Bank of Israel
Comptroller's Office

Financial Statements for 2001

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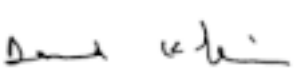
BANK OF ISRAEL
BALANCE SHEET AS OF DECEMBER 31, 2001 (TEVET 16, 5762)
(NIS million)

	Notes	31 December 2001	31 December 2000		Notes	31 December 2001	31 December 2000
Assets				**Liabilities and capital**			
Foreign exchange reserves	2	**102,367**	**93,606**	**Banknotes and coins in circulation**	8	**16,858**	**14,659**
International Monetary Fund	3	**875**	**474**	**International financial institutions**	9	**665**	**633**
Credit to the government	4	**5,514**	**5,946**	**Deposits of the government**	10	**4,259**	**7,120**
				Treasury bills deposit	11	**35,031**	**30,249**
Monetary loans	5	**802**	**781***	**Deposits of banking corporations**	12		
				Local-currency time deposits		45,062	50,586
				Other		19,154	15,314
Local-currency securities	6	**6,690**	**6,584**				
Other assets	7	**663**	**433***	**Other liabilities**	13	**2,972**	**2,795**
				Revaluation accounts	14	**6,659**	**960**
				Bank of Israel capital			
				Capital and general reserve	15	320	320
				Losses	16	(14,069)	(14,812)
Total		**116,911**	**107,824**	**Total**		**116,911**	**107,824**

* Reclassified

The accompanying notes are an integral part of the financial statements.



Dr. David Klein
Governor

Zvi Auerbach
Comptroller

March 6, 2002

BANK OF ISRAEL
PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDING DECEMBER 31, 2001
(NIS million)

	Notes	2001	2000*
Interest income from			
Foreign exchange reserves	19	3,890	4,544
Monetary loans		51	71
The government	20	1,959	1,747
Other	21	15	28
Total interest income		**5,915**	**6,390**
Interest paid			
To banks and the public	22	6,137	7,605
To the government	23	707	1,062
Other	24	84	93
Total interest paid		**6,928**	**8,760**
Net interest paid		**1,013**	**2,370**
Other financial income from (expenses on)			
Securities and derivatives	25	2,390	359
Exchange-rate differentials		73	(3,669)
Other	26	23	(73)
Total other financial income (expenses)		**2,486**	**(3,383)**
Profit (loss) on financial transactions		**1,473**	**(5,753)**
Expenses on printing banknotes and minting coins		**19**	**6**
Administrative and general expenses	27	**711**	**943**
Net profit (loss)		**743**	**(6,702)**

* Reclassified.

The accompanying notes are an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS FOR 2001

1. Accounting policies

a. General

The financial statements are presented in accordance with generally accepted accounting principles adapted for the special activity of a central bank, and taking into consideration the accounting and reporting guidelines for the European System of Central Banks issued by the European Central Bank.

The financial statements are presented in nominal NIS (New Israel Sheqalim). Income and expenses are entered on an accrual basis and are included in the balance-sheet items on which they accrued.

b. Foreign currency

Assets and liabilities denominated in foreign currency are translated into NIS at the representative exchange rates published by the Bank of Israel for the balance-sheet date.

Income and expenses in foreign currency are recorded in the Profit and Loss Account at the representative exchange rates prevailing on the value dates of the transactions.

From 2000 exchange-rate differentials are recorded in revaluation accounts. When balances are realized, realized exchange-rate differentials are transferred to the Profit and Loss Account.

Realization is calculated monthly; separate calculations are performed for all foreign-currency assets in each currency, and for all foreign-currency liabilities in each currency, and are made on the basis of the average cost of the balances. A balance of loss in the revaluation accounts is transferred to the Profit and Loss Account at the end of the year in which it occurred. Unrealized losses in one currency are not offset against unrealized profits in other currencies.

Accrued exchange-rate differentials to 31 December 1999 were defined as realized exchange-rate differentials.

Details of the exchange rates are as follows:

	31 December			Rate of change	
	2001	2000	1999	2001	2000
	(NIS)			(percent)	
$	4.4160	4.0410	4.1530	9.3	–2.7
Euro	3.9075	3.7628	4.1750	3.8	–9.9
Special drawing rights (SDR)[a]	5.5447	5.2626	5.7037	5.4	–7.7
First currency basket[b]	3.1980	3.9516	4.2711	6.2	–7.5
Currency basket[c]	4.4654	4.1726	4.4134	7.0	–5.5

[a] Based on a weighted 4-currency basket consisting of US$, €, ¥, and £.

[b] In effect until July 31, 1986, and consisting of: US$ 0.3500; £ 0.1295; and € 0.4667.

[c] In effect since May 2, 2000, and consisting of: US$ 0.6698; £ 0.0453; € 0.2493; and ¥ 7.2411. (The currency basket in effect from April 30, 1996, to May 1, 2000, consisted of: US$ 0.6741; £ 0.0589; € 0.2282; and ¥ 6.5437.)

Details of the Consumer Price Index are as follows:

	31 December			Rate of change	
	2001	2000	1999	2001	2000
CPI[a]				(percent)	
November	171.1	168.7	168.5	1.4	0.1
December	170.9	168.5	168.5	1.4	0.0

[a] 1993 average = 100.

c. Securities

Tradable local- and foreign-currency securities are shown at market value on the balance-sheet date.

Unrealized profits arising from the difference between the market value of securities and their adjusted cost are included in the Revaluation Accounts item in the balance sheet; unrealized losses are taken at the end of the year to the Profit and Loss Account (see Note 14).

The adjusted cost of securities is their par value *plus* accrued interest, accrued CPI-indexation differentials, and the balance of the premium or discount. The premium or discount is applied from the time of the purchase of the security until its maturity.

Profit from securities includes interest income shown under the item 'Interest income from the government,' and under income from (expenses on) the realization of securities, and reduction in value at the end of the year which are shown under 'Income from securities and derivatives.'

d. International financial institutions

The International Monetary Fund (IMF)

The Bank of Israel's participation in the IMF *minus* its liability for participation is shown under assets in the item 'The International Monetary Fund' (see Note 3).

Special drawing rights (SDR) allocated by the IMF are shown under liabilities in the item 'International financial institutions' (see Note 9).

Other financial institutions

The Bank of Israel's participation in other international financial institutions consists of an initial participation in the capital of the international institutions and additional participation payments for increases in those institutions' capital. The Bank of Israel's participation in other international financial institutions is included under 'Other assets' according to the cost in the currency in which the participation was paid. Liabilities to international financial institutions are shown under liabilities in the item 'International financial institutions.'

The Bank of Israel participates in the following institutions:

IBRD (The International Bank for Reconstruction and Development)
IDA (The International Development Association)
IFC (The International Finance Corporation)
EBRD (The European Bank for Reconstruction and Development)

MIGA (The Multilateral Investment Guarantee Agency)
IDB (The Inter-American Development Bank)
IIC (The Inter-American Investment Corporation)

e. Buildings and equipment

Buildings and equipment are stated at cost net of cumulative depreciation. Depreciation is calculated by the straight-line method for the estimated useful life:

Buildings	—	from fifty to seventy years;
Vehicles	—	six and a half years;
Computers	—	four years;
Other equipment	—	ten years.

For purchases of more than NIS 34,000 per item, the cost of the equipment purchase is recognized as fixed property; for purchases under this amount the costs are recognized as general expenses.

f. Treasury bills deposit

The Treasury bills deposit reflects the par value (the redemption price) of Treasury bills held by the public *less* the balance of the discount from their date of issue. Treasury bills sold by the government to the Bank of Israel but not yet sold to the public are not included in this deposit.

The discount is the difference between the par value (the redemption price) of the Treasury bills and the proceeds of their sale to the Bank (the issue price). The discount is reduced by the compound interest method, based on the interest rate published by the Accountant-General in the Ministry of Finance at the time the series was issued.

Profits and losses arising from selling Treasury bills to the public are taken to the Profit and Loss Account when they are sold to or purchased from the public.

g. Employee pensions, severance pay, and vacation pay

The liability for employee pensions and severance pay is actuarially computed on an accrual basis which reflects the liability accrued to the date of the financial statements for pensions and severance pay payments to employees.

Provision for vacation pay is computed on the basis of vacation due accrued to the balance-sheet date.

h. Revaluation accounts

There are separate revaluation accounts for each item (currency, security), which are transferred to the Profit and Loss Account when the item is realized in whole or in part.

The balance of the loss in the Revaluation Accounts item is transferred to the Profit and Loss Account at the end of the year.

i. Derivative financial instruments

The Bank of Israel uses derivative financial instruments in its monetary and foreign exchange activities.

1. Activity in derivative financial instruments in Israel:

a) NIS/US$ swaps

NIS/*US*$ swaps implemented by the Bank of Israel with domestic banks are shown net, i.e., the balance of dollars to be received from the banks (translated according to the exchange rate on the balance-sheet date) *minus* the balance of NIS to be transferred to the banks. A debit balance is shown under the item 'Other assets' and a credit balance under 'Other liabilities.'

Interest income on these transactions is shown in the Profit and Loss Account under the item 'Interest paid to the banking corporations and the public.'

b) Purchase and sale options on the US$/NIS exchange rate

The balance of options to the date of the financial statement is shown in Note 18, 'Contingent liabilities and special commitments.'

Expenses arising from the exercise of options during the period of the statement, and expenses expected from their exercise in accordance with the representative exchange rate of the dollar on the balance-sheet date, *minus* income from the premium on the options, are given in the item 'Other financial income from (expenses on) securities and derivatives.' The income from the premium on options is spread evenly over the duration of the options using the straight-line method. Advance income on the premium *plus* expenses accrued due to the difference between the exercise rate and the representative dollar exchange rate on the balance-sheet date is included in the 'Other liabilities' item.

c) Future remittances of Treasury bills

The balance of the liability on Treasury bills for future remittance up to the date of the financial statement is given at par (redemption price) in Note 18, 'Contingent liabilities and special commitments.'

Receipts on account of future issues of Treasury bills is included in the balance sheet under 'Other liabilities.'

2. Derivative financial instruments in activities abroad:

a) Repurchase agreements (Repo), and Reverse repo

The balances of Repo and Reverse repo agreements are included in the balance sheet as 'Foreign exchange reserves.' In the Profit and Loss Account the results of the transactions are included in 'Interest income from foreign exchange reserves.'

b) Foreign-currency swaps

The transactions are shown at net value, i.e., the balance of future foreign-currency receipts (in one of the currencies) *less* future foreign-currency remittances (in the other currency). In the balance sheet the transactions are included in 'Foreign exchange reserves.' In the Profit and Loss Account the results of these transactions are included in 'Interest income from foreign exchange reserves'.

c) Futures

The balances of futures contracts at market prices on the date of the financial statement are given in Note 18, 'Contingent liabilities and special commitments.'

In the Profit and Loss Account the change in the interest rate in the contracts is given under 'Other financial income from (expenses on) securities and derivatives.'

j. Transfer of profits

In accordance with the Bank of Israel Law, 5714–1954, the Bank must transfer its net profits to the government within sixty days of the end of each business year. Since the Bank incurred losses in past years, the profits in 2001 have been offset against the accrued losses, as will be future profits.

k. Matched timing

Local-currency income from the government on account of government securities is taken to the Profit and Loss Account on an accrual basis. Accrued income from government securities not yet received in cash from the government is deducted from profit to be paid to the government in years when profit is transferred, or is added to the balance of loss in years when there is no transfer of profit to the government. This income is added to profit transferred to the government only in years when such transfer actually takes place.

2. Foreign exchange reserves

The currency composition of the Bank of Israel's reserves matches the economy's import-financing and debt-servicing needs. The Bank of Israel thereby reduces the purchasing-power exposure of the reserves to changes in cross rates, and thus to some extent hedges against the exchange-rate risk of Israel's external debt.

This item consists of:

	31 December		31 December	
	2001	2000	2001	2000
	(NIS million)		($ million)	
Tradable securities[a]	90,091	92,137	20,401	22,800
Short-term deposits	24,721	11,562	5,598	2,861
Demand deposits	1,341	787	304	195
Derivative financial instruments[b]	(13,786)	(10,880)	(3,122)	(2,692)
Total	**102,367**	**93,606**	**23,181**	**23,164**

[a] At their market value (see note 1.c).

[b] Derivative financial instruments are shown net, i.e., future foreign-currency assets *minus* future foreign-currency liabilities (see note 1.i.2).

3. The International Monetary Fund (IMF)

The balance with the IMF (the reserve tranche) consists of the foreign-currency payment made by Israel to the Fund and constitutes part of the quota allocated to Israel.

The quota in the IMF
Each member country is allocated a quota which determines the basis of that country's financial and organizational ties with the Fund. The quota is related to the country's economic situation (national income, exports, balance of payments, level of the reserves) and determines its voting rights. Part of the quota is deposited in the country's central bank in notes and deposits indexed to Special Drawing Rights, and part (called the reserve tranche) is transferred to the Fund in foreign currency, and can be withdrawn.

Up to 1998 Israel drew its entire foreign-currency payment, putting up against these withdrawals a non-interest-bearing deposit in favor of the Fund. In 1999 the Fund increased members' participation, and Israel's rose by SDR 262 million. The foreign-currency payment for this increase, SDR 66 million, was deposited in the Fund, and has not been withdrawn.

The IMF financial transaction plan
In October 1999 Israel joined the group of countries which participate in financing the Fund's operational budget. The operational budget is one of the mechanisms through which the Fund makes foreign-currency loans available to member countries in need of such loans. Participation in the operational budget increases Israel's reserve tranche, against a reduction in the Fund's deposits in the Bank of Israel. In 2001 the balance of Israel's reserve tranche increased by SDR 67.4 million due to the operational budget.

Loan repayments are divided between countries whose reserve tranche/quota ratio is higher than the average ratio of all the Fund's member countries which participate in its operational budget.

This item consists of:

	31 December		31 December	
	2001	2000	2001	2000
	(NIS million)		(SDR million)	
International Monetary Fund (IMF) quota	5,149	4,886	928	928
minus liability for the quota[a]	4,274	4,412	771	838
Total[b]	**875**	**474**	**157**	**90**

[a] The balance of the liability to the IMF is in notes and deposits.
[b] The surplus of the reserve tranche over the 'basic sum' bears interest at a rate set by the IMF from time to time. Israel's 'basic sum' (on which no interest is paid) is SDR 33 million. The annual rate of interest on 31 December 2001, was 2.2 percent (on 31 December 2000, it was 4.3 percent).

4. Credit to the government

Credit to the government consists mainly of long-term advances. These advances to the government were made until 1988, and are currently as follows:

	31 December	
	2001	2000
	(NIS million)	
Long-term advances[a]		
Indexed[b]	4,455	4,816
Unindexed[c]	913	996
Credit for binational funds	146	134
Total	**5,514**	**5,946**

[a] The interest and indexation differentials for each year are due for payment on 31 December of that year. The principal is due to be paid in annual payments, the last of which will be in the year 2012.

[b] This credit is indexed to the first currency basket. NIS 4,454 million of it bears an interest rate of 8 percent, also indexed to that basket (the amount outstanding on 31.12.2000 was NIS 4,815 million).

[c] This credit bears interest at prime rate plus 2 percent. The average rate of interest during 2001 was 10.7 percent (13.4 percent in 2000).

5. Monetary loans

Under section 42 of the Bank of Israel Law, 5714–1954, the Bank of Israel may make monetary loans to the banking corporations.

In 2001 the average rate of interest on the monetary loans was 6.5 percent (in 2000, 8.9 percent).

The average rate of interest on the monetary loans on 31 December 2001 was 3.5 percent (on 31 December 2000 it was 7.7 percent).

6. Local-currency securities

This item consists of tradable government securities indexed to the last CPI known on the balance-sheet date. They are shown at market value (see Note 1.c).

This item consists of:

	31 December	
	2001	2000
	(NIS million)	
Time to redemption from balance-sheet date		
Less than one year	812	1,431
Between one and two years	832	393
Between two and three years	889	651
Between three and four years	1,366	803
Between four and five years	179	1,168
Between five and seven years	772	400
Seven years or longer	1,840	1,738
Total	**6,690**	**6,584**

The yield to maturity on the local-currency securities portfolio on 31 December 2001 was 3 percent, and the portfolio's average period to maturity was 4.5 years (on 31 December 2000 the yield to maturity was 6.1 percent, and the average period to maturity was 4.4 years).

7. Other assets

This item consists mainly of:
a. Participation in international financial institutions (see Note 1.d);
b. Net balance of NIS/US$ swaps (in 2000 this was shown under 'Other liabilities' (see Notes 1.*i*.1(a) and 18);
c. Loans to employees;
d. Buildings and equipment net of cumulative depreciation (see Note 1.e);
e. Other loans (in 2000 these were shown together with the monetary loans under 'Loans').

8. Banknotes and coins in circulation

This item consists of:

	31 December, 2001		31 December, 2000	
	Quantity	NIS	Quantity	NIS
	(million)		(million)	
Banknotes in circulation				
NIS 20	21	424	21	424
NIS 50	43	2,135	42	2,079
NIS 100	86	8,622	76	7,599
NIS 200	24	4,833	19	3,778
Coins in circulation	**–**	**809**	**–**	**744**
Other	**–**	**31**	**–**	**31**
Commemorative coins	**–**	**4**	**–**	**4**
Total		**16,858**		**14,659**

9. International financial institutions

This item consists of:

	31 December	
	2001	2000
	(NIS million)	
Special Drawing Rights allocated[a]	593	564
Liabilities to international financial institutions[b]	72	69
Total	**665**	**633**

[a] Special drawing rights (SDR) are money which member countries of the International Monetary Fund (IMF) have undertaken to buy from it. The Fund allocates SDRs to member countries relative to the size of their quotas. To date Israel has been allocated SDR 106.4 million.
[b] Liabilities in bills or deposits to the following institutions: IDB, MIGA, EBRD, IDA, IBRD (see note 1.d).

10. Deposits of the government

Government deposits comprise deposits for financing its budgetary activity and other deposits.

Government deposits for financing the budget
These are defined as deposits that the government may use to finance its budgetary and extra-budgetary activity and, accordingly, to which section 45(b) of the Bank of Israel Law, 5714-1954, applies. Financial movements arising from government budgetary and extra-budgetary activity in Israel and abroad and financial movements with the Bank of Israel are recorded in this item.

Other deposits
Other deposits include a bond-price stabilization local-currency deposit and various foreign-currency deposits. The bond-price stabilization deposit represents the proceeds from the purchase at source of government securities by the Bank of Israel in order to stabilize prices on the Tel Aviv Stock Exchange (TASE). In accordance with an agreement with the Ministry of Finance, the proceeds are placed in a special deposit on behalf of the government, but may not be used to finance government expenses. At the request of the Ministry of Finance the bond-price stabilization arrangement was ended in January 1993, and the deposit is being drawn down gradually against the redemption of such bonds purchased in the past. The redemption of these bonds will end in the year 2009.

This item consists of:

	31 December		31 December	
	2001	2000	2001	2000
	(NIS million)		($ million)	
Deposits for budget financing				
Local currency[a]	**(14,951)**	**(14,162)**		
Foreign currency				
Borrowing under US government guarantee[b]	16,101	14,224	3,646	3,520
US government economic aid[b]	2,394	5,048	542	1,249
Current deposit	389	1,235	88	306
Total	**18,884**	**20,507**	**4,276**	**5,075**
Total deposits for budget financing	**3,933**	**6,345**		
Other deposits				
Bond-price stabilization local-currency deposit[a]	201	241		
Other foreign-currency deposits	100	446	23	110
Total other deposits	**301**	**687**		
Accrued interest on government deposits	**25**	**88**		
Total	**4,259**	**7,120**		

[a] Local-currency government deposits bear (when in debt) or pay (when in credit) interest at prime. The average prime rate in 2001 was 8.4 percent (in 2000 it was 10.9 percent).

[b] Government foreign-currency deposits derived from borrowing under US government guarantee or from US government economic aid earn interest at the rate paid on US Treasury bills with an average of 6 months to maturity. The rate of interest on 31 December 2001, was 1.8 percent (on 31 December 2000 it was 6.2 percent).

11. Treasury bills deposit

The Short-Term Loan Law, 5744–1984, authorizes the government to issue bonds to be sold only to the Bank of Israel; the Bank, in carrying out its functions, would sell them to and buy them from the public to reduce or expand the money supply, respectively. The government, however, may not use the proceeds of sales of bonds to the Bank of Israel for anything apart from repaying the loan in accordance with this Law or paying the interest on it. Hence the proceeds of the sale of Treasury bills to the public and other activities connected with Treasury bills are dealt with in a special account for such activities only.

The Treasury bills deposit includes accrued interest of NIS 1,356 million (in 2000, NIS 1,441 million).

12. Deposits of banking corporations

a. Local-currency time deposit

The Bank of Israel receives local-currency time deposits from the banking corporations. The deposits are allocated by auction for periods of a day, a week, or a month. They are not considered liquid assets for purposes of the banking corporations' reserve requirements.

This item consists of:

	31 December	
	2001	2000
	(NIS million)	
Daily deposits	12,000	11,500
Weekly deposits	9,000	19,000
Monthly deposits	24,000	20,000
Total	**45,000**	**50,500**
Accrued interest on deposits	62	86
Total	**45,062**	**50,586**

The average rate of interest on time deposits in 2001 was 6.9 percent (in 2000 it was 9.4 percent).
The average rate of interest on the balance of deposits on 31 December 2001, was 4.7 percent (on 31 December 2000 it was 8.2 percent).

b. Other deposits

Banks' other local-currency deposits in the Bank of Israel serve as liquid assets against residents' local-currency and foreign-currency deposits. The reserve requirement ranges from 0 percent to 6 percent, according to the term of the deposit.

Foreign-currency demand deposits serve as liquid assets against nonresidents' foreign-currency deposits.

Secondary foreign-currency reserve-requirement deposits serve as liquid assets against residents' and nonresidents' foreign-currency deposits.

The secondary reserve requirement against the public's foreign-currency deposits is 10 percent. At least half of this, i.e., 5 percent, is deposited in the Bank of Israel, and the rest abroad. The Bank of Israel pays interest on the secondary foreign-currency reserve-requirement deposits at a rate similar to the interbank interest rate abroad.

This item consists of:

	31 December		31 December	
	2001	2000	2001	2000
	(NIS million)		($ million)	
Local-currency demand deposits	**8,381**	**6,214**		
Foreign-currency deposits				
Against foreign-currency reserve requirement				
Foreign-currency demand deposits	598	858	135	212
Secondary foreign-currency reserve requirement[a]	8,640	7,883	1,957	1,951
Total deposits against foreign-currency reserve requirements	**9,238**	**8,741**	**2,092**	**2,163**
Unrestricted deposits	1,535	359	348	89
Total foreign-currency deposits	**10,773**	**9,100**	**2,440**	**2,252**
Total	**19,154**	**15,314**		

[a] Deposits against the secondary foreign-currency reserve requirement include accrued interest of NIS 36 million (in 2000, NIS 147 million).

13. Other liabilities

This item consists mainly of:

a. Provision for employee pensions and severance and vacation pay;
b. Deposits of the U.S.–Israel Binational Industrial Research and Development Fund and a deposit of the U.S.–Israel Binational Science Fund;
c. Expected expenses against the exercise of options on the dollar/NIS exchange rate *less* advance payments;
d. Other creditors;
e. Net balance on NIS/US$ swaps transactions in years when the net balance is in credit (see Notes 1.*i*.1(a), 7 and 18. In 2000 the net balance was in credit).

14. Revaluation accounts

Revaluation accounts include unrealized profits from the revaluation of the following items (see also Note 1.b, 1.c, and 1.h):

This item consists of:

	31 December 2001	
	2001	2000
	(NIS million)	
Foreign-currency balances	5,247	22
Tradable local-currency securities[a]	530	–
Tradable foreign-currency securities	882	938
Total	**6,659**	**960**

[a] In 2000 a loss accrued, which was transferred to the Profit and Loss Account.

15. The Bank's capital

This item consists of:

	31 December	
	2001	2000
	(NIS million)	
Share capital	60	60
General reserve	260	260
Total	**320**	**320**

16. Losses

In accordance with the Bank of Israel Law, 5714–1954, the Bank must transfer its net profits to the government within sixty days of the end of each business year. Losses incurred by the Bank accrue in this item, and will be offset against future profits.

This item consists of:

	31 December	
	2001	2000
	(NIS million)	
Loss brought forward from previous year[a]	(15,966)	(9,264)
Income from the government to which the principle of matched timing applies	146	–
Profit (loss) in current year	743	(6,702)
Total loss	**(15,077)**	**(15,966)**
less matched timing balance[a]	1,008	1,154
Total	**(14,069)**	**(14,812)**

[a] The loss brought forward from 2000 was increased by NIS 533 million and the matched timing balance was increased by the same amount. This balance arose in previous years because the principle of matched timing was not applied to securities earmarked for liabilities for pensions, severance pay, and vacation pay.

17. Assets and liabilities by indexation base

	31 December 2001				31 December 2000*			
	In local currency	In foreign currency	Non-financial items	**Total**	In local currency	In foreign currency	Non-financial items	**Total**
	(NIS million)				(NIS million)			
Assets								
Foreign-currency balances[a]		102,367		**102,367**		93,606		**93,606**
Balance in the IMF		875		**875**		474		**474**
Credit to the government[b]	913	4,601		**5,514**	996	4,950		**5,946**
Monetary loans*	802			**802**	781			**781**
Local-currency securities[c]	6,690			**6,690**	6,584			**6,584**
Other assets[d]*	(5,778)	6,203	238	**663**	178	23	232	**433**
Total assets	**2,627**	**114,046**	**238**	**116,911**	**8,539**	**99,053**	**232**	**107,824**
Liabilities								
Banknotes and coins in circulation	16,858			**16,858**	14,659			**14,659**
International monetary institutions		665		**665**	1	632		**633**
Government deposits	(14,752)	19,011		**4,259**	(13,927)	21,047		**7,120**
Treasury-bills deposit	35,031			**35,031**	30,249			**30,249**
Deposits of banking corporations	53,443	10,773		**64,216**	56,800	9,100		**65,900**
Other liabilities[d,e]	2,813	159		**2,972**	8,307	(5,512)		**2,795**
Revaluation accounts	5,777	882		**6,659**	22	938		**960**
Bank of Israel capital			(13,749)	**(13,749)**			(14,492)	**(14,492)**
Total liabilities	**99,170**	**31,490**	**(13,749)**	**116,911**	**96,111**	**26,205**	**(14,492)**	**107,824**
Surplus assets (liabilities)	**(96,543)**	**82,556**	**13,987**	**–**	**(87,572)**	**72,848**	**14,724**	**–**

* Reclassified.

[a] These include NIS 3,064 million indexed to the US Consumer Price Index (NIS 3,069 million on 31 December 2000).

[b] Foreign-currency credit to the government includes long-term advances totalling NIS 4,455 million denominated in NIS and indexed to the exchange rate against the first currency basket (NIS 4,816 million on 31 December 2000).

[c] Local-currency securities indexed to the Consumer Price Index.

[d] NIS/$ swaps are shown in the balance sheet net, in accordance with the balance (see note 1.i.1). In 2001 the net balance was negative, and is therefore shown under “other assets” (in 2000 it was shown under “other liabilities”). This table shows dollars to be received in the “foreign currency” column (NIS 6,182 million on 31 December 2001; NIS 5,657million on 31 December 2000), and NIS to be paid in the “local currency” column (NIS 5,977 million on 31 December 2001; NIS 5,722 million on 31 December 2000), so that the balances of these items are negative.

[e] Other local-currency liabilities include NIS 25 million deriving from expenses expected on exercising US$/NIS exchange-rate options (NIS 9 million on 31 December 2000).

18. Contingent liabilities and special commitments

	31 December	
	2001	2000
	(NIS million)	
1. Contingent liabilities[a]		
Documentary credits and guarantees for government imports and exports		
Documentary credits	47	23
Guarantees	57	75
Other contingent liabilities		
Uncalled amounts for shares and participation in international financial institutions	3,589	3,271
2. Special commitments		
Derivative financial instruments in activity in Israel		
Currency swaps with domestic banks		
Future receipts of dollars[b]	6,182	5,657
Future payments of NIS[c]	5,977	5,722
$/NIS purchase options	1,148	1,014
$/NIS sales options	574	525
Future remittances of Treasury bills (at par) (price at redemption)	600	320
Derivative financial instruments in activity abroad		
Currency swaps and forward transactions		
Future receipts of foreign currency	1,082	3,899
Future payments of foreign currency	1,070	3,504
Repurchase agreements (Repo) and Reverse Repo (RRepo)		
Repo	18,294	13,917
Reverse Repo	4,512	2,702
Futures		
Sales commitments	2,736	531
Purchase commitments	452	554

[a] Several claims were made on the Bank of Israel. The Bank of Israel does not consider it necessary to make a special provision for these claims, as the chances that they will be upheld are slight.

[b] The balance of swaps on the balance-sheet date was $1,400 million ($1,400 million in 2000).

[c] Including interest of NIS 8 million accrued to the balance-sheet date (NIS 4 million in 2000).

19. Interest income from (interest paid on) foreign exchange reserves

This item consists of:

	Year to 31 December	
	2001	2000*
	(NIS million)	
Tradable securities[a]	3,621	4,086
Short-term deposits	585	541
Demand deposits	30	47
Derivative financial instruments[b]	(346)	(130)
Total	**3,890**	**4,544**

* Reclassified.

[a] Income from (expenses on) interest includes indexation differentials and premium reductions and discounts.

[b] Income from (expenses on) interest on derivatives is shown net.

20. Interest income from the government

This item consists of:

	Year to 31 December	
	2001	2000*
	(NIS million)	
Long-term advances		
Indexed	385	412
Unindexed	106	145
From binational funds	63	65
From government deposits	882	732
From local-currency securities	523	393
Total	**1,959**	**1,747**

* Reclassified.

[a] Government deposits bear (when in debit) or pay (when in credit) interest (see note 10).

21. Other interest income

This item consists of interest income from

a. The IMF;
b. Other loans.

22. Interest paid to the banks and the public

This item consists of:

	Year to 31 December	
	2001	2000*
	(NIS million)	
In local currency		
On banks' local-currency time deposits	3,219	4,327
on swaps	170	181
On Treasury bills deposit	2,328	2,579
On bank's deposits	4	3
In foreign currency		
On banks' deposits	416	515
Total	**6,137**	**7,605**

* Reclassified.

23. Interest paid to the government

This item consists of:

	Year to 31 December	
	2001	2000*
	(NIS million)	
In local currency[a]	20	30
In foreign currency	687	1,032
Total	**707**	**1,062**

* Reclassified.

[a] On the bond-price stabilization deposit (see note 10).

24. Other interest paid

This item consists mainly of interest paid:

a. To international financial institutions;
b. On deposits of the U.S.–Israel Binational Industrial Research and Development Fund and a deposit of the U.S.–Israel Binational Science Fund.

25. Income from (expenses on) securities and derivative financial instruments

This item consists of:

	Year to 31 December	
	2001	2000*
	(NIS million)	
Securities[a]		
In foreign currency	2,470	647
In local currency	0	(172)
Derivative financial instruments	(80)	(116)
Total	**2,390**	**359**

* Reclassified.

[a] Including income from the realization of securities and from decline in their value at the end of the year (see Note 1.c).

26. Other income (expenses)

This item consists of:

	Year to 31 December	
	2001	2000*
	(NIS million)	
In local currency	29	(71)
In foreign currency	(6)	(2)
Total	**23**	**(73)**

* Reclassified.

27. Administrative and general expenses

This item consists of:

	Year to 31 December	
	2001	2000
	(NIS million)	
Wages and general expenses[a]	488	448
Provision for employees' entitlements[b]	223	495
Total	**711**	**943**

[a] Including pensions.

[b] Including pension and vacation provisions. Pension provisions in 2000 included non-recurring costs arising from updates of actuarial assessments of pension liabilities.

EXPLANATORY REMARKS TO THE FINANCIAL STATEMENTS

1. MAIN DEVELOPMENTS

The main assets on the Bank of Israel's balance sheet are the foreign exchange reserves, accounting for 88 percent of the total balance sheet, and the main liabilities are the banks' time deposits and the Treasury bills deposit which together constitute 69 percent of the Bank's total liabilities. The main components in the Bank's income and expenses are receipts and payments of interest on these items, the realization of securities, and income from (or expenses on) exchange-rate differentials on the foreign exchange reserves.

The foreign exchange reserves, annual average, rose in 2001 in dollar terms by 6.4 percent, but were stable during the year. As a result of the depreciation of the NIS, the reserves increased in local-currency terms.

Interest rates worldwide fell in 2001, so that interest income from investment of the foreign exchange reserves were lower than in 2000. On the other hand, the drop in interest led to capital gains (due to the rise in bond prices) which exceeded the loss in interest income. Income from exchange-rate differentials together with the capital gains resulted in total income from the foreign exchange reserves, in local-currency terms, reaching NIS 13.7 billion, compared with NIS 0.7 billion in 2000. Only part of the exchange-rate differentials on the reserves were realized and entered in the Profit and Loss Account; the balance, i.e., the unrealized exchange-rate differentials, are included in the Revaluation Accounts item in the balance sheet.

The main instruments which the Bank of Israel has used to operate its monetary policy in the last few years were the banking corporations' local-currency time deposits with

Table 1
Exchange-Rate Differentials[a] on Foreign-Currency Balances, 2000–2001

(NIS millions, at current prices)

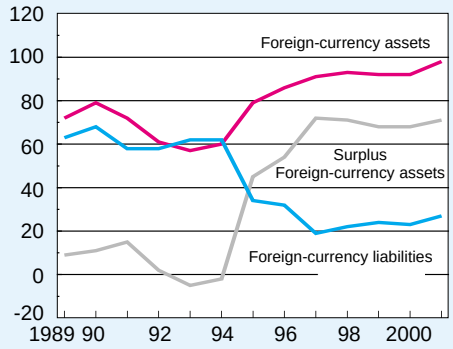
	2000	2001
Assets		
Foreign-exchange reserves	–4,336	7,387
Credit to the government—binational funds	–4	12
Other accounts—international financial institutions	–32	42
Liabilities		
Government deposits	572	–1,746
Banks' foreign-currency deposits	255	–874
International financial institutions	50	–35
Other liabilities—NIS/$ swaps	–156	525
Other liabilities—deposits of the binational fund	4	–13
Total	**–3,647**	**5,298**
Realized exchange-rate differentials	–3,669	73
Unrealized exchange-rate differentials	22	5,225

[a] Due to the adjustment of foreign-exchange balances to the rate of exchange.

the Bank, and Treasury bills.[1] In 2001, for the third year in succession, the downward trend of the rate of interest in Israel continued (Table 7), reducing the Bank of Israel's interest payments on these deposits from NIS 6.9 billion in 2000 to NIS 5.5 billion in 2001. The average balance of time deposits and the Treasury bills deposit increased in 2001. The increase in the maximum permitted sales of Treasury bills during the year enabled their sales to the public to rise, and time deposits fell by a similar amount.

The government's local-currency deposits have had a negative balance for several years, while its foreign-currency deposits have a positive balance larger than the negative one in local-currency deposits. The government's total deposits contracted by NIS 2.9 billion in 2001 from their level in 2000; the main decline, of about NIS 2 billion, occurred in foreign-currency deposits, while those in NIS went down by NIS 0.9 billion (i.e., the debit balance rose). The decline was due to the government's foreign-currency payments abroad and local-currency payments to the Bank of Israel, while in the domestic market the government absorbed money, thereby offsetting part of the fall in its deposits (Table 5). By using deposits which have accumulated from previous years, the government avoids having to borrow in the current year, but this use of the deposits is restricted as there is a legal limit to the amount of credit the Bank of Israel can grant the government. From the aspect of monetary policy it is better for the government to finance its budget each year than to accumulate balances in the Bank of Israel in some years and use them in others.

Figure 1
Foreign-Currency Assets, Liabilities, and Surplus Foreign-Currency Assets of the Bank of Israel,* 1989–2001



* Percent of balance sheet, end-of-year, at current prices.

The monetary base (banknotes and coins in circulation and the banks' demand deposits with the Bank of Israel) expanded very rapidly in 2001, by NIS 4.4 billion (Tables 3 and 5). In the first half of the year the government absorbed money, and in the second half, mainly towards the end of the year, it injected a significant amount, essentially because of the slowdown in tax revenues. Over the year as a whole the government absorbed NIS 4.3 billion; the Bank of Israel injected NIS 7.7 billion during the year.

As in the past, the Bank did not intervene in the foreign currency market, neither buying from nor selling to the public.

Banknotes and coins in circulation increased by NIS 2.2 billion in 2001, having fallen by NIS 0.9 billion in 2000. The rise in 2001 may have been one effect of Palestinian terrorist attacks which led to increased use of cash by Palestinians and Israelis trading with them.

The drop in interest rates in Israel and abroad contributed to the rise in the Bank of Israel's profit.

In 2001 the Bank of Israel's profit was NIS 0.7 billion, compared with a loss of NIS 6.7 billion in 2000. This sharp turnaround was due to the direct and indirect effects of the drop in interest rates in Israel and abroad. As a result of the decline in interest rates, the Bank's interest payments (mainly on time deposits and Treasury bills) went down faster than did its interest income (mainly interest on the foreign exchange reserves), significantly reducing the Bank's losses on interest payments from previous years' levels. Net interest

[1] The bank also uses other instruments, which are also shown in the financial statements: monetary loans, NIS/US$ swaps, and sales of dollar options, but these are small compared with the time deposits and the Treasury bills deposit.

Table 2
Indicators of the Bank of Israel Profit, 1990–2001

	Profit (loss)	Realized exchange-rate differentials[a]	Net foreign-currency assets end-of-year	Change in currency-basket exchange rate during year	Treasury bills and time deposits *minus* monetary loans 31 Dec	Average interest rates	
						Time deposits	Monetary loans
	NIS billion		*$ billion*	*percent*	*NIS billion*	*percent*	
	At current prices				*at current prices*		
1990	1.5	0.5	1.5	10.6	0		14.4
1991	1.9	0.8	2.0	11.2	–1		15.5
1992	1.7	0.6	0.3	16.3	–5		12.1
1993	1.3	–0.2	–0.8	6.3	–10		10.7
1994	1.8	0.4	–0.3	5.7	–8		12.7
1995	2.5	1.4	6.0	6.3	9		14.9
1996	–0.5	0.5	8.6	1.6	21	16.2	14.9
1997	–1.1	2.1	17.5	4.1	51	13.9	13.5
1998	10.9	13.1	18.4	20.4	63	11.9	11.5
1999	–8.7	–3.5	17.7	–3.2	73	12.2	11.8
2000	–6.7	–3.7	18.0	–5.5	80	9.4	8.9
2001	0.7	0.1	18.7	7.0	79	6.9	6.5

[a] Until 1999 all exchange-rate differentials were defined as realized.

payments in 2001 totaled NIS 1 billion, down from NIS 2.4 billion in 2000.

Although falling interest rates abroad reduced interest income from overseas investments, they led to a rise in bond prices abroad, i.e., to capital gains, which exceeded the drop in interest income.

The NIS depreciated against the currency basket by 7.0 percent in 2001, having appreciated by 5.5 percent in 2000. As the Bank has a surplus of assets over liabilities in foreign currency (98 percent of its assets are in or indexed to foreign currency, and only 27 percent of its liabilities), the depreciation increased the Bank's income from exchange-rate differentials. Although most of the exchange-rate differentials in 2001 remained unrealized, and were therefore not included in the Bank's profit, the modest realization that did take place resulted in income of NIS 0.1 billion, which is included in the Profit and Loss Account, whereas in 2000 exchange-rate differentials showed a loss of NIS 3.7 billion.

A change has been introduced in the presentation of the Profit and Loss Account for 2001, whereby income and expenses are shown by type, and not by balance sheet item.

The Bank of Israel's financial statements are presented in accordance with generally accepted accounting principles, adapted for the special activity of a central bank, taking into consideration the accounting rules of the European Central Bank. As a result, a change has been introduced in the presentation of the Profit and Loss Account for 2001, whereby income and expenses are shown by type, and not by balance-sheet item as in the past. Interest income and payments for all balance-sheet items are shown together, followed by income from (or expenses on) the realization of securities held by the Bank (in local and foreign currency) and from exchange-rate differentials, and other income (expenses).

Table 3
Composition of Changes in the Monetary Base and Foreign Reserves, 1998–2001

(current prices)

	1998	1999	2000	2001	2000 IV	2001 I	2001 II	2001 III	2001 IV
NIS million									
1. Change in monetary base (1) = (2 + 3 + 4 + 5)	242	3,927	311	4,364	–465	2,251	1,282	–1,900	2,731
Injection (+)/absorption (–)									
2. Government and National Institutions	1,901	4,067	–2,729	–2,611	5,719	–3,964	–1,184	677	1,860
3. Bank of Israel	–2,664	–365	2,729	7,675	–6,164	6,193	2,393	–2,511	1,600
4. Foreign-currency conversions at Bank of Israel	1,746	0	0	0	0	0	0	0	
5. Adjustments[a]	–741	225	311	–700	–20	22	73	–66	–729
$ million									
Banks' foreign-currency activity with the Bank of Israel									
6. Foreign-currency sales to Bank of Israel (6) = (8 – 9 – 7)	–492	0	0	0	0	0	0	0	0
7. Public-sector transfers to banks[b]	–163	–259	–345	–20	2	–44	5	–40	59
8. Change in deposits with Bank of Israel	–369	585	–462	91	38	468	–426	209	–160
9. Transfers to (–)/from (+) rest of world	286	844	–117	111	36	512	–431	249	–219
10. Adjustments[c]	–343	–197	–275	–216	–2	–42	27	–56	–145
Contribution to reserves									
11. Private sector[d] (11)=(9+10)	–57	647	–392	–105	34	470	–404	193	–364
12. Public sector[e]	2,399	–806	1,041	122	1,055	204	–363	1,212	–931
13. Change in reserves[f] (13)=(11+12)	2,342	–159	649	17	1,089	674	–767	1,405	–1,295

[a] Adjustments include: transfers from abroad by the National Institutions through the banks, defined as public-sector injection (in row 2). Government and Bank of Israel domestic foreign-currency receipts from and payments to the private sector (e.g., income tax receipts in foreign currency) do not change the monetary base, as they are transferred directly from the private sector to the government: on the one hand they are defined as government absorption and on the other they are defined as the private sector's contribution to the foreign reserves (without going via the Bank of Israel's trading-room floor).

[b] NIS/$ swaps and other domestic foreign-currency payments.

[c] Transfers from abroad by the public sector through the banks, e.g., by the National Institutions.

[d] Including income tax payments by the private sector in foreign currency.

[e] Transfers by the government and the National Institutions, and Bank of Israel income from the foreign reserves (interest income, capital gains and cross-rate differentials).

[f] Including the change in accrued interest on the foreign reserves.

2. MAIN ITEMS

a. The foreign exchange reserves

The foreign exchange reserves make up the largest part of the Bank of Israel's assets. At the end of 2001 the reserves totaled $ 23.2 billion, about 88 percent of all the Bank's assets. Changes in the reserves are caused by a variety of factors. The government receives aid from the US government, and in most of the last few years has borrowed abroad. Against these the government incurs foreign currency expenses in repaying debts and financing other expenditure abroad, so that its contribution to the reserves can be positive or negative. The commercial banks have foreign-currency deposits, most of which are intended to meet the reserve requirement, and some of which are unrestricted deposits. In the last few years the Bank of Israel has not bought foreign currency from nor sold it to the public, so that this factor has no effect on the size of the foreign exchange reserves, and a change in the banks' foreign-currency deposits in the Bank of Israel causes the same change in the reserves.[2] The bank receives income on the investment of the reserves abroad, and this income augments the reserves. The annual average of the foreign exchange reserves was 6.4 percent higher in 2001 than in 2000, but their end-year level was the same as that at the end of 2000.

The government withdrew about $ 1.3 billion from the foreign exchange reserves to make payments abroad for current expenses, interest, and loan repayments. In 2001 the government raised $ 1 billion abroad via a bonds issue, but it used this to finance expenses overseas, and therefore did not deposit it in its accounts with the Bank of Israel. At the end of the year part ($ 150 million) of the US economic aid was received.

The Bank of Israel's contribution to the foreign exchange reserves totaled $ 1 billion. Interest income and capital gains came to $ 1.5 billion, but the weakening of several other currencies against the dollar, and in particular that of the euro, gave rise to negative exchange-rate differentials of $ 0.3 billion. The rise of $ 0.2 billion in prices abroad of foreign-currency securities was not realized, and was therefore not recorded in the Profit and Loss Account. The private sector transferred abroad $ 0.1 billion of its foreign-currency deposits in the Bank of Israel.

The Bank's income from the foreign exchange reserves in NIS terms in 2001 amounted to NIS 13.7 billion, compared with income of NIS 0.7 billion in 2000. Interest income and capital gains totaled NIS 6.3 billion, but NIS 1.1 billion of this was offset by the strengthening of the US$ against other currencies. The weakening of the NIS against the US$ in 2001 was reflected in income of NIS 8.5 billion from (realized and unrealized) exchange-rate differentials.

The Bank of Israel invests the foreign exchange reserves mainly in tradable securities with a relatively short horizon,[3] to ensure an appropriate level of liquidity and to avoid the danger of wide swings in the value of the portfolio which could occur in the wake of fluctuations in the financial markets. The average horizon of the foreign reserves portfolio, which for several years was twelve months, was raised to sixteen months in 1999; this was a long-term strategic move based on findings of research carried out by the Bank which showed that the yield on investment with that horizon was expected to be higher over time, after taking the incremental risk into account.

[2] In the past the Bank of Israel intervened in the foreign-currency market (for instance, in 1995 and 1997 it had to buy foreign currency from the public), and this affected the size of the foreign exchange reserves.

[3] For a detailed review of the investment of the foreign exchange reserves see the 2001 Report of the Foreign Currency Department of the Bank of Israel.

The currency composition of the Bank of Israel's reserves matches the economy's import-financing and debt-servicing needs, thus reducing the purchasing-power exposure of the reserves to changes in cross rates, and to some extent hedging against the exchange-rate risk of Israel's external debt. Hence, changes in the value of and yield on the foreign reserves should be measured in terms of the same currency composition as their uses and not in terms of any specific currency.

The holding-period rate of return on the investment of the reserves, in terms of uses, was 6.4 percent in 2001; it was affected by the reduction in yields mainly in the short part of the yield curve, which resulted from the expansionary monetary policy pursued particularly in the US, but also in Europe, against the background of the slowdown in economic activity. Falling yields were reflected by rising government bond prices. The

Table 4
Foreign Reserves—Total, Income, and Yields, 1999–2001

				Rates of change (percent)	
	1999	2000	2001	2000	2001
Total foreign reserves					
$ million					
End of year	22,515	23,164	23,181	3	0
Annual average	21,955	22,156	23,569	1	6
Income					
NIS million					
Total	**–510**	**715**	**13,655**		
Interest and capital gains	3,069	5,050	6,268		
NIS/$ exchange rate differentials	–190	–2,490	8,500		
Cross-rate differentials ($/other currencies)	–3,389	–1,845	–1,113		
$ million					
Total	**–83**	**780**	**1,194**		
Interest and capital gains	743	1,248	1,465		
Cross-rate differentials ($/other currencies)	–826	–468	–271		
Yields					
Percent					
In terms of NIS[a]—total	–0.8	1.8	11.8		
Interest and capital gains	3.2	6.9	6.4		
NIS/$ exchange-rate differentials	–3.9	–4.8	5.1		
In terms of euro[a]—total	15.3	12.9	10.6		
In terms of $[a]—total	–0.6	4.6	5.1		
Interest and capital gains	3.2	6.9	6.4		
In terms of use[b] of foreign reserves[a]	**3.3**	**6.8**	**6.4**		
Market return[c]	**3.2**	**6.8**	**6.1**		

[a] Yields (annual, compounded daily) refer to income from the foreign reserves, including profit or loss arising from changes in market prices.
[b] Geographical composition of imports, and the currency composition of debt servicing.
[c] In terms of use of foreign reserves (for international comparison).

arbitrariness of measuring yield in terms of any specific currency is highlighted by comparing the yield in dollar terms, 5.1 percent, with that in terms of the euro, 10.6 percent, and by the high volatility of the yields in terms of both these currencies evident for years (Table 4). The yield in terms of NIS was 11.8 percent, compared with 1.8 percent in 2000. The yield in 2001 reflected the weakening of the NIS against the currency composition of the basket of uses.

The yield on investing the reserves can be compared with the 'market yield' by means of the yield on an appropriate benchmark. The benchmark is a hypothetical portfolio which consists of various assets reflecting the Bank's long-term investment strategy. The average horizon of the investments in the benchmark is sixteen months, and the benchmark also satisfies other criteria, such as liquidity and credit risk. Market yields of the assets in each currency are weighted according to that currency's share in the basket of uses. The actual yield in 2001, 6.4 percent, was higher than that of the benchmark (6.1 percent). In managing the portfolio, the Bank of Israel deviates only marginally, if at all, from the currency composition of uses, so that this factor has a relatively small effect on the yield in terms of uses. The main contribution of investment decisions arises from the focus on keeping the average horizon of the portfolio to about sixteen months, and on determining the composition of the assets in it.

b. Government accounts

In accordance with the law, the Bank of Israel is the government's sole banker in Israel. Hence, the government holds all its local-currency accounts and some of its foreign-currency accounts in the Bank of Israel. It is permitted to hold accounts abroad not via the Bank of Israel.

Long-term advances

Long-term advances are loans which were granted to the government in the distant past. They bear interest, and most of them are indexed to the NIS exchange rate against the first currency basket. The government paid NIS 0.5 billion in 2001 in interest on these advances, and NIS 0.4 billion of principal.

Exchange-rate differentials on the long-term advances are paid when the exchange rate of the NIS against the first currency basket at the end of a year is higher than the last exchange rate for which the government paid such differentials. In 1999 and 2000 the NIS appreciated against the first currency basket, and in 2001 it depreciated against the basket. The exchange rate at the end of 2001 did not reach its level at the end of 1998, so that in 2001, as in 1999 and 2000, no exchange-rate differentials were due.

Government deposits

Government deposits divide into three categories: (a) deposits for budget financing, (b) other deposits, and (c) the Treasury bills deposit.

Deposits for budget financing, both local-currency deposits and foreign-currency deposits, are defined as deposits which the government can use to finance budgetary activities, and which are therefore covered by section 45b of the Bank of Israel Law, 5714–1954. The government's deposits were classified in 1997 by the Accountant-General, and the Bank of Israel operates according to that classification.

The local-currency deposits for budget financing consist of all the local-currency deposits except for (a) the deposit to stabilize bond prices (see Note 10 to the financial statements, above) and (b) the Treasury bills deposit. Since 1994 the local-currency

deposits have had significant negative balances,[4] on which the government pays interest at prime (when the balances are in credit, the government receives interest at prime from the Bank of Israel). The foreign-currency deposits for financing the budget include the deposit of economic aid received from the US once a year, the deposit of capital raised some years ago under the US government guarantee, and a current deposit. On the first two of these deposits (i.e., economic aid and money borrowed under US government guarantee), the Bank of Israel pays interest at the rate paid on US Treasury bills with six months to maturity; no interest is paid on the current deposit.

Table 5
Government Deposits with the Bank of Israel, 1999–2001

(NIS million, current prices)

	1999	2000	2001
End-year balances			
Government deposits for budget financing			
Local-currency deposits	–13,645	–14,162	–14,951
Foreign-currency deposits	19,195	20,507	18,884
Total government deposits for budget financing	**5,550**	**6,345**	**3,933**
Other deposits[a]	1,173	775	326
Total	**6,723**	**7,120**	**4,259**
Net change in government deposits	**–9,329**	**397**	**–2,861**
Sources of change			
Government contribution to foreign reserves[b]	–3,443	–517	–5,811
Government injection	–3,139	3,493	4,341
Government–Bank of Israel financial flow[c]	–2,783	–2,653	–1,369
Adjustments[d]	36	74	–22

[a] Including the local-currency deposit to stabilize bond prices, another deposit in foreign currency, and interest accrued on government deposits (see note 10 on Deposits of the Government).

[b] Government income and expenses abroad, loans received and loan repayments abroad.

[c] Interest payments and redemption of government bonds held by the Bank of Israel; commission from the government; interest payments, repayment of principal, and payment of indexation differentials on credit to the government interest payments by the Bank of Israel on government deposits (in local and foreign currency); cross-rate differentials on government foreign-currency deposits; and transfer to the government of Bank of Israel's profit.

[d] Including accrued interest on government deposits to the end of the year; interest payments by the government on credit from the Bank of Israel for binational funds (these payments are included under 'Government injection,' but in this table they are also included under 'Government–Bank of Israel financial flow'); bond redemptions by tourists in Israel (these redemptions reduce the government's local-currency deposits, but are not included in 'Government injection').

The balance of the deposits used for financing the budget is determined by the Accountant-General according to current budget-financing requirements, with the government's borrowing requirements, and with tax revenues. In 2001 the government reduced the balance of the budget-financing deposits by NIS 2.4 billion, which enabled it to cut its borrowing from the public by the same amount. Reducing the deposits used for financing the budget so that they come closer to the level needed to finance the government's current budgetary activity will restrict the ability of the Ministry of Finance to continue using them, and any increase in the budget deficit will have to be met by extra borrowing to finance government activity.

[4] Except for a few days in 2000 when they were actually in credit.

The foreign-currency component of the government's budget-financing deposits, in local-currency terms, fluctuates with changes in the NIS exchange rate: depreciation increases them and appreciation reduces them in NIS terms. As the balance of the government deposits contracted in 2001, future appreciation of the NIS is likely to oblige the government to borrow.

The credit balance of the foreign-currency deposits is larger than the debit balance of the local-currency deposits, so that in total the government deposits for budget financing have a positive balance. Managing the government's accounts in this way, with a large debit balance in some accounts and a large credit balance in others, is abnormal. Moreover, the government could have reduced its expenses by converting its foreign-currency accounts into local currency, since in the last few years the prime interest rate in Israel was higher than the sum of the interest rate paid on the government's foreign-currency deposits and the rate of depreciation. On the other hand, as the government makes payments in foreign currency, holding some of its deposits in foreign currency reduces to some extent the currency risk incurred by holding local-currency balances to meet foreign-currency payments.

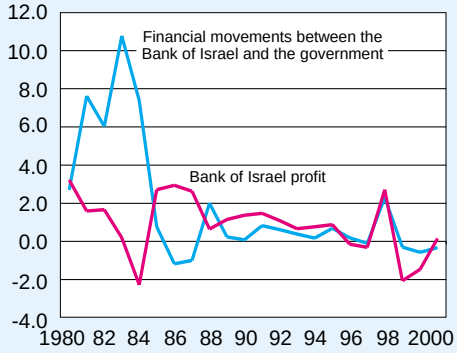
The government has two different definitions for the deposit of the capital raised under US government garauntees: 'extra-budgetary deposit,' and 'deposit for financing the budget.'

This method of financial management has another implication: the Ministry of Finance defines the deposit of the capital raised under US government guarantees as extra-budgetary, and so, in line with the rules it has determined, income and expenses related to this deposit are not included in the budget statistics of income, expenses, and deficit.[5] Thus, for example, the government took some of the guarantees deposit to make loans to the private sector, on which it receives interest from that sector. Interest payments abroad by the government on the part of the guarantees which it lent to the private sector are not recorded as expenses in the budget. Only if there is a difference between the interest the government pays abroad and the interest it receives from the private sector is the difference recorded in the budget as a government income or expense. The Ministry of Finance also considers the Bank of Israel's interest payments on the guarantees deposit as extra-budgetary income, and does not record them in the budget as income.

For several years the government used the money raised abroad under US guarantees, and the interest payments it made on this money (except for $ 1.9 billion lent to the private sector) are a government expense which should be included under interest paid by the government. The government should adjust the classification of its statistical methods and its accounts to conform with the economic substance of its activity.

The government's local-currency budget-financing accounts declined by NIS 0.8 in 2001. During the year it absorbed some NIS 4.3 billion from the public, which offset some of the reduction in the deposits (most of the absorption took place in the first half of the year, with some injection of money in the last few months of the year). However, the government financed some of its expenses abroad from its local-currency accounts, thus reducing those deposits. The annual average debit balance was NIS 10.5 billion in 2001, compared with a debit balance of

Figure 2
Total Financial Movements between the Bank of Israel and the Government, and the Bank of Israel Profit,* 1980–2001



* Percent of GDP, at current prices

[5] The Ministry of Finance has two different definitions for the same deposit, 'extra-budgetary deposit,' and 'deposit for financing the budget,' and it uses whichever definition is appropriate to its current requirements.

NIS 6.7 billion in 2000 (the debit balance declined in the middle of 2001, but started increasing again towards the end of the year).

The government receives or pays interest at prime on the credit and debit balances in its deposits. The debit in its local-currency deposits rose faster than the rate at which interest fell, so that total interest charged on these accounts in 2001, about NIS 0.9 billion, was higher than in 2000 (when it was NIS 0.7 billion). The foreign-currency deposits for financing the budget declined by NIS 1.6 billion ($ 0.8 billion; see Note 10 to the financial statements). Other foreign-currency deposits, which are not defined as deposits for financing the budget, declined by NIS 0.3 billion in 2001.

Treasury bills

The deposit arising from the sale of Treasury bills to the public is formally a government deposit, but the government cannot use this deposit for its regular activities. The Bank of Israel uses the deposit in the implementation of its monetary policy. There is a legal limit, specified in the law which was in force in 2001, to the size of the balance of Treasury bills; the limit is updated twice a year.[6] The combination of the Treasury bill ceiling, the inflation target, and the constraint imposed by the exchange-rate regime (the crawling band)—all of which were determined by the government—made the Bank of Israel develop another channel for absorbing money from the public: local-currency time deposits of the banking corporations in the Bank of Israel. Treasury bills and time deposits are to some extents substitutes for each other, but as Treasury bills are traded in the market and contribute to the development and improvement of the short-term money market, they are preferable to time deposits.

The Treasury bills ceiling was updated in mid-2001, and the Bank of Israel increased its sales of Treasury bills to the public in the second half of the year, and concurrently reduced the balance of time deposits. The annual average balance of the Treasury bills deposit in 2001 was NIS 46.5 billion, up from NIS 25.8 billion in 2000, and during the year it increased by NIS 4.8 billion. Time deposits rose by NIS 0.5 billion, annual average, although during the year they declined by NIS 5.5 billion (Table 7).

c. Banking corporations' deposits

The local-currency time deposits of the banking corporations continued rising in 2001, but more slowly than in previous years. The average level of the deposits in 2001 was NIS 46.5 billion, up from NIS 46.0 billion in 2000. During the year they went down by NIS 5.5 billion. In 2001 the Bank of Israel continued the downward trend of the rate of interest, and this led to a decline in the rate of interest in the auctions for time deposits, so that the average annual interest rate on these deposits in 2001 was 6.9 percent, compared with 9.4 percent in 2000 and 12.2 percent in 1999.

A large share of government payments are made via the banks, and a large share of government receipts from the public (taxes etc.) are collected, in cash, by the Post Office Bank.

The banking corporations' demand deposits are used for carrying out most government payments, and collecting part of the taxes and other receipts for the government. A small part of the payments by the government are made via the Post Office Bank, which is not defined as a banking corporation, while the Post Office Bank's share in collecting payments made to the government (mainly taxes and other compulsory payments) is relatively high. The estimates in Table 6 show that government injected NIS 3.6 billion

[6] The limit is updated according to the rise in the CPI or in the money supply, whichever is higher. The rise in the CPI is calculated against the CPI in November 1994; the money supply is compared with that in October 1994.

The ceiling on Treasury bills was abolished in February 2002.

via the banking corporations in 2001, and the public withdrew NIS 9.1 billion in cash from the banks. Most of these withdrawals were used for payments to the government via the Post Office Bank, many of which (NIS 6.9 billion) are made in cash.

There has been no change since 1998 in the level of NIS/$ swap transactions, in which the Bank of Israel borrows local currency from the banks and lends them dollars for the same term; in 2001 they again totaled $ 1.4 billion. The Bank of Israel paid interest of NIS 0.2 billion to the banks in 2001 (the same as in 2000). Exchange-rate differentials on swap transactions totaled NIS 0.5 billion in 2001, compared with a negative figure of NIS 0.2 billion in 2000.

There was no significant change in the monetary auctions which the Bank makes available to the banking corporations, and their average level remained at about NIS 0.8 billion. The average rate of interest on these loans in 2001 was 6.4 percent, down from 8.9 percent in 2000.

Table 6
Deposits of the Banking Corporations with the Bank of Israel, 1999–2001

(NIS million, current prices)

	1999			2000			2001		
	In NIS	In foreign currency	Total	In NIS	In foreign currency	Total	In NIS	In foreign currency	Total
Change in banking corporations' deposits[a]	**257**	**2,811**	**3,068**	**1,256**	**–1,641**	**–385**	**2,166**	**1,674**	**3,840**
Activity with the government[b]	10,775	–1,082	9,693	4,582	–1,407	3,175	3,724	–87	3,637
Withdrawal (–) of banknotes from Bank of Israel	–10,051		–10,051	–6,022		–6,022	–9,123		–9,123
Activity with Bank of Israel[c]	–509	324	–185	2,558	233	2,791	7,480	1,402	8,882
Transfers from (+) and to (–) abroad		3,532	3,532		–502	–502		460	460
Foreign-currency conversions at Bank of Israel	0	0	0	0	0	0	0	0	0
Adjustments	42	37	79	138	35	173	85	–101	–16
Deposit of banknotes by Post Office Bank in Bank of Israel[d]	6,383		6,383	6,947		6,947	6,905		6,905

[a] This does not include the change in time deposits.

[b] Government injection via the banking corporations' demand deposits.

[c] Depositing time deposits, the purchase of Treasury bills, the sale of goverment bonds, and various interest payments.

[d] Deposits of banknotes mainly by the Post Office Bank; these deposits are a government absorption, and are included under 'Government injection.'

Table 7
Accounts of the Banking Corporations with the Bank of Israel, 1998–2001

(daily average, current prices)

	1998	1999	2000	2001	2000 IV	2001 I	2001 II	2001 III	2001 IV
Local-currency deposits and credit[a]									
NIS billion									
1. Demand deposits	4.5	5.5	6.6	7.8	7.0	7.5	7.6	7.8	8.1
2. Time deposits	36.9	44.1	46.0	46.5	46.2	47.8	46.5	46.0	45.6
3. Monetary loans	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
4. Net deposits (= 1 + 2 + 3)	40.6	48.8	51.8	53.4	52.5	54.5	53.2	53.1	52.9
5. Net deposits *plus* swaps	45.9	54.6	57.5	59.3	58.2	60.2	59.1	59.0	58.9
6. Net deposits *plus* swaps and Treasury bills[b]	67.1	78.6	83.3	89.8	86.0	89.5	88.4	90.0	91.1
Foreign-currency deposits and credit[a]									
$ billion									
7. Deposits	1.9	2.0	2.2	2.4	2.2	2.4	2.4	2.4	2.4
8. Net deposits *less* swaps[c]	0.5	0.6	0.8	1.0	0.8	1.0	1.0	0.9	1.0
NIS billion									
9. Net deposits *less* swaps[c]	1.8	2.4	3.3	4.0	3.4	4.0	4.1	4.0	4.1
10. Total net deposits *plus* swaps and Treasury bills (= 6 + 9)	68.8	81.0	86.5	93.8	89.4	93.4	92.5	94.0	95.2
Rates of interest (percent)[d]									
11. Monetary loans	11.5	11.8	8.9	6.5	8.0	7.4	6.8	6.0	5.6
12. Time deposits	11.9	12.2	9.4	6.9	8.5	7.9	7.2	6.5	6.1

[a] Items 1–10 include accrued interest.
[b] Net deposits *plus* NIS swaps for remittance and Treasury bills deposit (excluding the part of the deposit arising from the replacement of government bonds by Treasury bills).
[c] Deposits *less* dollar swaps to be received.
[d] Annual rate, based on quarterly and yearly calculations respectively.

ISRAEL'S PAYMENT AND SETTLEMENT SYSTEMS

Israel's settlement system comprises the banks' clearing house [the paper-based Banks' Clearing House (BCH) and the automated Banks' Clearing Center (BCC, or Masav, its Hebrew acronym)], the clearing house of the Tel Aviv Stock Exchange (TASE), and the Bank of Israel (BoI) (Figure 1).

The banks' clearing house handles payment orders given in the form of checks, various debits and credits, and electronically transferred payments. The TASE clears the securities traded in it and settles the financial value of the trade. The BoI settles interbank trade in NIS versus the dollar (US$) and in liquidity. The central accounting system in the BoI serves as the final settlement agent for all the economy's settlement systems.

Israel's payment and settlement systems should be changed to accord with international standards.

Israel does not have an all-encompassing law which regulates all the payment and settlement systems. The existing situation regarding settlement is based on several laws and related regulations and agreements: the Bank of Israel Law authorizes the Bank to administer, regulate and direct the currency system and to regulate and direct the banking system in Israel. The Bank may also accept deposits from banking corporations (Articles 3 and 48 of the Bank of Israel Law, 5714–1981). Check clearance is regulated by the Banking (Service to Customers) Regulations, which determines the finality of check clearance, and by the clearing house regulations set by its committee.

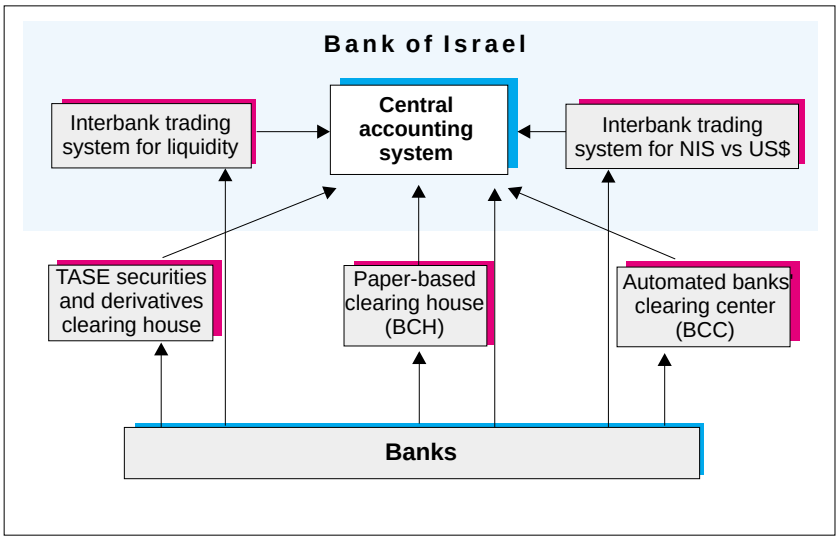
In the current settlement systems frequency of settlement is not uniform. In the banks' clearing house, the TASE clearing house, and the central accounting system in the BoI, settlement takes place once a day, at the end of the business day, while interbank trade in liquidity or in NIS versus US$ is settled separately for each transaction in the course of the day.

The timing of finality of clearance in the different settlement systems is not uniform either. Although in the banks' clearing house settlement takes place on the business day on which the transaction is carried out, the results of the settlement are not final at that time because the clearing house regulations permit transfers with retroactive value dates (for example, the return of checks one or two days after presentation). Settlement of trade in the TASE is carried out on the day after the trade date (customers are credited or debited provisionally on the trade date). Settlement of interbank trade in NIS versus US$ takes place two days after the trade date.

The Bank of Israel has started examining Israel's payment and settlement systems with a view to reforming them by introducing changes in accordance with the instructions of the Bank for International Settlements (BIS)[7] and establishing a payment and settlement system in which large-value fund transfers would be settled in real time—a Real Time Gross Settlement (RTGS) system. Such a system, which is operational in all advanced countries, would reduce settlement risk, simplify the performance of transactions, and improve Israel's financial stability.

[7] In the last few years central banks and international financial institutions have been paying more attention to the issue of settlement. The Committee on Payment and Settlement Systems appointed by the BIS set international standards for payment and settlement systems, and these were adopted by the European Monetary Union (EMU) and other countries.

The sett ement systems in Israe



Israel's payment and settlement systems

The banks' clearing house—the paper-based Banks' Clearing House (BCH) and the automated Banks' Clearing Center (BCC)

The banks' clearing house is regulated by agreement between its members, i.e., the commercial banks in Israel and in the Palestinian Autonomy, the Post Office Bank and the Bank of Israel. The activity of the clearing house is directed by the clearing house committee, which is appointed by the Governor of the Bank of Israel. The committee has fourteen members: seven, including the chairman of the clearing house, from the Bank of Israel, and seven representatives of the commercial banks. The committee's functions are to determine operating procedures and work rules for the paper-based and automated clearing houses, and to supervise the clearing houses. Members who decide to participate in sittings at which settlement takes place are called direct participants, and they also represent non-participating members, called represented members. The results of the settlement in both the paper-based and automated systems are entered in the banks' accounts in the Bank of Israel.

In accordance with agreements signed by Israel and the Palestinian Authority, banks operating in the Autonomy may be members of the banks' clearing house. As direct participant banks must have an account with the Bank of Israel, and the banks in the Palestinian Autonomy do not have such accounts, they participate as members represented by a direct participant Israeli bank.

At the end of 2001 the banks' clearing house had 48 members, 19 of whom operated in the Palestinian Autonomy.

Membership of the banks' clearing house

No. of Banks	Description
24	Banking corporations in Israel, auxiliary corporations
3	Branches of foreign banks
1	The Post Office Bank
1	The Bank of Israel
19	Commercial banks in the Palestinian Autonomy (including branches of foreign banks)

The number of participants, by type of settlement

	No. of participants	
Type of settlement	Direct	Represented
Magnetic and manual	14	33
Electronic	4	32
Non-magnetic debits and credits	16	31
In the banks' Clearing center	15	33
Foreign currency checks	12	3

Settlement of paper-based payment orders

The BCH settles checks and other paper-based payment orders. Most of the checks are settled by electronic means, which combine a reading of the magnetic data imprinted on checks when they are issued and data entered into the banks' computers when the checks are deposited, i.e., the amounts on the checks, the date of deposit, and the branch where they are deposited.

The rest of the checks are settled by magnetic means, in which all the relevant information is recorded on and read from the lower part of the check. A small proportion of checks do not have all the details in magnetized form, and these are settled manually.

The payment messages are settled on the evening of the business day they were deposited in the banks (banks' business day closes at 15:00). Banks may refuse to honor payment messages for reasons which are numerated in the clearing house regulations; such messages are generally returned on the day following their presentation, and in some cases the regulations allow their return two days after presentation. Returned messages are entered with the value date of the day they were presented, i.e., with a retroactive value date.

Settlement of payment orders transmitted via electronic media

Settlement of debit and credit orders transmitted via electronic means takes place in the BCC, which operates according to the regulations of the banks' clearing house.

Debits and credits are transferred to the BCC during the day on which they are carried out by the banks and by customers authorized to send payment orders directly to the BCC, and they are settled that evening at the current day's value date. As in the paper-

based system, participants may return debits and credits for various reasons defined in the regulations; these allow payment orders which have been settled via the BCC to be returned within five days of being presented. Such returned orders have the value date of the day prior to their return.

Settlement by both methods (i.e., via the BCH and the BCC) takes place once per business day for all messages, debits and credits alike. The results are entered in the banks' accounts with the Bank of Israel on the day following the settlement at the value date of the day the messages were presented in the clearing house. As the possibility exists of a debit or credit being returned with a retroactive value date, the banks' balances in the central accounting system of the Bank of Israel and in the accounts of the banks' customers are only final after a one or two day lag.

Large-value-payment settlement systems

The Bank of Israel operates two systems for settling large payments: one is for interbank trade in NIS versus US$, and the other for interbank trade in liquidity.

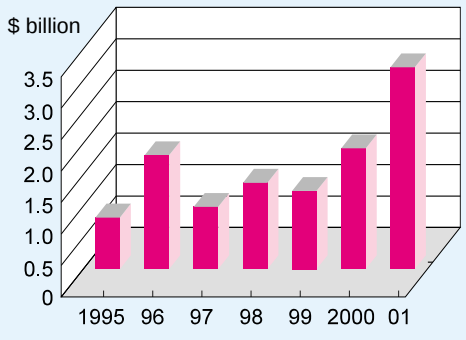
Interbank trade in NIS versus US$

Since mid-1994 the foreign exchange market in Israel has operated a system of continuous bilateral trading of NIS versus US$. The system uses the payment versus payment (PVP) method. The introduction of this system in the Bank of Israel was possible because the banks, which are the authorized market makers, hold both foreign-currency and NIS accounts in the Bank, and settlement is performed by transferring from one account to another.

Once the Bank of Israel has ascertained that the orders of the two parties to a transaction are in agreement and has confirmed them to the parties, settlement is final and irrevocable, despite the fact that it is entered in the Bank of Israel books only two business days after the transaction date. In settlement of this type, banks participating in the settlement bear no credit risk, since the Bank of Israel guarantees that the transaction will go through even if one of the parties breaches its terms in the two days between the transaction date and the date it is entered into the books. In effect the Bank is assuming the credit risk of the participants in the settlement, as it is guaranteeing the settlement at the time of the transaction even though at that time the balances in the participants' accounts are not final.

The Bank introduced the continuous bilateral trading system in 1994 to encourage the development of interbank trading, which till then had been at a low level, and to enable small banks—for whom the risks involved in conversion transactions are higher than those borne by large banks—to take part in bilateral trading. If these risks had to be covered by the banks, the cost of transactions with small banks would be raised, and could effectively exclude them from the market.

Figure 3
Total interbank trade in NIS versus US$, 1995–2001



Interbank trade in liquidity

The Bank of Israel operates a system for settling interbank trade in liquidity. Relatively large amounts are settled via this system during the day, and the interest on most of these transactions is the same as that on the Bank's monetary auctions. This trade is bilateral, and is settled via the central accounting system of the Bank of Israel.

The system enables banks to borrow from or lend to other banks at the previous day's value date. In order to reduce the credit risk of the loan, the lending bank only issues the payment order, at the previous day's value date, after the borrowing bank has given the order to repay the loan (at current value).

The Bank of Israel allows settlement at the previous day's value date because in the banks' clearing house settlement is not final on the day of presentation. The interbank-transfer system enables banks to avoid debit balances at the Bank of Israel and to satisfy the liquidity requirements related to activities of the banks' paper-based and automated clearing houses. In practice banks use the system to advance and take credit in excess of the total value of activity in the clearing house.

The TASE clearing house

The TASE clearing house settles transactions in securities carried out in the stock exchange and provides other securities-related services such as the payment of interest on bonds and the payment of dividends. Derivatives are settled in the MAOF clearing house, which is a subsidiary of the TASE clearing house.

Settlement of securities transactions takes place on the trade date, and is conditional on the results of the financial settlement performed on the next day in the banks' accounts at the Bank of Israel. The commercial banks debit and credit their customers on the day the transaction is performed, but they (the banks) are debited and credited the next day.

The Bank of Israel's central accounting system

The Bank of Israel's central accounting system serves as final settlement agency for all Israel's settlement systems. The system settles local-currency transactions of the government and the banks, as well as the results of the settlement in the various other settlement systems (the TASE, the BCH and BCC, and various Bank of Israel systems). The Bank's accounting system is updated daily. As the accounting system handles transactions from other settlement systems with retroactive value dates, the local-currency balances in banks' accounts at the Bank of Israel are not final on the processing date, but only about two days later.

2. THE BANK OF ISRAEL'S ROLE IN THE SETTLEMENT SYSTEM

The Bank of Israel is responsible for the stability of the country's payment system. The bank acts as final settlement agency for all the settlement systems in Israel, and directly

operates two systems for large-value payments. The Bank is authorized to supervise most of the payment systems and settlement procedures. Its authority derives both from the fact that it operates payment systems directly, and from its function of banking supervision.

The Bank, via its representatives, is also active in the banks' clearing house committee and in the stock exchange directorate, but plays only a small part in developing and operating the payment and settlement systems unless the private sector for any reason does not initiate the establishment of such systems.

The payment and settlement systems are regulated and supervised on two levels:

a) By means of legislation, which sets out the Bank of Israel's authority and deals with bank–customer relations (in banks participating in the payment system).

b) By means of the clearing house regulations which determine settlement arrangements such as times of settlement, the format of the report to the Bank of Israel on the results of settlement, rules for settling disagreements between clearing house members and the conditions for accepting new members. The regulations apply to both the paper-based and the electronic clearing houses.

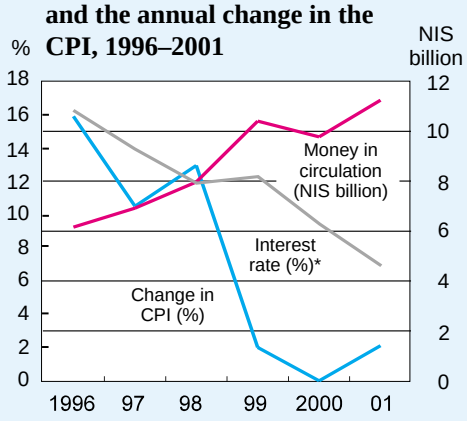
3. PAYMENT MEDIA

Cash payments

Banknotes and coin in circulation totaled NIS 16.8 billion at the end of 2001 (NIS 14.7 billion at the end of 2000). Alongside price stability in the last few years, the amount of cash in circulation has grown continuously, and between 1995 and 2001 it increased by 61 percent, at current prices. The increase resulted from population growth, a significant drop in the inflation rate, and a decline in the interest rate.

The amount of cash withdrawn from automatic teller machines (ATMs) surged by 86 percent, at current prices, between 1995 and 2001. Withdrawals and deposits via bank tellers rose by 12 percent by 78 percent respectively in the same period.[8]

Figure 4
Banknotes and coins in circulation, the interest rate, and the annual change in the CPI, 1996–2001



* Average interest-rate on the Bank of Israel's daily monetary deposit auctions.

Non-cash payments

Paper-based payments

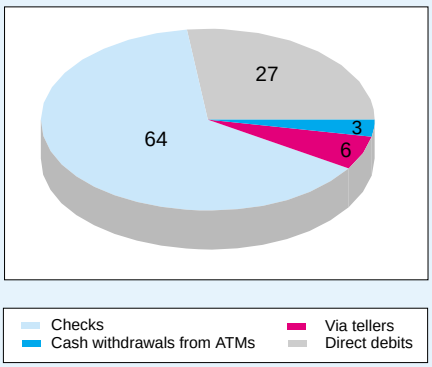
Most payments are made via paper-based instruments such as checks and magnetic or non-magnetic debits and credits. The commercial banks allow their customers to draw checks on their accounts. Checks deposited in a commercial bank up to 15:00 are credited at that day's value date. The bank can return checks on the day after their presentation in

[8] Based on data from the banks' monthly returns to the Supervisor of Banks.

the clearing house, and in such cases the payers' and payees' balances are updated in accordance with the return at the value date of the day they were presented. (In certain cases returns are permitted up to two days after presentation.) Although the use of checks is widespread, the share of withdrawals by check in total debits[9] in the payment systems has fallen from some 78 percent in 1995 to about 61 percent in 2001.

The number of debits via checks went down by 26 percent in the years from 1995 to 2001, and the average amount per check increased by 47 percent. The value of all debits rose by only two percent in 1995–2001, but their composition changed: the value of transactions by check declined by 20 percent, direct debits rose by 70 percent, and cash transactions also increased.

Figure 5
Debits, by type, 2001
Percent



Payments via electronic media

Payments via electronic media take place via the Banks' Clearing Center, The TASE clearing house, and the large-value-payments system operated by the Bank of Israel.

a) Direct debits and credits, and since January 2001 also one-time credits, are settled via the BCC; in 2001 these totaled NIS 1.946 billion, up from NIS 467 billion in 2000. In contrast, the number of credit transfers increased by only 8 percent. Total debits transferred via the BCC came to NIS 129 billion in 2001, a 5 percent increase from the level in 2000.

b) The TASE clearing house settles transactions in securities, while the MAOF clearing house handles the various derivatives. The value of equity and bond transactions carried out in the TASE in 2001 reached NIS 161 billion, slightly below the NIS 166 billion in 2000. The value of total activity in bonds rose by 77 percent in 2001, but this was offset by a 45 percent drop in activity in shares.

Activity in the MAOF clearing house surged ahead between 1995 and 2001. In 2001 activity in dollar options, in terms of basis asset, was almost double that in 2000 (a rise of 94 percent), mainly due to exchange-rate volatility. On the other hand, activity in the Tel Aviv 25 index, in terms of basis asset, went down by 19 percent.

c) Total interbank trade in NIS versus US$ increased by 73 percent in 2001, to NIS 14 billion (excluding interbank swap transactions).

d) Total interbank trade in liquidity (in one-day terms)[10] reached NIS 692 billion, a rise of 11 percent from the previous year's level, while the number of transactions increased by 53 percent. The average transaction per month was NIS 213 million in 2001, down from NIS 233 million in 2000. The average rate of interest on interbank transfers was in most cases the same as the average rate in the Bank of Israel's daily monetary auctions.

Payments via magnetic cards

Credit cards are used extensively in Israel, mainly in retail trade and services, and to

[9] Total debits here refer to debits by check, direct debits, and cash withdrawals via a teller and from ATMs.

[10] The transactions are for one day or a few days. Total activity is calculated in terms of one day, i.e., a transfer for two days will be doubled, as if two transactions were performed.

some extent also for public services. In most cases the customer's account is debited once a month for transactions during the previous month. The credit card companies make credit available to their customers in accordance with agreements between the companies and the banks. The total value of credit card debits rose to NIS 77 billion in 2001 from NIS 70 billion in 2000.

Other magnetic cards are also used, some prepaid and for specific purposes such as public phones and mobile phones, but their use is fairly limited.

The subject of an electronic purse has been examined in the past. Trials were carried out, but these were not successful, and currently there is very little activity in this field.

On-line banking

In the last two years great progress has been made in the area of banking services via the internet and other communication services. Most banks grant their customers direct access to their accounts from their home computers, mobile phones and internet. On-line banking is used for data retrieval, for performing transactions in accounts, and for making various deposits. The range of transactions which can be performed in this way varies from bank to bank. Some enable many activities to be carried out on-line, such as trading in securities, foreign currency transactions, transfers between a customer's accounts, transfers to a third party, making different types of deposits, and submitting requests for loans; others offer data retrieval only.

The total value of transactions via computer to computer communication in 2001 was NIS 125 billion,[11] mostly sales and purchases of securities, while that of transactions via the internet, mainly local-currency deposits and withdrawals and activity in securities, was NIS 18 billion.

The average monthly level of banking activity via the internet was 66 percent higher in 2001 than in the last quarter of 2000. Average monthly activity computer to computer was 16 percent higher in 2001 than in the last quarter of 2000.

4. PLANS FOR THE FUTURE

Until the 1990s Israel's financial and capital markets were highly regulated. Only Israelis participated in the settlement system, and they were well known to each other and to the Banking Supervision; hence the risks to which they were exposed were perceived as being relatively small. The situation has been changing in the last few years: as foreign-exchange control was removed, the economy became more open, and at the same time globalization of the financial markets surged ahead. In addition, political developments led to a rise in the number of foreign banks participating in the domestic settlement system, including banks in the Palestinian Autonomy.

Worldwide changes and changes among the participants in the settlement systems in Israel—which pose significant risks such as credit risk, liquidity risk and systemic risk—necessitate changes in the existing settlement systems.

The development of settlement and payment systems worldwide advanced rapidly in the last decade, due to the establishment of the European Monetary Union (EMU), the

[11] The main activities were local-currency withdrawals and deposits, transfers between a customer's accounts, transfers to third parties, purchases and sales of securities, and foreign currency transactions.

globalization process, and advances in computers and communications. The EMU spearheaded far-reaching changes in various spheres, including payments and settlement, and these have been adopted by other countries too.

The above are some of the reasons which motivated the Bank of Israel to initiate reform of Israel's payments and settlement systems. The reform will incorporate changes to the existing systems, the establishment of a new large-payments system, and perhaps also the enactment of a new comprehensive law governing payments and settlement.

Changes to the existing systems

The core principles relating to payment systems, defined by the BIS Committee on Payment and Settlement Systems (CPSS) include directives regarding final settlement at least once a day, by the end of the processing day. In Israel's current system, settlement is on a net basis for the whole system; in other words, all the transfers in each of the clearing houses are settled simultaneously once per business day. The balances at the end of the processing day are not final, however, as transfers can be made with retroactive value dates within the next two days. Furthermore, the periods to final settlement in the different systems are not uniform.

The Bank of Israel is aiming to achieve a situation in which the balances in the accounts of the participants in the settlement system will be final at the end of the processing day.

The establishment of a Real Time Gross Settlement System

A Real Time Gross Settlement (RTGS) system is one in which settlement takes place in the course of the business day (i.e., in real time) and not at the end of the day. Each payment is settled individually, on an order-by-order basis, within a short time from the issue of the payment order, and the settlement is final. The settlement risk in such a system incurred by participating banks is lower than in a system with settlement once a day, since an RTGS system ensures finality of each settlement activity.

An RTGS system would also improve efficiency and reduce the risks in the other payment systems which use the delivery versus payment (DVP) or the payment versus payment (PVP) systems. For example, in the securities clearing house, which uses DVP, at present securities are transferred the day after the transactions, as that is when payment is received; linking the securities settlement system to the RTGS system would reduce participants' exposure to credit risk and/or liquidity risk.

The introduction of an RTGS system would also reduce systemic risk, in other words it would lower the effect of the failure of a particular bank on the ability of the other banks to meet their commitments. It would also spread the pressure of settlement over the whole working day, enhancing participants' ability to cope with liquidity problems.

The Bank of Israel is actively engaged in setting up such a system in Israel.

A "Payments and settlement system in Israel" Law

The Bank of Israel will examine the possibility of a law which would comprehensively regulate matters related to payments and settlement in Israel.

STATISTICAL APPENDIX

Appendix Table 1
Selected Data from the Bank of Israel Balance Sheet, 1985–2001

(NIS million, at current prices)

	Assets								Liabilities															
											Government deposits			Banking corporations' deposits								Bank's capital		
	Foreign exchange reserves	Balance with IMF	Credit to the govern-ment	Monetary loans	Local-currency securities	Other assets		Total assets	Banknotes and coins in circu-lation	International monetary institutions	For budget financing[b]	Other	Treasury-bills deposit	Total	Time deposits	Local-currency demand deposits	In foreign currency	US$	Other liabilities	Reval-uation accounts	Total liabilities	Matched timing balance	Losses	Bank's capital and general reserve
						assets	loans[c]																	
	1.1	1.2	1.3	1.4	1.5	1.6.1	1.6.2	1	2.1	2.2	2.3.1	2.3.2	2.4	2.5	2.5.1	2.5.2	2.5.3	2.5.3.1	2.6	2.7	2	3.1	3.2	3.3
1985	5,578		7,380	69	1,118	112	323	14,580	648	201	720	531	118	10,656		1,498	9,158	6,107	428		13,302	978	0	300
1986	7,230		7,379	234	765	129	266	16,003	1,198	222	1,950	521	149	10,667		1,689	8,978	6,040	401		15,108	575	0	320
1987	9,377		7,380	907	649	300	298	18,911	1,671	275	2,150	539	780	12,398		2,479	9,919	6,447	410		18,223	368	0	320
1988	7,391		9,047	3,547	858	373	306	21,522	2,015	320	3,699	727	599	12,976		1,180	11,796	6,530	541		20,877	325	0	320
1989	10,464		9,039	4,234	1,047	348	477	25,609	2,645	340	4,982	917	1,604	13,814		1,114	12,700	6,470	743		25,045	244	0	320
1990	12,935		8,968	2,562	1,332	300	504	26,601	3,271	367	2,976	1,053	2,079	15,472		1,030	14,442	7,052	850		26,068	213	0	320
1991	14,379		8,809	5,137	1,476	419	338	30,558	3,784	413	3,294	1,318	3,771	16,624		1,260	15,364	6,730	916		30,120	118	0	320
1992	14,185		8,644	10,507	1,775	446	546	36,103	4,793	1,190	4,366	1,617	5,711	17,004		1,111	15,893	5,750	1,102		35,783	0	0	320
1993	19,063		8,373	16,501	1,965	508	471	46,881	5,652	1,286	7,945	1,701	6,519	22,291		2,088	20,203	6,766	1,167		46,561	0	0	320
1994	20,507		8,080	15,011	1,896	630	544	46,668	6,454	1,366	8,912	1,648	6,896	19,603		3,190	16,413	5,438	1,388		46,267	81	0	320
1995[c]	26,048	-5	7,773	4,027	3,045	268	502	41,658	7,916	1,245	4,734	1,661	12,948	11,263		1,007	10,256	3,272	1,365		41,132	206	0	320
1996	37,631	-1	7,448	959	4,856	289	283	51,464	9,222	728	4,290	1,588	17,183	16,636	5,071	3,502	8,062	2,480	1,748		51,394	206	-456	320
1997	71,896	0	7,109	1,443	5,090	320	93	85,952	10,373	617	5,598	1,630	20,322	46,547	32,810	6,021	7,715	2,182	1,891		86,978	206	-1,551	320
1998	94,325	0	6,760	796	5,528	356	42	107,807	11,935	714	14,239	1,813	23,355	52,709	40,078	4,701	7,931	1,906	2,102		106,866	621	0	320
1999	93,504	375	6,367	785	6,049	395	25	107,499	15,605	680	5,550	1,172	25,519	64,461	48,762	4,958	10,741	2,586	2,302		115,289	621	-8,731	320
2000	93,606	474	5,946	781	6,584	427	6	107,824	14,659	633	6,345	775	30,249	65,900	50,586	6,214	9,100	2,252	2,795	960	122,316	621	-15,433	320
2001	102,367	875	5,514	802	6,690	658	5	116,911	16,858	665	3,933	326	35,031	64,216	45,062	8,381	10,773	2,440	2,972	6,659	130,660	1,008	-15,077	320
2000[d]																								
January	89,808	365	6,365	784	6,139	451	18	103,930	13,239	664	9,255	1,060	26,053	61,184	46,118	6,385	8,681	2,127	2,802		114,258	621	-11,269	320
February	88,604	354	6,363	816	6,202	502	18	102,859	12,788	643	9,359	934	26,855	61,171	46,623	5,977	8,571	2,126	2,342		114,092	621	-12,174	320
March	91,297	356	6,363	816	6,548	542	18	105,938	12,937	647	13,363	871	26,017	61,717	45,782	6,550	9,384	2,331	2,215		117,767	621	-12,770	320
April	89,636	353	6,363	816	6,696	600	18	104,482	13,373	648	15,353	1,138	26,909	57,897	43,098	5,963	8,836	2,190	2,319		117,637	621	-14,096	320
May	92,434	362	6,368	988	6,810	654	19	107,635	13,378	665	16,835	1,126	24,900	59,261	41,819	8,250	9,192	2,205	2,258		118,423	621	-11,728	320
June	90,607	359	6,365	808	6,766	737	11	105,653	13,339	698	16,302	1,115	26,849	56,729	40,076	7,651	9,002	2,204	2,312		117,344	621	-12,632	320
July	90,150	354	6,365	808	6,665	792	11	105,145	13,414	691	13,536	931	27,447	59,553	43,600	6,830	9,123	2,233	2,375		117,948	621	-13,743	320
August	88,394	342	6,362	768	6,710	856	11	103,443	13,471	669	13,718	868	27,813	59,774	45,566	5,208	9,000	2,248	2,431		118,744	621	-16,241	320
September	88,829	344	6,363	772	6,559	894	11	103,772	13,601	673	12,445	821	28,568	60,593	44,084	7,739	8,770	2,180	2,380		119,081	621	-16,251	320
October	90,503	363	6,366	768	6,564	946	11	105,521	13,972	684	15,086	917	28,747	58,529	42,099	7,303	9,127	2,206	2,317		120,252	621	-15,670	320
November	89,053	357	6,365	781	6,469	999	11	104,035	14,006	672	11,329	875	29,661	60,179	45,560	5,335	9,284	2,268	2,386		119,108	621	-16,013	320
December	93,606	474	5,946	781	6,584	427	6	107,824	14,659	633	6,345	775	30,249	65,900	50,586	6,214	9,100	2,252	2,795	960	122,316	621	-15,433	320
2001[d]																								
January	98,166	482	5,949	1,372	6,780	520	6	113,275	14,230	642	13,419	617	30,175	63,150	44,107	8,817	10,226	2,472	2,758	2,635	127,625	621	-15,291	320
February	96,693	478	5,948	2,421	6,644	500	6	112,690	14,501	633	7,941	250	30,315	68,488	50,405	8,262	9,821	2,388	2,776	1,973	126,877	621	-15,128	320
March	99.934	479	5,951	799	6,687	619	6	114,474	15,041	641	11,464	149	30,481	65,693	46,072	8,084	11,537	2,752	2,769	2,181	128,420	621	-14,886	320
April	96,930	476	5,949	689	6,725	539	6	111,313	15,295	638	11,260	293	30,734	63,065	46,084	6,833	10,148	2,452	2,778	1,130	125,194	621	-14,822	320
May	95,498	560	5,949	759	6,633	644	6	110,048	15,384	626	11,549	225	30,602	62,531	46,552	6,294	9,685	2,343	2,783	24	123,724	621	-14,617	320
June	96,096	561	5,950	759	6,799	683	5	110,853	15,580	624	10,396	176	30,842	63,701	45,065	8,826	9,809	2,355	2,779	368	124,466	621	-14,553	320
July	98,602	703	5,951	759	6,791	750	5	113,561	15,927	637	10,931	244	31,774	62,552	44,078	8,872	9,602	2,281	2,789	2,171	127,025	621	-14,404	320
August	101,711	725	5,953	781	6,871	824	5	116,870	16,306	653	11,021	132	32,707	62,279	47,054	5,369	9,856	2,313	2,797	4,301	130,197	621	-14,267	320
September	106,596	746	5,956	781	6,984	862	6	121,931	16,957	673	11,099	136	32,938	63,890	47,079	5,551	11,261	2,586	2,850	6,503	135,046	621	-14,056	320
October	102,871	728	5,954	1,631	6,464	804	5	118,457	16,638	658	7,121	288	33,127	65,822	47,589	8,377	9,855	2,302	2,848	4,900	131,401	621	-13,885	320
November	97,855	845	5,952	797	6,509	907	5	112,871	16,433	642	7,158	123	33,989	61,788	43,558	8,522	9,708	2,293	2,918	2,634	125,685	621	-13,754	320
December	102,367	875	5,514	802	6,690	658	5	116,911	16,858	665	3,933	326	35,031	64,216	45,062	8,381	10,773	2,440	2,972	6,659	130,660	1,008	-15,077	320

[a] Loans other than the monetary loans are shown in this column to correspond with the clasification in the balance sheet for 2001.

[b] Budget financing deposits in accordance with the 1997 definition.

[c] From 1995 the totals and the items shown are adjusted to what is shown in the balance sheet as of 31 December 2000. The main change is in showing accrued interest with the item on which it was accrued. Prior to 1995, interest was shown under "other assets" or "other liabilities."

[d] Monthly data are balances of balance-sheet items at the end of the appropriate months.

Appendix Table 2
Bank of Israel Income and Expenses, 1985–2001

(NIS million, at current prices)

	Income										Expenses																
	From foreign exchange reserves		From credit to the government		From loans						On government deposits			On banking corporations' deposits													
														Interest payments on				Exchange-rate differentials on									
	Total	*of which:* exchange-rate differentials	Total	*of which:* exchange-rate differentials	Total	*of which:* exchange-rate differentials	From local currency securities	From the IMF [a]	Other	Total income	Total	*of which:* exchange-rate differentials	On Treasury-bills deposit [b]	Local-currency time deposits	Local-currency demand deposits	Foreign-currency deposits	Swaps	Foreign-currency deposits	Swaps	international financial institutions [a]	On other liabilities	Printing banknotes and minting coins	Administration and general	Total expenses	*minus* income from unrealized exchange-rate differentials	Net income	Real profit according to the definition of the Joint Ministry of Finance/Bank of Israel Committee
	1.1	1.1.1	1.2	1.2.1	1.3	1.3.1	1.4	1.5	1.6	1	2.1	2.1.1	2.2	2.3.1	2.3.2	2.3.3	2.3.4	2.3.5	2.3.6	2.4	2.5	2.6	2.7	2	3	4	5
1985	2,809	2,450	5,798	4,696	462	163	747		57	9,873	650	620			567	459		6,397			181	11	36	8,300		1,573	
1986	723	310	1,265	708	105	1	189		27	2,309	4	-8			320	429		552			45	12	48	1,410		899	
1987	1,449	923	2,145	1,429	147	10	108		62	3,911	417	6			387	433		1,198			72	5	115	2,627		1,284	
1988	1,522	982	1,693	785	260	42	59		29	3,563	978	468			223	501		1,294			81	6	69	3,152		411	
1989	1,855	912	1,524	569	338	32	102		18	3,836	905	177			124	802		934			75	8	82	2,930		906	
1990	2,136	1,008	2,102	1,102	657	22	184		53	5,132	958	175			67	1,056		1,414			92	7	107	3,701		1,431	112
1991	3,595	1,873	1,736	748	698	60	89		8	6,126	1,429	294			41	946		1,542			111	14	126	4,209		1,917	420
1992	4,013	2,580	1,847	920	1,012	81	155		-11	7,016	1,614	505			14	840		2,336			282	11	248	5,345		1,671	301
1993	2,052	1,034	1,122	272	1,805	28	231		66	5,276	1,657	433			18	706		1,018			201	17	397	4,014		1,262	184
1994	1,490	920	1,417	529	2,316	8	406		61	5,690	757	164	928		65	711		808			190	11	374	3,842		1,848	-109
1995 [c]	3,543	1,620	1,429	534	1,068	21	312	-83	99	6,367	536	195	1,404		9	676	94	625	-119	83	52	33	464	3,858		2,509	869
1996	2,155	536	927	88	591	11	586	-12	79	4,326	598	308	2,439	263	9	354	571	71	-215	28	57	18	589	4,782		-456	1,346
1997	5,545	2,617	837	55	249	7	615	2	54	7,302	1,208	761	2,720	3,167	8	290	489	373	-547	50	68	11	561	8,397		-1,095	2,389
1998	19,581	14,866	2,085	1,266	109	9	485	0	-76	22,185	2,396	2,664	2,714	4,372	9	353	340	1,150	-874	161	82	54	494	11,251		10,934	3,890
1999	-509	-3,579	691	0	113	0	375	13	93	775	-326	-53	2,911	5,384	4	394	415	-29	10	11	64	45	623	9,505		-8,731	3,868
2000	714	-4,335	617	-5	91	0	222	-22	41	1,663	-244	-572	2,671	4,326	3	515	181	-255	157	-21	62	6	942	8,344	22	-6,702	
2001	13,655	7,387	567	12	51	0	523	55	35	14,886	1,582	1,746	2,329	3,218	3	416	170	874	-525	56	63	19	711	8,918	5,224	743	
2000																											
January	-1,708	-2,125	-467	-2	6	0	-29	-9	-3	-2,209	-378	-345	247	433	0	42	23	-164	99	-13	3	0	36	329		-2,538	
February	-1,040	-1,373	566	-2	9	0	-9	-9	-3	-486	-262	-245	212	396	0	37	21	-106	70	-15	4	0	62	419		-905	
March	-75	-457	52	0	9	0	122	1	0	109	-26	-33	221	409	0	40	20	-11	8	4	5	1	34	705		-596	
April	-597	-1,033	52	0	6	0	-18	-3	3	-557	76	40	222	363	0	40	17	20	-13	-4	6	0	41	769		-1,326	
May	3,638	3,196	56	4	10	0	137	12	9	3,862	675	619	224	354	0	43	16	290	-186	23	10	0	45	1,495		2,367	
June	-660	-1,063	49	-3	9	0	-40	-4	5	-642	-310	-391	217	326	0	43	14	-183	118	-6	3	1	40	262		-904	
July	-330	-814	52	0	6	0	-41	-5	5	-312	43	5	238	358	0	46	14	2	-1	-7	6	1	100	798		-1,111	
August	-2,239	-2,684	49	-3	9	0	-51	-10	-2	-2,244	-345	-381	222	359	0	46	14	-179	113	-16	3	1	36	254		-2,498	
September	662	222	52	1	7	0	72	2	4	798	132	95	212	340	0	43	12	43	-28	4	6	0	44	808		-10	
October	1,767	1,329	56	4	6	0	79	7	6	1,919	560	532	227	344	0	48	11	245	-158	13	9	0	38	1,338		581	
November	1	-367	50	-1	8	0	-5	-4	7	56	-160	-199	196	315	0	45	10	-98	62	-5	4	1	29	399		-343	
December	1,296	829	50	-3	6	0	4	1	13	1,370	-249	-269	233	329	0	47	9	-118	73	3	4	1	438	768	22	579	
2001																											
January	2,357	1,983	50	3	5	0	97	8	7	2,704	509	500	188	328	0	51	9	216	-134	12	9	1	56	1,245	1,317	142	
February	-170	-724	45	-1	5	0	79	-2	5	-38	-128	-131	196	287	0	40	10	-58	35	-2	4	1	55	442	-642	163	
March	1,416	739	49	3	5	0	88	2	3	1,563	400	409	212	310	0	48	12	180	-112	4	8	1	44	1,107	214	242	
April	-512	-989	45	-2	4	0	124	-3	2	-339	-278	-271	223	283	0	40	11	-118	74	-3	3	1	43	280	-683	64	
May	-574	-1,116	46	0	5	0	166	-6	6	-358	-34	-31	180	287	0	39	14	-13	8	-7	5	7	37	524	-1,088	205	
June	1,154	658	47	1	4	0	85	2	4	1,298	147	157	180	268	0	37	15	73	-45	3	6	-1	42	727	508	63	
July	2,305	1,761	48	1	4	0	98	12	6	2,477	207	215	206	259	0	34	14	102	-62	13	7	-4	43	823	1,504	150	
August	2,874	2,367	48	2	4	0	31	25	5	2,986	241	256	195	255	0	32	14	121	-74	20	7	5	41	857	1,991	137	
September	2,681	2,177	49	3	4	0	93	22	0	2,849	433	445	203	239	0	31	15	213	-130	19	-4	2	103	1,124	1,514	211	
October	-1,520	-2,076	44	-2	4	0	-77	-18	0	-1,566	-383	-351	195	254	0	24	20	-170	104	-15	3	0	39	72	-1,808	171	
November	-1,085	-1,625	44	-2	4	0	1	-15	7	-1,044	-260	-217	172	238	0	19	20	-107	67	-12	3	2	120	262	-1,437	131	
December	4,549	4,233	51	6	3	0	-265	30	-9	4,360	728	765	179	210	0	20	17	434	-256	23	11	4	88	1,460	3,835	-935	

[a] Income from the IMF and expenses on international financial institutions until 1995 are shown under "expenses on other liabilities."

[b] Expenses on Treasury bills deposits until 1993 are included under expenses on government deposits in NIS.

[c] From 1995 the figures and items have been presented so that they correspond to the format of the profit and loss account for 2001. Exchange-rate differentials (realized and unrealized) are shown under the items to which they apply throughout the table.

Appendix Table 3
Government Deposits, 1985–2001

(million, at current prices)

	Government budget-financing deposits[a]								Other deposits			Accrued interest on government deposits[b]	Total government deposits
	In local currency		In foreign currency										
			Deposit of US government economic aid		Deposit of money borrowed under US government guarantee		Current		Bond-price stabilization,	Other foreign-currency deposit			
	Current, NIS	Gold deposit, NIS	NIS	$	NIS	$	NIS	$	NIS	NIS	$	NIS	NIS
1985	185						535	357	0	531	354		1,251
1986	1,599						351	236	0	521	350		2,471
1987	–62		1,857	1,207			355	231	0	539	350		2,689
1988	1,393		1,866	1,033			440	243	89	638	353		4,426
1989	2,934		1,655	843			393	200	222	695	354		5,899
1990	934		1,751	855			291	142	330	723	353		4,029
1991	2,190	437	482	211			185	81	519	799	350		4,612
1992	948	734	2,337	846			347	126	647	970	351		5,983
1993	967	734	2,485	832	3,394	1,137	365	122	647	1,054	353		9,646
1994	–1,540	734	2,354	780	6,719	2,226	645	214	592	1,056	350		10,560
1995	2,600	734			581	185	819	261	546	1,097	350	18	6,395
1996	–2,644	734	2,971	914	2,432	748	797	245	411	1,143	352	33	5,878
1997	–5,759		3,467	980	6,739	1,906	1,151	326	356	1,238	350	36	7,228
1998	–4,821		4,024	967	13,399	3,221	1,637	394	292	1,455	350	66	16,052
1999	–13,645		4,007	965	13,783	3,319	1,405	338	267	846	204	59	6,723
2000	–14,162		5,048	1,249	14,224	3,520	1,235	306	241	446	110	88	7,120
2001	-14,951		2,394	542	16,101	3,646	389	88	201	100	23	25	4,259
2000													
January	–9,745		3,901	956	13,614	3,335	1,485	364	266	835	205	–41	10,316
February	–9,510		3,871	960	13,666	3,389	1,332	330	266	808	200	–141	10,293
March	–5,484		3,821	949	13,112	3,257	1,915	476	266	822	204	–217	14,234
April	–2,882		3,795	940	13,212	3,274	1,228	304	266	828	205	44	16,491
May	–1,620		3,429	823	13,838	3,320	1,187	285	266	846	203	14	17,961
June	–1,738		3,177	778	13,626	3,336	1,237	303	266	838	205	11	17,417
July	–4,728		3,154	772	13,705	3,355	1,406	344	258	619	152	54	14,467
August	–4,433		2,987	746	13,657	3,411	1,507	376	254	609	152	5	14,585
September	–5,820		2,937	730	13,816	3,433	1,512	376	252	614	152	–45	13,266
October	–3,598		3,035	734	14,282	3,452	1,366	330	242	625	151	50	16,003
November	–6,055		1,790	437	14,333	3,502	1,261	308	242	632	154	1	12,204
December	-14,162		5,048	1,249	14,224	3,520	1,235	306	241	446	110	88	7,120
2001													
January	-7,657		5,150	1,245	14,638	3,538	1,288	311	241	374	90	2	14,035
February	-12,907		4,940	1,201	14,627	3,557	1,282	312	236	101	25	-88	8,191
March	-9,877		4,999	1,192	15,023	3,584	1,320	315	231	91	22	-174	11,613
April	-9,064		4,086	987	14,894	3,598	1,345	325	226	69	17	-2	11,553
May	-8,556		3,674	889	15,044	3,640	1,387	336	221	76	18	-71	11,774
June	-10,383		4,216	1,012	15,210	3,652	1,354	325	221	98	23	-143	10,572
July	-9,359		3,432	815	15,422	3,664	1,437	341	221	20	5	2	11,175
August	-9,289		3,281	770	15,674	3,678	1,355	318	216	-15	-3	-69	11,153
September	-9,635		3,258	748	16,115	3,700	1,362	313	213	59	14	-135	11,236
October	-12,222		2,099	490	15,889	3,712	1,356	317	207	97	23	-17	7,409
November	-10,579		1,889	446	15,409	3,640	439	104	207	12	3	-96	7,281
December	-14,951		2,394	542	16,101	3,646	389	88	201	100	23	25	4,259

[a] In accordance with the 1997 definition.
[b] Since 1995 accrued interest on government deposits is shown in the balance of government deposits.

Appendix Table 4
Composition of Change in the Monetary Base and Foreign Reserves, 1989–2001

(at current prices)

	Changes in monetary base and their sources					Banks' foreign-currency activity with the Bank of Israel							
		Injection (+)/absorption (–)									Contribution to reserves		
	Change in monetary base	Government and National Institutions	Bank of Israel	Foreign-currency conversions at Bank of Israel	Adjustments[a]	Foreign-currency sales to (–) Bank of Israel	Public-sector transfers (+) to banks	Increase in (+) deposits with Bank of Israel	Transfers to (–)/from (+) rest of world	Adjustments	Private sector	Public sector	Change in reserves
	(1) = (2+3+4+5)	(2)	(3)	(4)	(5)	(6) = (8–9–7)	(7)	(8)	(9)	(10)	(11) = (9+10)	(12)	(13) = (11+12)
	NIS million					*$ million*							
1989	565	–2,388	569	2,383		–2,388	277	–464	1,644	–927	717	526	1,239
1990	541	3,578	–2,754	–282		–780	158	–345	276	–828	–552	1,538	985
1991	744	4,552	323	–2,118	–2,013	737	99	–730	–1,566	–682	–2,248	2,231	–17
1992	860	5,156	2,979	–5,290	–1,985	2,040	37	–1,079	–3,156	–754	–3,911	2,744	–1,167
1993	1,837	2,628	3,956	–3,161	–1,586	1,095	347	892	–550	–114	–664	1,916	1,252
1994	1,903	4,940	–3,856	1,927	–1,108	–646	589	–1,759	–1,702	294	–1,408	1,819	411
1995[b]	–720	1,324	–20,230	19,160	–973	–6,383	2,201	–2,547	1,634	336	1,970	–557	1,413
1996	3,801	5,926	–7,607	6,451	–970	–2,044	129	–835	1,079	–221	859	2,408	3,266
1997	3,670	1,234	–20,204	23,324	–684	–6,948	–614	–320	7,242	–261	6,981	1,776	8,757
1998	242	1,901	–2,664	1,746	–741	–492	–163	–369	286	–343	–57	2,399	2,342
1999	3,927	4,067	–364	0	224	0	–259	585	844	–197	647	–806	–159
2000	311	–2,729	2,729	0	311	0	–345	–462	–117	–275	–392	1,041	649
2001	4,364	–2,611	7,675	0	–700	0	–20	91	111	–216	–105	122	17
2000													
January	–939	–4,030	3,099	0	–8	0	–21	–470	–449	–23	–472	–42	–514
February	–859	–454	–349	0	–57	0	–9	–10	–1	–22	–23	–3	–26
March	722	–1,884	2,705	0	–98	0	–57	195	253	–87	166	536	702
April	–151	–2,622	2,513	0	–43	0	–24	–151	–127	–30	–157	–305	–462
May	2,293	–1,898	4,007	0	184	0	–30	5	35	13	49	–86	–37
June	–638	–1,081	370	0	74	0	4	–11	–15	18	2	6	9
July	–748	2,666	–3,350	0	–63	0	–6	18	24	–19	5	–122	–117
August	–1,564	–345	–1,544	0	326	0	–128	3	131	–49	82	–74	8
September	2,660	1,202	1,442	0	16	0	–75	–79	–4	–74	–78	76	–2
October	–65	–2,400	2,407	0	–72	0	–3	15	18	–18	0	–198	–198
November	–1,934	1,631	–3,708	0	143	0	–12	51	63	21	84	–203	–119
December	1,534	6,488	-4,863	0	-92	0	17	-28	-44	-5	-49	1,456	1,407
2001													
January	2,173	-5,326	7,784	0	-285	0	-1	208	209	-72	137	427	565
February	-284	4,574	-4,802	0	-56	0	-29	-93	-64	-41	-105	-109	-214
March	362	-3,212	3,211	0	363	0	-14	353	367	71	438	-114	324
April	-997	-1,010	171	0	-158	0	18	-311	-328	-17	-345	-75	-421
May	-450	-929	403	0	76	0	-19	-118	-99	1	-98	-214	-312
June	2,729	755	1,818	0	155	0	7	3	-3	43	40	-74	-34
July	393	-334	637	0	89	0	-31	-82	-50	-12	-62	416	354
August	-3,124	300	-3,340	0	-84	0	-5	24	29	-26	3	435	438
September	833	711	192	0	-71	0	-4	267	270	-19	251	361	612
October	2,507	2,343	727	0	-563	0	27	-290	-317	-104	-421	-26	-447
November	-60	-3,038	2,986	0	-8	0	32	-13	-45	28	-18	-895	-912
December	283	2,555	-2,113	0	-158	0	0	142	142	-69	74	-10	64

[a] In 1989 and 1990 adjustments to the monetary base were included in the injection from foreign-currency conversions at the Bank of Israel.
[b] From 1995 the various items are shown in accordance with the definitions in effect on 31 December 2001.

Appendix Table 5
The Main Monetary Instruments,[a] 1985–2001

(million, at current prices)

	Foreign exchange reserves		Monetary loans	Treasury bills	Time deposits	Swaps with banking corporations		
						Receipt of $ from banks		NIS transferred to banks
	NIS	$	NIS	NIS	NIS	$	NIS	
1985	5,578	3,720	69	118				
1986	7,230	4,864	235	149				
1987	9,377	6,095	907	780				
1988	7,391	4,091	3,547	599				
1989	10,464	5,331	4,234	1,604				
1990	12,935	6,316	2,562	2,079				
1991	14,379	6,298	5,137	3,771				
1992	14,185	5,132	10,507	5,711				
1993	19,063	6,384	16,501	6,519				
1994	20,507	6,795	15,011	6,896				
1995	26,048	8,309	4,009	12,948		1,650	5,173	5,146
1996	37,631	11,575	957	17,183	5,000	1,850	6,014	6,062
1997	71,896	20,332	1,426	20,322	32,500	1,400	4,950	4,951
1998	94,325	22,674	796	23,355	40,000	1,400	5,824	5,843
1999	93,504	22,515	784	25,519	48,700	1,400	5,814	5,863
2000	93,606	23,164	781	30,249	50,500	1,400	5,657	5,718
2001	102,367	23,181	802	35,031	45,000	1,400	6,182	5,970
2000								
January	89,808	22,001	784	26,053	46,000	1,400	5,715	5,737
February	88,604	21,975	815	26,855	46,500	1,400	5,645	5,693
March	91,297	22,677	815	26,017	45,700	1,400	5,636	5,586
April	89,636	22,215	815	26,909	43,000	1,400	5,649	5,669
May	92,434	22,177	988	24,900	41,700	1,400	5,835	5,781
June	90,607	22,186	807	26,849	40,000	1,400	5,718	5,741
July	90,150	22,069	807	27,447	43,500	1,400	5,719	5,726
August	88,394	22,076	768	27,813	45,500	1,400	5,606	5,664
September	88,829	22,075	771	28,568	44,000	1,400	5,634	5,653
October	90,503	21,877	768	28,747	42,000	1,400	5,792	5,739
November	89,053	21,757	781	29,661	45,500	1,400	5,730	5,750
December	93,606	23,164	781	30,249	50,500	1,400	5,657	5,718
2001								
January	98,166	23,729	1,372	30,175	44,000	1,400	5,792	5,747
February	96,693	23,515	2,421	30.315	50,300	1,400	5,757	5,779
March	99,934	23,839	799	30,481	46,000	1,400	5,869	5,814
April	96,930	23,419	689	30,734	46,000	1,400	5,795	5,863
May	95,498	23,106	759	30,602	46,500	1,400	5,786	5,799
June	96,096	23,072	759	30,842	45,000	1,400	5,831	5,833
July	98,602	23,426	759	31,774	44,000	1,400	5,893	5,873
August	101,711	23,865	781	32,707	47,000	1,400	5,967	5,927
September	106,596	24,477	781	32,938	47,000	1,400	6,097	6,049
October	102,871	24,030	1,631	33,127	47,500	1,400	5,993	6,049
November	97,855	23,117	797	33,989	43,500	1,400	5,926	5,930
December	102,367	23,181	802	35,031	45,000	1,400	6,182	5,970

[a] Accrued interest is not included in the balance of an item (except for foreign exchange reserves and Treasury bills since 1995).