

## CHAPTER IX

# ACTIVITIES OF THE BANK OF ISRAEL

### 1. SUMMARY OF THE BALANCE SHEET AT THE END OF 1980<sup>1</sup>

#### (a) Main Developments

The Bank of Israel's balance sheet totaled IS56.3 billion at the end of 1980, compared with IS25.4 billion the year before—an increase of 122 percent, as against 100 percent in 1979. The faster growth this year is explained primarily by the larger devaluation of the sheqel (113.5 as against 86 percent) and the acceleration of inflation (133 vs. 111 percent).

Discounting these factors, the main balance sheet items grew more slowly this year. This was particularly noticeable in credit for financing exports and in the Bank's securities portfolio, although both items increased in real terms. The government debt rose in nominal terms at about the same rate as in 1979, while foreign exchange reserves expanded at a slightly lower rate this year.

The main item on the liabilities side—foreign currency deposits of banking institutions—also grew more slowly in dollar terms. This was a result of the smaller volume of foreign currency deposits by the public and the depreciation of deposits denominated in Deutsche marks owing to the weakening of that currency against the dollar. On the other hand, Israeli currency deposits of local banks expanded to about the same extent as the inflation rate, after declining in 1979. Banknotes in circulation rose twice as fast as last year, but still trailed behind the inflation rate.

#### (b) Foreign Currency Accounts Abroad

Foreign reserves held by the Bank of Israel<sup>2</sup> grew more slowly than in 1979—\$210 million or 8 percent, as against \$328 million or 15 percent; this brought the level up from \$2,570 million at the end of 1979 to \$2,780 million. The contribution of the private and public sectors to the change in the reserves

<sup>1</sup> Most of this section is from the Bank of Israel's Financial Statements for the Year 1980, published in February 1981.

<sup>2</sup> Foreign exchange reserves are defined as gold, foreign exchange, and foreign securities, less deposits of foreign banks and foreign currency deposits of banking institutions in Israel against nonresidents' deposits.

**Table IX-1**  
**CLAIMS ON AND LIABILITIES TO FOREIGNERS IN GOLD**  
**AND FOREIGN EXCHANGE 1979-80**

(\$ million)

End of year	1980	1979	Increase
<b>Assets</b>			
Gold, foreign currency, and securities in foreign currency	3,394.0	3,120.5	273.5
Other foreign currency assets	89.6	37.8	51.8
Total claims on the rest of the world	<b>3,483.6</b>	<b>3,158.3</b>	<b>325.3</b>
<b>Liabilities</b>			
Allocation of Special Drawing Rights	109.0	84.6	24.4
Liabilities to IMF	92.5	95.4	-2.9
Foreign currency deposits of foreign banks	5.3	13.0	-7.7
Other liabilities	11.8	12.0	-0.1
Nonresidents' deposits (Patach)	608.2	536.9	71.3
Total liabilities to the rest of the world	<b>826.9</b>	<b>741.9</b>	<b>85.0</b>
Net claims on the rest of the world (foreign currency assets)	<b>2,656.7</b>	<b>2,416.4</b>	<b>240.3</b>
<b>Net foreign exchange reserves with the Bank of Israel<sup>a</sup></b>			
	<b>2,780.5</b>	<b>2,570.6</b>	<b>209.9</b>

<sup>a</sup> Defined in note 2.

was similar in both years: the private sector reduced the reserves by \$870 million, compared with \$800 million in 1979, while the public sector contributed some \$1,100 million in both years. The larger diminution of reserves by the private sector in 1980 took place despite an improvement in its current account position, and is apparently explained by the steeper decline this year in capital imports.

The improvement in the private sector's current account was due to a real decrease in imports following the slowing of economic activity, and a continued real expansion of exports. On the other hand, the sector's terms of trade worsened this year, mainly because of the rise in oil prices; as a result, the civilian import surplus shrank by only some \$300 million.

Most of the decline in the sector's capital imports was in short-term movements, while unilateral transfers and medium- and long-term imports remained at roughly last year's level.

A breakdown of the public sector's contribution to the incremental reserves shows no marked change from last year: government and Jewish Agency transfers from abroad totaled some \$900 million, and Bank of Israel income from interest and exchange rate differentials on gross foreign currency assets

added up to \$210 million, as compared with the 1979 figure of \$265 million.<sup>3</sup>

The growth of reserves was recorded in the first seven months of the year, when they rose by \$377 million; in the remaining five months they were drawn down by \$167 million. The public sector contributed some \$900 million to the increment during the first period and only \$200 million during the rest of the year. The private sector reduced the reserves mainly in the first and last third of the year—by \$380 million and \$350 million respectively. In the middle third it drew the level down by only \$140 million. This uneven pattern apparently reflected changes in short-term capital movements, such as the repayment of short-term credit from abroad, particularly in the first quarter, owing to the extra interest charge on foreign currency credit which was introduced in 1979; this contributed to the decline in such credit in 1980 as well, and hence in the repayment of short-term credit.

The Bank's foreign currency assets held abroad reached \$3,395 million at the end of 1980, as against \$3,120 million the year before—an increase of 9 percent. The difference between the gross and net figures mainly represented the commercial banks' obligatory liquidity deposits with the Bank of Israel against nonresidents' deposits.

### **(c) Government Accounts**

Credit to the government expanded by IS1.3 billion to reach IS5.5 billion by year's end. The government pumped IS4.9 billion into the economy in 1980, compared with IS1.5 billion in 1979.<sup>4</sup> The slower growth of the government's debt to the Bank of Israel in comparison with its liquidity injection was due to several factors: the government transferred IS4.8 billion in foreign currency to finance its domestic activities, and Bank of Israel profits to the tune of IS3.1 billion were transferred to the government (this does not constitute a liquidity absorption); on the other hand, the government was charged with IS4.2 billion in interest and exchange rate differentials on its debt to the Bank (this does not constitute a liquidity injection). In fiscal 1980/81 the injection amounted to roughly IS4 billion, or IS2.7 billion excluding the Jewish Agency.

The overall influence of the government on aggregate domestic demand is estimated as the excess of its domestic expenditure over its revenue from taxes and other compulsory payments. This excess reached IS11 billion in 1980, compared with IS2 billion in 1979. It was financed by foreign currency transfers,

<sup>3</sup> The slower growth of the Bank's income in dollar terms mainly reflected the downward revaluation of assets in German marks by some \$138 million as a result of the weakening of that currency against the dollar by about 12 percent.

<sup>4</sup> These sums include the liquidity injection by the Jewish Agency. Excluding Jewish Agency operations, the government injection totaled IS3.8 billion in 1980, compared with IS0.9 billion in 1979.

net capital mobilization, Bank of Israel profits, and credit from the Bank of Israel.

The government's liquidity injection did not proceed at an even pace during the year, as it was influenced by fluctuations in its expenditures, tax collections, and net capital mobilization. In the first quarter the injection was relatively high, running at a monthly average of IS580 million; this was in contrast to the usual pattern, for the government generally absorbs liquidity during this period, which constitutes the final quarter of the fiscal year. Subsequently the pumping of money into the economy slowed (a monthly average of IS330 million from April to June), and there was even an average absorption of IS216 million in July and August. This slowdown and subsequent absorption mainly reflected the sharply higher volume of bond issues to the public during this period. The last third of the year once more saw a larger injection, which reached an average of IS660 million a month, even though total bond issues to the public declined but slightly during this period.

#### **(d) Loans and Discounts**

This item totaled IS19.3 billion at the end of 1980, as against IS8 billion the year before. Most of the balance consisted of the Bank's participation in export funds, which grew by 147 percent to reach IS18.8 billion, of which IS16.2 billion (\$2.1 billion) was in foreign currency and IS2.6 billion in local currency. The other components were IS0.2 billion in directed credit for domestic activity and the IS253 million balance of the special loan granted to banks to reduce their liquidity deficiencies.

Most of the growth in the credit balance was accounted for by the export funds, especially those providing credit in foreign currency, where the figure rose by \$284 million (15 percent) to reach \$2.1 billion. It should be noted that the changes in the credit item reflected only the direct participation of the Bank of Israel in directed domestic credit.<sup>5</sup>

The bulk of the \$284 million increase in the foreign currency export funds was accounted for by the Diamond Fund, which rose by \$206 million (22 percent) to reach \$1.1 billion at the end of 1980. The Imports-for-Export Fund expanded by \$49 million (16 percent) to stand at \$364 million. There was hardly any change in the Export Shipments Fund, which finished the year with a balance of \$605 million. The total increase in Bank of Israel credit lagged a little behind the rate of growth of exports in dollar terms.

The rapid increase in the Diamond Fund occurred despite the slowing of activity in the industry this year and the reduction of the Bank of Israel's participation in October—from 80 to 70 percent in the financing of inventories and

<sup>5</sup> The credit item in the balance sheet does not include exemptions from obligatory liquidity deposits in the funds.

from 90 to 80 percent in the financing of exports. The industry apparently took greater advantage of the subsidized credit available from this source following the sharp rise in world interest rates; this applies in particular to the financing of stocks.

The Export Shipments Fund totaled \$605 million at the end of 1980, compared with \$593 million the year before, a rise of only \$12 million, following a \$207 million (54 percent) increase in 1979. The average balance for the year was 26 percent higher than in 1979. The rate of financing in this fund was reduced in October 1980 from 85 to 80 percent.

The Imports-for-Export Fund reached \$364 million at the end of 1980, as against \$315 million in the previous year—a growth of \$49 million, or 16 percent. The rate of financing in this fund was reduced in October from 80 to 75 percent.

In April 1980 the interest rates in the foreign currency export funds were increased, being set at 60 percent of the interbank rate abroad. In the Diamond Fund the rate was raised in October to 70 percent of the foreign rate.

Local currency credit granted by the Bank through the export production funds grew in 1980 by IS1.6 billion to total IS2.6 billion. This resulted from the expansion of exports and from the raising of the Bank's participation in the funds from 65 to 75 percent in compensation for the reduction of the liquidity exemptions to a similar extent.

The special loan granted to banks, which was made conditional on their restraining the growth of nondirected credit in both local and foreign currency, was reduced by 25 percent and stood at IS253 million at the end of 1980.

#### (e) **Securities**

The Bank's securities portfolio consists of indexed government bonds acquired by the Bank in its capacity as the government's agent and for regulating secondary market trade, as well as nontradable bonds (Employers Loan and the Defense Loan) purchased by the Bank from firms as from 1978, after the freezing of directed credit for the domestic market.

The revalued balance of the Bank of Israel's portfolio reached IS3.9 billion at the end of 1980, as against IS1.5 billion the year before, an increase of 165 percent. The tradable securities portfolio rose from IS0.9 billion to IS2 billion, or by 111 percent. This modest increase, which includes revaluation, also reflected bond redemptions and the Bank's intervention in the secondary market, which resulted in a net sale of IS0.2 billion, in contrast to a net purchase on a similar scale in 1979. Most of the sales were made when the secondary market was booming, and were mainly intended to moderate fluctuations.

The nontradable securities portfolio expanded from IS0.5 billion at the end of 1979 to IS1.9 billion, a jump of 264 percent. The portfolio consists pre-

Table IX-2

## STATEMENT OF CHANGES IN ASSETS AND LIABILITIES FOR THE YEAR ENDED DECEMBER 31, 1980

	Total assets and liabilities (IS million)				Assets and liabilities in or linked to foreign currency (in terms of U.S. \$ million)			
	Balance on 31.12.79	Balance on 31.12.80	Increase		Balance on 31.12.79	Balance on 31.12.80	Increase	
			IS million	%			\$ million	%
<b>Assets</b>								
Foreign assets	11,165	26,294	15,129	135.5	3,158	3,484	326	10.3
Government debt	4,209 <sup>a</sup>	5,459 <sup>a</sup>	1,250	29.7	740	563	-177	-23.9
Loans and discounts								
In foreign currency	6,589	16,213	9,624	146.1	1,864	2,148	284	15.2
In local currency	1,400	3,070	1,670	119.3				
Securities	1,478	3,824	2,446	165.5				
Other assets	576 <sup>a</sup>	1,362 <sup>a</sup>	786	136.5	122	139	17	13.9
Total assets	25,417	56,322	30,905	121.6	5,884	6,334	450	7.6
<b>Liabilities</b>								
Banknotes and coins in circulation	1,376	2,537	1,161	84.4				

Foreign liabilities	426 <sup>a</sup>	828 <sup>a</sup>	402	94.4	121	110	-11	-9.1
Foreign currency deposits of the government and National Institutions	1,040	2,334	1,294	124.4	294	309	15	5.1
Foreign currency deposits of banking institutions in Israel	19,461	42,288	22,827	117.3	5,505	5,603	98	1.8
Against residents' deposits — restitution	10,025	19,635	9,610	95.9	2,836	2,602	-234	-8.3
Against residents' deposits — other	7,538	18,062	10,524	139.6	2,132	2,393	261	12.2
Against nonresidents' deposits	1,898	4,591	2,693	141.9	537	608	71	13.2
Deposits of banking and financial institutions in Israel	904	2,007	1,103	122.0				
Other liabilities	2,210 <sup>a</sup>	6,328 <sup>a</sup>	4,118	186.3	277	334	57	20.6
Total liabilities	<b>25,417</b>	<b>56,322</b>	<b>30,905</b>	<b>121.6</b>	<b>6,197</b>	<b>6,356</b>	<b>159</b>	<b>2.6</b>
Foreign exchange reserves held by the Bank of Israel <sup>b</sup>					<b>2,570</b>	<b>2,780</b>	<b>210</b>	<b>8.2</b>

NOTE: The notes at the end of the chapter are an integral part of the financial statements.

<sup>a</sup> Consists of sums in or linked to foreign currency and unlinked sums.

<sup>b</sup> Defined as gold, foreign exchange, and foreign securities, less deposits of foreign banks and foreign currency deposits of banking institutions in Israel against nonresidents' deposits (see notes 2 and 7).

dominantly of nontradable loan certificates acquired under repurchase agreements from local firms as a substitute for directed credit, as well as bonds issued as cover for savings schemes and acquired from banks outside the Stock Exchange. Excluding revaluation, this component rose by IS0.4 billion, almost all of it Employers Loan certificates purchased from firms.

#### **(f) Banknotes and Coins in Circulation**

On February 22, 1980 it was announced that the Israeli pound would be replaced by the sheqel. Banknotes and coins denominated in sheqalim and new agorot were put into circulation, while the Israeli pound continued to be legal tender.<sup>6</sup> By the end of the year, more than 90 percent of total currency in circulation consisted of banknotes denominated in sheqalim, but only 52 percent of the coins were new agorot.

The balance of banknotes and coins in circulation reached IS2.5 billion at the end of 1980, as opposed to IS1.4 billion the year before—an increase of IS1.1 billion, or 84 percent, compared with 41 percent in 1979. This year's growth rate was lower than the 98 percent rise in the money supply; the proportion of currency in the money supply thus fell from 34 percent in 1979 to 31 percent.

The acceleration of inflation necessitated the introduction into circulation (on December 14, 1980) of a IS100 banknote (bearing the portrait of Ze'ev Jabotinsky). At the same time the proportion of the larger banknotes—IS50, IS100, and IL500—rose to about 85 percent of total currency in circulation, compared with 71 percent at the end of 1979. The IS100 note (which was in circulation for only half a month in 1980) accounted for 14 percent of the total.

#### **(g) Israeli Currency Deposits of Banking Institutions**

Banking institution deposits in Israeli currency with the Bank of Israel totaled IS2 billion at the end of 1980, compared with IS0.9 billion the year before; this was an increase of 122 percent and reversed the 16 percent contraction in 1979. This year's growth reflected the expansion of the public's local currency deposits—both demand deposits and negotiable certificates of deposit—after several years of significant real decline. The reversal of trend apparently reflected an adjustment to the inflation rate, and was apparently also connected with the much heavier volume of stock market trade this year, which necessitated the holding of large deposits by the public.

<sup>6</sup> On that date only the 1, 5, and 25 agorot coins ceased to be legal tender; these, however, could be exchanged for sheqalim at Bank of Israel branches.



Table IX-3

## BANKNOTES AND COINS IN CIRCULATION BY DENOMINATION, 1979-80

End of period	1979		1980	
	IS million	%	IS million	%
<b>Banknotes</b>				
Israeli pound series				
IL1 and IL½	—	—	0.4	—
IL5	2.9	0.2	2.5	—
IL10	32.2	2.4	8.8	—
IL50	38.7	2.9	11.4	1
IL100	279.1	21.1	19.7	1
IL500	971.1	73.3	169.1	7
Total	<b>1,324.6</b>	<b>100.0</b>	<b>211.9</b>	<b>9</b>
Sheqel series				
IS1	—	—	30.4	1
IS5	—	—	28.7	1
IS10	—	—	212.6	9
IS50	—	—	1,624.2	66
IS100	—	—	357.3	14
Total	—	—	<b>2,253.2</b>	<b>91</b>
Total banknotes	<b>1,324.6</b>	<b>100.0</b>	<b>2,465.1</b>	<b>100</b>
<b>Trade coins</b>				
Israeli pound series				
1-500 prutot	0.2	0.5	0.2	—
1 agora	0.3	0.7	0.3	1
5 agorot	1.0	2.6	0.9	2
10 agorot	3.9	9.6	3.3	7
25 agorot	1.2	3.0	1.0	2
IL½	3.7	9.3	2.7	5
IL1	15.3	37.9	8.9	18
IL5	14.7	36.4	6.3	13
Total	<b>40.3</b>	<b>100.0</b>	<b>23.6</b>	<b>48</b>
Sheqel series				
1 new agora	—	—	0.4	1
5 new agorot	—	—	0.9	2
10 new agorot	—	—	9.6	19
IS½	—	—	14.8	30
Total	—	—	<b>25.7</b>	<b>52</b>
Total trade coins	<b>40.3</b>	<b>100.0</b>	<b>49.3</b>	<b>100</b>
Total banknotes and trade coins	<b>1,364.9</b>		<b>2,514.4</b>	
<b>Commemorative coins</b>				
Israeli pound series	11.4		17.6	
Sheqel series	—		4.6	
Total	<b>11.4</b>		<b>22.2</b>	
Total banknotes and coins	<b>1,367.3</b>		<b>2,536.6</b>	

**Table IX-4**  
**INTEREST RATES PAID BY THE BANK OF ISRAEL ON IS DEPOSITS OF**  
**BANKING AND FINANCIAL INSTITUTIONS<sup>a</sup>**

(Percentages)

Type of asset	Breakdown of required liquid cover by interest rates paid				
	Total liquidity requirement	Interest rate steps			
		0	22	63	75
Ordinary demand deposits	55	15	37.5	2.5	Balance
Time deposits					
2-3 months	17	6	7	4	Balance
3-4 months	15	5	7	3	Balance
4-5 months	13	5	6	2	Balance
5-6 months	11	4	5	2	Balance
6+ months	9	3	4	2	Balance
Negotiable certificates of deposit					
3+ months	18	6	9	3	Balance
Nondirected credit in IS	5	—	—	5	Balance

<sup>a</sup> Rates in force on December 31, 1980.

#### (h) Foreign Currency Deposits of Banking Institutions

The banking institutions' foreign currency deposits with the Bank of Israel represent their required cover against three types of deposits of the public: those of German restitution recipients (Patam restitution—formerly Pazak and Tamam); other ordinary residents' deposits (Patam); and deposits of nonresidents, exporters, and new immigrants (Patach). The balance of all these foreign currency deposits in the Bank of Israel at the end of the year stood at \$5.6 billion, equal to IS42 billion (about three-fourths of the Bank's balance sheet). The increase in these deposits came to 117 percent, compared with 113 percent last year; in dollar terms, however, there was hardly any change. A breakdown of these deposits shows that residents' restitution accounts rose 96 percent to IS19.6 billion; in dollar terms the balance fell 8 percent, from \$2.8 billion at the end of 1979 to \$2.6 billion. Part of the decline is explained by the weakening of the German mark<sup>7</sup> against the dollar, but there was a real decrease even in DM terms, reflecting both an increased conversion of these deposits into local currency and the transfer by heirs of some \$65 million of deposits to Patam accounts.

<sup>7</sup> The overwhelming majority of residents' restitution deposits are held in German marks.

Residents' deposits (Patam) went up from \$2.1 billion at the end of 1979 to \$2.4 billion a year later, a 12 percent rise in dollar terms. But after deducting interest payments and transfers from residents' restitution accounts, there was apparently a real decline in these deposits too.

Nonresidents' deposits grew by 13 percent during 1980 to reach \$608 million.

## 2. STATEMENT OF INCOME AND EXPENSES FOR 1980<sup>8</sup>

### (a) Net Income and Its Appropriation

The Bank of Israel's net income for 1980 totaled IS3.6 billion, compared with IS1.5 billion the year before—a 145 percent increase. Some two-thirds of the net income this year stemmed from the revaluation (in local currency terms) of the excess of the Bank's assets in or linked to foreign currency. Excluding these revaluation increments, net income totaled IS1.2 billion, as against IS0.4 billion last year, a growth of 222 percent.

The net income was appropriated as follows: IS500 million was provided for increasing the Bank's capital and the general reserve, while the remaining IS3.1 billion was transferred to the government.

### (b) Income

Total income for the year was IS32.5 billion, in contrast to IS12.9 billion in 1979, an increase of 152 percent. In accordance with generally accepted accounting practice, these figures include the revaluation of assets in or linked to foreign currency. Excluding revaluation, the Bank's income for 1980 was IS7.3 billion, as against IS2.2 billion the year before. Following is an analysis of the main components.

Interest on the investment of foreign currency assets abroad rose from IS0.8 billion (\$265 million) in 1979 to IS2.3 billion (\$368 million). This substantial increase stemmed from a rise in interest rates on the major world currencies and a higher average level of foreign exchange reserves.

Interest income from loans and rediscounts grew from IS0.5 billion in 1979 to IS2 billion, reflecting both the higher interest rates on such credit and the higher average balance this year.

Income earned on the Bank's securities portfolio came to IS2.1 billion, as against IS0.5 billion in 1979. This item consists mainly of indexation increments and interest. The sharp jump resulted from the acceleration of inflation and an increase in the average balance of the portfolio. It should be noted that part of this income is not included in the Bank's net income due to the matched timing principle (see note 1 to the Financial Statements).

<sup>8</sup> See note 1.

Net interest income from the government's debt reached IS379 million this year, as compared with IS57 million in 1979. The growth is attributable to a long-term advance granted at the end of March 1980 and to the volume of provisional advances extended to the government during 1980 (in 1979 it did not resort to provisional advances in most months). The interest paid by the Bank of Israel on government deposits was set off in the Bank's statement of income and expenses against interest received on the government's debt to the Bank.

### (c) Expenses

The Bank of Israel's expenditures totaled IS27.2 billion in 1980, as against IS11.1 billion the year before, a 145 percent increase. The increment includes revaluation differentials on foreign currency liabilities, which arose from the devaluation of the Israeli currency during the year. Most of the differentials were on foreign currency deposits of banks, which reached IS20.5 billion in 1980. Excluding revaluation, the Bank's expenses totaled IS4.4 billion, compared with IS1.5 billion in 1979.

The dominant expenditure item is interest paid on the commercial banks' obligatory liquidity deposits in foreign currency; this reached IS3.4 billion, nearly three-fourths of the total expenditure in 1980. Higher interest rates were mainly responsible for the growth of this item.

Interest paid on the banks' obligatory liquidity deposits in local currency rose from IS0.1 billion in 1979 to IS0.5 billion, owing to both higher interest rates and the expansion of the average balance of these deposits.

## 3. DIRECTED BANK OF ISRAEL CREDIT<sup>9</sup>

The granting of directed credit is the responsibility of the Credit Control Department of the Bank of Israel, which is assisted by committees comprising representatives of the various government ministries. The credit is actually provided by joint funds of the Bank of Israel and the commercial banks, and is intended primarily to meet the working capital requirements of export enterprises. Besides making financing available for preferred purposes, the credit contains a hidden subsidy in the form of a below-market rate of interest, which is made possible by the low rate charged by the Bank of Israel on its participation in the various funds. (For a breakdown of the funds' sources of financing and their interest rates see Table IX-5.)

Directed export credit is given partly in Israeli currency at 57 percent interest,

<sup>9</sup> The data on directed credit in this section differ somewhat from those in Chapter VIII, since the figures here are based on the weekly liquidity statements submitted by the banks to the Credit Control Department, which include the directed credit granted by investment banks, whereas in Chapter VIII they are based on monthly reports and do not include directed investment bank credit.

Table IX-5

## STRUCTURE AND TERMS OF DIRECTED CREDIT FUNDS, 1979-80

(Percentages)

End of period	Sources of funds in 1979				Sources of funds in 1980			
	Commercial banks	Bank of Israel		Interest rate in 1979	Commercial banks	Bank of Israel		Interest rate in 1980
		Liquidity exemptions	Rediscounts or loans			Liquidity exemptions	Rediscounts or loans	
<b>Export funds in foreign currency</b>								
Imports for export production	5.0	—	95.0	6.0	5.5	—	94.5	11.7
Regular export shipments	5.0	—	95.0	6.0	5.5	—	94.5	11.7 <sup>a</sup>
Special export shipments	5.0	—	95.0	11.0	5.5	—	94.5	19.5 <sup>a</sup>
Diamonds	—	—	100.0	7.9	—	—	100.0	15.2
<b>Export funds in Israeli currency</b>								
Export production	7.5	27.5	65.0	26.0	5.5	19.5	75.0	57.0
Citrus	7.5	27.5	65.0	26.0	5.5	19.5	75.0	57.0
Indirect exports	7.5	27.5	65.0	36.0	5.5	19.5	75.0	66.5
<b>Working capital funds in Israeli currency</b>								
Supervised farm credit	15.0	85.0	—	40.0	5.0	—	95.0	55.0
Assistance to agricultural settlements	15.0	—	85.0	44.0	40.0	—	60.0	57.0
Industry and crafts	15.0	35.0	50.0	40.0	15.0	—	85.0	55.0
Assistance to industrial enterprises <sup>a</sup>	15.0	—	25.0	44.0	40.0	—	60.0	57.0
General fund	15.0	35.0	50.0	40.0	15.0	—	85.0	55.0
Employers Loan Fund	—	10.0	90.0	<sup>b</sup>	—	10.0	90.0	<sup>b</sup>

<sup>a</sup> The credit is given in various currencies; the interest rate appearing here relates solely to that on dollar credits.<sup>b</sup> The interest rates vary in accordance with the rates specified in the relevant bond issues.

and partly in foreign currency (by the Diamond Fund at 15 percent interest, and by other funds mostly at 12 percent in U.S. dollar terms). Working capital credits are given in Israeli currency at 56 percent interest, and go mainly to industry and agriculture (apart from the Employers Loan Fund, credit from which is linked to the consumer price index). For the sake of comparison it should be noted that in 1980 the market rate of interest was about 30 percent on nondirected dollar credits (including a 12 percent surcharge, which was reduced to 9 percent in December 1980) and over 100 percent for Israeli currency loans.

The balance of directed credit in Israeli and foreign currency provided by the export and working capital funds came to IS20.2 billion at the end of 1980, compared with IS8.3 billion the year before—an increase of 143 percent, as against 126 percent in 1979. In real terms the increase was roughly 4 percent, similar to the 1979 figure. The year reviewed saw a further rapid growth of directed export credit, in contrast to the sluggish increase in credit for domestic activities. Outstanding directed export credit in foreign and Israeli currency came to IS19.7 billion at the end of 1980, up 145 percent from the previous year and 151 percent on an annual average. The increment reflected both the devaluation of the sheqel and the expansion of export volume in dollar terms. Export credit in Israeli currency rose 137 percent in 1980, and that in foreign currency by 147 percent; the relatively similar growth of these two components contrasted with the pattern in previous years, when the cheaper local currency credit expanded more rapidly.

As opposed to the steep rise in export credit, that for domestic activities increased only 85 percent. This is explained by the Bank of Israel's policy of restraining the real growth of such financing in favor of export credit. All the incremental credit for the domestic market originated in a new fund which provides conversion loans to agriculture.

#### **(a) Export Funds**

These funds finance all stages of export production, through the Export Production Fund (in Israeli currency); the import of inputs through the Imports-for-Export Fund (in foreign currency); and shipments through the Export Shipments Fund (in foreign currency). There are also two branch funds: the Diamond Fund (in foreign currency) and the Citrus Fund (in Israeli currency). The Indirect Export Fund assists enterprises supplying intermediates for production for the foreign market. In addition, there are special arrangements for export transactions requiring long-term financing.

The IS19.7 billion balance of directed export credit at the end of 1980 consisted of IS3.4 billion in Israeli currency and IS16.3 billion (\$2,157 million) in foreign currency, of which IS8.6 billion (\$1,143 million) was in the Diamond Fund.

Directed export credit, as mentioned, continued to expand strongly in 1980. The balance of the funds granting finance in Israeli and foreign currency, apart from the Diamond Fund, grew during the year by 134 percent (145 percent on an annual average). This reflected increases of 137 percent in the Israeli currency funds and 133 percent in the foreign currency funds. In dollar terms the latter grew 9 percent, compared with a 22 percent gain in overseas commodity sales. The Imports-for-Export Fund expanded by 16 percent; the rate of financing provided from this source was reduced, but the interest rate remained unchanged. The Export Shipments Fund increased by a mere 3 percent owing to the lowering of the rate of financing in October 1980, which found expression only at the end of the year and not in the average balance (which was up 29 percent in dollar terms).

The growth of directed export credit in Israeli currency (137 percent in December levels and 134 percent on an annual average) reflected rises of 134 percent in the Export Production Fund and 146 percent in the Citrus Fund; in the Indirect Export Fund growth was a more moderate 93 percent.

The Diamond Fund also expanded strongly—at a 29 percent annual rate in dollar terms. This was accompanied by a real increase in imports and exports of diamonds, in contrast to the two preceding years, when they declined in real terms. The rapid growth of this fund in 1980 occurred in spite of the reduction of the rate of financing by the Bank of Israel—apparently because of the heavier resort to this source, which also provides credit for maintaining diamond stocks—and is explained by the increase in the subsidy component of such financing.

In the year reviewed the Bank of Israel followed a policy of bringing the interest rates on directed credit into line with those charged on nondirected (free market) credit. In the Export Production Fund the rate was hiked from 26 to 57 percent. In December 1980 it was decided to reduce this fund by 20 percent by lowering the rate of financing from 70 to 57 percent of the return per export dollar; at the same time, in order to keep the subsidy at a relatively fixed level, it was decided to scale down the interest rate as follows: from January to March 1981 to 41.5 percent, and from April onward to 38 percent of the basic bank rate charged for approved overdraft facilities. In addition, at the beginning of the financial year 1981/82 the Bank of Israel introduced a change in the Imports-for-Export Fund, allowing the borrower to obtain credit not only in dollars but in other currencies as well—an arrangement previously in force only in the Export Shipments Fund.

#### **(b) Working Capital Funds for Domestic Production**

The year reviewed saw a continuation of the downtrend in directed credit for domestic production (excluding the funds providing assistance to various sectors and conversion loans to agriculture), which began at the end of 1977

**Table IX-6**  
**DIRECTED EXPORT CREDIT, 1979-80**  
 (IS million)

	1979		1980		Percent increase	
	End-year balance	Average balance	End-year balance	Average balance	End-year balance	Average balance
<b>In Israeli currency</b>						
Export production	1,225	891	2,867	2,105	134.0	136.3
Citrus	172	96	423	215	145.9	124.0
Indirect export	45	38	87	76	93.3	100.0
Conversion loans to agriculture	—	—	41	7	—	—
<b>Total</b>	<b>1,442</b>	<b>1,025</b>	<b>3,418</b>	<b>2,403</b>	<b>137.0</b>	<b>134.4</b>
<b>In foreign currency</b>						
Imports for export production	1,092	756	2,713	1,781	148.4	135.6
Export shipments	2,112	1,175	4,645	3,057	119.9	160.2
Special arrangements outside the funds	75	53	292	144	289.3	171.7
<b>Total, excl. Diamond Fund</b>	<b>3,279</b>	<b>1,984</b>	<b>7,650</b>	<b>4,982</b>	<b>133.3</b>	<b>151.1</b>
In \$ million	(928)	(781)	(1,014)	(972)	(9.3)	(24.4)
Diamond Fund	3,316	2,101	8,634	5,452	160.4	159.5
<b>Total foreign currency credit</b>	<b>6,595</b>	<b>4,085</b>	<b>16,284</b>	<b>10,434</b>	<b>146.9</b>	<b>155.4</b>
In \$ million	(1,866)	(1,608)	(2,157)	(2,035)	(15.6)	(26.6)
<b>Total credit from export funds</b>	<b>8,037</b>	<b>5,110</b>	<b>19,702</b>	<b>12,837</b>	<b>145.1</b>	<b>151.2</b>

SOURCE: Liquidity report of the banking institutions.



Table IX-7

## DIRECTED CREDIT FOR DOMESTIC PRODUCTION, 1979-80

(IS million)

	1979		1980		Percent increase	
	End-year balance	Average balance	End-year balance	Average balance	End-year balance	Average balance
<b>Credit from working capital funds</b>	175	183	420	366	140.0	100.0
Industry and crafts	25	21	95	69	280.0	228.6
Assistance to agricultural settlements	29	18	72	69	148.3	283.3
Conversion loans to agriculture	—	—	149	112	—	—
Other funds <sup>a</sup>	121	144	104	116	-14.0	-19.4
<b>Credit from outside the funds</b>	49	23	11	14	-77.6	-39.1
Bank of Israel loans	41	19	4	5	-90.2	-73.7
Liquidity exemptions	8	4	7	9	-12.5	125.0
Total directed credit for domestic production	224	206	431	380	92.4	84.5

<sup>a</sup> Excludes linkage differentials; includes emergency credit.

SOURCE: Liquidity report of the banking institutions.

following the government's decision to freeze credit for domestic market purposes.

Outstanding credit from the funds providing assistance to industry and agriculture rose by a daunting 280 and 148 percent respectively. This is explained by the continuation of the policy of the government and Bank of Israel to assist agricultural settlements and industrial enterprises in financial straits by enabling them to shift to export production. One of the measures adopted to aid agriculture was the establishment of a fund to provide conversion loans, i.e. the conversion of outstanding short-term credit for financing approved investments to long-term loans of up to seven years and linked 70 percent to the consumer price index.

The average rate of interest in the working capital funds went up from 40.6 percent at the end of 1979 to 56.2 percent at the end of the year surveyed. This change can be attributed to the Bank of Israel's policy of bringing the interest rates on directed credit into line with those charged in the free market.

#### 4. FOREIGN EXCHANGE CONTROL

In September 1978 the control of foreign exchange was transferred from the Ministry of Finance to the Bank of Israel, after it was recognized that this function ought to be performed within the framework of monetary policy, in coordination with the government's economic policy. Basic changes in policy and in the general permit are determined together with the Treasury.

Foreign exchange control is exercised at the Bank of Israel by two units: the Economic Unit and the Permits Unit. The former deals with changes in the general permit, procedures for authorized dealers, informational activity, and the conducting of economic surveys and studies in relevant areas. The Permits Unit deals with applications which require a special permit, including investment in or the establishment of companies abroad.

##### (a) General Permit

The general permit defines those activities which Israeli residents are permitted to undertake in foreign currency and with foreign residents. From time to time the permit is revised in the light of general economic and monetary developments and in accordance with the policy of the government and Bank of Israel. In 1980 the following changes were made:

1. To discourage the use of dollars in transactions between local residents, a ban was imposed in February 1980 on direct transfers of foreign currency between local residents' deposit accounts. At the same time special permits were issued where direct transfers were important for conducting international transactions: to exporters, shipping and aviation companies, travel agents, and insurance companies.

2. The amount of foreign currency in cash which an Israeli resident may hold in his possession or take abroad was reduced to \$500, or its equivalent in another currency; no change was made in the maximum of \$3,000 (or its equivalent in another currency) in all forms which he may hold in his possession or take abroad.

3. The list of gold coins permitted to be held for investment was enlarged to 11. An Israeli resident may purchase and sell such coins only through authorized dealers, and on condition that the coins are deposited physically with them.

4. The obligation to deposit in a local resident's foreign currency account or to convert into Israeli currency every foreign currency loan obtained from an authorized dealer was abrogated.

5. The section of the general permit pertaining to transit transactions was broadened to permit, under certain conditions, brokerage transactions, in which an Israeli resident purchases and sells goods abroad without bringing them to this country.

### **(b) Circulars of the Controller of Foreign Exchange**

In addition to amendments to the general permit, the Controller of Foreign Exchange from time to time issues circulars to banks and authorized dealers. They clarify and explain the rules pertaining to the general permit, as well as the policy and activities of the Controller of Foreign Exchange. They prescribe the examinations, records, and reports required from authorized dealers. The principal subjects dealt with in 1980 and the first quarter of 1981 were as follows:

1. Extension of the freeze on the right of Israeli residents to obtain foreign currency loans directly from foreign residents. This freeze, which went into force in November 1979, was extended several times, the last time to May 1981.

2. The extra interest charged on foreign currency loans granted by the commercial banking system in Israel was reduced from 12 to 9 percent; at the same time the negative interest charged on deposits in connection with loans obtained directly from abroad was lowered from 17 to 4.5 percent (the 30 percent deposit requirement remains in force).

3. Directives were issued pertaining to the leasing of equipment from foreign residents, with a distinction made between transactions which constitute the import of services and those which actually constitute import transactions on credit. The last-mentioned are now subject to all the directives of the Credit Control Department of the Bank of Israel which apply to foreign supplier credit, including the interest charge on bank guarantees given in connection with supplier credit.

### **(c) New Method of Classifying and Encoding Foreign Currency Transactions**

In April 1981 a new system went into effect for classifying and encoding transactions and other activities conducted in foreign currency between Israeli and foreign residents. This replaces the directives issued by the Treasury in December 1977. The new system is intended to classify, in accordance with the revised definitions, payments and receipts flows between the Israeli economy and the foreign sector and within the Israeli economy itself. This will permit the preparation of a report giving combined data on foreign currency transactions by banks, authorized dealers, and others allowed to conduct such transactions other than through an authorized dealer. The system will also make it possible to construct the country's balance of payments on a cash-flow basis.

## 5. ADMINISTRATION OF STATE LOANS

### (a) Issue and Redemption of Noncompulsory Government Securities<sup>10</sup>

In 1980 the Bank of Israel doubled its issues of government bonds to the public and institutional investors, from IS2.3 billion the year before to IS5.2 billion; in real terms, however, this represented a drop of 15 percent. Redemptions, including principal, interest, and indexation increments, increased from IS1.2 billion to IS2.1 billion—in real terms a 23 percent decline.

In the first quarter of 1980 there was a negative net capital mobilization owing to jitters over a possible worsening of indexed bond terms—a trend begun in the last quarter of the previous year. In the last three quarters of 1980 there was a positive net mobilization, with the highest figures being posted in July and August. The net figure for the year as a whole came to IS3.1 billion, as against IS1.1 billion in 1979.

After it had offered only partially indexed bonds to the public since December 1975, the Bank of Israel reverted to full indexation this year. The bonds, which went on sale in July, carry interest of 3 percent p.a., payable once a year and subject to a 35 percent tax. The issues are for ten years, but may be redeemed after six years from issue date. If cashed in ahead of maturity, the bonds will be linked to the next to the last consumer price index published; if held until the end of ten years, they will be linked to the most recent published index. With the resumption of fully indexed issues, the sale was discontinued of dollar-option bonds linked 80 percent to the index, with a 7 percent coupon.

The public bought IS3.1 billion of government bonds in 1980, as against IS1.5 billion the year before. Despite this respectable increase, the general public's share in total bond purchases dipped to 60 percent, compared with 67 percent in 1979 and 77 percent in 1978. Most of the bonds bought by the public were of the new fully indexed issues.

Commercial banks took IS1 billion of bonds this year as cover for their savings schemes, as compared with IS0.4 billion last year. Purchases of the special savings scheme issues (the double- and dollar-option types) were very low, for the second consecutive year, amounting to only IS47 million. On the other hand, the banks bought heavily of the 80 percent indexed bonds with a 7 percent coupon and the 100 percent indexed bonds with a 3 percent coupon. One reason for this was that because of the restrictions placed on purchases of

<sup>10</sup> The data in this section reflect the operations of the State Loans Administration of the Bank of Israel, but do not include issues by other financial institutions. The latter came to IS7.1 billion in 1980, compared with IS2.9 billion the year before. The total amount issued appears in the analysis of the bond market in Chapter VIII, "The Money and Capital Markets".

the aforementioned savings scheme issues (banks were not allowed to buy such securities as long as the outstanding balance, together with that part of their portfolio that was frozen, was not reduced to under 60 percent of the banks' total savings scheme balance), in 1980 the savings schemes were covered mostly through tradable bonds. In addition, demand for the special bonds issued for banks by the Bank of Israel fell off, since the bulk of their savings scheme accumulation was covered by bonds issued by the group of concerns to which they belong.

Apart from bank purchases for savings scheme cover, financial institutions bought IS1.2 billion of government bonds from the Bank of Israel; IS0.7 billion worth were taken by pension, provident, and advanced study funds, and IS0.5 billion were against insurance company deposits.

#### **(b) Distribution and Redemption of Compulsory Loans**

The face value of compulsory loan certificates (the Savings, Defense, War, and Cost-of-Living Allowance Loans) distributed in 1980 added up to IS201 million, as against IS85 million the year before. These figures represent the value of certificates delivered to recipients through the mail or through banking institutions. This year the delivery was continued of Defense Loan certificates for 1970-73, Savings Loan certificates for 1970-75, War Loan certificates for 1973-75, and Cost-of-Living Allowance Loan certificates, while the distribution was begun of War Loan certificates to companies and self-employed (1974, linked to the 1976 index) and 1976 Savings Loan certificates to employers. In the year reviewed 370,000 certificates were sent out, compared with 430,000 in 1979.

The Bank of Israel continued its efforts to locate those whose certificates had been returned in previous years. During the first three months it concentrated on the Cost-of-Living Allowance Loan, which fell due on April 1, 1980. In 1980 the Bank remailed 83,000 certificates, as against 172,000 in the previous year. For the public's convenience the Bank of Israel operates an efficient computer terminal system, which provides up-to-date information on compulsory loan holdings of individuals and companies.

As stated, in April 1980 the Cost-of-Living Allowance Loan fell due for final redemption. The amount redeemed during the year was IS16.7 million face value, or IS120.2 million redemption value (including accrued interest and indexation increments). In August the final redemption was begun of the following Savings Loan series: the last third of the 1974 Loan, the second third of the 1975 Loan, and the first third of the 1976 Loan. All 1976 Savings Loan certificates with a face value of up to IS100 also reached maturity. Total redemption in 1980 of the 1970-76 series amounted to IS36.6 million face value, or IS400.3 million redemption value (including indexation increments, accrued interest, and interest on late redemptions); in 1979 the figures were

Table

## NONCOMPULSORY STATE LOAN ISSUES

(IS

		1979	
	Interest rate (%)	Gross issues (1)	Redemption of principal (2)
<b>A. Medium- and long-term</b>			
1. To the public and for savings schemes			
For 10 years, 80% indexation	4.0, 6.0, 7.0	1,713.3	—
For 10 years, 90% indexation	4.0	—	—
For 10 years, full indexation	3.0, 4.0	—	0.1
For 10 years, double-linkage option	5.0	84.6	—
For 6 years, full linkage to dollar	5.5	—	—
For 8 years, 70% linkage to dollar	6.0	—	—
For 5 years, option-type	4.84	—	63.4
For 7 years, full indexation	3.25, 6.5	—	26.0
Absorption Loan <sup>b</sup>	4.0	—	3.0
Other <sup>c</sup>	—	—	0.9
2. For savings schemes			
For 6 years, linked option	4.25	102.0	—
For 6 years, dollar option	5.0	5.5	—
3. For financial institutions			
For 17, 20 years, for social insurance funds	5.0, 6.5	210.4	1.6
Insurance Companies Loan	8.2, 5.8, 6.2	174.0	1.8
7½% Bank Defense Loan	7.5	—	3.4
Total medium- and long-term loans	—	2,289.8	100.2
<b>B. Short-Term Loan<sup>d</sup></b>	—	20.5	28.1

<sup>a</sup> The data in this table reflect the operations of the State Loans administration; they do not include the other data appearing in the economic analysis of the bond market in Chapter VIII.

## IX-8

AND REDEMPTIONS, 1979-80<sup>a</sup>

million)

Interest and linkage increments (3)	Net issue (1-2-3) (4)	1980			
		Gross issues (5)	Redemp- tion of principal (6)	Interest and linkage increments (7)	Net issue (5-6-7) (8)
102.8	1,610.5	1,246.3	—	447.7	798.6
16.0	-16.0	—	—	36.6	-36.6
49.4	-49.5	2,777.4	0.1	111.5	2,665.8
17.6	67.0	27.3	—	45.6	-18.3
0.6	-0.6	—	—	0.7	-0.7
0.4	-0.4	—	—	1.2	-1.2
409.3	-472.7	—	14.7	148.8	-163.5
279.9	-323.9	—	41.3	757.9	-799.2
40.7	-43.7	—	3.0	89.5	-92.5
1.1	-2.0	—	0.5	1.7	-2.2
—	102.0	44.8	—	—	44.8
—	5.5	1.9	—	—	1.9
43.0	165.8	651.6	2.8	136.0	512.8
76.8	95.4	482.5	0.7	176.9	304.9
40.1	-43.5	—	3.3	89.8	-93.1
<b>1,095.7</b>	<b>1,093.9</b>	<b>5,231.8</b>	<b>66.4</b>	<b>2,043.9</b>	<b>3,121.5</b>
3.0	-10.6	—	—	—	—

<sup>b</sup> Includes payments under the Compensation Interest on Compulsory Loans Law.<sup>c</sup> Includes loans under the Absentees' Property Law, unlinked loans, and other loans.<sup>d</sup> Sales and redemptions by the Bank of Israel.

Table IX-9

REDEMPTION OF COMPULSORY STATE LOANS, 1979-80<sup>a</sup>

(IS million)

	1979			1980		
	Redemption of principal	Interest and indexation increments	Total	Redemption of principal	Interest and indexation increments	Total
Defense Loan, 1970-73	9.8	179.6	189.4	6.1	50.4	56.5
Savings Loan, 1970-76	36.6	363.7	400.3	39.8	227.0	266.8
War Loan, 1973-75 <sup>b</sup>	11.5	140.4	151.9	6.1	43.0	49.1
Cost-of-Living Allowance Loan	16.7	103.5	120.2	0.1	0.2	0.3

<sup>a</sup> Includes payments under the Compensation Interest on Compulsory Loans Law.<sup>b</sup> Includes payments on account of the Voluntary War Loan.

IS39.8 million and IS266.8 million respectively—i.e. there was some decline in face value and an increase in redemption value.

In September 1980 the first interest coupon of the following loans fell due: the 1974 Military Procurements War Loan; the 1974 Land Appreciation War Loan, and the 1973 Voluntary War Loan (second, third, and fourth series). In October the second interest coupon of the 1970 Defense Loan fell due. The amount of all compulsory loan interest coupons cashed in during 1980 totaled IS32.7 million.

The Defense and War Loan Laws provide for the cashing in of certificates ahead of maturity in the case of the elderly, needy disabled persons, and heirs upon the death of the registered owners. The regulations concerning early redemption have been amended to also include companies and other enterprises experiencing financial hardships. Early redemption is also permitted in the case of Voluntary War Loans, with the approval of the Minister of Finance, and as compensation for waiving the receipt of development loans, with the approval of the Ministry of Industry, Trade, and Tourism. In 1980 early redemptions amounted to IS21.3 million face value, or IS341.2 million redemption value, as against IS10.8 million and IS85.5 million respectively in 1979.

Because of the continued acceleration of inflation, the interest on late compulsory loan redemptions was raised to 48 percent in July 1980 and to 68 percent in January 1981. The interest is now calculated four times annually instead of twice annually. Total payments on account of the Absorption Loans



came to IS17.5 million in 1980, compared with IS6.4 million the year before.

Under the arrangement for the early purchase of nonnegotiable Employers Loan certificates to compensate for the reduction of subsidized credit for domestic purposes, the Bank of Israel in 1980 redeemed certificates with a total face value of IS135.2 million and a currently adjusted value on the date of repurchase of IS503.3 million; of this, IS135.0 million (IS501.9 million adjusted value) was in place of working capital credits and IS170,000 (IS1.4 million adjusted value) in place of conversions of development loans.

### **(c) Bank of Israel Open-Market Operations**

The Bank of Israel operates in the secondary bond market to stabilize trade in government bonds and to promote private saving through the purchase of such paper, taking into account the prevailing monetary situation of the economy. The Bank's operations this year were aimed primarily at preventing sharp fluctuations in bond prices without altering the market trends.

In 1980 the Bank of Israel's Stock Exchange transactions tumbled 67 percent in real terms. In January, April, and November it was a net seller of bonds in response to the lively demand for such securities during these months. In January, following the sagging of bond prices in the latter part of 1979, the Bank of Israel met a heavy demand for such paper, bringing up its share in total Stock Exchange bond trade to 20 percent. In April there was another upsurge in the public's demand for bonds, and the Bank accounted for 12 percent of total turnover.

The increased activity of institutional investors (mutual funds and savings schemes) enabled the Bank to reduce its intervention in the bond market. Beginning in April its weight in total transactions gradually declined, and by October it fell to a paltry 0.2 percent of total Stock Exchange turnover. In November the Bank again stepped up its intervention in the market. During this month prices jumped precipitously on several different days, forcing the Bank to intervene in order to prevent a "buyers only" market.

### **(d) Foreign Loans**

The Bank of Israel handles the conversion (redemption in local currency) of the Independence and Development Loans (Israel Bonds). The Bonds, which are issued abroad, can be converted ahead of maturity and redeemed in Israel by institutions, investors, tourists, new immigrants, and returning Israeli residents, in accordance with the conditions prescribed by the Controller of Foreign Exchange and the relevant regulations.

Foreign loan conversions in Israel increased 12 percent in 1980 to reach \$164 million (\$147 million principal and \$17 million interest), compared with \$147 million in 1979. In current IS terms the figure was IS835 million. The

Table IX-10

## BANK OF ISRAEL OPEN-MARKET OPERATIONS, 1978-80

(IS million)

	Net purchases (sales -) on the Stock Exchange								Total transactions	Percent of total Stock Exchange trade
	Index-linked					Double-option	Dollar-linked	Total		
	(3% int.) 100%	80%	90%	(4% int.) 100%	Others					
1978	—	11.8	11.3	-21.9	-2.3	10.4	0.4	9.7	179.3	12.4
1979	—	192.1	4.0	-22.9	-2.9	-9.7	-0.1	160.5	610.4	16.3
1980	-24.1	-97.5	-5.3	-86.1	-7.3	-11.0	-0.4	-231.7	347.5	4.9
January	—	-14.3	0.7	-4.7	0.2	-1.6	—	-19.7	92.3	19.7
February	—	-10.5	0.7	-1.8	0.1	-1.0	—	-12.7	29.5	6.4
March	—	-4.8	-0.2	-1.6	-0.2	-1.0	0.1	-7.7	10.1	3.2
April	—	-35.2	-2.7	-9.1	-1.1	-2.2	-0.1	-50.4	52.4	12.3
May	—	-17.2	-0.6	-3.6	-0.5	-0.6	—	-22.5	23.8	6.3
June	—	-2.5	-0.3	-1.9	-0.1	-1.7	—	-6.5	8.6	2.0
July	—	-8.8	-0.1	-1.1	—	-0.4	—	-10.4	11.0	1.8
August	—	-0.5	-0.6	-4.8	—	—	—	-5.9	8.1	1.2
September	0.1	5.6	-0.1	-1.3	—	-0.3	-0.1	3.9	7.7	1.0
October	-0.5	—	—	—	—	-0.2	—	-0.7	1.4	0.2
November	-12.6	-4.3	-0.6	-37.9	-3.3	-0.7	-0.2	-59.6	59.5	7.1
December	-11.1	-5.0	-1.5	-18.3	-2.2	-1.3	-0.1	-39.5	43.1	3.6

weight of conversions in Israel in total foreign loan redemptions rose appreciably to stand at 60 percent, compared with 46 percent in 1979.

A breakdown of conversions by holder shows a continued increase by tourists, who accounted for 38 percent of the total (\$62 million), as against 34 percent (\$50 million) in 1979. The share of institutions, returning Israeli residents, new immigrants, and investors fell off.

## 6. ISSUE OF CURRENCY AND COMMEMORATIVE COINS AND MEDALS

### (a) Trade Coins

In 1980 the issue of trade coins was about 3.5 times greater than in the previous year, mainly due to the introduction of the sheqel coins in February. At the end of 1980 a new IS100 brownish-orange banknote bearing the portrait of Ze'ev Jabotinsky was put into circulation. At the beginning of 1981 a one-sheqel coin went into circulation; it weighs 5 grams, has a 23 mm. diameter, and on the obverse features a chalice from the period of the War of the Jews against the Romans (66-70 C.E.) and the inscription "Israel Sheqel".

**Table IX-11**  
**COINS MINTED IN 1979-80**

Coin	In Israel	Abroad	Total
<b>Israeli pound series</b>			
1 agora	2,599,634	—	2,599,634
10 agorot	4,752,333	—	4,752,333
IL1	10,840,424	—	10,840,424
Total	18,192,391	—	18,192,391
<b>Sheqel series</b>			
1 new agora	—	200,000,000	200,000,000
5 new agorot	—	69,532,000	69,532,000
10 new agorot	10,000	167,932,000	167,942,000
IS½	—	52,308,000	52,308,000
Total	10,000	489,772,000	489,782,000
Grand total	18,202,391	489,772,000	507,974,391

**Table IX-12**  
**COMMEMORATIVE COINS ISSUED BY THE BANK OF ISRAEL, 1979/80-1980/81**

Coin		Face value (in IL)	Weight (grams)	Diameter (mm.)	Number issued <sup>a</sup>		
					B.U.	Proof	Total
Independence Day, 5740-1980	(silver)	200	26.0	37	30,000	20,000	50,000
	(gold)	5,000	17.28	30	—	10,000	10,000
Hanukka, 5741-1980		(in IS)					
	(silver)	1	14.4	30	23,750	15,450	39,200
Ze'ev Jabotinsky	(silver)	25	26.0	37	20,000	12,300	32,300
	(gold)	500	17.28	30	—	7,500	7,500

<sup>a</sup> Includes coins which remained unsold by the Israel Government Coins and Medals Corporation.

## **(b) Commemorative and Special Coins**

The theme of the 1980 commemorative Independence Day coin is "Peace". The silver series was minted in B.U. and proof form,<sup>11</sup> with a silver and copper content (900/100). The gold series was issued only in proof form, and is made of gold and copper (900/100).

In 1980 the Bank issued another in the series of Hanukka coins. It features a Hanukka lamp from the island of Corfu; it was minted in B.U. and proof form, and its composition is silver and copper (850/150).

A special coin was issued in gold and in silver to mark the centenary of Ze'ev Jabotinsky's birth. The silver coin was issued in B.U. and proof form and has a 900/100 silver and copper content; the gold coin was issued in proof form, and has a 900/100 gold and copper content.

As in previous years, the Bank issued a special mint set, identical to the trade coins in circulation. This set commemorates the 25th anniversary of the Bank of Israel, and is the last set denominated in agorot and Israeli pounds. This series of 35,000 units per denomination is made of nickel, and bears a special mint mark in the form of a tiny Star of David and the Hebrew date 5740.

## **(c) Committee for the Planning of Currency and Commemorative Coins**

This committee assists the Bank in planning the banknotes and trade and commemorative coins to be issued, and recommends to the Governor of the Bank the designs which it has chosen from among those submitted by competing artists. (The members of this committee are listed at the end of this chapter.)

# **7. SUPERVISION OF BANKING AND FINANCIAL INSTITUTIONS**

## **(a) General**

In 1980 the Department of the Examiner of Banks engaged mainly in the continued monitoring of the operations of the commercial banking system and activities designed to help preserve its stability; a wide variety of measures to protect bank customers, help enforce Bank of Israel directives, and improve the system of reporting; and various arrangements connected with the changeover to the sheqel. Other activities included the promotion of banking legislation and dissemination of information in the field of banking.

One subject which occupied the Department of the Examiner of Banks in recent years was the termination of the practice of value-dating various banking

<sup>11</sup> B.U.—with a smooth edge; proof form—with a milled edge.

**Table IX-13**

**BANKING AND FINANCIAL INSTITUTIONS UNDER BANK OF  
ISRAEL SUPERVISION, 1978-80**

End of year	1978	1979	1980
Commercial banks <sup>a</sup>	24	25	25
Cooperative credit societies	3	2	2
Mortgage banks <sup>a</sup>	16	16	16
Investment banks <sup>b</sup>	9	9	9
Other financial institutions	11	11	12
<b>Total</b>	<b>63</b>	<b>63</b>	<b>64</b>

<sup>a</sup> Excludes four inactive banks and the Israel Bank of Agriculture, which is defined as a commercial bank but operates mainly as an investment bank; includes the Maritime Bank, which is defined as an investment bank but operates mainly as an ordinary banking institution.

<sup>b</sup> Includes the Israel Bank of Agriculture but not the Maritime Bank.

transactions.<sup>12</sup> This was finally abolished in 1980, following discussions with the representatives of the banks.

The Department of the Examiner of Banks introduced a uniform procedure whereby conversions from one currency to another and transfers from one account to another are recorded on the day the conversion or transfer is actually effected and not on the day of commitment. Previously foreign currency transactions were recorded in different ways by the various banks, and the Bank of Israel's method differed from that used by most commercial banks.

At the end of 1980 there were 64 banking institutions operating in Israel under the supervision of the Examiner of Banks. Of these, 30 engaged in regular banking business; they comprised 25 commercial banks, two cooperative credit societies, and three other institutions subject to the liquidity regulations. The commercial banks and credit cooperatives operated 1,040 branches (including main offices) in Israel and 32 branches in Judea, Samaria, the Gaza Strip, and Golan Heights. Total assets of the branches of the regular banking institutions in Israel reached IS299.5 billion at the end of 1980.

<sup>12</sup> The reference is to the value-dating of checks or cash deposited in demand or overdraft accounts one or two days after their actual deposit. As a result of this practice, the effective interest charged on credit granted from these sources was higher than the basic interest rate, with the difference depending on the turnover velocity rather than the amount of credit.

In 1980 a new banking institution was founded with a specialist activity—Leumi and Partners Investment Bankers Ltd.

The number of foreign branches of Israeli banks rose to 100 by the end of the year reviewed. These included 12 subsidiaries with 46 offices, 30 branches and agencies, and 24 representative offices. Total assets of the branches and subsidiaries at the end of 1980 reached \$12.2 billion.

## **(b) Activities of the Department of the Examiner of Banks**

### **1. *Legislation***

a. The proposed Banking Law (Licensing) was submitted for its second and third reading.<sup>13</sup>

b. A proposed Banking Law (Customers' Services), which will give a statutory basis to some of the relationships between banking institutions and their customers, was submitted to the Knesset this year.<sup>13</sup>

c. At the end of January 1980 an amendment to the Banking Ordinance went into force forbidding the payment of a postdated check before the date written thereon.

d. During the year a bill was submitted to the Knesset to minimize the writing of checks without cover. This will be achieved by laying down procedures for discontinuing certain bank services to offenders.<sup>13</sup>

### **2. *Financial Reports for the Public***

At the recommendation of the Minister of Finance, the Institute of Certified Public Accountants in Israel decided to postpone the enforcement of Opinion No. 23, regarding the impact of inflation on financial statements. To maintain uniformity in the preparation of financial statements, the Examiner of Banks requested the banking institutions not to incorporate in their financial statements, at this stage, explanatory notes regarding the effect of inflation on bank profits. It was decided that in nonconsolidated financial statements of the banking institutions their investments in subsidiary and associated companies should be presented on a net book value basis (equity method), rather than the historical cost basis used in the past.

### **3. *Branching***

The freeze on the licensing of new branches remained in force in 1980. The installation of automatic tellers in most of the country's banks can be regarded as a partial substitute for the opening of new branches.

### **4. *Customer Protection***

More than 2,000 complaints concerning the banking system were received from the public in 1980 by the unit dealing with such matters. The lessons

<sup>13</sup> Enacted in March 1981.

drawn in the course of dealing with some of the complaints were instrumental in issuing new procedural directives or the amendment of existing directives, both by the Examiner of Banks and by the bank managements, in matters concerning the protection of customers and the quality of the services provided.

#### *5. Commercial Bank Audits*

During the year 200 general audits were conducted in the commercial banks, and 130 audit reports were sent to the banks examined. As in previous years, the audits covered many diversified subjects.

#### *6. Follow-up and Evaluation of Commercial Banks*

In 1980 emphasis was given to problems associated with the analysis of the operations of banks as groups of companies, consisting of various types of banking institutions and other business enterprises. The expansion of Israeli banks through subsidiaries, branches, agencies, and representative offices abroad made it necessary to examine their new investment plans and to follow the expansion of existing branches.

#### *7. Audits of Specialized Banking Institutions*

In auditing the investment banks and financial institutions, the Bank of Israel team checked to see that they did not deviate from their special fields and examined their methods of calculating interest and indexation increments, commission charges, and other service fees. The unit dealing with mortgage banks engaged primarily in verifying their statements of sources and uses of funds. Other subjects dealt with were the early withdrawal of deposits, the provision of credit in excess of authorized limits, short-term flows of funds, and the publication of financial statements.

#### *8. Research and Publications*

In addition to the 1979 Annual Survey of Israel's Banking System in Hebrew and a digest in English, as well as a survey of the system's development in the first half of 1980, the research unit dealt with various other subjects, among them:

- a. Economies of scale, organizational efficiency—a cost analysis.
- b. The marginal cost of credit granted in a liquidity deficiency position.
- c. The influence of the credit freeze on the banking system in general and on individual banks in particular.
- d. The impact on the banking system of the abolition of value-dating.
- e. Measurement of the effective cost of overdraft credit facilities.
- f. Adjustment of financial statements for inflation in Israel's large and medium-sized commercial banks.

#### *9. Interbank Clearinghouse*

In 1980 the Clearinghouse Committee almost completed its work in connection with the transition to the magnetic clearing of checks. The number of non-



magnetized checks dropped to negligible proportions, so that the changeover was to all intents and purposes completed. After the sheqel was introduced in place of the Israeli pound, the Clearinghouse Committee laid down a number of rules to ensure the orderly operation of the clearinghouse during the transitional period.

#### 10. *Arab Banks*

In 1980 negotiations were completed between the owners and directors of the Bank of Palestine in the Gaza Strip and the Department of the Examiner of Banks, following which this bank can be reopened for business.

#### 11. *Advisory Committee on Matters Relating to Banking Business*

The Committee discussed various subjects relating to the banking system, including the Annual Survey of Israel's Banking System by the Examiner of Banks, the proposed Banking Law (Licensing), the proposed Banking Law (Customers' Services), the proposed Bank Accounts Law (Checks without Cover) and the reporting of unpaid promissory notes, the adjustment of banking institutions' financial statements for inflation, and the amending of the directives regarding the obligation of banking institutions to make their financial statements public. The Committee also dealt with certain circulars issued by the Examiner of Banks concerning procedural matters.

A steering committee was appointed this year to examine the possibility of establishing an automated central clearinghouse.

### 8. THE BANK OF ISRAEL AS REPRESENTATIVE OF THE STATE IN INTERNATIONAL FINANCIAL INSTITUTIONS

The Bank of Israel represents the State in all matters connected with its membership in the International Monetary Fund, the World Bank Group, and the Inter-American Development Bank. It keeps these institutions abreast of current developments in the economy as well as economic policies and plans, handles all financial transactions with them, and actively follows the discussions and the decision-making process of their boards. Where matters of an overall economic nature are concerned, the Bank of Israel acts in concert with the Ministry of Finance; on matters of political significance it coordinates its activities with the Ministry for Foreign Affairs.

#### (a) **International Monetary Fund (IMF)**

The IMF, which is the central institution of the international monetary system today, conducts its business on three different levels: (1) it monitors developments in the international system of payments, with the aim of facilitating its orderly functioning and ensuring its stability; (2) it holds annual consultations with all member countries on the state of their economies and current economic policies, in order to curb trends endangering the stability of the exchange rate system; (3) it extends financial assistance to member countries experiencing

Table IX-14

## ISRAEL'S FINANCIAL RELATIONS WITH THE INTERNATIONAL MONETARY FUND, 1954-81

(Millions of SDRs)<sup>a</sup>

	1954	1957	1959	1964	1966	1969	1970	1971	1974	1975	1976	1978	1979	1980	1981 <sup>b</sup>
<b>General Resources Account</b>															
1. Israel's quota in IMF	4.5	7.5	25.5	50.0	90.0	90.0	130.0	130.0	130.0	130.0	130.0	205.0	205.0	307.5	307.5
2. Use of IMF resources	—	1.9	—	12.5	—	45.0	—	20.0	65.0	175.8	77.0	72.4	—	31.6	25.6
Credit tranches <sup>c</sup>	—	1.9	—	12.5	—	45.0	—	20.0	65.0	32.5	12.0	—	—	31.6	25.6
Special facilities	—	—	—	—	—	—	—	—	—	143.3	65.0	72.4	—	—	—
<b>Special Drawing Rights Department</b>															
1. Net cumulative allocation of SDRs	—	—	—	—	—		15.1	29.0	42.8	42.8	42.8	42.8	64.1	85.4	106.4
2. Net cumulative use of SDRs	—	—	—	—	—		15.1	15.9	40.3	40.8	34.2	21.8	59.3	76.7	95.3

<sup>a</sup> Until 1969 all amounts are quoted in dollars.<sup>b</sup> End of first quarter.<sup>c</sup> Includes reserve tranche (until 1978 the gold tranche).

balance of payments difficulties, making it conditional on the implementation of corrective economic measures.

In 1980 Israel had no particular need for IMF assistance, and apart from drawing on its reserve tranche in January in the amount of SDR 31.6 million,<sup>14</sup> it did not submit applications for aid. The two IMF missions which visited Israel during the year dealt with administrative and legal matters connected with foreign currency control (March 1980) and with the routine annual consultation with Israeli authorities (February 1981). The members of the latter mission met with the country's leading economic figures and held numerous technical discussions with Bank of Israel and Ministry of Finance officials. After its visit the mission drew up a report on the state of Israel's economy, which was submitted to and discussed by the IMF Board of Directors. In May 1981 the Board of Directors reviewed the mission's report and approved the conclusions.

In January 1980 and January 1981 Israel received two new allocations of SDR 21.3 million each, bringing its net cumulative allocation of SDRs to 107 million.

## **(b) The World Bank Group**

### **1. *International Bank for Reconstruction and Development (IBRD)***

This intergovernmental institution deals primarily with the identification, evaluation, preparation, implementation, and financing of development projects in developing countries.

Israel is no longer eligible for aid from the World Bank. Because of the constraint on its resources, the World Bank began in the mid-1970s to "phase out" developing members with a high per capita national income from the list of countries eligible for its aid, and Israel was the first to be stricken off the list. However, it continued to receive disbursements of loans approved in earlier years; in 1980 this amounted to \$15 million, bringing the cumulative total of loans disbursed to \$267 million (out of \$284 million approved). The \$17 million undisbursed balance is earmarked for the completion of highway construction and a sewerage project (\$2 million and \$9 million respectively) and for the provision of industrial investment credit (\$7 million).

### **2. *International Development Association (IDA)***

This affiliated institution performs the same functions as the World Bank and is managed by the same Board of Directors, but grants aid only to the poorest nations and on far softer terms than those of the World Bank.

The sixth replenishment of IDA resources during the period under review was intended to increase its capital from \$21 billion to \$32 billion. Israel's present participation in the Association's resources is \$2.1 million; like a

<sup>14</sup>The average value of an SDR in 1980 was \$1.30 (as against \$1.29 in 1979).

large majority of the developing nations, Israel decided this year to participate in the present replenishment only in an amount required to maintain its voting power.

### 3. *International Finance Corporation (IFC)*

This World Bank affiliate promotes private investments in developing countries by participating in private loans as well as in share capital where the availability of private capital on reasonable terms to the local investor is limited.

The IFC too is now increasing its capital, from \$110 million to a targeted level of \$650 million. Israel's participation to date amounts to only \$50,000, but it was decided this year to increase this by \$500,000.

## 9. ECONOMIC RESEARCH

As usual, the Bank's Annual Report includes much of the current research on the Israeli economy conducted by the Research Department. Among the other current research carried out by the Department's economists in 1980 were the following:

- (a) *Recent Economic Developments*, Nos. 29, 30, and 31.
- (b) The Governor's report on the increase in the money supply for the period between August 31, 1979 and March 31, 1980.
- (c) The Governor's report on the increase in the money supply for the period between April 30, 1980 and July 31, 1980.
- (d) The Governor's report on the increase in the money supply for the period between July 31, 1980 and November 30, 1980.
- (e) Periodic internal surveys on monetary developments and macroeconomic policy.
- (f) *Economic Indicators*—a weekly publication.

In addition to current research, the Department carried out a number of basic studies of specific subjects, of which the following will be published in *Economic Review* No. 53:

- (a) "Monetary Policy in Israel".
- (b) "Price Adjustment Equations of Israel's Industrial Output, 1964-77".
- (c) "The Effect of Inflation on Stock Yields, 1965-79 (Updated)".
- (d) "Capital Structure, Inflation, and the Cost of Capital in Israeli Industry".

At the 1980 conference on "Issues in the Economy of Israel" held by the Falk Institute for Economic Research, the Department's economists presented the following papers (in Hebrew):

- (a) "Inflation, Floating Exchange Rates, and Monetary Policy".
- (b) "Allocation of Financial Savings in Israel".
- (c) "The Effect of Monetary Variables on the Consumption Function".
- (d) "Efficiency, Returns to Scale, and Factor Allocation in Israel's Public Hospitals".

- (f) "The Effect of Inflation on Different Population Groups in Israel".
- (g) "The Subsidy Component of Export Credit".

The following studies have been completed but not yet published (the English titles are provisional):

- (a) "Growth of the Labor Supply in 1965-80".
- (b) "Inflationary Expectations in Israel".
- (c) "The Slowing of the Productivity Gain in the Principal Economic Sectors".
- (d) "The Distribution of Imports by End Uses, 1971-79".
- (e) "The Overall Impact of World Price Increases on Israel's Economic Wellbeing in the 1970s".
- (f) "Disinflation and Incomes Policy".
- (g) "The Variability of Consumer Prices in a Period of Inflation".

## 10. ADVISORY COMMITTEE AND ADVISORY COUNCIL

As usual, most of the sessions of the Bank of Israel's Advisory Committee and Advisory Council were devoted to economic and monetary developments in general and to the Bank of Israel's policies in particular. In the early part of the year these two bodies discussed the various measures taken by the Bank to curb the monetary expansion, in particular the effects of restraining credit by the imposition of legal restrictions on nondirected (free market) credit at the end of 1979.

The problem of the banks' liquidity deficiencies during the year was the subject of detailed discussion in the Advisory Committee, and in January it decided to amend the directives dealing with fines for such deficiencies. At the same time it examined the possibility of lowering the liquidity ratios on deposits. In August the Committee held exhaustive deliberations on credit policy, following which it updated the ceilings on nondirected credit, increased the commercial banks' participation in directed export credit funds, and studied the possibility of giving larger loans to banks if they should run into liquidity problems for which they are not responsible.

The Advisory Committee also dealt with the revision of government bond issue terms as part of a comprehensive discussion of the subject of capital mobilization. Besides discussing economic and monetary developments, the Advisory Committee dealt with general subjects related to the central bank's activities, including indexation problems in the Israeli economy, the development of new savings instruments, the State Comptroller's Report, and so forth.

The Advisory Council approved the planned issue of coins and banknotes during the year, as described in section 6 of this chapter. It also approved the Bank of Israel's balance sheet and statement of income and expenses for 1979.

**BALANCE SHEET AS AT DECEMBER 31, 1980**  
**AND**  
**STATEMENT OF INCOME AND EXPENSES FOR THE YEAR ENDING**  
**DECEMBER 31, 1980**

**BANK OF**  
**BALANCE SHEET AS**

(Millions of

<b>Assets</b>	<b>Notes</b>	<b>Dec. 31, 1980</b>	<b>Dec. 31, 1979</b>
Foreign assets			
Gold, foreign exchange and foreign securities	2	25,618	11,031 <sup>a</sup>
Other foreign assets		676	134
		26,294	11,165
Government debt			
Long-term debt	3	4,300	2,667
Provisional advances		1,159	1,542
		5,459	4,209
Loans and discounts			
In foreign currency		16,213	6,589
In local currency		3,070	1,400
		19,283	7,989
Securities	4		
Marketable		2,000	949
Nonmarketable		1,924	529
		3,924	1,478
Other accounts	5	1,362	576 <sup>a</sup>
Total		<b>56,322</b>	<b>25,417</b>

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

<sup>a</sup> Revised datum.

# ISRAEL

AT DECEMBER 31, 1980

sheqalim)

Liabilities	Notes	Dec. 31, 1980	Dec. 31, 1979
Banknotes and coins in circulation		2,537	1,376
Allocations of Special Drawing Rights	6	823	299
Foreign liabilities			
Liabilities to the IMF	2	698	337
Other liabilities	7	130	89
		828	426
Foreign currency deposits of the govt. and National Institutions		2,334	1,040
Foreign currency deposits of banking institutions in Israel			
Against resident deposits—restitution		19,635	10,025
Against resident deposits—other		18,062	7,538
Against nonresident deposits		4,591	1,898
		42,288	19,461
Deposits of banking and financial institutions in Israel		2,007	904
Other deposits	8	405	200
Other accounts	9	4,100	1,211
Capital and general reserve	10	1,000	500
Total		56,322	25,417



**STATEMENT OF INCOME AND EXPENSES FOR THE YEAR ENDED  
DECEMBER 31, 1980**

(Millions of sheqalim)

	Notes	1980	1979
<b>Income<sup>a</sup></b>			
From investments abroad		15,187	6,360
From the government		4,442	2,461
From loans and discounts		10,128	3,197
From "liquidity loans" to banking institutions		110	104
From banking institutions in respect of liquidity deficiencies		66	67
From securities	12	2,066	476
Interest on foreign currency loans to the public from local banks and from abroad	13	381	187
Other income		95	20
<b>Total income</b>		<b>32,475</b>	<b>12,872</b>
<b>Expenses<sup>a</sup></b>			
On foreign currency deposits of banking institutions in Israel	14	23,867	9,895
On local currency deposits of banking and financial institutions in Israel		509	129
On foreign currency deposits of the government and National Institutions		1,374	522
On other deposits and liabilities		1,192	415
Administrative and general expenses		157	77
Printing banknotes and minting coins		59	38
<b>Total expenses</b>		<b>27,158</b>	<b>11,076</b>
Surplus of income over expenses		5,317	1,796
Less: Income from the government subject to matched timing	1a	1,726	330
<b>Net income</b>		<b>3,591</b>	<b>1,466</b>
<b>Appropriation statement</b>			
Transfer to general reserve	10	500	498
Transfer to the government		3,091	968
<b>Total</b>		<b>3,591</b>	<b>1,466</b>

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

<sup>a</sup> Income and expenses include exchange rate and devaluation differentials on assets and liabilities arising from changes in the exchange rate of the sheqel. Net income includes IS2,434 million in exchange rate and devaluation differentials (in 1979: IS1,106 million).

## NOTES TO THE FINANCIAL STATEMENTS, DECEMBER 31, 1980

### (a) Accounting Policies

#### 1. *Basis of Recording and Presentation*

Income and expenses are recorded on the accrual basis.

Income from the government is recorded on the accrual basis, but is included in the net income of the Bank on a matched timing basis, i.e. the Bank includes in its net income for the financial year sums due from the government only when they are budgeted and paid by the latter in the fiscal year ending the following March 31. Income receivable from the government after March 31 of the following year is deducted in the Statement of Income and Expenses as "Income from the government subject to matched timing" and is included in the balance sheet in "Other accounts (liabilities)" (see also note 1h).

Accrued interest and income receivable are included in "Other accounts (assets)", except for accrued interest and linkage differentials on securities denominated in local currency, which are included in the balance sheet in "Securities". Accrued interest and expenses payable are included in "Other accounts (liabilities)".

#### 2. *Foreign Currency Accounts*

Assets and liabilities in foreign currency are translated into sheqalim at the representative rates published by the Bank of Israel. The rate for the U.S. dollar on December 31, 1980 was IS7.548 and on December 31, 1979—IS3.535.

Special Drawing Rights (SDR) are translated into sheqalim on the basis of the SDR-U.S. dollar rate, i.e. IS9.6343 per SDR on December 31, 1980 and IS4.6601 on December 31, 1979.

#### 3. *Gold*

Gold is stated at the rate of SDR 35 per fine ounce

#### 4. *Foreign Securities*

These are stated at their foreign currency cost (weighted average purchase price) or market value, whichever is lower—calculated separately for each type of security.

#### 5. *Securities Denominated in Local Currency*

These are stated in the balance sheet at the adjusted value (nominal value plus accrued interest and linkage differentials) or market value, whichever is lower—calculated separately for each type of security. Securities not quoted on the Stock Exchange are stated at their adjusted value. Linkage differentials are calculated on the basis of the last consumer price index published before the balance sheet date.

#### 6. *Premises and Equipment*

Bank premises and equipment (included in "Other accounts") are recorded at cost net of accumulated depreciation.

#### 7. *Participation in International Financial Institutions*

The participation is included in "Other accounts (assets)" at cost. The cost includes amounts required to maintain the value of the participation in foreign currency terms, in accordance with the terms of the participation in the various institutions (for the participation in the IMF see note b).

#### 8. *Employee Pensions and Severance Pay*

Provision for employee pensions and severance pay, which is actuarially computed and adjusted at the balance sheet date, is included in "Other accounts (liabilities)".

Part of the domestic securities has been earmarked against the employee pension and severance pay liability. Income from these securities is not subject to matched timing, and is set off in the Statement of Income and Expenses against the increase in the liability.

**(b) Gold, Foreign Exchange, and Foreign Securities: Liabilities to the IMF**

"Gold, foreign exchange, and foreign securities" include IS85 million in holdings of Special Drawing Rights (SDR) in the IMF (on December 31, 1979: IS22 million) and the Reserve Position in the IMF amounting to IS247 million (on December 31, 1979: IS147 million).

This Reserve Position balance, which may be drawn upon unconditionally, represents the excess of the quota over the liability o/a of this quota. In December 1980 Israel's quota in the IMF was enlarged, under the Seventh Quota Increase, from SDR 205 million to SDR 308 million.

Accounts with the Fund include the Reserve Position (appearing in "Gold, foreign exchange, and foreign securities") and the liability o/a of the Compensatory Financing Facility (appearing in "Liabilities to the IMF").

	IS million		SDR million	
	Dec. 31, 1980	Dec. 31, 1979	Dec. 31, 1980	Dec. 31, 1979
General Account:				
Quota	2,963	955	308	205
Less: Liability	2,716	808	282	173
Reserve Position	<b>247</b>	<b>147</b>	<b>26</b>	<b>32</b>
Liability o/a Compensatory Financing Facility	<b>698</b>	<b>337</b>	<b>72</b>	<b>72</b>

The government's liability to the Fund, amounting to SDR 84 million in respect of the Oil Facility and Compensatory Financing Facility, is not included in the accounts of the Bank (on December 31, 1979: SDR 152 million).

**(c) Government Debt—Long-Term**

This item consists mainly of (1) IS4,000 million linked to the basket of foreign currencies, bearing unlinked interest of 5 percent per annum, and repayable over the years 1983–2004; interest and linkage differentials are payable on December 31 of each year (balance of the debt on December 31, 1979: IS2,500 million); (2) U.S. \$33 million (on December 31, 1979: same amount).

**(d) Securities**

"Marketable securities" consist of government bonds, mostly linked to the consumer price index; their market value is IS2,275 million (on December 31, 1979: IS1,025 million). "Nonmarketable securities" include mainly (1) compulsory government bonds purchased from firms in accordance with the Government Loans (Sundry Provisions) Law, 5738–1977; (2) bonds purchased from banking institutions, under repurchase agreements, from their frozen savings scheme portfolios.

**(e) Other Accounts (Assets)**

This item consists mainly of (1) accrued interest and other income; (2) premises and equipment net of accumulated depreciation; (3) participation in the following international financial institutions: the International Bank for Reconstruction and Development (IBRD), International Development Association (IDA), International Finance Corporation (IFC), and Inter-American Development Bank (IDB).

**(f) Allocations of Special Drawing Rights**

In 1980 Israel received SDR 21 million from the IFM; this was the second installment of the SDR 64 million allocation of 1979.

At the end of 1980 the balance amounted to SDR 85 million (on December 31, 1979: SDR 64 million).

**(g) Other Foreign Liabilities**

This item includes liabilities to international financial institutions amounting to IS90 million (on December 31, 1979: IS43 million) and deposits of foreign banks amounting to IS40 million (on December 31, 1979: IS46 million).

**(h) Other Deposits**

This item consists mainly of deposits of the U.S.-Israel Binational Industrial Research and Development Fund and a deposit of the U.S.-Israel Binational Science Fund.

**(i) Other Accounts (Liabilities)**

This includes mainly (1) accrued interest and other expenses; (2) income from the government subject to matched timing (see notes a1 and 1); (3) provision for employee pensions and severance pay.

**(j) Capital and General Reserve**

In 1980, IS500 million was transferred to the general reserve from net income and IS100 million was transferred from the general reserve to capital. The Bank's capital at the balance sheet date is thus IS200 million, and the general reserve—IS800 million (on December 31, 1979: IS100 million and IS400 million respectively).

**(k) Contingent Liabilities**

The contingent liabilities are as follows: (1) uncalled amounts on account of shares and participations subscribed to international financial institutions—IS908 million (on December 31, 1979: IS425 million); (2) documentary credits—IS341 million (on December 31, 1979: IS78 million); (3) other liabilities—IS13 million (on December 31, 1979: IS53 million).

**(l) Income from Securities**

This item does not include income from securities held against the employee pensions and severance pay liability, and which partly covered the increase in the liability (see note a8).

This item includes this year IS1,726 million income subject to matched timing (in 1979: IS330 million); this is deducted from the excess of income over expenses (see note a1). The accumulated income subject to matched timing is IS2,229 million (on December 31, 1979: IS503 million).

**(m) Interest on Foreign Currency Loans to the Public from Local Banks and from Abroad**

This item includes interest from banking institutions in respect of their foreign currency loans to Israeli residents and interest on deposits with the Bank of Israel, in respect of loans received by the public directly from abroad.

**(n) Expenses on Foreign Currency Deposits of Banking Institutions in Israel**

Until March 1979 the government participated in the interest paid on restitution deposits. The government's participation in the months January-March 1979 amounted to IS31 million.

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MAY 31, 1980

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*Deputy Governors*  
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<sup>a</sup> Members of the Advisory Committee are also members of the Advisory Council.

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