

## BANK OF ISRAEL

The Government and  
Finance Committee of the Knesset  
Jerusalem

In accordance with sections 59 and 60 of the Bank of Israel Law, 5714-1954, I respectfully submit herewith the Annual Report of the Bank of Israel for 1977.

The Report is based on material prepared by the Research Department of the Bank. Most of the statistical data in Parts One and Two were supplied by the Central Bureau of Statistics. There is a marked discrepancy between the estimates of economic growth derived from different statistical sources. Considerable caution is therefore called for in interpreting the year-to-year changes in some of the basic trends.

The dominant feature of the year surveyed was the sluggish expansion of economic activity. But even more so than in previous years, the overall growth rate masks disparate and even contradictory trends. Exports continued to make impressive headway and led the advances recorded in agriculture, industry, transport, and tourism; on the other hand, the construction and allied industries remained in the doldrums.

The improvement in the balance of payments in the past two years eliminated the threat of a financing crisis which confronted the economy in 1974 and 1975. This development, together with the buildup of spare production capacity, has created the possibility of a gradual, controlled renewal of economic growth after it came to a standstill in 1974. But there is a danger that the resumption of growth will be led by the expansion of public and private consumption rather than exports; this would again widen the import surplus and aggravate the balance of payments problem.

The economy is capable of resuming the gradual growth of activity accompanied by the slowing of inflation and strengthening of the balance of payments. But this depends on our ability to freeze over the next few years the expansion of public services and payments for income maintenance, thereby moderating the rise in the standard of living and releasing the resources required for mending the balance of payments.

The foreign currency reform introduced at the end of October 1977 has made our policy tools more effective, but it is not a substitute for a bold policy of fiscal and incomes restraint. Such a policy is the key to renewed growth coupled with an improvement in the balance of payments and the braking of inflation.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'A. Gafni', with a long, sweeping horizontal stroke extending to the right.

**Arnon Gafni**

**Governor**

**Bank of Israel**