

BANK OF ISRAEL

The Government and
Finance Committee of the Knesset
Jerusalem

In accordance with sections 59 and 60 of Bank of Israel Law, 5714-1954, I respectfully submit herewith the Annual Report of the Bank of Israel for 1981.

After a decade of accelerating inflation and sluggish growth, the main economic policy targets set for 1981 were the slowing of the price advance and the encouragement of economic activity, while avoiding any worsening of the balance of payments.

To achieve these objectives, taxes were cut on consumer goods, the subsidies increased on basic products, and direct taxes were lowered. The tight credit policy was continued and adjusted to the growth and balance of payments targets.

This combination of measures resulted in the expansion of business sector activity, the toning down of inflation, and the further expansion of exports despite the world market slump.

On the other hand, the government demand surplus swelled this year. This surplus generates inflationary pressure and crowds out private investment. To realize the economic goals, it is essential to reduce this surplus by cutting government spending instead of raising taxes. Contraction of the demand surplus would divert resources to stimulating growth and reducing the balance of payments deficit.

A striking feature of the year reviewed was a sharp rise in real wages and per capita private consumption. This development calls for considerable caution in determining wage policy for 1982. Keeping wages from rising faster than productivity while reducing the tax burden on both employers and employees is a precondition for preserving the high level of employment in the economy.

Only by restraining the growth of private consumption, cutting public

spending, and creating the proper conditions for renewed economic growth
can we achieve economic stability, internal and external alike.

Sincerely yours,



Jerusalem, 9 Sivan, 5742
May 31, 1982

Dr. Moshe Y. Mandelbaum
Governor
Bank of Israel