy therefore had to resort to short-term capital movements to finance the import surplus, with a consequent sharp dwindling of foreign exchange reserves and an unprecedented growth in short-term indebtedness.

Unilateral transfers, which totalled some \$ 1.7 billion this year, covered only about half the deficit, compared with 82 percent in 1973 and nearly the entire sum in 1972. Other convenient sources of foreign funds—foreign investments in Israel, Development Loan (State of Israel Bonds), and U.S. government loans—covered only 12 percent of the import surplus in 1974, as against 30 percent in 1973 and 48 percent in 1972.

Several factors aggravated the deficit financing problem this year. First of all, the unparalleled surge of capital imports in the postwar months of 1973 perforce led to the contraction of the traditional sources of capital, such as Jewish Agency transfers and the Development Loan, which could be expanded to only a limited extent in 1974. Other factors were the strong devaluation expectations which persisted throughout most of the year, the worsening of the political and military situation, the economic slowdown, and the resulting uncertain business outlook in Israel and the world in general. All these depressed the flow of private loan and investment capital to Israel, as well as some categories of private transfers. The devaluation of the Israeli pound came too close to the end of the year to boost long- and medium-term capital imports in 1974, but foreign exchange reserves did turn steeply upward and presumably the full effects of the devaluation will be felt in 1975.

**Table**  
**DEFICIT, TRANSFERS, AND THE**  
(\$)

	1971	1972	1973	1974
<b>A. Current account and long-term capital movements</b>				
Balance on current account	-1,209.0	-1,101.0	-2,642.0	-3,356.0
Unilateral transfers	756.3	1,051.8	2,172.5	1,674.2
Balance on current account and transfers	<b>-443.7</b>	<b>-49.2</b>	<b>-469.5</b>	<b>-1,681.8</b>
Long-term capital movements				
Investments from abroad, net Independence and Development	74.7	143.0	185.2	71.0
Loans, net	179.5	184.0	359.0	165.0
U.S. government loans	244.1	205.3	251.5	147.0
Other loans	200.2	191.0	204.5	227.0
Total long-term capital movements	<b>698.5</b>	<b>723.3</b>	<b>1,000.2</b>	<b>610.0</b>
Total capital imports	<b>1,463.8</b>	<b>1,775.1</b>	<b>3,172.7</b>	<b>2,284.2</b>
Surplus of capital imports over deficit on current account	<b>254.8</b>	<b>674.1</b>	<b>530.7</b>	<b>-1,071.8</b>
<b>B. Israeli investments abroad, net</b>	<b>-11.2</b>	<b>-0.6</b>	<b>-12.5</b>	<b>-9.6</b>
<b>C. Nonfinancial sectors</b>				
Short-term credit from rest of the world	9.0	-36.0	..	..
Short-term credit to rest of the world	-63.0	-38.8	..	..
Trade credit	-22.0	-30.0	..	..
Other short-term assets	-41.0	-8.8	..	..
Total	<b>-54.0</b>	<b>-74.8</b>	<b>55.8</b>	<b>140.7</b>
<b>D. Financial sectors</b>				
Foreign deposits	326.1	357.3	347.2	350.6
With commercial banks	355.8	363.3	351.1	350.7
With Bank of Israel	-29.7	-6.0	-3.9	-0.1
Loans to foreigners	-35.4	-24.0	-288.0	-56.0
Commercial banks	-30.0	6.0	-270.0	-80.0
Bank of Israel (incl. clearing accounts)	-5.4	-30.0	-18.0	24.0
Foreign exchange reserves				
Changes in reserves <sup>a</sup>	-593.4	-1,008.2	-885.7	841.2
Central monetary institutions	-284.9	-551.7	-691.7	759.2
Other monetary institutions	-308.5	-456.5	-194.0	82.0
Adjustments				
Foreign currency valuation adjustments	53.3	17.1	223.8	87.2
Special Drawing Rights	13.9	14.0		
Total change in reserves due to economic transactions	<b>-526.2</b>	<b>-977.1</b>	<b>-661.9</b>	<b>928.4</b>
<b>E. Net errors and omissions</b>	<b>45.9</b>	<b>45.1</b>	<b>-28.7</b>	<b>-282.3</b>

NOTE: A minus sign denotes debits, and a positive value credits.

<sup>a</sup> A minus sign denotes an increase in reserves.

V-1  
**CAPITAL ACCOUNT, 1971-74**  
 million)

1973, quarterly				1974, quarterly			
I	II	III	IV	I	II	III	IV
-285.0	-488.0	-572.0	-1,297.0	-661.0	-923.0	-912.0	-860.0
241.3	268.0	252.7	1,410.5	348.7	500.2	414.2	411.1
-43.7	-220.0	-319.3	113.5	-312.4	-422.8	-497.8	-448.9
46.4	53.5	65.0	20.3	4.6	21.3	23.3	21.8
51.0	42.0	11.0	255.0	80.0	43.0	6.0	36.0
51.5	47.8	75.8	76.4	31.8	4.8	25.9	84.5
23.5	36.2	82.2	62.6	2.2	60.2	38.1	126.5
172.4	179.5	234.0	414.3	118.6	129.3	93.3	268.8
413.7	447.5	486.7	1,824.8	467.3	629.5	507.5	679.9
128.7	-40.5	85.3	527.8	-193.7	-293.5	-404.5	-180.1
-6.3	-2.9	-2.6	-0.7	-5.2	-9.9	-6.1	11.6
-2.7	67.5	-43.9	34.9	76.0	10.3	30.6	23.8
-21.0	117.3	323.8	-72.9	-70.6	-0.8	-87.3	509.3
-20.0	116.3	320.7	-65.9	-70.6	-8.6	-81.5	511.4
-1.0	1.0	3.1	-7.0	—	7.8	-5.8	-2.1
-89.0	-107.0	-166.0	74.0	139.0	-33.0	15.0	-177.0
-52.0	-98.0	-181.0	61.0	120.0	-23.0	13.0	-190.0
-37.0	-9.0	15.0	13.0	19.0	-10.0	2.0	13.0
-262.8	-202.9	-211.9	-208.1	119.3	348.6	462.1	-88.8
-234.9	-141.8	-87.4	-227.6	199.4	239.3	318.2	2.3
-27.9	-61.1	-124.5	19.5	-80.1	109.3	143.9	-91.1
141.5	165.1	47.8	-130.6	36.7	13.2	-33.4	70.7
-121.3	-37.8	-164.1	-338.7	156.0	361.8	428.7	-18.1
111.6	3.4	138.1	-224.4	-101.5	-34.9	23.6	-169.5

The country's foreign exchange reserves shrank appreciably this year, reaching their nadir shortly before the devaluation. Balances held by the Bank of Israel stood at \$ 1.1 billion at year's end, as against \$ 1.7 billion the year before. Along with the contraction of reserves, Israel fully utilized its Special Drawing Rights and drew its gold tranche and first credit tranche from the International Monetary Fund. The economy also stepped up its short-term borrowing, with outstanding liabilities on account of such loans tripling from \$ 190 million in 1973 to \$ 564 million.

Israel's foreign currency debt reached \$ 6,250 million after rising \$ 1.1 billion. Given the galloping global inflation, this may not have been a significant increase, but the much less favorable terms this year—the hiking of interest rates on the one hand and the shorter maturities of the new loans on the other—aggravated the problem and increased the short-term debt servicing burden. In 1975 Israel will have to repay about \$ 1 billion on account of principal, as against some \$ 500 million the year before. To this must be added the high interest payments, which apparently will come to approximately \$ 500 million in 1975, compared with some \$ 400 million in 1974. The sheer magnitude of this debt constitutes a heavy strain on the balance of payments, and necessitates, besides the financing of the mounting import surplus, the allocation of huge sums for servicing the country's foreign indebtedness.

The growth of the foreign debt outstanding, combined with the heavy drain on foreign exchange reserves, increased Israel's net foreign liabilities to an unprecedented extent, from \$ 158 million in 1972 and about \$ 500 million in 1973 to \$ 1.8 billion in the year reviewed.

## 2. BACKGROUND TO THE CAPITAL IMPORT DEVELOPMENTS

Israel's capital imports slumped in 1974, with both the public and private sector flows being affected. The downturn, however, followed a massive increase in the last quarter of 1973; the 1974 volume actually far eclipsed the average for the two preceding years.

The change in the public sector's capital inflow must be viewed against the backdrop of developments after the Yom Kippur War, when foreign transfer receipts expanded enormously. U.S. government transfers, consisting of grants and loans, reached record dimensions during this period, and the contributions of World Jewry to the emergency fund-raising campaigns and purchases of the Development Loan (State of Israel Bonds) were also up strongly. The national emergency continued in 1974, but its impact on capital imports waned in the second half of the year. The swelling capital inflow in the last quarter of 1973 diminished the sources of funds originally intended for transfer to Israel in 1974. These factors depressed the capital

**Table V-2**  
**CAPITAL IMPORTS, BY SECTOR, 1971-74**  
(\$ million)

	1971	1972	1973	1974	1973, quarterly				1974, quarterly			
					I	II	III	IV	I	II	III	IV
<b>Private sector</b>												
Unilateral transfers	612	783.4	777.9	775.9	168.6	195.8	204.3	209.2	189.9	186.8	191.2	208.0
Personal restitution	231	291.5	264.3	317.1	57.0	67.4	69.0	70.9	94.0	72.2	60.5	90.4
Other transfers	306	391.1	378.1	349.1	82.4	98.5	110.7	86.5	70.9	87.7	102.6	87.9
Transfers to nonprofit institutions	75	100.8	135.5	109.7	29.2	29.9	24.6	51.8	25.0	26.9	28.1	29.7
Investments from abroad, net	75	143.0	185.2	71.0	46.4	53.5	65.0	20.3	4.6	21.3	23.3	21.8
Long-term loans	166	170.0	181.0	79.0	33.0	45.0	81.0	22.0	4.0	32.0	1.0	42.0
<b>Total private sector</b>	<b>853</b>	<b>1,096.4</b>	<b>1,144.1</b>	<b>925.9</b>	<b>248.0</b>	<b>294.3</b>	<b>350.3</b>	<b>251.5</b>	<b>198.5</b>	<b>240.1</b>	<b>215.5</b>	<b>271.8</b>
<b>Public sector</b>												
Unilateral transfers	151	267.4	1,394.4	898.3	72.7	72.4	48.0	1,201.3	158.8	313.4	223.0	203.1
To National Institutions	156	209.4	606.4	273.3	49.7	47.4	29.0	480.3	60.8	68.4	57.0	87.1
Intergovernmental transfers	-5	58.0	788.0	625.0	23.0	25.0	19.0	721.0	98.0	245.0	166.0	116.0
Long-term loans	459	411.3	635.0	460.0	94.0	81.0	88.0	372.0	110.0	76.0	69.0	205.0
Independence and Development Loans	180	184.0	359.0	165.0	51.0	42.0	11.0	255.0	80.0	43.0	6.0	36.0
U.S. government loans	229	191.4	236.7	149.3	46.6	34.5	76.6	79.0	33.7	7.4	26.6	81.6
Other loans	50	35.9	39.3	145.7	-3.6	4.5	0.4	38.0	-3.7	25.6	36.4	87.4
<b>Total public sector</b>	<b>610</b>	<b>678.7</b>	<b>2,029.4</b>	<b>1,358.3</b>	<b>166.7</b>	<b>153.4</b>	<b>136.0</b>	<b>1,573.3</b>	<b>268.8</b>	<b>389.4</b>	<b>292.0</b>	<b>408.1</b>
Total capital imports	<b>1,463</b>	<b>1,775.1</b>	<b>3,173.5</b>	<b>2,284.2</b>	<b>414.7</b>	<b>447.7</b>	<b>486.3</b>	<b>1,824.8</b>	<b>467.3</b>	<b>629.5</b>	<b>507.5</b>	<b>679.9</b>
Less: Israeli investments abroad		0.6	12.5	9.6	6.3	2.9	2.6	0.7	5.2	9.9	6.1	-11.6
Total, excl. Israeli investments abroad	<b>1,463</b>	<b>1,774.5</b>	<b>3,161.0</b>	<b>2,274.6</b>	<b>408.4</b>	<b>444.8</b>	<b>483.7</b>	<b>1,824.1</b>	<b>462.1</b>	<b>619.6</b>	<b>501.4</b>	<b>691.5</b>

**Table V-3**  
**INCREASE IN MAIN CATEGORIES OF FOREIGN CURRENCY ASSETS**  
**AND LIABILITIES, 1971-74**

(\$ million)

	1971	1972	1973	1974
<b>A. Assets</b>				
Net foreign exchange reserves at the				
Bank of Israel	214	495	628	-627
Foreign currency valuation adjustments	50	19	165	56
Change due to economic transactions	164	476	463	-683
Other liquid assets	320	478	305	-192
Foreign currency valuation adjustments	3	—	58	31
Change due to economic transactions	317	478	247	-223
<b>B. Liabilities</b>				
Foreign currency debts	808	651	1,012	1,157
Foreign currency valuation adjustments	—	—	136	108
Change due to economic transactions	—	—	876	1,049
Liquid foreign currency liabilities of				
commercial banks	355	356	399	422
Foreign currency valuation adjustments	-2	—	43	71
Change due to economic transactions	357	356	356	351
<b>C. Other short-term capital</b>	89	99	254	-85

imports of the public sector, besides resulting in a highly irregular flow owing to the unequal distribution of U.S. government loans and grants over this period and the surge of contributions at the beginning of the year.

For the first time since 1966, the capital imports of the private sector fell off. Those items that are mainly economically motivated underwent a drastic change. Among the underlying causes were the deep dent in foreign investment in Israel, a smaller long- and medium-term borrowing from overseas sources, and the shrinking of immigrant transfers, which was partly offset by an increase in transfers of Israelis. In other types of private capital imports, which are less affected by economic considerations, the changes were comparatively slight.

In analyzing the capital inflow the year reviewed can be divided into two subperiods, the turning point being the devaluation of the Israeli pound on November 9. Most components of the private capital import expanded after the devaluation; however, growth was smaller than expected, and in part was connected with institutional arrangements unrelated to the devaluation.

Most of the influences retarding the flow of capital to the economy apparently gained strength in 1974, in contrast to previous years, when trends were more inconsistent and mixed. These factors began to operate in 1973, when the security situation took a turn for the worse, immigration slackened, the property market boom began to fizzle out, the domestic share market went into a nosedive, and international interest rates began to rise. These trends not only picked up momentum in 1974, but they were joined by a number of other forces working in the same direction, notably the mounting of devaluation expectations, which were actually quite high throughout most of the year. In the second half of 1974 the economy began to show signs of losing vigor, for the first time since the recession of 1966-67, and the public became increasingly pessimistic on this score. Moreover, the world economy began to wobble, and the energy crisis further clouded the business outlook in the countries affected.

These developments, together with those that appeared in 1973 and grew more potent in the year reviewed, caused private capital imports to dip precipitously until the devaluation of the IL. However, the record rate of internal inflation, and in its wake the strong expectation of a hike in indirect taxes, apparently spurred the transfer of foreign currency by Israeli residents for executing current domestic transactions.<sup>1</sup>

The devaluation was followed by an upsurge in private capital imports, but whereas nonresidents stepped up their transfers to this country only slightly, local residents and commercial banks quickly liquidated their financial investments abroad. It seems that the adjustment of the asset portfolios of nonresidents depends on variables not always connected with developments in the Israeli economy. Their mild reaction to the devaluation is explained by the influence of other variables, such as the recession in the major Western economies, where most of Israel's capital inflow originates, and the mood of hesitancy prevailing there. On the other hand, Israelis and others subject to more stringent foreign currency restrictions than those applicable to nonnationals are much more sensitive to domestic economic developments; hence their immediate response to the devaluation.

<sup>1</sup> The higher the rate of domestic inflation, the more the conversion of foreign currency into IL as soon as possible after the execution of a transaction within the country reduces the losses from an imminent devaluation.

Foreign loan permits increased in volume in 1974, but the amount actually utilized declined. Moreover, it seems that the lag between the approval of an investment in Israel and implementation of the project by foreign entrepreneurs lengthened. It is therefore obvious that the contraction of private capital imports in 1974 was due to adverse economic conditions, while government policy did not impose an effective constraint on the inflow of capital.

### 3. UNILATERAL TRANSFERS

The Yom Kippur War was a turning point as regards the size and composition of nonrecurring foreign transfer receipts. Those of the private sector, which previously had formed the bulk of such receipts, failed to expand, while public sector transfers swelled enormously, bringing up their share of the total to fully two-thirds in 1973. In the year reviewed the flow of public sector transfers slacked off from their record volume in the immediate postwar period, but it still far eclipsed the prewar figure, standing at \$ 1,674 million as against \$ 2,173 million in 1973 and \$ 1,051 million in 1972.

Public sector transfers, which are not affected by economic considerations, added up to \$ 898 million in 1974, with sharp fluctuations around the trend. Those to the Jewish Agency spurted after the fighting, just as they had done after the Six Day War, a reflection of the readiness of World Jewry to come to Israel's aid in an emergency. At the same time there was a record increase in U.S. government grants, which even surpassed Jewish Agency transfers. It is important to note that the exceptional magnitude and weight of intergovernmental transfers in total public sector transfer receipts in a sense constitutes a greater risk to the economy,<sup>2</sup> since fluctuations in such items are generally sharper than in transfers from traditional sources.

Private sector transfers, which are influenced more by economic considerations, remained stable during the first three quarters of 1974, but their composition altered. In the final quarter the curve turned upward, which can be only partly explained by the devaluation of the Israeli pound. Until the devaluation private transfers were probably affected by the same factors which operated in 1973 but whose intensity changed in the year surveyed. On the one hand, those forces stimulating the inflow of capital to Israel, including the acceleration of domestic inflation and a prospective hiking of indirect taxes, became more pronounced; on the other hand, expectations of an imminent devaluation, which persisted throughout most of the year, the sagging of immigration from affluent countries, and the national

<sup>2</sup> Quite apart from the political aspect.

**Table V-4**  
**UNILATERAL TRANSFERS, 1971-74**

(\$ million)

	1971	1972	1973	1974	1973, quarterly				1974, quarterly			
					I	II	III	IV	I	II	III	IV
<b>Personal restitution from</b>												
<b>West Germany</b>	230.7	291.5	264.3	317.1	57.0	67.4	69.0	70.9	94.0	72.2	60.5	90.4
Lump-sum	135.3	169.3	98.0	117.8	25.1	25.1	25.9	21.9	51.9	23.1	18.7	24.1
Pensions	95.4	122.2	166.3	199.3	31.9	42.3	43.1	49.0	42.1	49.1	41.8	66.3
<b>Personal transfers in cash</b>	303.4	386.0	370.1	343.3	80.4	96.5	108.7	84.5	69.4	68.8	101.0	86.1
Immigrants	112.8	166.7	147.5	99.3	35.8	42.5	43.9	25.3	15.9	23.2	27.4	32.8
Others	190.6	219.3	222.6	244.0	44.6	54.0	64.8	59.2	53.5	63.6	73.6	53.3
<b>Personal transfers in kind</b>	13.3	13.1	16.0	15.8	4.0	4.0	4.0	4.0	4.5	3.9	3.6	3.8
<b>Total personal transfers from the rest of the world</b>	<b>547.4</b>	<b>690.0</b>	<b>650.4</b>	<b>676.2</b>	<b>141.4</b>	<b>167.9</b>	<b>181.7</b>	<b>159.4</b>	<b>167.9</b>	<b>162.9</b>	<b>165.1</b>	<b>180.3</b>
<b>Personal transfers to the rest of the world</b>	11.1	8.0	8.0	10.0	2.0	2.0	2.0	2.0	3.0	3.0	2.0	2.0
<b>Total net personal transfer receipts</b>	<b>536.3</b>	<b>682.6</b>	<b>642.4</b>	<b>666.2</b>	<b>139.4</b>	<b>165.9</b>	<b>179.7</b>	<b>157.4</b>	<b>164.9</b>	<b>159.9</b>	<b>163.1</b>	<b>178.3</b>
<b>Institutional transfers</b>	234.3	310.2	742.3	383.0	78.9	77.3	54.0	532.1	85.8	95.3	85.1	116.8
Nonprofit institutions	75.1	100.8	135.5	109.7	29.2	29.9	24.6	51.8	25.0	26.9	28.1	29.7
Jewish Agency	155.6	204.7	602.0	268.5	48.5	46.2	28.2	479.1	59.6	67.2	55.8	85.9
Transfers in kind	3.6	4.7	4.8	4.8	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
<b>Net transfers to the government</b>	-5.3	58.0	788.0	625.0	23.0	25.0	19.0	721.0	98.0	245.0	116.0	116.0
<b>Total unilateral transfers</b>	<b>765.3</b>	<b>1,050.8</b>	<b>2,172.7</b>	<b>1,674.2</b>	<b>241.3</b>	<b>268.2</b>	<b>252.7</b>	<b>1,410.5</b>	<b>348.7</b>	<b>500.2</b>	<b>414.2</b>	<b>411.1</b>

emergency had a moderating effect on the capital inflow. These contrasting influences caused a structural change in transfers to the private sector: a sharp contraction in those by new immigrants during the first nine months of the year, and an increase in the figure for Israelis. After the devaluation the stream of private transfers swelled, most of the growth consisting of personal restitution payments (which are only moderately affected by devaluation), while transfers of Israeli residents fell off—a development hard to explain.

The amount of personal restitution brought to Israel rose by \$ 53 million, from \$ 264 million in 1973 to \$ 317 million. Most of the increment can be attributed to institutional arrangements. At the beginning of 1974 an intergovernmental transfer was received which was included in nonrecurring restitution payments, while toward the end of the year pension payments expanded under a new agreement with the West German government, which increased the number of persons eligible for pensions. Besides these factors, there were several others stimulating transfers in 1974, but their impact was relatively weak. Nonrecurring restitution receipts increased in the last quarter of the year; presumably this was due chiefly to the devaluation, the expectation of which had previously prompted recipients to hold up the transfer of such income to Israel. The appreciation of the DM against the dollar and the annual adjustment of restitution items for the cost-of-living rise in Germany also increased the flow of such funds.

Immigrant transfers fell off sharply in 1974, totalling some \$ 100 million as against \$ 148 million in 1973 and \$ 167 million in 1972. The downtrend began in the last quarter of 1973 and continued through the first quarter of 1974; it was followed by a mild upturn which lasted until year's end, but the level still fell short of the average for the two preceding years. The postdevaluation growth of such receipts was smaller than expected, the main reason apparently being the steady contraction of immigration from the Western countries over the last two years.

Transfers by Israelis from abroad amounted to \$ 244 million in 1974, compared with \$ 223 million in 1973 and \$ 220 million in 1972. The growth of this item and its movement during the year—a rise before the November devaluation and a downswing thereafter—are not easily explained. There is reason to believe that the official definition of this item does not fully reflect its composition.<sup>3</sup> Jewish Agency transfers were, at \$ 273 million, smaller than in 1973, when the figure in the last quarter alone hit a staggering \$ 480 million. It was only natural that such receipts should fall off from this extraordinarily high level, a result of the intensified fund-raising among World Jewry during the last three months of 1973, especially the immediate postwar period. Almost half the proceeds of the 1974 emergency

<sup>3</sup> This item is officially defined as pensions, gifts, and legacies from abroad.

campaign, which were double the sum raised in the 1973 campaign, were advanced and transferred before the end of 1973.

Nonprofit institution transfers drifted slowly upward during 1974 to reach \$ 110 million. These receipts, the bulk of which passes through the Jewish Agency, represent the allocation of the various campaign funds among the different institutions according to a certain key. There is thus room to believe that there is a connection between the sum recorded as Jewish Agency transfers and that allocated to nonprofit institutions. In the last three months of 1973 the huge increase in Jewish Agency transfers pulled up the figure for nonprofit institutions to a new high, while in 1974 it ran at roughly its level in the first three quarters of 1973.

U.S. government grants totalled \$ 790 million in 1974, compared with \$ 834 million the year before. Of this sum, \$ 705 million was a special military grant for financing procurements in the U.S., \$ 50 million was for economic and technical aid, and \$ 35 million for the absorption of Jewish immigrants from the Soviet Union.

#### 4. FOREIGN INVESTMENT IN ISRAEL

Foreign investment shrank perceptibly in 1974, reversing the steady uptrend of the last few years. The net amount came to only \$ 60 million, as contrasted with \$ 172 million in 1973 and \$ 143 million in 1972. The curve started to turn down in the last quarter of 1973 and fell more precipitately in the first quarter of 1974 to virtually hit rock bottom. The last three quarters of the year saw a slight pickup, but the level remained below that in previous years.

The path traced by foreign investments since the final quarter of 1973 tends to bear out the assumption of a close connection between the worsening of the security situation and the contraction of such capital. But a number of other developments at home and abroad conspired to reinforce the declining trend. Among these were the expectation of an impending devaluation which lasted for the better part of the year, the slowdown of economic activity and the belief that this trend would persist due to the various restraining measures introduced by the authorities, the contraction of domestic capital formation, the setback in the real estate market, and the share market slump. In addition, the sliding into a recession of the leading Western economies, the source of the investment capital inflow to Israel, and the further darkening of the business horizon by the energy crisis may also have had an adverse effect.

The combined impact of these factors was to sharply depress foreign investment in Israel, which failed to perk up even after the devaluation of the Israeli pound. Israeli investments abroad, on the other hand, increased substantially during the first three quarters of 1974 and sagged conspicuously after the devaluation. The

**Table V-5**  
**FOREIGN INVESTMENT IN ISRAEL, 1971-74**  
(\$ million)

	1971	1972	1973	1974	1973, quarterly				1974, quarterly			
					I	II	III	IV	I	II	III	IV
<b>Investment in Israel by nonresidents</b>												
In foreign currency	62.5	124.3	156.0	45.1	39.5	43.9	54.2	18.4	0.4	16.7	14.1	13.9
Investments	85.9	171.8	234.5	129.5	61.0	62.0	71.6	39.9	29.8	39.8	28.3	31.6
Investments re-patriated	-23.4	-47.5	-78.5	-84.4	-21.5	-18.1	-17.4	-21.5	-29.4	-23.1	-14.2	-17.7
In Israeli currency (from blocked accounts)	-0.7	3.0	-8.2	-11.6	-4.3	0.6	0.2	-5.6	-4.9	-2.3	-1.6	-2.8
In Development Bonds	5.3	7.3	12.5	10.6	5.9	2.8	2.1	1.7	1.6	2.7	1.8	4.5
In kind	2.0	1.0	8.6	9.6	0.3	2.0	4.4	1.9	3.3	0.3	4.4	1.6
<b>Total</b>	<b>69.1</b>	<b>135.6</b>	<b>168.9</b>	<b>53.7</b>	<b>42.3</b>	<b>49.3</b>	<b>60.9</b>	<b>16.4</b>	<b>0.4</b>	<b>17.4</b>	<b>18.7</b>	<b>17.2</b>
Reinvestment of profits	5.6	7.4	16.3	18.4	4.1	4.2	4.1	3.9	4.6	4.6	4.6	4.6
<b>Total, net</b>	<b>74.7</b>	<b>143.0</b>	<b>185.2</b>	<b>72.1</b>	<b>46.4</b>	<b>53.5</b>	<b>65.0</b>	<b>20.3</b>	<b>5.0</b>	<b>22.0</b>	<b>23.3</b>	<b>21.8</b>
<b>Israeli investments abroad</b>												
Direct <sup>a</sup>		-0.5	-0.5	-0.1	—	-0.1	-0.3	-0.3	-0.1	-0.1	0.2	-0.1
Portfolio												
Private individuals	9.9	2.5	6.4	5.1	2.5	2.2	1.4	0.3	5.0	1.9	1.7	-3.5
Banks	-2.9	-1.4	6.6	4.6	3.8	0.6	1.5	0.7	0.3	8.1	4.2	-8.0
<b>Total</b>		<b>0.6</b>	<b>12.5</b>	<b>9.6</b>	<b>6.3</b>	<b>2.9</b>	<b>2.6</b>	<b>0.7</b>	<b>5.2</b>	<b>9.9</b>	<b>6.1</b>	<b>-11.6</b>
<b>Net foreign investment in Israel</b>		<b>142.4</b>	<b>172.7</b>	<b>62.5</b>	<b>40.1</b>	<b>50.6</b>	<b>62.4</b>	<b>19.6</b>	<b>-0.2</b>	<b>12.1</b>	<b>17.2</b>	<b>33.4</b>

<sup>a</sup> Excluding investments in the administered areas.

Table V-6

**FOREIGN INVESTMENT IN ISRAEL, QUARTERLY, 1969-74**  
(\$ million)

	Securities listed on the Tel Aviv Stock Exchange	Direct investment and unlisted securities	Investment in approved enterprises	Total
1969 I	3.0	13.3	1.2	17.5
II	4.3	5.7	2.2	12.2
III	3.3	5.3	0.8	9.4
IV	2.9	2.8	3.0	8.7
1970 I	5.4	5.3	0.8	11.5
II	0.8	6.8	0.9	8.5
III	2.3	8.4	0.8	11.5
IV	2.7	6.0	0.8	9.5
1971 I	3.4	14.2	1.0	18.6
II	4.4	13.6	2.7	20.7
III	4.7	15.1	1.0	20.8
IV	6.1	19.4	7.3	32.8
1972 I	4.0	22.4	3.0	29.4
II	18.0	30.0	4.9	52.9
III	8.0	31.6	1.9	41.5
IV	9.4	33.8	6.1	49.3
1973 I	13.3	45.2	2.8	61.3
II	11.5	48.3	2.0	61.8
III	7.0	62.6	1.9	71.5
IV	4.7	34.2	1.5	40.4
1974 I	2.8	23.6	0.9	27.3
II	5.8	30.6	1.0	37.4
III	2.1	24.5	1.6	28.2
IV	4.1	29.8	2.6	36.5

restrained response of foreign investors to the change in the exchange rate can be attributed to their concern with those factors that continued to retard the flow of investments, of which uncertainty as to future developments abroad and a reassessment of Israel's economic prospects were the most important. The possibility of immediately realizing devaluation gains through the liquidation of financial investments in foreign currencies explains the prompt reaction of Israelis to the devaluation.

Foreign currency conversions by nonresidents for buying securities on the Tel Aviv Stock Exchange fell steeply in 1974. Such investments amounted to only \$ 15 million, compared with \$ 37 million in 1973 and \$ 40 million in 1972. This development, which began in 1973, was very likely connected with the Israeli share market reverses during this period. There was also a sizable decline in other types of investment. Transfers for business capital expenditure, both for the establishment of new concerns and the expansion of existing ones, and for the purchase of unlisted shares sagged to about two-thirds of their level in 1973; investments in approved enterprises fell off to about the same extent.

Foreign capital investments approved by the government Investment Center were also much lower in 1974. Excluding approved foreign currency loans of shareholders, the figure came to only \$ 76 million, compared with \$ 144 million in 1973 and \$ 104 million in 1972. The drop was particularly sharp in hotel investment, which had peaked in 1972 after a record tourism year in 1971. Permits for the floating of financial institution equity issues abroad were also down steeply. By contrast, approvals of investment projects in the service industries doubled in 1974 to reach \$ 24 million.

The adverse turn in foreign investment approvals in the year reviewed was due not to administrative restrictions but mainly to investors' economic considerations.

Up to the devaluation purchases of foreign securities by Israeli residents and banks swelled to record proportions in anticipation of a change in the parity of the Israeli pound. Immediately after the devaluation a large percentage of these securities were thrown on the market, as investors decided to cash in on their devaluation gains. In the final accounting, there was a net purchase of foreign securities this year, and this contributed to the general decline in net foreign investment in Israel.

## 5. FOREIGN LOANS

Gross long- and medium-term foreign loan receipts totalled some \$ 1 billion this year, while repayments came to nearly \$ 500 million. Proceeds from this source were roughly the same as in the two preceding years, if the one-time spurt in sales of the Independence and Development Loans (State of Israel Bonds) in the last quarter of 1973 is disregarded.

In real terms, however, the level dipped noticeably in 1974 because of the rise in world commodity prices (Israel directly finances its overseas purchases of some commodities with the help of such loans). In 1974 the economy borrowed much more heavily for short terms, the balance of such loans trebling from \$ 190 million at the end of 1973 to \$ 564 million. After contracting in 1973, the value of foreign loan permits issued to the private sector rose strongly in the year reviewed despite

Table V-7

**APPROVALS OF FOREIGN INVESTMENTS IN UNLISTED ISRAELI SHARES,  
BY BRANCH, 1970-74**

(\$ thousand)

Branch	1970	1971	1972	1973	1974
Agriculture	50	64	—	14	—
Industry	21,336	24,367	46,173	27,665	23,798
Shipping	21	2,567	—	—	32
Transport	—	66	1,442	628	88
Public works	—	31	428	—	—
Hotels	13,353	9,959	32,975	16,594	3,843
Real estate	4,770	10,656	11,319	18,880	15,065
Financial institutions <sup>a</sup>	225	29,006	6,430	68,352	9,175
Other services	3,654	4,049	4,774	11,823	24,029
<b>Total</b>	<b>43,409</b>	<b>80,765</b>	<b>103,541</b>	<b>143,956</b>	<b>76,030</b>

<sup>a</sup> Permits granted to financial institutions to issue shares abroad.

SOURCE: Investment Center.

the smaller number of permits issued.

Medium- and long-term foreign loan proceeds of the public sector failed to match their 1973 volume. This was due entirely to sagging Independence and Development Loan sales, which netted \$ 165 million in all of 1974 as contrasted with \$ 255 million in the last quarter of 1973 alone. The tumbling of such sales, which were even below their net level in 1972 and 1973, is probably explained by the very brisk sales immediately after the war, which reduced the number of potential buyers of additional bonds, besides resulting in an increased conversion, *inter alia* for donating the proceeds to the United Jewish Appeal.<sup>4</sup> U.S. government military credits totalled \$ 335 million in 1974, of which \$ 110 million was on account of the preceding U.S. fiscal year; in 1973 gross receipts from this source totalled \$ 300 million. These funds are intended solely for financing military procurements, and are made available when the purchases are executed in the U.S.

<sup>4</sup> The deepening recession in the major Western economies, where the bonds are sold, presumably also spurred the conversion of this paper for donation to the United Jewish Appeal.

**Table V-8**  
**LONG- AND MEDIUM-TERM FOREIGN LOANS, 1970-74**  
 (\$ million)

	1970	1971	1972	1973	1974	1973, quarterly				1974, quarterly			
						I	II	III	IV	I	II	III	IV
<b>Loans received</b>													
Government	699	638	701	910	794	151	159	158	442	190	157	144	303
Development and Independence Loans	231	285	300	502	326	84	82	47	289	115	83	37	91
Other	149	318	311	326	214	71	73	121	61	35	60	33	86
Total	<b>848</b>	<b>956</b>	<b>1,012</b>	<b>1,236</b>	<b>1,008</b>	<b>222</b>	<b>232</b>	<b>279</b>	<b>503</b>	<b>225</b>	<b>217</b>	<b>177</b>	<b>389</b>
<b>Loans repaid</b>													
Government	184	179	291	275	334	57	78	70	70	80	81	75	98
Development and Independence Loans	96	105	116	143	161	33	40	36	34	35	40	31	55
Other	108	150	141	145	135	38	28	40	39	31	28	32	44
Total	<b>292</b>	<b>329</b>	<b>432</b>	<b>420</b>	<b>469</b>	<b>95</b>	<b>106</b>	<b>110</b>	<b>109</b>	<b>111</b>	<b>109</b>	<b>107</b>	<b>142</b>
<b>Net loans received</b>													
Government	515	459	410	635	460	94	81	88	372	110	76	69	205
Thereof: Development and Independence Loans	135	180	184	359	165	51	42	11	255	80	43	6	36
Other	41	168	170	181	79	33	45	81	22	4	32	1	42
Total	<b>556</b>	<b>627</b>	<b>580</b>	<b>816</b>	<b>539</b>	<b>127</b>	<b>126</b>	<b>169</b>	<b>394</b>	<b>114</b>	<b>108</b>	<b>70</b>	<b>247</b>

Besides these credits, the government raised loans through foreign banks and financial institutions, including one for \$ 38.5 million from the International Monetary Fund in October. These loans were concentrated in the last quarter of the year, and were connected with the government's efforts to bolster Israel's foreign currency reserves just before and after the devaluation.

Net long- and medium-term foreign loans to the private sector dropped appreciably, from \$ 181 million in 1973 to \$ 79 million. This unprecedented decline was due to the shrinkage of gross receipts, repayments remaining at roughly the previous year's level. Most of the decrease was in credits to shipping and air companies, which fell from \$ 264 million at the end of 1973 to \$ 147 million owing to a smaller import of ships and aircraft in 1974. Loans to tourist concerns and hotels plummeted from \$ 15 million in 1973 to a mere \$ 1 million owing to the slump in tourism. The postdevaluation period saw an upturn in private sector borrowing, but smaller than expected. Presumably the administrative procedures involved in obtaining loans partly explain the lagged response of private borrowers.

The value of foreign loan permits issued to the private sector by the Treasury was substantially greater than in 1973, with the bulk of the permits going to commercial banks. Most of the increase took place in September, when the figure hit the \$ 200 million mark. The volume of permits this year was probably connected primarily with the dwindling of Israel's foreign exchange reserves: since this greatly affects the behavior of private individuals in this country and abroad, there was urgent need to raise foreign currency. One way of doing this was to issue more foreign loan permits; the increase was particularly large in September, not long before the devaluation, when reserves fell to a dangerously low level.

**Table V-9**  
**FOREIGN LOAN PERMITS, 1972-74**  
(\$ million)

Quarter	1972		1973		1974	
	Value	No.	Value	No.	Value	No.
I	179	154	69	60	114	36
II	131	97	9	49	90	57
III	125	95	38	80	351	70
IV	111	78	51	36	120	47
Total	546	424	167	225	675	210

SOURCE: Ministry of Finance.

Despite the larger foreign borrowing authorized, the amount actually obtained declined. What effectively constrained the expansion of such funds was probably the prevailing market conditions: the rise in international interest rates, mounting expectations of a devaluation of the Israeli pound, and the economic slowdown here. The rise in private overseas borrowing in the last quarter of 1974, before the devaluation, was apparently connected with transactions carrying the Treasury's exchange rate guarantee.

## 6. FOREIGN EXCHANGE RESERVES

After expanding greatly in each of the three preceding years, the Bank of Israel's foreign reserve assets dipped sharply in 1974 to stand at \$ 1,070 million, as against \$ 1,697 million at the end of 1973. This brought the level back to where it was at the end of 1972, but given the high rate of global inflation, it was actually lower in real terms. Aggravating the situation was the enormous growth of overseas purchases during this period, which meant that the reserves covered a much smaller portion of

Table V-10

### FOREIGN EXCHANGE RESERVES HELD AT BANK OF ISRAEL, 1973-74

(\$ million)

End of month	Gross reserves	Less: Foreign bank deposits	Less: Patach deposits	Net reserves	Change in net reserves		
					Before adjustment	Exchange rate differentials	Adjusted for differentials
1973 December	1,810	—	113	1,697			
1974 January	1,623	—	110	1,513	-184	-67	-117
February	1,624	1	105	1,517	3	57	-54
March	1,648	—	114	1,534	17	35	-18
April	1,580	—	116	1,464	-70	22	-92
May	1,538	4	121	1,413	-51	1	-52
June	1,416	8	110	1,298	-115	-17	-98
July	1,307	8	107	1,192	-106	-3	-109
August	1,194	—	112	1,082	-110	-28	-82
September	1,145	2	116	1,027	-55	3	-58
October	1,047	12	122	913	-114	23	-137
November 9				879	-34		
November	1,162	—	129	1,033	120	25	93
December	1,200	—	129	1,071	38	11	27
Jan.-Dec.					-627	62	-689
Jan.-Nov. 9					-818	30	-848
Nov. 9-Dec.					191	32	155

the import bill in 1974. Whereas in 1972-73 they were sufficient to cover four months' imports, in the year reviewed they covered less than two months' imports.

The bulk of the reserves at the Bank of Israel is in European currencies; the strengthening of these currencies against the dollar in 1974 therefore appreciated the reserves in dollar terms. The revaluation increment for the year was \$ 62 million, offsetting approximately 9 percent of the overall contraction.

The reserves began to diminish in the first months of the year, the decline growing more pronounced close to the date of the devaluation.<sup>5</sup> After the devaluation the curve turned upward, a trend which carried over into early 1975. The shrinkage of reserves in 1974 was connected with a number of basic developments in the domestic economy and abroad, which led to the growth of the deficit on goods and services and to difficulties in financing it from traditional sources. But the pattern of the contraction, i.e. the change in the pace at which the reserves dwindled and their expansion toward the end of the year, was chiefly a function of the varying intensity of devaluation expectations.

The steady reduction of reserves until the devaluation compelled the Bank of Israel to liquidate some of its foreign investments while maintaining a higher liquid asset cover for its current transactions (which tend to increase during periods of plunging reserves). This impelled the Bank, among other things, to draw on its remaining resources in the International Monetary Fund<sup>6</sup>—a step which affected the liquidity but not the size of the reserves. The Bank also drew its first credit tranche from the IMF,<sup>7</sup> which had the effect of increasing the reserves.

Along with the contraction of reserves at the Bank of Israel, government deposits with foreign banks tumbled \$ 110 million to total only \$ 58 million at the end of 1974. These continued to sag even after the devaluation, in contrast to the increase in the economy's other liquid asset holdings abroad.

The volume of foreign business transacted by Israeli commercial banks drifted steadily downward during the first three quarters of 1974, reversing the rising trend of previous years. Loans and deposits with foreign banks fell from \$ 1,328 million at the beginning of 1974 to \$ 1,154 million by the end of September, while foreign bank loans and deposits in Israel decreased from \$ 838 million to \$ 582 million. Toward year's end foreign business picked up smartly, loans and deposits with foreign banks rising from roughly \$ 1.1 billion to \$ 1.2 billion in the final quarter. At the same time there was a steep jump in loans from foreign banks, which doubled to reach some \$ 1.1 billion.

<sup>5</sup> November 9, 1974

<sup>6</sup> On April 19 the Bank of Israel drew its gold tranche in the amount of \$ 39 million and on October 4 it converted \$ 30 million of Special Drawing Rights into various currencies.

<sup>7</sup> On November 13 Israel drew its first credit tranche in the amount of \$ 39 million.

**Table V-11**  
**FOREIGN CURRENCY ASSETS, 1973-74**  
(\$ million)

	End-year balances		1973, quarterly				1974, quarterly				Increase	
	1973	1974	I	II	III	IV	I	II	III	IV	1973	1974
<b>A. Foreign exchange reserves at Bank of Israel</b>												
1. Foreign currency assets												
with Bank of Israel	1,809.8	1,199.7	1,449.2	1,518.5	1,607.1	1,809.8	1,648.0	1,415.6	1,144.5	1,199.7	580.3	-610.1
Reserves	1,690.7	1,150.3	1,371.4	1,399.5	1,488.1	1,690.7	1,528.8	1,335.8	1,064.7	1,150.3		
Gold	46.3	46.4	46.1	46.2	46.2	46.3	46.4	46.4	46.4	46.4		
Gold quota in IMF	39.2	—	—	39.2	39.2	39.2	39.2	—	—	—		
Special Drawing Rights	33.6	3.0	31.7	33.6	33.6	33.6	33.6	33.4	33.4	3.0		
Change due to:												
Foreign currency valuation adjustments and SDR allocation											165.4	56.3
Transactions and transfers											414.9	-666.4
2. Deposits in Bank of Israel	112.7	129.1	171.2	168.8	124.7	112.7	113.6	118.1	118.0	129.1	47.2	16.4
Foreign banks	—	—	3.5	3.5	6.8	—	—	7.8	2.0	—		
Patach	112.7	129.1	167.7	165.3	117.9	112.7	113.6	110.3	116.0	129.1		
3. Net balances with Bank of Israel	<b>1,697.1</b>	<b>1,070.6</b>	<b>1,278.0</b>	<b>1,349.7</b>	<b>1,482.4</b>	<b>1,697.1</b>	<b>1,534.4</b>	<b>1,297.5</b>	<b>1,026.4</b>	<b>1,070.6</b>	<b>627.5</b>	<b>-626.5</b>
<b>B. Net foreign currency balances</b>												
4. Gross foreign currency balances	1,496.1	1,304.0	1,238.3	1,367.4	1,490.7	1,496.1	1,538.6	1,422.4	1,231.4	1,304.0	305.4	-192.1

Government deposits abroad	168.5	58.4	76.8	144.8	143.6	168.5	130.9	124.0	76.9	58.4	111.4	-110.1
Bank deposits abroad	1,327.6	1,245.6	1,161.5	1,222.6	1,347.1	1,327.6	1,407.7	1,298.4	1,154.5	1,245.6	194.0	-82.0
Change in gross foreign currency balances due to:												
Foreign currency valuation adjustments											58.4	30.9
Transactions and transfers											247.0	-223.0
5. Total foreign currency assets (1+4)	3,305.9	2,503.7	2,687.5	2,885.9	3,907.8	3,305.9	3,186.6	2,838.0	2,375.9	2,503.7	885.7	-802.2
Change due to foreign currency valuation adjustments and SDRs											223.8	87.2
Transactions and transfers											661.9	-889.4
6. Foreign-held deposits	1,741.9	2,164.0	1,362.2	1,539.9	1,861.3	1,741.9	1,696.4	1,708.2	1,608.2	2,164.0	395.8	422.1
In commercial banks	1,741.9	2,164.0	1,358.7	1,536.4	1,854.5	1,741.9	1,696.4	1,700.4	1,606.2	2,164.0		
Foreign bank deposits and loans	837.9	1,101.7	654.6	755.1	997.1	837.9	735.6	701.2	581.8	1,101.7		
Nonresident deposits	904.0	1,062.3	704.3	781.3	857.4	904.0	960.8	999.2	1,024.4	1,062.3		
In Bank of Israel (excl. Patach)	—	—	3.5	3.5	6.8	—	—	7.8	2.0	—		
7. Net foreign currency assets (5-6)	1,564.0	339.7	1,325.1	1,346.0	1,236.5	1,564.0	1,490.2	1,129.8	767.7	339.7	489.9	-1,224.3

Net foreign currency assets plummeted from \$ 1.6 billion to \$ 340 million during 1974. This development, which followed a rapid and continuous growth in the past few years, was due chiefly to the heavy depletion of the country's foreign currency assets in the first ten months of 1974 and the swelling of the banking system's foreign liabilities in the last quarter, reflecting the efforts of the commercial banks and the government to bolster the country's reserve position.

## 7. FOREIGN CURRENCY DEBT<sup>8</sup>

Israel's foreign currency liabilities continued to swell in 1974, the outstanding balance moving up from \$ 5.1 billion and \$ 4.1 billion at the end of 1973 and 1972 respectively to \$ 6.25 billion.<sup>9</sup> In money terms this was the biggest rise ever recorded, but it loses some of its significance in real terms, when allowance is made for the rampant world inflation.<sup>10</sup>

The grave deterioration in Israel's balance of payments—the growth of the current deficit and the diminished possibility of financing it from convenient sources—led to an increase in foreign debts outstanding and a sizable depletion of reserves held at the central bank, with a consequent jump in net foreign liabilities. The decrease in reserves plus the rise in outstanding foreign indebtedness totalled \$ 1.8 billion in 1974, as against approximately \$ 500 million in 1973 and \$ 158 million in 1972. Another negative repercussion of the eroding balance of payments position is the mounting pressure of the debt servicing burden in the immediate future. This has been aggravated by the higher average rate of interest payable on the foreign debts and the shortening of the maturity schedule: the weight of long-term loans declined in 1974 to 86 percent and that of short-term debts doubled to about 9 percent to stand at over \$ 500 million, triple the 1973 figure. This change in the maturity structure will have a crunching effect: an estimate based on existing loan contracts places principal repayments in 1975 at \$ 968 million,<sup>11</sup> well above the

<sup>8</sup> The economy's foreign currency debt is not identical with its external debt, which also includes Israeli currency liabilities abroad, balances in clearing accounts, foreign investment in Israel, and deposits of foreign nationals in Israeli banks.

<sup>9</sup> The increase in foreign currency liabilities includes currency revaluations but not some of the other adjustments; hence it does not completely correspond to the change in loans as shown in the balance of payments.

<sup>10</sup> A rise in foreign prices actually reduces the amount of real resources which an economy must forgo in order to finance its external debt. Assuming that other factors remain constant, this enables the borrowing country to finance its debt by a smaller quantitative increase in exports or a smaller decrease in imports.

<sup>11</sup> The prognosis of principal repayments has always fallen short of actual outlays, mainly

Table V-12

## ISRAEL'S FOREIGN CURRENCY DEBT, BY REPAYMENT DATE, 1967-74

(\$ million)

	1967	1968	1969	1970	1971	1972	1973	1974
	<b>Repayment date</b>							
Up to one year	198	301	244	398	475	434	549	968
Thereof: Short-								
term loans	78	92	82	115	183	187	187	564
One to two years	141	135	195	195	224	263	329	504
Two to three years	82	114	135	174	202	241	351	423
Three to four years	87	112	122	136	159	268	327	439
Four to five years	85	110	109	117	192	238	369	481
Total	<b>1,556</b>	<b>1,902</b>	<b>2,121</b>	<b>2,622</b>	<b>3,430</b>	<b>4,081</b>	<b>5,093</b>	<b>6,250</b>
	<b>Percentage distribution by repayment date</b>							
Up to one year	12.7	15.8	11.5	15.2	13.9	10.6	10.8	15.5
Thereof: Short-								
term loans	39	31	34	39	39	43	34	58
One to two years	9.0	7.1	9.2	7.4	6.5	6.4	6.5	8.1
Two to three years	5.3	6.0	6.4	6.6	5.9	5.9	6.9	6.8
Three to four years	5.6	5.9	5.7	5.2	4.6	6.6	6.4	7.0
Four to five years	5.5	5.8	5.1	4.5	5.6	5.8	7.3	7.7
Five years or more	61.9	59.3	62.0	61.1	63.5	64.6	62.1	55.0
Total	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
	<b>Cumulative percentage distribution</b>							
Up to one year	12.7	15.8	11.5	15.2	13.9	10.6	10.8	15.5
Up to two years	21.7	22.9	20.7	22.6	20.4	17.0	17.3	23.6
Up to three years	27.0	28.9	27.1	29.2	26.3	22.9	24.2	30.4
Up to four years	32.6	34.8	32.8	34.4	30.9	29.5	30.6	37.4
Up to five years	38.1	40.6	37.9	38.9	36.5	35.3	37.9	45.1
Five years or more	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

entire net capital import of the private sector in 1974.

A classification of the loans by repayment period shows that 45 percent will fall due within five years; this compares with 38 percent at the end of 1973 and 35 percent at the end of 1972. This adverse change is mostly explained by the jump in short-term indebtedness, which will account for 58 percent of the payments due next

because of the cashing in of Independence and Development (State of Israel) Bonds ahead of maturity and the redemption of short-term loans for more than 90 days but less than one year in the same year they were received. In 1973 total repayments in the coming year were forecast at \$ 549 million, while they actually came to \$ 756 million; in the previous year the figures were \$ 434 million and \$ 607 million respectively. Hence the actual outlay in 1975 may very likely exceed \$ 1 billion.

Table V-13

## INDICATORS OF THE DEBT SERVICING BURDEN, 1967-74

(\$ million)

	1967	1968	1969	1970	1971	1972	1973	1974
(1) Interest payments	86	92	109	133	147	180	261	403
(2) Principal payments	169	229	252	292	330	432	420	469
(3) Total debt servicing	255	321	361	425	477	612	681	872
(4) Exports of goods and services	930	1,132	1,265	1,361	1,814	1,129	2,654	3,436
(5) Unilateral transfers	521	435	450	649	765	1,051	2,173	1,633
(6) Ratio (3/4) (%)	27.4	28.4	28.5	31.2	26.3	28.7	25.7	25.4
(7) Ratio (3/[4+5]) (%)	17.6	20.5	20.9	21.1	18.5	19.2	14.1	17.2

year on account of principal.<sup>12</sup> The share of liabilities payable within two to five years also rose.

Together with the heavier principal repayments, the average rate of interest payable on foreign currency debts rose in 1974, a result of the increased weight of short-term obligations, which carry a relatively high interest, and the upping of interest rates in the international money market over the past two years. Consequently, Israel's interest outlay reached \$ 403 million in 1974, up sharply from the \$ 262 million expended in 1973 and \$ 180 million in 1972. The average rate on long-term liabilities (excluding State of Israel Bonds) reached 4.9 percent in 1974, with that on new loans (excluding Bonds and foreign military credits) coming to fully 10 percent. Interest on medium-term debt averaged 9.6 percent, rising to 11.2 percent on new loans. Taking long- and medium- term loans together (apart from Bonds), the average rate was 5.4 percent, compared with 5.1 and 4.9 percent in 1973 and 1972 respectively. After adjusting for the advance in world prices, however, this nominal increase turns into a decline.

One conventional indicator of the pressure of an economy's debt servicing burden is the proportion of foreign currency receipts on current account allocated to this item. Since 1970 the ratio of debt servicing to export proceeds has drifted

<sup>12</sup> The change in the maturity schedule in the year reviewed was similar to that in 1970, when an attempt was made to bolster foreign currency reserves. Short-term indebtedness rose steeply, bringing up the proportion falling due within one year to 15.2 percent, roughly the same as in 1974.

Table V-14

ISRAEL'S FOREIGN DEBT, BY CURRENCY, 1972-74<sup>a</sup>

(\$ million)

	1972		1973		1974	
	\$ m.	Percent of total	\$ m.	Percent of total	\$ m.	Percent of total
<b>Total foreign debt</b>	<b>3,985</b>	<b>100.0</b>	<b>4,995</b>	<b>100.0</b>	<b>6,210</b>	<b>100.0</b>
In dollars	3,291	82.6	4,074	81.6	5,043	81.2
In sterling	78	2.0	85	1.7	85	1.4
In DM	583	14.6	763	15.3	1,001	16.1
In other currencies	33	0.8	73	1.5	81	1.3
<b>Direct government debt</b>	<b>3,092</b>	<b>100.0</b>	<b>3,831</b>	<b>100.0</b>	<b>4,762</b>	<b>100.0</b>
In dollars	2,560	82.8	3,176	82.9	4,051	85.1
In sterling	7	0.2	5	0.1	3	—
In DM	496	16.0	642	16.8	698	14.7
In other currencies	29	0.9	8	0.2	10	0.2
<b>Nongovernmental debt</b>	<b>893</b>	<b>100.0</b>	<b>1,164</b>	<b>100.0</b>	<b>1,448</b>	<b>100.0</b>
In dollars	731	81.9	898	77.1	992	68.5
In sterling	71	8.0	80	6.9	82	5.7
In DM	87	9.7	121	10.4	303	20.9
In other currencies	893	100.0	1,164	100.0	1,448	100.0

<sup>a</sup> Excluding liabilities to the World Bank denominated in various currencies.

downward, evidence of some easing of pressure on the balance of payments from this source.

In Israel it is customary to include unilateral transfers from abroad with foreign currency income on current account; save for 1974, this does not alter the general trend, though it reduces the absolute level. The change of trend in 1974 was caused by the relatively small growth of unilateral transfers, due *inter alia* to the rocketing of such receipts in the last quarter of 1973.<sup>13</sup> Thus Israel's external debt servicing burden did not change greatly between 1973 and 1974, but the adverse developments in the maturity structure will make their impact felt in 1975, significantly augmenting principal and interest payments.

Direct government debts were, at \$ 4,692 million, up \$ 831 million in 1974, compared with increases of \$ 738 million in 1973 and \$ 450 million in 1972. Other foreign currency liabilities rose \$ 326 million to stand at \$ 1,554 million. The

<sup>13</sup> See the discussion in section 3.

debt on account of the Independence and Development Loans added up to \$ 1.9 billion at the end of the year surveyed, and its weight in total foreign currency liabilities edged down from 34 percent in the two preceding years to 31 percent. Foreign military credits totalled \$ 1.2 billion, compared with \$ 906 million in 1973 and \$ 709 million in 1972. In 1974 these three loans made up about half the country's foreign currency debt, a notch below their 52 percent share in 1972-73.

During the past three years the currency distribution of the debt did not vary greatly. About 82 percent was in dollars, 1-2 percent in sterling, 15-16 percent in marks, and the remainder in other currencies. Any change in the currency distribution can normally be only marginal, since it depends on the composition of the debt in the preceding year, which consists mostly of long-term obligations that cannot be readily converted into other currencies, and on new borrowings in the current year, which are mainly from sources providing dollar loans. Nevertheless, in 1974 there were striking changes in the currency distribution of the debt of the public and private sectors, but since they were in opposite directions, they balanced themselves out, leaving the overall distribution virtually untouched. In direct government liabilities the percentage in dollars rose while that in marks declined; other liabilities showed an opposite development (and even more pronounced), the proportion in DM rising and that in dollars dipping. This was apparently connected with the urgent need to raise capital abroad in the face of shrinking foreign reserves while insuring private borrowings against exchange rate changes.

Foreign currency valuation adjustments, particularly for the appreciation of the DM against the dollar, added \$ 108 million to the total debt outstanding in 1974, compared with \$ 136 million the year before.