

B. THE ECONOMY'S ACTIVITY VIS-À-VIS ABROAD—THE FINANCIAL ACCOUNT

The trend of growth in the flow of Israelis' investment abroad, which has characterized the economy for the past 6 years, continued in 2014. The private sector's financial investments in foreign shares continued, as did the growth in foreign currency reserves, as a result of continued foreign exchange purchases by the Bank of Israel. The increase in investment in shares, combined with price increases in the capital market, led to a change in the composition of the private sector's asset portfolio abroad. There was an increase in the portion of shares in the portfolio, resulting in an increase in the portion of risk assets as well.

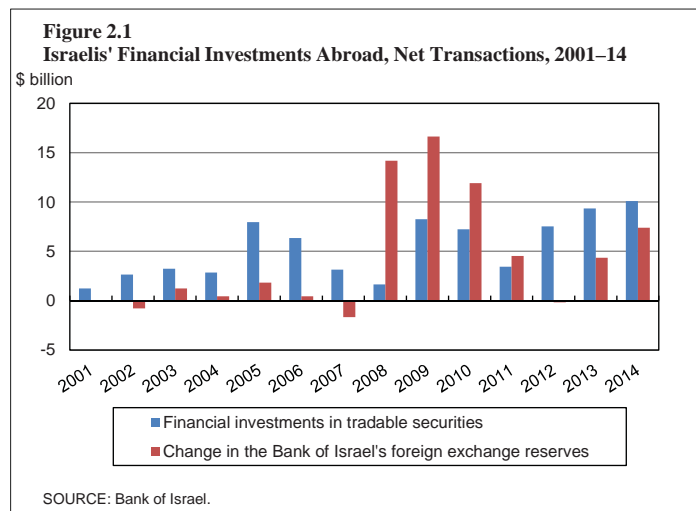
In terms of nonresidents' investment in the Israeli economy, there was significant growth in investment in securities in all channels in 2014, particularly investment in government bonds and *makam*, compared to large realizations in those channels in the previous three years. There was also significant growth in 2014 in the value of Israeli shares held by nonresidents. The dominance of the increase in the Bank of Israel's foreign exchange reserves in Israelis' overall activity vis-à-vis abroad was reflected in the rapid growth of total short-term assets, and led to continued improvement in the economy's liquidity in foreign exchange.

1. ISRAELIS' INVESTMENTS ABROAD

In 2014, the trend of growth in the flow of Israelis' investments abroad and in the Bank of Israel's foreign exchange reserves continued.

In recent years, the increase in the flow of investments abroad derived mainly from financial investments by the nonbank private sector in foreign shares.

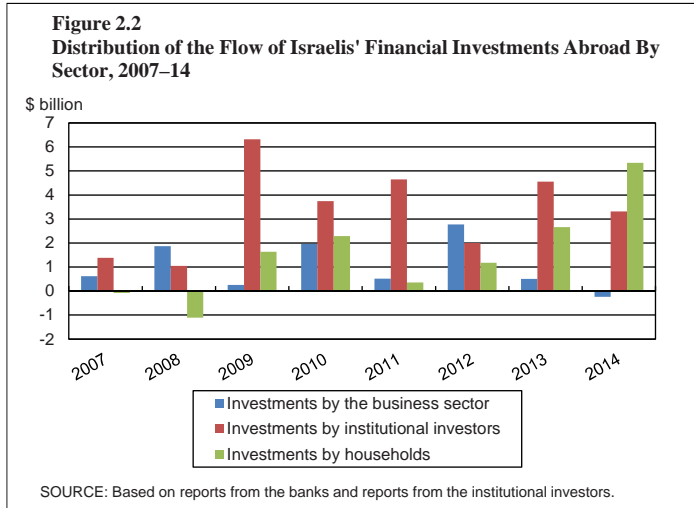
In recent years, the foreign exchange reserves also increased markedly, as a result of the Bank of Israel's foreign exchange purchasing policy.



The trend of growth in financial investments abroad was concentrated in investments by households and by institutional investors in the past two years.

The institutional investors began investing abroad as part of the diversification of their investments since the tax reform in 2004, which cancelled the tax discrimination on investments abroad.

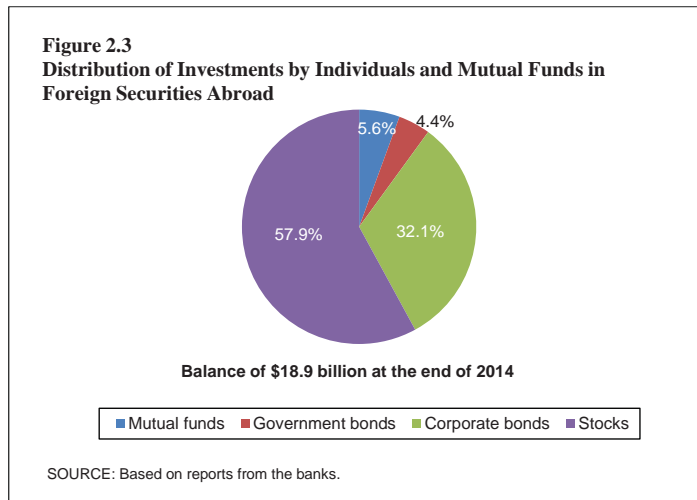
In 2014, households (individuals and through mutual funds) were prominent, with a flow of financial investments abroad totaling about \$5.7 billion, of which about \$3.1 billion was invested in foreign bonds—a significant increase over previous years.



At the end of 2014, the balance of households' (individuals and mutual funds) investment abroad was concentrated mainly in shares and corporate bonds.

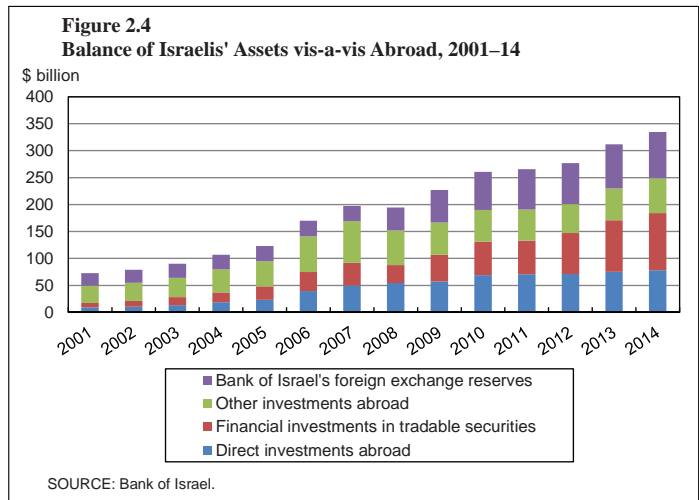
Households invest abroad mainly in shares and corporate bonds. Investment in foreign government bonds is relatively small (4.5 percent).

An analysis of investment concentration shows that households' investments in corporate bonds are spread over a large number of bonds.



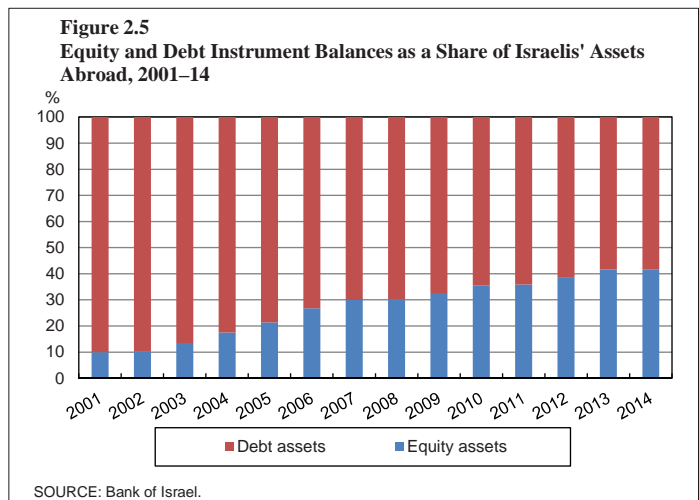
The trend of growth in Israelis' investment abroad in recent years was reflected in continued growth of the balance of assets vis-à-vis abroad.

The increase in investments abroad, combined with share price increases on the international markets led to a continued increase in the balance of assets vis-à-vis abroad, which was about \$334 billion at the end of 2014.



The increase in the balance of Israelis' investments in foreign shares was also reflected in an increase in their portion within the assets portfolio abroad.

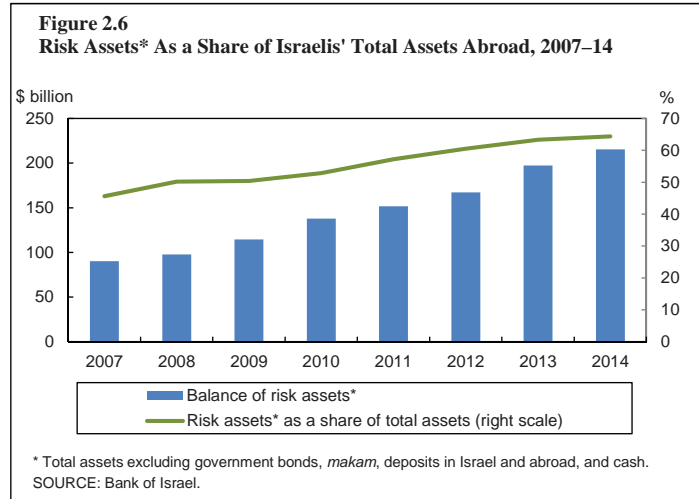
The change in the mix of assets held abroad by Israelis indicates a continued decline in the share of deposits, to about 9 percent of the assets portfolio at the end of 2014. In contrast, there was a continued increase in shares, to about 40 percent of the portfolio at the end of 2014.



The change in the mix of assets abroad was also reflected in the upward trend in the weight of risk assets*.

In 2014, the long-term upward trend in the weight of risk assets out of total assets abroad continued.

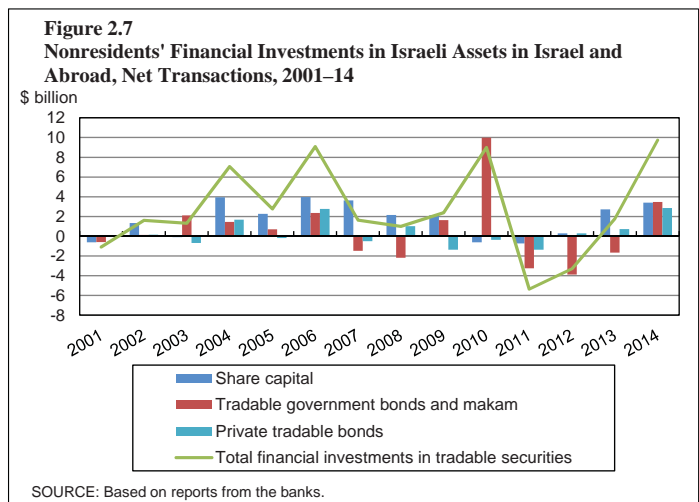
Since 2007, the rate of risk assets has increased by about 19 percentage points, to about 64 percent. The share price increases in the markets between 2012 and 2014 contributed to this.



2. NONRESIDENTS' INVESTMENT IN ISRAEL

In 2014, there was an increase in the flow of financial investments by nonresidents in Israel, in contrast to the trend between 2011 and 2013.

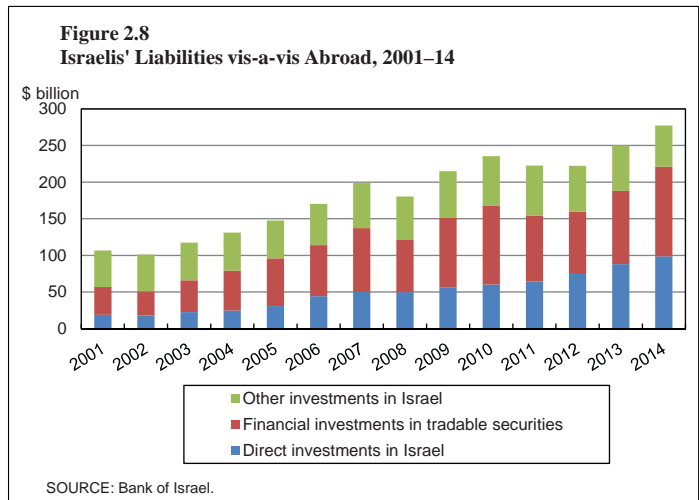
Nonresidents' financial investments were concentrated in government bonds and *makam* and in Israeli shares traded in Israel and abroad. Investments in government bonds and *makam* in 2014 were prominent against the background of the extended period of nonresidents' realizations of short-term debt instruments, which began in mid-2011.



The increase in investments combined with the increase in share prices was reflected in continued growth of the balance of liabilities to abroad in 2014.

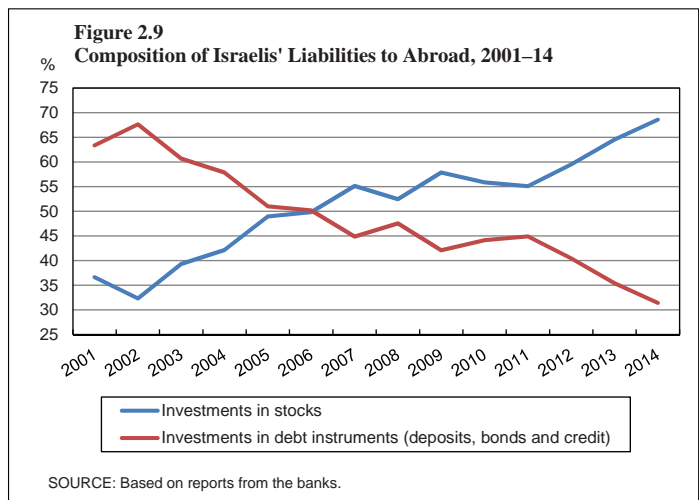
The gross balance of liabilities to abroad was about \$277 billion at the end of 2014.

The significant growth in the flow of financial and direct investments, together with the increase in share prices, led to an increase of about 10.9 percent in the balance of liabilities to abroad.



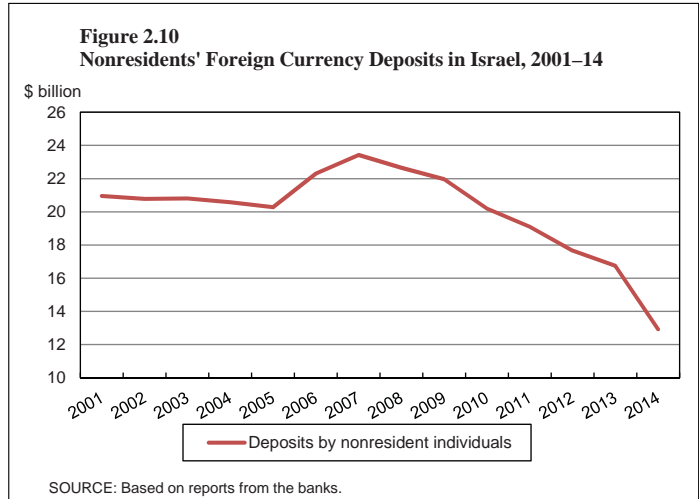
In 2014, the change in the composition of liabilities to nonresidents continued, toward increased capital liabilities.

Similar to the composition of Israelis' asset portfolio abroad, there was also a marked upward trend in the weight of shares (about 68 percent), and a decline in the weight of deposits, bonds and credit (about 31 percent) in liabilities toward nonresidents.



The sharp downward trend in nonresidents' deposits in Israeli banks contributed to the change in the composition of liabilities to abroad.

The trend of net withdrawals from nonresidents' foreign exchange deposits in Israeli banks continued in 2014. This trend began in 2007, and accelerated in 2013 and 2014, when they totaled about \$5 billion.

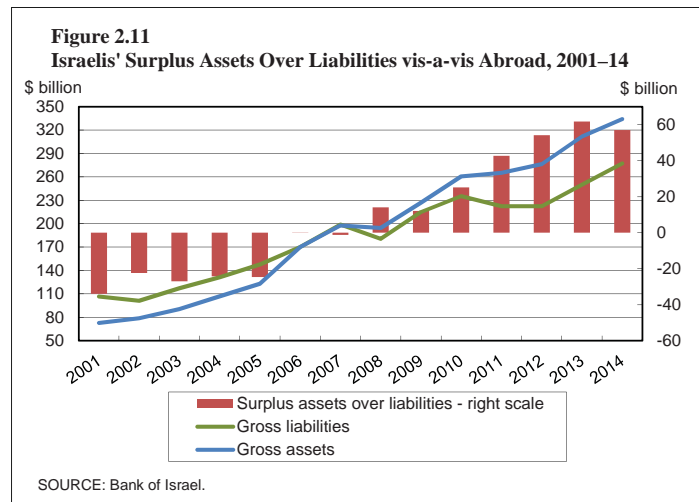


3. SURPLUS ASSETS OVER LIABILITIES VIS-À-VIS ABROAD

In 2014, the upward trend in the surplus of assets over liabilities vis-à-vis abroad was halted.

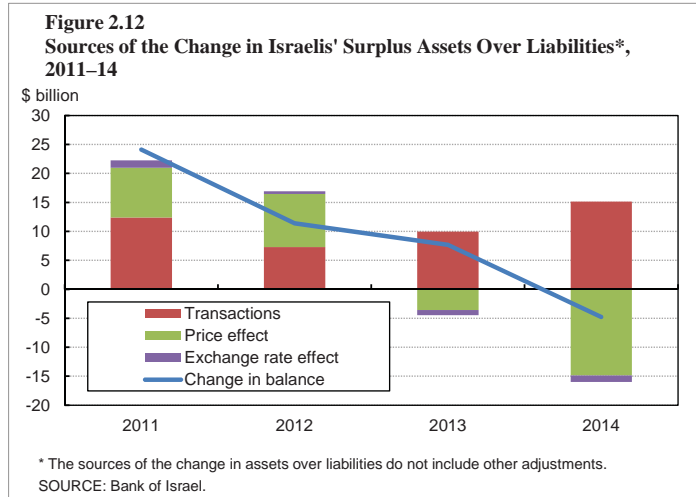
The continued increase in the value of gross liabilities vis-à-vis abroad (about \$27 billion, 10.9 percent) was only partly offset by the flow of Israelis' investments abroad in all channels (about \$22 billion, 7.2 percent). As a result, the surplus of assets over liabilities declined for the first time since 2009, to \$51.4 billion at the end of 2014.

In contrast, the increase in the surplus of assets over liabilities vis-à-vis abroad in debt instruments only (negative external debt) continued, reaching \$97 billion at the end of 2014.



The decline in the surplus of assets in 2014 reflected the significant price effect on the increase in liabilities to nonresidents.

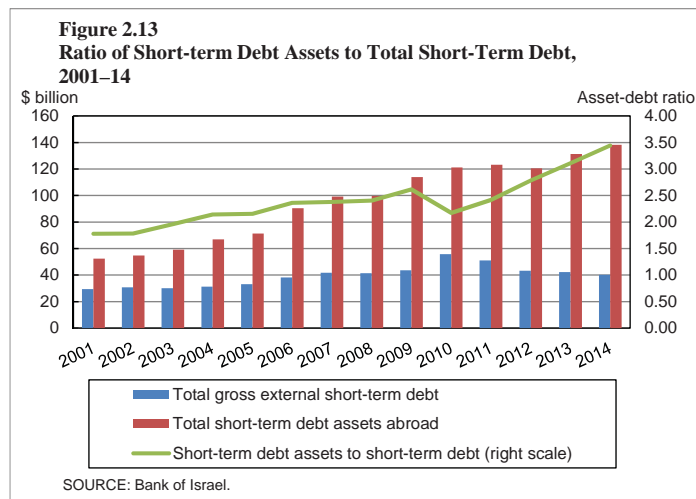
In 2014, the flow of Israelis' investments abroad was about \$15 billion greater than the flow of nonresidents' investments in Israel. Despite this, the price effect on the increase in the value of liabilities was about \$20 billion greater than its effect on the value of assets. Nonresidents hold shares of a small number of large Israeli companies, including Teva, the value of which increased markedly, mainly in the first half of the year.



The continued improvement in liquidity vis-à-vis abroad.

In 2014, the upward trend in the short-term debt assets to short-term debt ratio continued, mainly due to the increase in the Bank of Israel's foreign exchange reserves.

The volume of short-term debt assets was 3.4 times greater than the volume of short-term debt at the end of the year. In 2013–14, the increase in liquidity vis-à-vis abroad was mainly the result of an increase in short-term debt assets. In 2011–12, the increase in this ratio was mainly the result of a decline in short-term debt against the background of nonresidents' exits from *makam*.

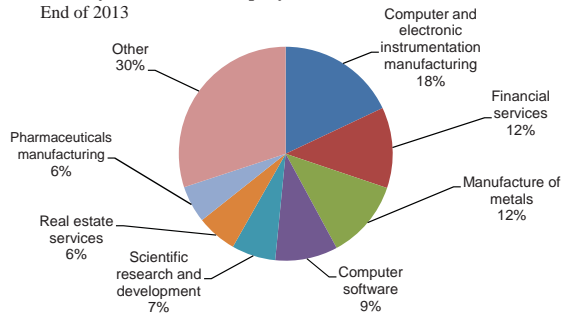


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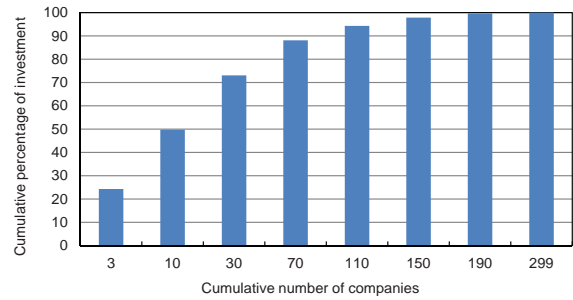
CONCENTRATION AND INDUSTRY DISTRIBUTION OF DIRECT INVESTMENTS

Figure 2.14
Distribution of Nonresidents' Direct Investment in Israel* by Industry of the Israeli Company
End of 2013



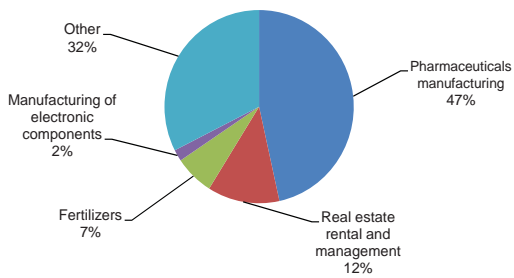
* Nonresidents' direct investments in Israel are concentrated in the computers, financial services and metal manufacturing industries. Industries that comprise 2 percent or less of nonresidents' total direct investment are grouped in "Other".

Figure 2.15
Concentration of Nonresidents' Direct Investment in Israel*
End of 2013



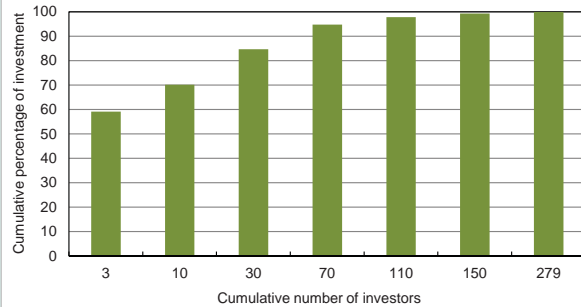
* Nonresidents' direct investment in Israel is relatively concentrated. About 70 percent of investment is invested in 30 companies.

Figure 2.16
Distribution of Israelis' Direct Investment Abroad* by Industry of the Foreign Company
End of 2013



* Israelis' direct investment abroad is concentrated in the pharmaceuticals industry. Industries that comprise less than 2 percent of Israelis' total direct investment abroad are grouped in "Other".

Figure 2.17
Concentration of Israelis' Direct Investment Abroad
End of 2013



* Israelis' direct investment abroad is highly concentrated. About 70 percent of investment is held by 10 investors.

* Private nonbanking sector, reporting companies only, comprising 67 percent of the balance.

SOURCE: Based on company reports.

Main indicators of activity vis-à-vis abroad		2010	2011	2012	2013	2014
Indicators (percent)						
Financial robustness of the economy	Gross external debt to GDP	43.4	43.6	36.7	31.6	34.9
Liquidity vis-à-vis abroad	Short-term debt assets to total short-term debt	208.2	241.7	278.3	311.0	344.3
	Foreign exchange reserves to short-term debt assets	62.6	60.7	63.0	62.3	62.3
Risks to the value of Israeli's assets abroad	Risk assets* as a share of total assets	54.5	57.2	60.5	63.3	64.4
	Stocks as a share of total assets	34.8	34.1	36.8	39.6	39.2
Openness of the economy vis-à-vis abroad	Assets + liabilities (vis-à-vis abroad) as a share of GDP	198.5	201.6	187.8	185.9	218.5
	Imports + exports (goods and services) as a share of GDP	68.0	71.4	72.3	64.5	62.2
Real contribution of abroad to the economy (liabilities)	Flow of direct investment as a share of gross capital inflow	0.3	1.7	7.2	1.0	0.7
	Flow of direct investment as a share of GDP	2.2	3.8	3.0	3.9	2.3
Main raw figures - \$ billion						
Balances	Balance of assets abroad	252.8	265.2	276.5	311.8	334.3
	<i>of which:</i> Reserves	70.9	74.9	75.9	81.8	86.1
	Balance of liabilities to abroad	234.2	222.5	222.4	250.0	277.3
	Surplus assets over liabilities	18.6	42.7	54.1	61.8	57.0
	Net external debt	-53.7	-64.5	-72.0	-86.5	-97.2
Transactions	Israelis' investments abroad	28.4	17.8	8.4	22.4	24.7
	<i>of which:</i> Direct investments	8.0	9.2	3.3	4.7	4.0
	Financial investments	9.4	3.4	8.0	9.4	10.1
	Nonresidents' investments in Israel	18.1	5.4	1.1	12.4	9.5
	<i>of which:</i> Direct investments	5.5	9.1	8.1	11.8	6.4
	Financial investments	9.0	-5.4	-3.3	1.8	9.8
Basic account	Net current account surplus	7.9	3.9	2.1	6.9	8.1
	Net foreign direct investment	-2.6	-0.1	4.8	7.1	2.5
	Basic account surplus	5.3	3.9	6.9	14.0	10.5

* Risk assets: Total assets excluding government bonds, *makam*, deposits in Israel and abroad, and cash.

SOURCE: Bank of Israel.