

## Chapter 3

# *The Public's Financial Asset Portfolio*

The value of the public's portfolio of financial assets rose by 12.3 percent in nominal terms during 2003 and reached a total of NIS 1,385.9 billion following a moderate increase of 1.8 percent in 2002. The increase in the value of the portfolio in 2003 encompassed all local assets, while the foreign currency asset component contracted slightly.<sup>1</sup> The development of the asset portfolio in the course of the year was affected by two main factors—the decrease in the yield/risk ratio expected from investment in local assets, and by the capital market taxation reform.

The decrease in the yield/risk ratio on local assets from March onwards was reflected by a rise in the prices of all local financial assets (shares, bonds and Treasury bills), as compared to a decrease in the prices of foreign currency assets. The reduction in the Bank of Israel's interest rate resulting from the decline in inflation expectations supported the upturn in the prices of local assets. The reform in capital market taxation, which went into effect in 2003, was one of the reasons for the public's move from non-tradable assets (deposits at the banks and saving schemes) to tradable assets (Treasury bills and bonds).

A notable increase was recorded in the local and foreign share component of the portfolio in 2003, reflecting the rise in share prices. In the portfolio exclusive of the share component, the proportion of unindexed assets rose, while the proportion of CPI-indexed assets and foreign currency assets fell. The distribution of the asset portfolio by investment term remained largely unchanged. Among all terms, the proportion of assets held via the banks fell (the decrease encompassed all indexation types), while the proportion of bonds and Treasury bills increased.

### 1. MAIN DEVELOPMENTS

The value of the public's portfolio of financial assets rose by 12.3 percent in nominal terms during 2003 and reached a total of NIS 1,385.9 billion (Table 3.1) following a

<sup>1</sup> The reference here and hereafter is to assets that are denominated or indexed to foreign currency.

**Table 3.1**  
**The Financial Asset Portfolio of the Public, 1998–2003**

	Balance (NIS billion, current prices)						Composition and real change (percent)					
	1998	1999	2000	2001	2002	2003	1998	1999	2000	2001	2002	2003
<b>Total</b>	832.1	1,051.3	1,130.3	1,212.2	1,234.4	1,385.9	13.6	26.3	7.5	7.3	1.8	12.3
<b>Assets by indexation</b>												
Unindexed assets	208.4	258.5	320.2	374.7	385.3	432.3	25.0	24.6	28.3	30.9	31.2	31.2
CPI-indexed assets	386.2	403.7	406.0	425.9	463.1	472.5	46.4	38.4	35.9	35.1	37.5	34.1
Assets in or indexed to												
foreign currency	86.0	115.4	127.2	154.7	196.0	189.9	10.3	11.0	11.3	12.8	15.9	13.7
Shares in Israel	133.1	221.5	222.9	226.6	171.3	261.3	16.0	11.0	11.3	12.8	15.9	13.7
Shares abroad	18.5	52.2	54.0	30.3	18.7	30.0	2.2	5.0	4.8	2.5	1.5	2.2
<b>Assets by term to maturity<sup>a</sup></b>												
Short term	211.8	250.6	289.9	328.1	349.5	365.9	30.3	32.2	34.0	34.3	33.5	33.4
Medium term	330.3	357.2	384.2	434.1	479.8	502.2	47.3	45.9	45.0	45.4	45.9	45.9
Long term	156.4	469.8	179.3	193.1	215.0	226.6	22.4	21.8	21.0	20.2	20.6	20.7
<b>Commercial banks</b>												
Unindexed local-currency												
deposits	150.1	189.5	223.9	156.8	244.8	271.8	18.0	18.0	19.8	21.2	19.8	19.6
CPI-indexed deposits	19.7	18.4	28.9	28.9	32.0	46.7	2.4	1.8	2.6	2.4	2.6	3.4
Assets in or indexed to												
foreign currency	71.1	93.0	100.7	118.7	143.9	139.7	8.5	8.8	8.9	9.8	11.7	10.1
CPI-indexed savings schemes	96.7	100.7	91.3	88.7	102.7	76.9	11.6	9.6	8.1	7.3	8.3	5.5
Foreign-currency-indexed												
savings schemes	6.2	6.6	7.8	7.4	6.9	5.3	0.7	0.6	0.7	0.6	0.6	0.4
Unindexed savings schemes	1.4	1.9	2.5	4.1	6.9	5.5	0.2	0.2	0.2	0.3	0.6	0.4
<b>Assets by institutional composition</b>												
Total institutions <sup>b</sup>	295.5	327.5	345.4	370.0	386.7	424.1	35.5	31.2	30.6	30.5	31.3	30.6
Provident funds	107.3	116.8	119.8	123.5	119.5	134.3	12.9	11.1	10.6	10.2	9.7	9.7
Advanced study funds	31.8	37.7	42.0	47.8	46.9	54.4	3.8	3.6	3.7	3.9	3.8	3.9
Established pension funds	95.1	101.6	105.4	109.4	119.7	120.6	11.4	9.7	9.3	9.0	9.7	8.7
New pension funds	3.4	5.3	7.5	10.7	14.4	18.6	0.4	0.5	0.7	0.9	1.2	1.3
Life insurance schemes:												
guaranteed yield	38.9	40.2	40.6	41.5	44.5	43.8	4.7	3.8	3.6	3.4	3.6	3.2
Life insurance schemes:												
profit sharing	19.0	25.8	30.1	37.1	41.7	52.3	2.3	2.5	2.7	3.1	3.4	3.8
<b>The public directly</b>	<b>191.5</b>	<b>313.7</b>	<b>329.8</b>	<b>337.8</b>	<b>310.5</b>	<b>415.9</b>	<b>23.0</b>	<b>39.8</b>	<b>29.2</b>	<b>27.9</b>	<b>25.2</b>	<b>30.0</b>

<sup>a</sup> Excluding shares.

<sup>b</sup> Engaged in contractual saving.

SOURCE: Based on banks' financial statements, and data from TASE and the Ministry of Finance.

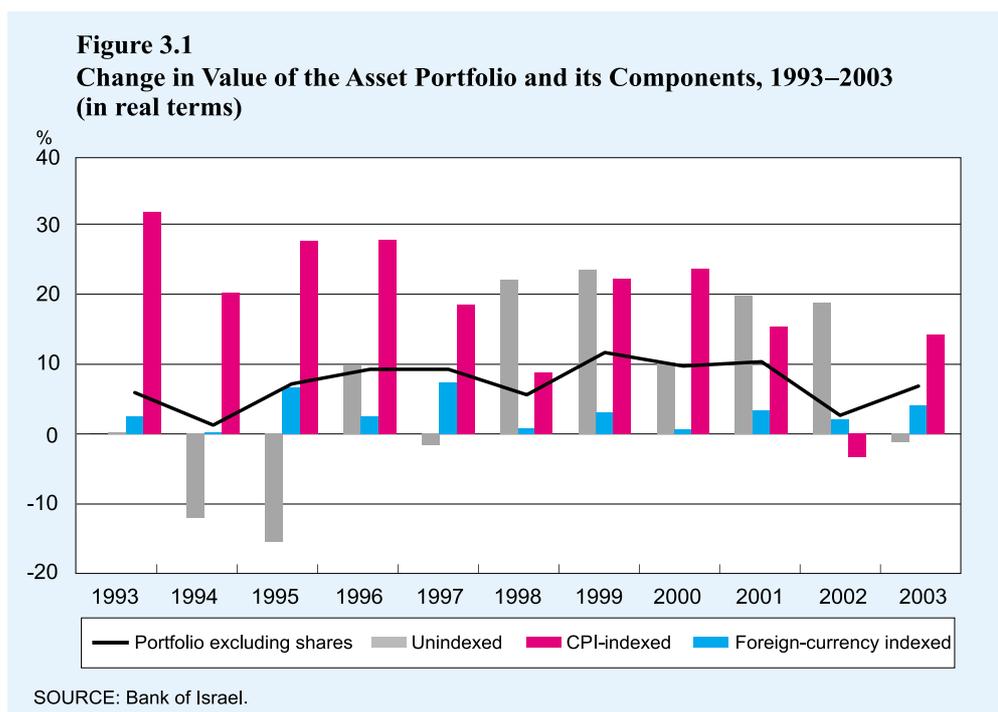
moderate increase of 1.8 percent in 2002. The increase in the value of the portfolio in 2003 encompassed all local assets, while the foreign currency asset component contracted slightly. The development of the asset portfolio in the course of the year was affected by two main factors—the decrease in the yield/risk ratio expected from investment in local assets, and by the capital market taxation reform.

The decrease in the yield/risk ratio on local assets from March onwards led to a large rise in the prices of all local financial assets, as compared to a decrease in the prices of foreign currency assets. A number of factors supported the upturn in the prices of local assets: the end of the war in Iraq in March and as a result, foreign investors' entry to emerging markets; the decrease in government spending under the new economic program; the improvement in Israel's geopolitical situation; and the receipt of US loan guarantees enabling the government to raise money in foreign markets. These developments created a positive climate in the local financial markets and contributed *inter alia* to a decrease in Israel's risk premium. This improvement, together with the large gap between the NIS interest rate and the interest rates in the USA and Europe, encouraged capital imports to Israel. Foreign investors' purchases of NIS securities contributed to an appreciation of the NIS against the dollar and to a rise in bond and share prices. The favorable turnaround in the financial markets and the improvement in the majority of risk indicators, including inflation risk, concurrent with the continued slowdown in real activity, supported a reduction in the Bank of Israel's interest rate during the year. The downward course of the Bank of Israel's interest rate resulting from the decline in inflation expectations increased investors' expectations of a real capital gain on investment in bonds and shares, thereby boosting the upturn in prices in the capital markets.

Concurrently, the reform in capital market taxation, which went into effect in 2003, led to a move from unindexed deposits and saving schemes (non-tradable assets) to Treasury bills and CPI-indexed bonds (tradable assets). Under the reform, all forms of tradable and non-tradable assets are now taxed at uniform rates, while the taxation advantages that depositors enjoyed in all types of saving schemes have been abolished, reducing the profitability of investing in them compared with tradable substitutes. Treasury bills were the only form of investment that remained untaxed in 2003. This provided them with a temporary advantage over unindexed deposits, which have similar features apart from tradability, and the proportion of these deposits in the portfolio fell. The expansion of the mutual funds, especially those specializing in unindexed NIS assets, facilitated the public's move from bank assets to Treasury bills and bonds.

The local and foreign share component expanded to a notable extent in 2003. The increase amounted to 50 percent in nominal terms, and contributed to a 12 percent growth in the asset portfolio. The proportion of shares in the portfolio rose from 15.4 percent in 2002 to 21 percent in 2003, reflecting the rise in share prices. Most of the share indexes in Israel rose by over 50 percent, while the indexes abroad went up by between 25 to 50 percent, following large decreases in Israeli and worldwide share indexes of as much as 30 percent in 2002. The upturn in the equity market resulted from the end of the war in Iraq, which encouraged foreign investors to enter emerging markets and Israel in particular, as well as the initial signs of a rebound in the world economy, principally in the area of high technology. Since the share component is notable for relatively high volatility, the public's asset portfolio will subsequently be presented without this component.

The value of the asset portfolio excluding shares rose by 4.8 percent in nominal terms in 2003 following an increase of 9.3 percent in 2002. The smaller rate of increase resulted from the large decline in inflation, from 6.5 percent in 2002 to 1.9 percent in 2003. In real terms, the increase amounted to 8.6 percent in 2003 compared with 2.7 percent in 2002. The real rate of increase in the value of the asset portfolio slowed from an average of 11 percent a year during 1999-2001 to 4.8 percent during 2002 and 2003 (Figure 3.1), apparently due to the continuing recession.

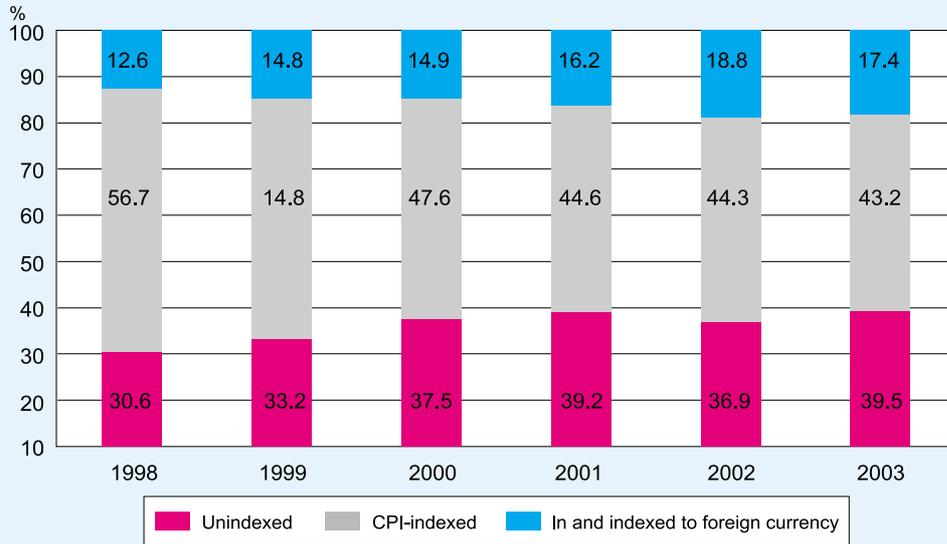


A long-term perspective shows that two main factors have affected the development of the asset portfolio—the downturn in inflation and the liberalization of the capital market.

The downturn in inflation has affected the composition of the public's asset portfolio since 1993. This development has been reflected by a gradual decrease in the proportion of CPI-indexed assets and by an increase in the proportion of unindexed assets (Figure 3.2).

An examination of the indexation composition of the portfolio over time shows that the CPI component has been contracting to a lesser extent. The process whereby the portfolio has adapted to the decline in inflation appears to be close to completion, and its stabilization reflects *inter alia* the public's preference for CPI-indexed assets in long-term saving out of risk-minimization considerations: 90 percent of saving schemes are CPI-indexed; the provident funds and the insurance companies hold two thirds of all tradable CPI-indexed bonds; and a large part of the pension funds' assets consist of

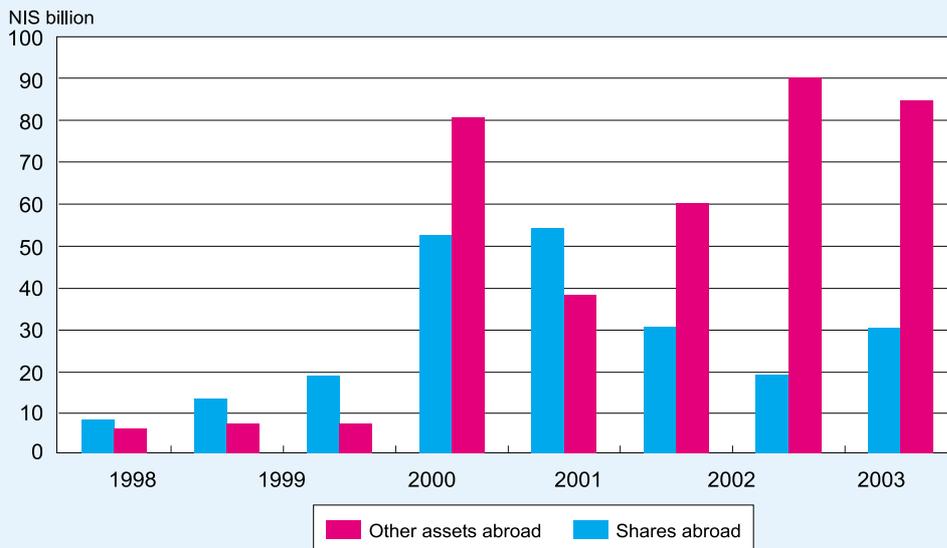
**Figure 3.2**  
**Indexation Composition of the Asset Portfolio,<sup>a</sup> 1998–2003**



<sup>a</sup> Excluding shares.  
 SOURCE: Bank of Israel.

earmarked bonds, which are also CPI-indexed. Investment in unindexed and foreign currency indexed bonds is affected more by short-term considerations.

**Figure 3.3**  
**Israelis' Assets Abroad, 1998–2003**



SOURCE: Bank of Israel.

**Table 3.2**  
**Distribution of the Public's Asset Portfolio, by Indexation, 1998–2003**

	(current prices)										
	Balance (NIS billion)						Composition (percent)				
	1998	1999	2000	2001	2002	2003	1999	2000	2001	2002	2003
Total	832.1	1,051.3	1,130.3	1,212.2	1,234.4	1,385.9	100.0	100.0	100.0	100.0	100.0
<b>Unindexed assets</b>	<b>208.4</b>	<b>258.4</b>	<b>320.0</b>	<b>374.5</b>	<b>385.3</b>	<b>432.2</b>	<b>24.6</b>	<b>28.3</b>	<b>30.9</b>	<b>31.2</b>	<b>31.2</b>
Cash and liquid deposits	45.0	53.7	57.7	68.1	62.4	73.2	5.1	5.1	5.6	5.1	5.3
Term deposits	120.5	156.1	190.2	216.8	210.1	211.7	14.8	16.8	17.9	17.0	15.3
Treasury bills	16.5	18.0	26.2	27.0	40.5	47.1	1.7	2.3	2.2	3.3	3.4
<i>Gilon</i> and <i>Shahar</i> bonds	24.9	28.8	43.6	558.9	65.5	94.8	2.7	3.9	4.9	5.3	6.8
Savings schemes	1.4	1.9	2.5	4.1	6.9	5.5	0.2	0.2	0.3	0.6	0.4
<b>CPI-indexed assets</b>	<b>386.2</b>	<b>403.7</b>	<b>406.0</b>	<b>425.9</b>	<b>463.1</b>	<b>472.5</b>	<b>38.4</b>	<b>35.9</b>	<b>35.1</b>	<b>37.5</b>	<b>34.1</b>
Savings schemes	96.7	100.7	91.3	88.7	102.7	76.9	9.6	8.1	7.3	8.3	5.5
CPI-indexed deposits	51.9	50.9	55.4	55.2	58.4	70.4	4.8	4.9	4.6	4.7	5.1
Tradable bonds	78.8	80.2	76.5	87.8	89.7	104.6	7.6	6.8	7.2	7.3	7.6
Other assets <sup>a</sup>	158.7	171.8	182.9	194.3	212.3	220.6	16.3	16.2	16.0	17.2	15.9
<b>Shares</b>	<b>151.6</b>	<b>273.7</b>	<b>276.9</b>	<b>276.9</b>	<b>190.0</b>	<b>291.3</b>	<b>26.0</b>	<b>24.5</b>	<b>21.2</b>	<b>15.4</b>	<b>21.0</b>
In Israel	133.1	221.5	222.9	226.6	171.3	261.3	21.1	19.7	18.7	13.9	18.9
Abroad	18.5	52.2	54.0	30.3	18.7	30.0	5.0	4.8	2.5	1.5	2.2
<b>Assets in and indexed to foreign currency</b>	<b>86.0</b>	<b>115.4</b>	<b>127.2</b>	<b>154.7</b>	<b>196.0</b>	<b>189.9</b>	<b>11.0</b>	<b>11.3</b>	<b>12.8</b>	<b>15.9</b>	<b>13.7</b>
Assets in Israel	79.3	87.1	89.2	94.7	106.0	105.5	8.3	7.9	7.8	8.6	7.6
<i>Pamah</i> (resident foreign-currency) restitutions deposits	18.4	16.7	15.3	16.9	20.7	21.6	1.6	1.4	1.4	1.7	1.6
Other <i>Pamah</i> (resident foreign-currency)	39.4	47.2	52.6	56.5	62.9	64.5	4.5	4.6	4.7	5.1	4.7
Foreign-currency-indexed deposits	6.3	4.5	2.8	3.4	4.5	4.8	0.4	0.2	0.3	0.4	0.3
Tradable bonds	9.1	12.1	10.8	10.5	10.9	9.3	1.2	1.0	0.9	0.9	0.7
Savings schemes	6.2	6.6	7.8	7.4	6.9	5.3	0.6	0.7	0.6	0.6	0.4
Assets abroad	7.1	80.5	38.0	60.0	90.1	84.4	7.7	3.4	4.9	7.3	6.1
Deposits abroad	7.1	24.7	30.0	41.9	55.8	50.4	2.3	2.7	3.5	4.5	3.6
<b>Securities abroad (excl. shares)</b>	<b>0.0</b>	<b>55.9</b>	<b>8.0</b>	<b>18.0</b>	<b>34.3</b>	<b>34.0</b>	<b>5.3</b>	<b>0.7</b>	<b>1.5</b>	<b>2.8</b>	<b>2.5</b>

<sup>a</sup> Assets held by provident and pension funds and life insurance schemes—mainly earmarked bonds.

SOURCE: Based on banks' financial statements, and data from TASE and the Ministry of Finance.

Another factor that affected the composition of the portfolio was the liberalization of the foreign currency market. This development was reflected *inter alia* by increased investment in foreign currency assets, and especially by the growth in Israeli residents' investments abroad. Figure 3.3 presents the development of Israeli residents' assets abroad, principally shares abroad (Israeli and foreign shares) and deposits.

The amount of assets that Israeli residents hold abroad increased rapidly in 1999, for two main reasons. The first reason was the effect of the external shock at the end of

1998, which resulted in local investors reducing their exposure to foreign currency risks. This led to a growth in demand for assets abroad. The other reason was the expansion of the high-tech industries in Israel and abroad during the years 1999-2000, which led to large rises in the high-tech shares. This development contributed to a growth in Israeli high-tech companies' stock issues abroad, part of the proceeds of which were left in deposits abroad. During the same period, the public's investments in shares abroad nearly doubled. (The following two years saw the opposite trend, as the world's equity markets fell.)

## 2. THE INDEXATION COMPOSITION OF THE ASSET PORTFOLIO

The proportion of unindexed assets in the portfolio excluding shares rose from 36.9 percent in 2002 to 39.5 percent in 2003 due to an increase in the proportion of unindexed

**Table 3.3**  
**Distribution of Assets, by Indexation (excluding shares), 1998–2003**

	(current prices)					
	1998	1999	2000	2001	2002	2003
<b>Unindexed assets</b>	<b>30.6</b>	<b>33.2</b>	<b>37.5</b>	<b>39.2</b>	<b>36.9</b>	<b>39.5</b>
Cash and liquid deposits	6.6	6.9	6.8	7.1	6.0	6.7
Term deposits	17.7	20.1	22.3	22.7	20.1	19.3
Treasury bills	2.4	2.3	3.1	2.8	3.9	4.3
<i>Gilon</i> and <i>Shahar</i> bonds	3.7	3.7	5.1	6.2	6.3	8.7
Savings schemes	0.2	0.2	0.3	0.4	0.7	0.5
<b>CPI-indexed assets</b>	<b>56.7</b>	<b>51.9</b>	<b>57.6</b>	<b>44.6</b>	<b>44.3</b>	<b>43.2</b>
Savings schemes	14.2	12.9	10.7	9.3	9.8	7.0
CPI-indexed deposits	7.6	6.5	6.5	5.8	5.6	6.4
Tradable bonds	11.6	10.3	9.0	9.2	8.6	9.6
Other assets	23.3	22.1	21.4	20.3	20.3	20.2
<b>Assets in and indexed to foreign currency</b>	<b>12.6</b>	<b>14.8</b>	<b>14.9</b>	<b>16.2</b>	<b>18.8</b>	<b>17.4</b>
<b>Assets in Israel</b>	11.6	11.2	10.5	9.9	10.1	9.6
<i>Pamah</i> (resident foreign-currency) restitutions deposits	2.7	2.1	1.8	1.8	2.0	2.0
Other <i>Pamah</i> (resident foreign-currency) deposits	5.8	6.1	6.2	5.9	6.0	5.9
Foreign-currency-indexed deposits	0.9	0.6	0.3	0.4	0.4	0.4
Tradable bonds	1.3	1.6	1.3	1.1	1.0	0.8
Savings schemes	0.9	0.8	0.9	0.8	0.7	0.5
<b>Assets abroad</b>	<b>1.0</b>	<b>10.4</b>	<b>4.5</b>	<b>6.3</b>	<b>8.6</b>	<b>7.7</b>
Deposits abroad	1.0	3.2	3.5	4.4	5.3	4.6
<b>Securities abroad (excluding shares)</b>	<b>0.0</b>	<b>7.2</b>	<b>0.9</b>	<b>1.9</b>	<b>3.3</b>	<b>3.1</b>

SOURCE: Based on banks' financial statements, and data from TASE and the Ministry of Finance.

bonds and Treasury bills (Table 3.3). The CPI-indexed asset component contracted from 44.3 percent of the portfolio in 2002 to 43.2 percent in 2003, reflecting a mixed trend: a decrease in the proportion of deposits and saving schemes, and an increase in the proportion of CPI-indexed bonds. The positive development in Treasury bills and (unindexed and CPI-indexed) bonds derived from a number of factors: the series of cuts in the Bank of Israel's interest rate resulting from the decline in inflation expectations and the appreciation of the NIS against the dollar; the reduced risk of investment in all terms of NIS assets; and the reduced profitability of investment in deposits and saving schemes resulting from the tax reform. Concurrently, the cost for the government of raising capital abroad decreased due to the receipt of US loan guarantees, and thereby made it possible to reduce the extent of government borrowing in the local bond market. This positive development had the effect of raising prices in that market. The public conducted most of their activity in the unindexed market via the mutual funds, which were exempt from capital gains tax on the sale of bonds in 2003. CPI-indexed bonds were notable for direct activity by the public, apparently due to the reduction in tax for individuals.

The proportion of foreign currency assets in the portfolio fell from 18.8 percent in December 2002 to 17.4 percent in December 2003, a change that mainly reflected the 6 percent appreciation of the NIS against the dollar following the large 10 percent depreciation in 2002. In 2003, a moderate decrease was recorded in all foreign currency assets—deposits, saving schemes and bonds. This was despite the fact that Gilboa dollar-indexed bonds at a nominal value NIS 8.8 billion were redeemed in 2003, without any further issues of these bonds. Although large in size, the Gilboa redemption does not appear to have led to major changes in the proportion of foreign currency assets. This was because those owning the bonds adjusted their holdings in good time.

### 3. DEVELOPMENT OF THE ASSET PORTFOLIO BY TERM TO MATURITY AND BY TRADABILITY

The timing composition in the public's asset portfolio remained largely unchanged in 2003 compared with December 2002. This was after the public had extended their investment duration in 2002. The proportion of short-term assets remained at a third of the asset portfolio, while the proportion of medium and long-term assets amounted to 46 percent and 20.7 percent respectively (Figure 3.4).

The distribution of the public's investments by timing composition reflected an increase in the proportion of tradable assets at the expense of non-tradable assets among all indexation types. Some 90 percent of the short-term asset component consisted of non-tradable assets—unindexed deposits or foreign currency indexed deposits. The demand for unindexed deposits declined because of the fall in interest rates that resulted from the Bank of Israel's interest rate cuts, which directly affected all bank interest

**Table 3.4**  
**Distribution of the Public's Asset Portfolio, by Term to Maturity,<sup>a</sup> 1999–2003**

	Balance (NIS billion)					Composition (percent)				
	1999	2000	2001	2002	2003	1999	2000	2001	2002	2003
<b>Total</b>	777.6	853.4	955.3	1,044.4	1,094.6	100.0	100.0	100.0	100.0	100.0
<b>Short-term assets</b>	<b>250.6</b>	<b>289.9</b>	<b>328.1</b>	<b>349.5</b>	<b>365.9</b>	<b>32.2</b>	<b>34.0</b>	<b>34.3</b>	<b>33.5</b>	<b>33.4</b>
Liquid local-currency assets	46.9	49.6	58.3	54.2	64.6	6.0	5.8	6.1	5.2	5.9
Unindexed deposits	131.2	159.5	176.6	178.6	177.2	16.9	18.7	18.5	17.1	16.2
CPI-indexed deposits	0.3	0.1	0.1	0.1	0.3	0.0	0.0	0.0	0.0	0.0
<i>Pamah</i> (resident foreign-currency deposits)	54.5	58.3	66.1	74.3	76.2	7.0	6.8	6.9	7.1	7.0
<i>Patzam</i> (exchange-rate-indexed time deposits)	3.7	2.2	2.4	2.7	2.7	0.5	0.3	0.3	0.3	0.2
Treasury bills	14.0	20.1	24.6	39.6	44.9	1.8	2.4	2.6	3.8	4.1
<b>Medium-term and other assets</b>	<b>357.2</b>	<b>384.2</b>	<b>434.1</b>	<b>479.8</b>	<b>502.2</b>	<b>45.9</b>	<b>45.0</b>	<b>45.4</b>	<b>45.9</b>	<b>45.9</b>
Savings schemes	109.2	101.6	100.1	116.5	87.7	14.0	11.9	10.5	11.2	8.0
Unindexed deposits	21.7	25.3	34.3	25.3	30.0	2.8	3.0	3.6	2.4	2.7
CPI-indexed deposits	18.1	28.8	28.8	31.8	46.6	2.3	3.4	3.0	3.0	4.3
Foreign-currency-indexed deposits	0.8	0.0	0.4	0.2	0.5	0.1	0.0	0.0	0.0	0.0
<i>Pamah</i> (resident foreign-currency deposits)	9.3	9.5	7.3	9.1	9.8	1.2	1.1	0.8	0.9	0.9
Bonds	40.9	46.7	59.8	63.6	92.9	5.3	5.5	6.3	6.1	8.5
Investment abroad	26.6	35.9	56.3	84.8	74.1	3.4	4.2	5.9	8.1	6.8
Provident funds	92.8	94.5	99.2	101.6	113.8	11.9	11.1	10.4	9.7	10.4
Advanced study funds	37.7	42.0	47.8	46.9	46.8	4.9	4.9	5.0	4.5	4.3
<b>Long-term assets</b>	<b>169.8</b>	<b>179.3</b>	<b>193.1</b>	<b>215.0</b>	<b>226.6</b>	<b>21.8</b>	<b>21.0</b>	<b>20.2</b>	<b>20.6</b>	<b>20.7</b>
Established pension funds	101.6	105.4	109.4	119.7	120.1	13.1	12.4	11.5	11.5	11.0
New pension funds	5.3	7.5	10.7	14.4	17.9	0.7	0.9	1.1	1.4	1.6
Life insurance plans										
Guaranteed-yield	40.2	40.6	41.3	44.3	43.7	5.2	4.8	4.3	4.2	4.0
Profit-sharing	22.6	25.8	31.7	36.6	44.9	2.9	3.0	3.3	3.5	4.1

<sup>a</sup> Excluding shares in Israel and abroad.

SOURCE: Based on banks' financial statements, and data from TASE and the Ministry of Finance.

rates, and due to the taxation of deposits under the tax reform. The proportion of foreign currency deposits fell as a result of the low interest rates on them and the expectations of continued calm in the foreign currency market. The proportion of Treasury bills in the asset portfolio increased, as did the share of liquid NIS assets, which offset the decrease in the proportion of deposits.

The growth in the proportion of medium-term assets reflected the increased share of indexed and unindexed bonds in the portfolio, although this was completely offset by the reduced investment in (mostly CPI-indexed) saving schemes.

The proportion of profit-sharing life insurance schemes and pension funds for new members to the public's total assets rose during 2003 due to an improvement in their

**Table 3.5**  
**Tradability of Asset Portfolio, 1999–2003**

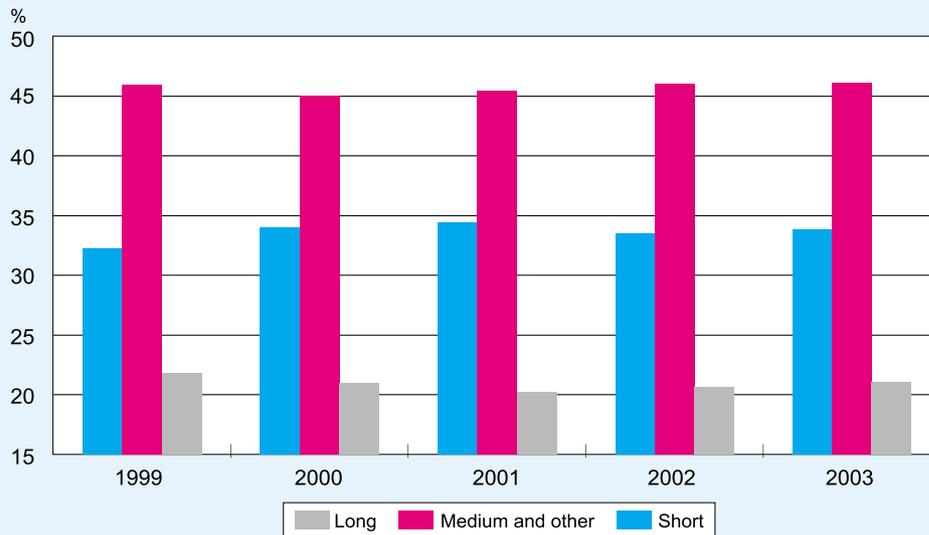
	(current prices)									
	Balance (NIS billion)					Composition (percent)				
	1999	2000	2001	2002	2003	1999	2000	2001	2002	2003
<b>Total</b>	1,103.5	1,130.4	1,212.2	1,234.5	1,385.9	100.0	100.0	100.0	100.0	100.0
<b>Tradable assets</b>	<b>468.7</b>	<b>441.9</b>	<b>459.0</b>	<b>430.9</b>	<b>581.1</b>	<b>42.5</b>	<b>39.1</b>	<b>37.9</b>	<b>34.9</b>	<b>41.9</b>
Tradable assets (excluding shares)	195.0	165.0	202.1	240.9	289.8	22.8	17.3	19.3	22.0	26.5
<b>Unindexed assets</b>	<b>46.8</b>	<b>69.8</b>	<b>85.8</b>	<b>106.0</b>	<b>141.9</b>	<b>4.2</b>	<b>6.2</b>	<b>7.1</b>	<b>8.6</b>	<b>10.2</b>
Treasury bills	18.0	26.2	27.0	40.5	47.1	1.6	2.3	2.2	3.3	3.4
<i>Gilon</i> and <i>Shahar</i> bonds	28.8	43.6	58.9	65.5	94.8	2.6	3.9	4.9	5.3	6.8
<b>CPI-indexed assets</b>	<b>80.2</b>	<b>76.5</b>	<b>87.8</b>	<b>89.7</b>	<b>104.6</b>	<b>7.3</b>	<b>6.8</b>	<b>7.2</b>	<b>7.3</b>	<b>7.6</b>
Tradable bonds	80.2	76.5	87.8	89.7	104.6	7.3	6.8	7.2	7.3	7.6
<b>Assets in and indexed to foreign currency</b>	<b>68.0</b>	<b>18.8</b>	<b>28.5</b>	<b>45.2</b>	<b>43.3</b>	<b>6.2</b>	<b>1.7</b>	<b>2.4</b>	<b>3.7</b>	<b>3.1</b>
Tradable bonds	12.1	10.8	10.5	10.9	9.3	1.1	1.0	0.9	0.9	0.7
Securities abroad (excl. shares)	55.9	8.0	18.0	34.3	34.0	5.1	0.7	1.5	2.8	2.5
<b>Shares in Israel and abroad</b>	<b>273.7</b>	<b>276.9</b>	<b>256.9</b>	<b>190.5</b>	<b>291.3</b>	<b>24.8</b>	<b>24.5</b>	<b>21.2</b>	<b>15.4</b>	<b>21.0</b>
<b>Non-tradable assets</b>	<b>634.8</b>	<b>688.4</b>	<b>753.2</b>	<b>803.6</b>	<b>804.8</b>	<b>57.5</b>	<b>60.9</b>	<b>62.1</b>	<b>65.1</b>	<b>85.1</b>
							<i>Excluding shares</i>			
<b>Unindexed assets</b>	211.7	250.4	288.9	279.3	290.3	19.2	22.1	23.8	22.6	20.9
Cash and liquid deposits	53.7	57.7	68.1	62.4	73.2	4.9	5.1	5.6	5.1	5.3
Term deposits	156.1	190.2	216.8	210.1	211.7	14.1	16.8	17.9	17.0	15.3
Savings schemes	1.9	2.5	4.1	6.9	5.5	0.2	0.2	0.3	0.6	0.4
<b>CPI-indexed assets</b>	323.4	329.6	338.2	374.4	367.9	29.3	29.2	27.9	30.2	26.5
Savings schemes	100.7	91.3	88.7	102.7	76.9	9.1	8.1	7.3	8.3	5.5
CPI-indexed deposits	50.9	55.4	55.2	58.4	70.4	4.6	4.9	4.6	4.7	5.1
Other assets <sup>a</sup>	171.8	182.9	194.3	212.3	220.6	15.6	16.2	16.0	17.2	15.9
<b>Assets in and indexed to foreign currency</b>	<b>99.6</b>	<b>108.4</b>	<b>126.1</b>	<b>150.9</b>	<b>146.6</b>	<b>9.0</b>	<b>9.6</b>	<b>10.4</b>	<b>12.2</b>	<b>10.6</b>
<i>Pamah</i> (resident foreign-currency) restitutions deposits	16.7	15.3	16.9	20.7	21.6	1.5	1.4	1.4	1.7	1.6
Other <i>Pamah</i> (resident foreign-currency)	47.2	52.6	56.5	62.9	64.5	4.3	4.6	4.7	5.1	4.7
Foreign-currency-indexed deposits	4.5	2.8	3.4	4.5	4.8	0.4	0.2	0.3	0.4	0.3
Savings schemes	6.6	7.8	7.4	6.9	5.3	0.6	0.7	0.6	0.6	0.4
Deposits abroad	24.7	30.0	41.9	55.8	50.4	2.2	2.7	3.5	4.5	3.6

<sup>a</sup> Assets held by provident and pension funds and life insurance schemes—mainly earmarked bonds.

SOURCE: Based on banks' financial statements, and data from TASE and the Ministry of Finance.

profits. Investors exploited the favorable developments in the capital market in order to increase their holdings of tradable assets, principally corporate bonds, at the expense of bank deposits. The proportion of the pension funds for established members and guaranteed-yield life insurance schemes fell. As a result, the long-term investment component remained largely unchanged.

**Figure 3.4**  
**Distribution of the Asset Portfolio (Excluding Shares) by**  
**Term to Maturity, 1999–2003**



SOURCE: Bank of Israel.

### **Box 3.1** **The Development of Structured Products**

During recent years, financial intermediaries have offered the Israeli public new forms of investment known as structured products that have existed in the Western world for several years. The balance of structured (mainly foreign currency) deposits in the banking system amounted to NIS 10 billion in September 2003, and in December 2003 issues of structured foreign currency indexed bonds totaled NIS 2.3 billion. Contributing to this development were the cut in the Bank of Israel's interest rate and worldwide interest rates, which reduced the relative attractiveness of bank deposits, and the increased sophistication of the financial markets. Structured products are financial products (usually a deposit or a bond) aimed at investors who are willing to take a certain degree of relatively low risk in return for a slightly higher return than that offered by fixed-income investments, such as government bonds or bank deposits.

These products guarantee the investor a full return on the investment principal, a guarantee that does not exist with equity investments, although the interest rates on structured deposits and bonds is lower than the usual market rates and some of them do not bear interest. In return for the waiver

of part of the interest obtained on fixed-income investment, the investor has as stated the chance of obtaining a final higher yield. This is dependent on several factors—mainly the development of the share indexes and the exchange rate or another underlying asset.

Two principal concepts are employed in the structured products market. The first concept is the range, which defines the conditions at which the investor is entitled to receive the yield guaranteed to him. This is a pre-agreed range of changes expected in one of the components of the structured product—for example, a certain level of the Libor interest rate or a certain level of the dollar-NIS exchange rate. If the actual changes exceed this range, the investor will not obtain any return on his money. The second concept is the coupon; the interest rate (return) paid on the structured product if the previously mentioned conditions are fulfilled. The coupon is sometimes the return on one of the indexes in the equity market, and is sometimes calculated in a more complicated manner, usually on the basis of interest rates abroad.

As a result of the tax reform, tax has been imposed on the interest rate on a structured product—a deposit or bond—10 percent on the nominal interest rate (coupon) and 15 percent on the real interest rate.

Since most structured deposits are for a relatively long term of 5-6 years and more, without exit stations, the investor has to wait until the end of the investment period. However, a structured bond is similar to a government bond. While the investor obtains the return guaranteed to him at the end of the bond's lifetime, he can sell it in the stock market on any trading day. The difference between a structured bond and a government bond is that with the former, the party offering the transaction (usually a financial organization from abroad) can decide to expedite the redemption of the bond—an action known as call—if that party perceives its risk exposure as being too high.