CHAPTER XIX

THE SECURITIES MARKET[1]

1. MAIN DEVELOPMENTS

In 1975 the market value of securities traded on the Tel Aviv Stock Exchange and bonds traded in foreign currency grew by 48 percent, following a rise of 66 percent in 1974 (and a 36 percent rise in each of the three preceding years). The proportion of the shares rose slightly after declining in 1973 and 1974, and that of bonds declined a little. This year the drop in the share of the securities traded in or linked to foreign currencies was arrested.[2] The braking of growth in the mobilization of net funds through bonds in local currency continued, but there was an increase in the issue of shares and capital promissory notes. The yield on shares was high this year (31 percent), approaching the yield on linked bonds (33 percent), but the return to holders of bonds traded in foreign currency was even higher - the index of their prices rose very rapidly (74 percent).

Among the important developments that influenced the securities market were the increase in the flow of funds by the public sector and the Bank of Israel, the focus of attention on the problem of foreign exchange reserves of the economy with the consequent expectation of a real devaluation, and a continuation of the uncertainty regarding the future terms of bond issues. All these operated against a background of declining real

1. This chapter deals with securities issued with a prospectus (including government and Jewish Agency securities which do not require a prospectus) registered for trading on the Exchange. Discussion on mobilization of funds by issue of bonds is not limited to bonds registered for trading; bonds awaiting registration for trading have also been covered at their estimated market value. Short-term bonds are not dealt with here but in Chapter XVII.

2. Prices estimated in Israeli pounds. In terms of dollars, the decline in the weight of these securities continued, as there were few new issues of this type of bond.

Table XIX-1

SECURITIES LISTED FOR TRADING ON THE STOCK EXCHANGE (LISTED AND MARKET VALUES) AND FOREIGN SECURITIES (MARKET VALUES), SELECTED YEARS, 1970-75

(IL million)

	Listed values		Market values				Weight at market prices in total listed securities portfolio				Percentage increase in 1975	
	1974	1975	1970	1972	1974	1975	1970	1972	1974	1975	Listed value	Market value
Bonds												
1) Dollar-linked	60	56	174	118	99	168					-6.6	69.7
2) Traded in foreign currency[a]	1.696	1.905	792	1.218	1,573	2.651					12.3	68.5
3) Total foreign currency (1+2)	**1,756**	**1,961**	**966**	**1,336**	**1,672**	**2,819**	**16.9**	**12.4**	**6.8**	**7.7**	**11.7**	**68.6**
4) Index-linked	4.067	6.086	1.566	2.437	8.236	12,741					49.6	54.7
5) Option-type linkage	4.628	4.572	1.807	3.667	9,448	11,857					-1.2	25.5
6) Total linked to c-o-l index (4+5)	**8,695**	**10,658**	**3,373**	**6,104**	**17,684**	**24,598**	**58.9**	**56.8**	**71.4**	**67.4**	**22.6**	**39.1**
7) Mixed linkage	—	—	28	6	—	—					—	—
8) Unlinked	26	21	37	19	19	14					-19.2	-26.3
9) Total bonds (3+6+7+8)	**8,721**	**10,679**	**4,404**	**7,465**	**19,375**	**27,431**	**76.9**	**69.4**	**78.2**	**75.2**	**22.5**	**41.6**
10) Bonds not yet listed for trade[b]	690	1.614	0	0	730	1.694						
11) Total bonds (9+10)	**9,411**	**12,293**	**4,404**	**7,465**	**20,105**	**29,125**	**76.9**	**70.4**	**81.2**	**79.9**	**30.6**	**44.9**
Shares												
12) Traded in Israeli currency	1.739	2.351	902	2,607	3.460	5,266					35.2	52.2
13) Traded in foreign currency	191	316	178	228	271	706					65.4	160.5
14) Total shares (12+13)	**1,930**	**2,667**	**1,080**	**2,835**	**3,731**	**5,972**	**18.9**	**26.4**	**15.1**	**16.4**	**38.2**	**60.1**
15) Convertible bonds	480	748	—	105	462	811					55.8	75.5
16) Total convertible bonds and securities (14+15)	**2,410**	**3,415**	**1,080**	**2,940**	**4,193**	**6,783**	**18.9**	**27.3**	**16.9**	**18.6**	**41.7**	**61.8**
17) Foreign securities[a]			246	344	463	566	4.29	3.20	1.87	1.55		22.2
18) Total securities portfolio[c] (11+16+17)			**5,730**	**10,749**	**24,761**	**36,474**	**100.0**	**100.0**	**100.0**	**100.0**		**47.9**
19) Total securities linked or traded in foreign currency (3+13+17)			1.390	1.908	2,406	4,091	24.2	17.8	9.7	11.2		70.0

[a] The market value of securities traded in foreign currency was calculated at the Natad rate (the Agio rate for the end of 1975 — 22.5%).
[b] The market value of bonds issued but not yet listed for trade estimated according to accumulated index differentials and interest.
[c] Including bonds which were not yet listed on the Stock Exchange.
SOURCE: Tel Aviv Stock Exchange: Foreign Exchange Department. Ministry of Finance.

disposable income for the first time since 1967.

The funds generated by the government, national institutions, and the Bank of Israel provide resources for the monetary institutions and the securities market. However, compared to the considerable expansion in the generation of these funds, there was also a large increase in acquisitions of foreign exchange by the private sector. This increase was necessary both to finance the structural deficit in the private sector's balance of payments and also from considerations of the need to adjust the financial assets portfolio in the light of the expected yield structure as is explained below. On all accounts, the rush into securities quoted in foreign currency slowed down the rate of monetary expansion so that this year the base for activities in local currency contracted and it may be assumed that this operated to reduce the demand for securities.

Public attention was focused on the problem of the economy's foreign exchange reserves, and together with the policy of creeping exchange rates, created expectations of a chain of devaluations including expectations of a devaluation in real terms. These factors gave rise to expectations of a higher yield on financial assets linked to foreign currency together with reduced uncertainty as to changes in exchange rates. In addition to the increased conversion of Israeli currency, it became more worthwhile to hold securities traded in foreign currency, causing a transfer of funds to these securities. Their weight in the financial asset portfolio rose slightly after a continuous decline during the preceding five years. At the same time there were practically no new issues of this class of bond.

Uncertainty regarding the terms of bond issues continued as conflicting rumors were put out during discussions of the subject in the media. It may be assumed that this uncertainty did not contribute positively to the development of the market.

There were additional factors which exerted a restraining influence on the bond market. The rate of inflation slowed down slightly, which made it less worthwhile to hold bonds in local currency linked to the consumer price index. This year too, as last, there were fluctuations in bond prices around a rising trend; these undermined the liquidity of the linked bonds as short-term investments. Rates of interest to borrowers rose, thus reducing the profitability of borrowing to invest in bonds; whereas the tax reform made it less worthwile for firms whose principal function is not to trade in securities to take low-interest loans in order to hold linked bonds. The hiking of the at-source tax deduction (from 25 percent to 35 percent) under the tax reform also diminished the profitability of bond-holding.

As a consequence of the reduced desirability of retaining index-linked bonds, there was

an exodus of funds from the securities market to securities traded in foreign currency whose profitability had risen meanwhile. Also, there was a reversion to shares and to deposits in savings schemes of the banks. With the transfer of funds from the direct holding of bonds to their indirect holding via banks' savings schemes, there was a certain fall in the demand for bonds, since banks are obliged to acquire bonds for 75 percent of their savings schemes. It is possible that this year too, monies flowed into the share market, which in previous years had found their way into the real estate market which is now in the doldrums. It is not impossible that institutional investors increased this year the "share" component of their financial asset portfolio at the expense of bonds.

The demotion of the domestic bond market went hand in hand with the more sluggish growth of the funds mobilized in this market. In 1975 bonds to the tune of IL7,892 million[3] were issued - a growth of 25 percent over 1974 (see Table XIX-2).

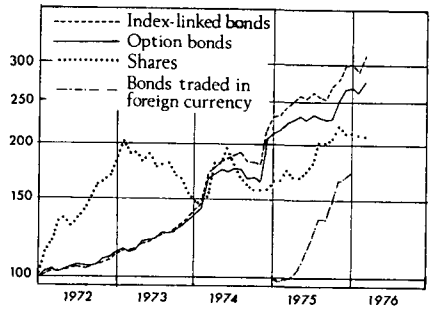
The net amount of capital raised through bond issues amounted to IL4,196 million as against IL3,562 million last year (an increase of about 18 percent), after redemption of principal and payment of interest and linkage increments on voluntary and compulsory loans that became tradable during the year.

There was a more sluggish rise in prices of bonds (index-linked and option-type bonds) - 28 percent, as against 56 percent last year. The increase in bond prices exceeded the rise in the consumer price index by 3.6 percent which was tantamount to a lowering of the real yield on bonds this year. The volume of trading in bonds was considerably greater than last year, although the rate of increase in 1975 (94 percent) was lower than in 1974.

In mid-December, several steps were taken which changed the course of development of the bond market. The issue of 100 percent linked bonds to the public was stopped; the linkage rate was brought down to 90 percent of the increase in the consumer price index, but the issue of full linkage bonds to institutional investors, whose asset portfolio is frozen continued As a result of this, institutional investors are cutting down operations in the market, barring trust funds. Measures were announced to counteract undeclared capital: the abolition of bearer bonds and the compulsory

Figure XIX-1

SECURITY PRICE INDEXES, 1972-76



Semilogarithmic scale.
SOURCE: Central Bureau of Statistics.

3. References to the issue of bonds do not relate to compulsory loans (unless otherwise indicated).

Table XIX-2
DOMESTIC PUBLIC ISSUES OF SECURITIES, 1974-75[a]
(IL million)

	1974				1975				
	Gross issues (1)	Redemption of principal (2)	Interest and linkage differentials (3)	Net proceeds (1–2–3) (4)	Gross issues (5)	Redemption of principal (6)	Interest and linkage differentials (7)	Net proceeds (5–6–7) (8)	Increase in net proceeds (8–4) (9)
Bonds									
Option-type	600	354	992	–746	3	212	938	–1,147	–401
Linked medium-term[b]	2,303	—	218	2,085	3,459	40	263	3,156	1,071
Linked long-term[c]	3,442	140	848	2,454	4,582	180	1,754	2,648	194
Tradable compulsory loans[d]	—	88	102	–190	—	79	231	–310	–120
Net sales from the Bank of Israel portfolio	–40	—	—	–40	–151	—	—	–151	–111
Total bonds in Israeli currency	**6,305**	**582**	**2,161**	**3,562**	**7,892**	**510**	**3,186**	**4,196**	**634**
Thereof: Government bonds[e]	2,005	256	1,066	683	2,011	132	999	880	197
Bonds traded in foreign currency	78	91	127	–140	174	95	214	–135	5
Non-tradable compulsory and voluntary[f] loans	2,632	89	789	1,754	2,761	298	489	1,974	220
Other securities									
Shares listed on the Exchange	304	—	—	304	467[g]	—	—	467[g]	163
Convertible securities	127	—	—	127	325	—	—	325	198

NOTE: The figures are rounded off.

[a] The criterion for the inclusion of various items in calculating the total issues for this table is economic not just accounting. Hence the divergences from Table XX-12. The discrepancy in the data on net issue of government bonds is due to the following corrections made in Tables XIX-2 and XIX-3: (1) exclusion of redemptions of compulsory loan which were made tradable and of interest payments and linkage for them; (2) exclusion of net sales from the Bank of Israel's portfolio; (3) the addition of temporary deposits with the Accountant-General in the absence of suitable issues for savings schemes.

[b] 6½% bonds for 7 and 11 years, 3¼% for 6 years, 4% for 10 years, 7½% for banks for 5 and 9 years ("Bank loans"). Including IL 70 million temporarily deposited at the Accountant-General in December 1975, given the lack of issue suitable for savings schemes.

[c] 6% bonds for 17 years, 6½% for 20 years, and money deposited by insurance companies.

[d] Absorption loans.

[e] Not including voluntary war loans.

[f] Compulsory defense loan 1970–73; compulsory savings loan 1970–75; war and voluntary loan 1973–74.

[g] The parent company of one of the commercial banks undertook to purchase IL 72 million of the bank's issues, while itself issuing shares to a greater value. In order to avoid a double counting of this issue, the sum was deducted from the value of the shares issued.

SOURCE: Bank of Israel, the State Loans Authority.

reporting of cash transactions of over IL 15,000. The intention to impose a turnover tax of 1.5 percent was also announced. The reduction of the linkage rate of new bonds was in itself expected to lift the price of the old bonds whose linkage rate was 100 percent. In practice such an increase did not materialize, apparently as the total effect of all the measures was to exacerbate the uncertainties in the capital market.

The share market which had lain dormant in 1973-74, after reaching a peak in 1972, turned the corner in May 1975. The issue of shares and convertible securities amounted to IL792 million, a growth of 19 percent over 1974. Despite the volume of new issues, this year a rapid rise in prices took place on the share market - 31 percent (as against 11 percent in the previous year). This rate of increase was greater than that of the consumer price index by 6 percent. The overall rate of return inclusive of shares grew to 31 percent this year (13 percent in 1974). The volume of trading in shares rose by 42 percent in comparison to the previous year; in substance, there is a reversal of the trend, following a decline in the trading volume in 1973 and 1974.

This turning point does not as yet represent any significant change in the development of the capital market. Bonds are dominant in the Israeli securities market: their weight in the financial asset portfolio is 80 percent, their volume of trading both within and without the Stock Exchange is 94 percent, and they preempt 84 percent of the net capital sources. The number of companies that seek their funds in the capital market is small and their financial weight in the shares issues market is 94 percent.

In the context of the market value for securities traded in foreign currency (their prices are given in IL further on), there was a rise of 81 percent in the securities registered on the Tel Aviv Stock Exchange and a rise of 22 percent in foreign securities. The increase in Natad deposits was rapid and phenomenal - 179 percent; apparently short-term investors have an interest in this account. The agio rate of Natad, which was nil at the beginning of the year, has risen gradually since May and reached a level of 22.5 percent by the end of December.

It should be emphasized that there are some limitations of the analysis of the financial asset portfolio made in this chapter.[4] Only a small portion of the bonds issued are bought directly by the public; but changes in the public's propensity to save through the channels of savings schemes or the various provident funds affect the composition of the financial asset portfolio. The same applies to the regulations and directives issued

4. Another defect in computing the volume of financial asset portfolio is the time-lag in registering the bonds issued for trading on the Stock Exchange (a time-lag of six months). An attempt has been made in this chapter to rectify this shortcoming.

by the Treasury in connection with the nature of the investment required from institutional investors. Within the limits of this chapter it is not possible to analyze the financial asset portfolio as a totality, and the analysis will be confined to only a segment of the portfolio. Among the assets omitted are means of payment, time deposits, and deposits in foreign currency.

2. THE BOND MARKET

The proportion of bonds tradable in Israeli currency in the securities portfolio dropped from 71 percent in 1974 to 67 percent this year. In 1975 the slowdown in net capital raised through bonds which began last year continued. Capital raised through bond issues expanded by 18 percent this year compared with 32 percent in 1974. This was less than the rise in the consumer price index which also indicates that this year the decline in real terms of net capital raised through bonds continued.

(a) *The Primary Market*

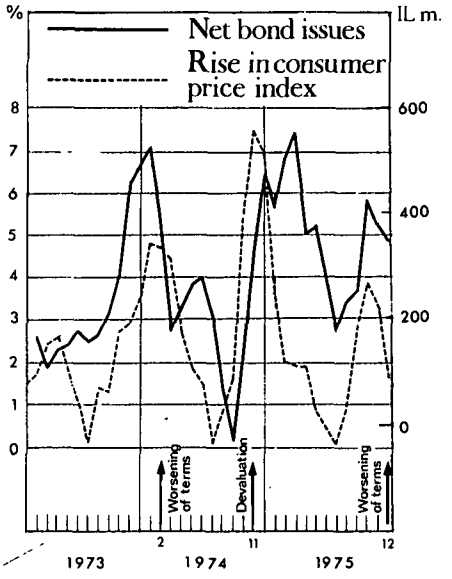
The net amount of capital raised (that is, less redemption of principal and interest and linkage payments) by new bonds, both medium- and long-term, was IL4,196 million, an increase of 18 percent over the previous year. In real terms, net capital raised by bonds dropped for reasons discussed above. Comparison of the net amount of capital raised in the two years, taking into account the price levels each year, shows a decline of 15 percent this year compared to 6 percent last year.

Net capital raised through government bonds totalled IL880 million, a rise of 29 percent compared to last year. It should be emphasized that one should be wary of attaching importance to the distinction between government and other bonds, as part of the receipts of new nongovernment bonds are also deposited with the Treasury. (This year 45.2 percent of these receipts were deposited with the Treasury). Apparently, the public directly purchased two thirds of government bond issues, while one third was purchased by institutional investors. Two thirds of the public's purchases of issues at source were government bonds, and one third bonds issued by financial institutions; 90 percent of bonds purchased by institutional investors were issued by financial institutions and 10 percent government

Figure XIX-2

NET ISSUES OF LINKED BONDS AND SECONDARY MARKET YIELDS, 1973–75

(three-month moving average)



SOURCE: Bank of Israel calculations.

Table XIX-3
DOMESTIC ISSUES OF SECURITIES TO THE PUBLIC, SAVINGS SCHEMES, PROVIDENT FUND, INSURANCE AND PENSION INSTITUTIONS, AND NET MOBILIZATION OF CAPITAL, 1975

(IL million)[a]

	Sales of securities (gross)						Estimated mobilized capital (net)					
Period	Total bonds IL	Savings schemes	Provident fund, insurance, and pension institutions	Others[b] (1-2-3)	Shares[c]	Convertible bonds	Redemption[d] of option loans, bonds held by the public, by provident, insurance, and pension funds	Redemption of tradable compulsory loans	Net acquisitions by the Bank of Israel on the Stock Exchange and over-the-counter	Total bonds, less redemptions and Bank of Israel acquisitions on the Stock Exchange (1-7-8-9)	Total capital mobilized net IL (5+6+10)	Bonds in foreign currency net
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10	(11)	
1974	6,346	1,679	2,718	1,949	304	127	2,552	190	40	3,562	3,993	-139
1975	8,044	2,135	3,751	2,158	467	325	3,387	310	145	4,196	4,988	-135
January	581	114	292	175	—	—	223	2	-29	385	385	-6
February	901	251	227	423	—	—	252	2	-49	696	696	13
March	700	95	379	226	—	—	195	2	69	435	435	-50
April	779	123	288	368	—	—	249	161	-78	441	441	-17
May	468	29	285	154	—	—	239	18	7	204	204	6
June	535	148	282	105	210	18	318	9	12	196	424	-41
July	554	277	226	51	14	5	332	5	64	153	172	-13
August	297	110	178	9	177	235	336	3	56	-98	314	-21
September	822	337	318	167	32	20	187	2	-3	636	688	-19
October	557	113	330	114	10	—	266	82	-11	220	230	-11
November	693	222	326	145	—	22	278	13	-25	427	449	-24
December	1,156	316[e]	618	222	24	25	510	10	132	504	553	47

[a] Rounded figures.
[b] To the public, mutual funds, etc.
[c] See note [g] in Table XIX-2.
[d] Maturity of principal and interest and linkage payments are included in redemptions.
[e] Includes IL 70 million deposited temporarily with the Accountant-General.
SOURCE: Bank of Israel, State Loans Administration.

issues.

One may assume that as the rate of return on bonds on the secondary market increases, the volume of bond purchases on the primary market drops (and new issues decline); this occurs if other factors are constant or where their influence in the period under discussion is not dominant. Figure XIX-2 shows this inverse relationship and the moving averages of the data are traced;[5] it also shows that the volume of issues during the year corresponds in general to the rate of proceeds on redemption in the secondary market.

An additional factor that no doubt influences net issues during the year is the anticipated rate of inflation; more rapid inflation raises the profitability of holding bonds relative to other nonlinked assets; higher demand for bonds in itself increases primary purchases; in addition, an increase in the secondary market purchases reduces yields in that market and strengthens the primary purchases.

Figure XIX-3 shows that indeed there exists a correspondence between the measure of net purchases of bonds in the primary market and the percentage changes (quarterly averages) in the consumer price index. The diagram assumes that the anticipated inflation can be represented as inflation de facto.

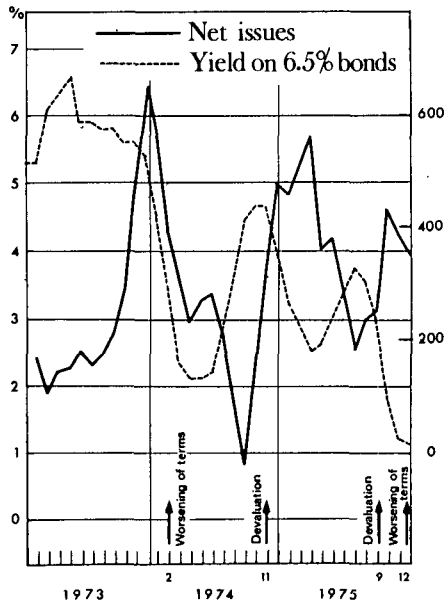
There should be taken into account shares issues which were bunched during June-September; it can be assumed that these issues attract funds which under other circumstances would have been invested in bonds, thus aggravating the depression in the bonds issue market in these months.

As for buyers of fresh bonds, there appears some decline in public participation and an increase in such institutional buyers as pensions and provident funds. This year, sales to the public (see Table XIX-3) of new bonds were of the order of IL2,158 million (an increase of 11 percent over the previous year). Savings schemes bought up fresh bonds worth IL2,135 million (an

Table XIX-3

NET BOND ISSUES AND RISE IN CONSUMER PRICE INDEX, 1973–75

(three-month moving average)



SOURCE: Central Bureau of Statistics and Bank of Israel calculations.

5. A moving average of 3 items was used as we did not intend to explain monthly fluctuations in the issues when there are random factors, and it is reasonable that these random effects will be offset in short periods of time (about 3 months). The presentation of quarterly data would be inferior to that chosen here, as it ignores completely monthly variations and is very arbitrary in using an inflexible unit of time (given annual quarters fixed in advance).

Table XIX-4

ARITHMETIC AVERAGE AND STANDARD DEVIATION OF MONTHLY CHANGES IN BOND AND SHARE PRICES AND YIELDS, 1972–75

(percentages)

	1972			1973			1974			1975		
	Average (1)	Standard deviation (2)	(1)/(2)	Average (1)	Standard deviation (2)	(1)/(2)	Average (1)	Standard deviation (2)	(1)/(2)	Average (1)	Standard deviation (2)	(1)/(2)
Index-linked bond prices	1.0	0.8	1.25	2.0	1.0	2.00	4.3	6.7	0.64	2.3	3.4	0.68
Option-type bond prices	1.1	1.3	0.85	1.7	1.5	1.13	3.9	8.5	0.46	2.0	2.7	0.74
Dollar-linked bond prices	0.5	1.9	0.26	0.9	4.4	0.20	0.3	5.2	0.06	5.2	7.3	0.71
Ordinary share prices	5.4	4.8	1.12	–1.8	4.9	—	1.2	7.3	0.16	2.3	3.5	0.66
Natad dollar rate	–0.1	0.7	—	0.6	1.6	0.38	2.7	8.3	0.33	3.1	3.1	0.99
Index-linked bond yields[a]	5.2	0.2	0.26	5.8	0.6	9.7	3.4	1.3	2.62	2.6	1.0	2.62

[a] The arithmetic average and standard deviation of yields to maturity not of rates of change, as with the other items.

increase of 27 percent), and insurance, pension, and provident funds bought new bonds issue, the public bought 27 percent, savings schemes--27 percent institutional buyers--47 percent. Figures for last year were: 30 percent, 27 percent, and 43 percent respectively. It is clear from the data that it is not possible to draw definitive conclusions, since bonds may be tranferred from one group to the other by means of the secondary market. (See Chapter XVIII: The Institutional Structure of the Capital Market.)

Following is an evaluation of the net mobilization of capital, less redemption of principal and payment of interest and linkage increments on various bonds (Table XIX-3). Net capital collection by means of medium-term bonds (including option-type bonds) was of the order IL3,156 million, an increase of 51 percent over the previous year. Net capital mobilization through long-term bonds (a majority of which are sold to pension and

Table XIX-5
VOLUME OF TRADING ON THE STOCK EXCHANGE, 1972-75[a]
(IL million)

	Bonds							
	Linked to the exchange rate	Linked to the c-o-l index	Option-type	Traded in foreign currency	Convertible into shares	Total	Shares	Total listed securities
1972	15.5	112.4	441.9	107.8	12.8	690.4	762.9	1,453.3
1973	11.7	250.5	676.0	120.6	79.3	1,138.1	633.0	1,771.1
1974	16.6	786.1	2,007.3	171.6	74.9	3,056.5	518.0	3,575.4
1975	54.9	1,338.0	1,873.2	251.0	103.1	3,620.2	780.3	4,400.5
1975 January	2.1	75.7	147.6	20.2	5.0	250.6	44.5	295.1
February	1.5	73.8	125.8	16.6	2.9	220.6	45.6	266.2
March	1.0	84.7	137.4	17.0	3.4	243.5	27.4	270.9
April	2.2	84.2	145.6	14.0	3.4	249.4	25.6	275.0
May	3.0	110.2	185.9	15.9	3.7	318.7	30.1	348.8
June	3.7	128.9	193.5	25.9	10.1	362.1	104.4	466.5
July	6.3	105.5	154.4	30.4	11.2	307.8	119.8	427.6
August	5.5	99.4	113.5	15.1	7.1	240.6	60.1	300.7
September	5.0	84.9	135.0	17.0	17.0	258.9	57.5	316.4
October	8.9	152.4	180.6	26.5	13.5	381.9	111.0	492.9
November	10.0	126.7	164.5	30.6	12.5	344.3	83.8	428.1
December	5.7	211.6	189.4	21.8	13.3	441.8	70.5	512.3
			Percent annual increase					
1972	0.7	97.9	110.0	31.1		66.0	102.1	206.7
1973	-24.5	112.9	53.0	11.9		64.7	-17.0	17.7
1974	41.8	213.8	196.9	42.3	-5.5	168.5	-18.3	109.0
1975	230.7	70.2	-6.7	46.2	37.6	18.4	50.4	23.1
			Percent distribution					
1972	1.1	7.7	30.4	7.4	0.6	47.5	52.5	100.0
1973	0.7	14.1	38.1	6.8	4.6	64.3	35.7	100.0
1974	0.5	22.0	56.1	4.8	2.1	85.5	14.5	100.0
1975	1.2	30.4	42.6	5.8	2.3	82.3	17.7	100.0

[a] Excluding trade in unlinked bonds, and short-term loans.
SOURCE: Tel Aviv Stock Exchange.

provident funds) amounted to IL2,648 million, 8 percent higher than last year. Thus, although there was an increase in terms of new bond purchases by pension and provident funds, there was an overall retardation in the pace of net institutional purchases of bonds.

The government's measures of December 1975 evoked a withdrawal of funds from the Exchange. The primary purchase of bonds by the public was arrested, and the average sale of medium-term bonds in January and February 1976 was IL150 million (as against a monthly average in 1975 of IL288 million); most of them were sold to institutional investors. Some decline would have occurred apparently even without the withdrawal of funds from the Exchange, since expectations of the deterioration of terms of the bond issue led to a large-scale purchase of bonds before the changes were introduced. In December 1975 the sale of medium-term bonds was 83 percent of the average issues of the first eleven months of the year and a similar picture emerged in respect of long-term bonds. In March and April 1976 the low level of medium-term bond issues continued; and a monthly average of IL143 million were sold. (For the purposes of a comparison of the data with the previous year it was necessary to include in this figure the temporary deposits of bank savings schemes with the Accountant-General.)

Raising capital by way of compulsory loans improved slightly on its volume in the previous year, despite the cessation of the collection of such loans due to the tax reform, since collection from self-employed persons already assessed continued, as also collection of Employer's Loans. The purchase of Voluntary War Loans was discontinued, and in 1975 only IL2.4 million was sold.

(b) *The Secondary Market*

Turnover in bonds both on and outside the Exchange rose by 94 percent, following a very considerable rise (110 percent) in the previous year (see Table XIX-10). The rate of increase in the trading volume of bonds was much faster (39 percent) than that of the market value of bonds registered for trading on the Exchange, and from this stemmed the rapid increase in the turnover rate of bonds. Eighty-two percent of bonds were traded off the Exchange in 1975 as against 70 percent in the previous year. Governmental bonds accounted for 90 percent of the total turnover on the floor. It is reasonable to assume that in trading outside the Exchange, bonds issued by other institutions are relatively more prominent (company bonds).

There was a fall of 6.7 percent in the turnover of option-type bonds (see Table XIX-5), as against an increase of 70 percent in trade in bonds linked to the consumer price index.

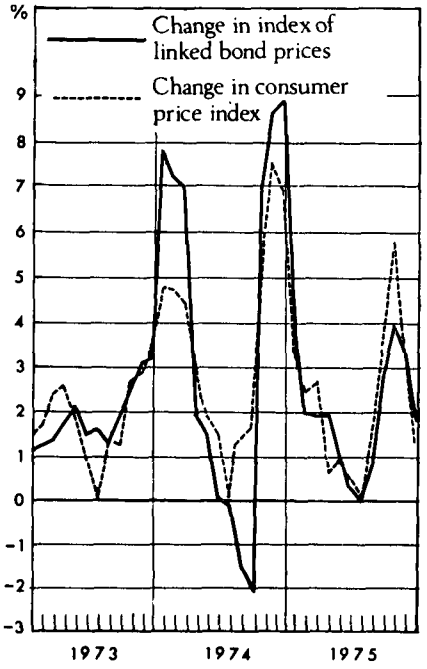
(In the absence of data on trading outside the Exchange, the significance of this discussion is limited.) However, in comparison to the market value of securities, the volume of option-type bonds trade was 50 percent greater than that of index-linked bonds.[6] (Today there are no new issues of option-type bonds.)

The fact that, relative to registered capital, trading in option-type bonds is greater than that in index-linked bonds is closely connected, inter alia, with the proximity of option-type bonds to their redemption dates. The closer the bond is to redemption, a given change in its market redemption yield will have a smaller effect on its price. Under conditions of uncertainty as to the long-term bonds prospects, the investor would choose option-type bonds; all the more so, if account is taken of expectations of a sharp increase in the consumer price index in the next year or two.

Table XIX-4

CHANGES IN LINKED BOND AND CONSUMER PRICES, 1973-75

(three-month moving average)



SOURCE: Central Bureau of Statistics.

Trading in option-type and index-linked bonds thrieved during the year; but during the months of July, August, and September there was a setback. This depression corresponded with the timing of share issues: in August when share issues were at their peak, the depression hit the bottom. This lack of interest in bonds caused a drop in their values, and in the month of August yield rates on option-type and index-linked bonds reached their highest levels of the year.

Prices of linked and option-type bonds rose during the year by 28 percent (see Table XIX-7) as against 56 percent in the previous year. The rise in real values (correcting for the rise in the c-o-l index) was 3.6 percent during the year,[7] against a 0.3 percent fall in the previous year. As in previous years, the rise in index-linked bonds was more rapid than those of option-type bonds.

6. The rate of turnover in trading, i.e., the relation between the volume of transactions on the exchange and the market value of bonds registered for trading, was 0.158 for option-type bonds and 0.105 for bonds linked to the c-o-l index.

7. When assessing movements in the value of the financial asset portfolio, allowance must be made for the rate of interest deducted in computing index prices at 3.5 percent to 4 percent per annum for various bonds.

Table XIX-6

AVERAGE REAL NET YIELDS TO MATURITY OF BONDS TRADED ON THE STOCK EXCHANGE, 1975
(percentages)

Years to maturity	Traded in dollars				Index-linked					Option-type	
					3¼%	4%	Absorption loan		6½%		
	0–2	2–5	5+	Total	5–6	9–10	½–1½	4–5	5–6	2–3	3–4
January	8.7	8.9	8.6	8.8	2.6	—	0.6	4.4	3.4	2.9	3.2
February	9.0	8.9	8.8	8.9	2.7	—	–0.1	2.8	2.7	2.4	2.3
March	9.5	9.4	9.3	9.4	3.1	—	–1.0	2.9	2.5	2.4.	2.5
April	9.3	8.6	8.5	8.6	3.1	2.4	–2.0	2.0	2.3	2.0	2.0
May	9.0	7.7	7.6	7.6	3.7	2.5	0.7	3.1	3.0	3.4	3.0
June	4.9	6.1	6.5	6.1	4.0	3.0	0.4	3.3	3.4	3.5	3.5
July	3.9	4.1	4.5	4.2	4.4	3.1	0.1	3.7	3.6	4.1	4.0
August	2.9	3.5	4.0	3.6	4.9	3.4	1.9	4.2	4.2	4.4	4.3
September	3.5	3.5	3.8	3.6	4.0	2.9	1.5	2.6	2.8	2.8	2.7
October	1.8	2.7	3.3	2.8	2.4	2.4	–6.7	1.8	1.7	0.7	1.1
November	2.4	2.1	2.4	2.2	2.2	2.1	–6.2	1.1	0.9	–0.7	0.1
December	2.3	2.0	2.6	2.2	2.2	2.0	–2.3	2.4	1.0	0.2	0.6

SOURCE: Monthly Bulletin of Statistics, Central Bureau of Statistics—for bonds traded in dollars; Bank of Israel computations—for index-linked (the four most actively traded bonds in each group).

For the reasons described above, the fall in values in May, July, and August stood out prominently during the year. In September, with the anticipation and announcement of a variety of governmental measures (purchase tax, a 10 percent devaluation, increase in fuel prices) the rise in prices reached a peak, around 7 percent. The change in bond values corresponded in general to fluctuations in the consumer price index with various time-lags. As the rate of inflation grew (and along with it anticipated inflation), the public would be prepared to pay more for bonds in the market; thus the rate of inflation influences the index of bond prices, all things being equal. This nexus persisted throughout 1975, generally, as may be seen in Figure XIX-4.

This year, too, there were many fluctuations in bond prices, both option-type and index-linked, relative to their rising trend (see Table XIX-4). The ratio of average increase in values to their standard deviation was slightly higher this year than the previous year but it is still a long way from the ratio obtained in 1972 and 1973. The values of option-type bonds fluctuated less than index-linked bonds, which accords with the relative proximity of the former to their redemption dates.

The government's economic steps in December had contradictory effects on the secondary market. The narrower linkage of new bond issues had an expected and immediate effect in raising the values of old bonds. The linkage reduction from 100 percent to 90 percent lowers the net maturity yield rate of the new bonds; the extent of the decline is dependent on the rate of the expected increase in the consumer price index. In the context of the 4

Table XIX-7
MONTHLY INDEX OF SECURITY PRICES ON THE TEL AVIV STOCK EXCHANGE, 1975
(December 1974 = 100)

End of period	Bonds traded in Israeli currency					Shares		Bonds traded in foreign currency	Natad rate index[a]	Bonds traded in foreign currency corrected for the Natad rate	Bonds convertible into shares
	Index-linked			Linked to foreign exchange rate							
	Total	Linked to index only	Option-type		Total	Ordinary	Preferred				
1972	51.6	48.8	53.7	86.1	51.9	112.5	104.8				
1973	64.2	62.0	65.6	97.9	64.4	89.2	66.4				
1974	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1975 January	101.2	100.8	101.5	102.6	101.3	99.9	100.4	98.8	100.0	98.8	100.2
February	105.3	105.7	105.1	102.4	105.3	103.4	106.1	99.7	100.0	99.7	100.3
March	107.2	108.3	106.5	100.5	107.1	101.9	105.4	101.3	100.0	101.3	99.7
April	109.4	111.0	108.4	102.7	109.3	101.3	105.4	105.3	100.0	105.3	99.6
May	107.3	107.9	106.9	118.7	107.3	105.0	110.5	106.8	107.2	114.5	102.4
June	110.4	111.1	109.9	140.2	110.5	112.5	119.4	113.4	109.8	124.5	108.7
July	108.4	109.2	107.9	158.1	108.6	121.7	122.7	116.2	117.7	136.8	112.9
August	107.4	107.9	107.1	159.2	107.7	121.0	120.7	116.1	117.3	136.2	110.3
Sept.	115.4	117.4	114.2	176.6	116.0	124.7	122.2	115.5	128.3	148.2	111.1
October	119.3	121.6	117.9	188.5	119.9	133.1	127.6	119.9	138.7	166.3	117.2
Novemb.	126.9	129.4	125.3	190.5	127.5	130.9	123.4	120.8	140.0	169.1	117.1
Decemb.	127.9	130.7	126.2	182.1	128.4	131.0	122.1	120.2	145.0	174.3	114.1

[a] On the Thursdays nearest to the end of the month.
SOURCE: Central Bureau of Statistics; prices of bonds traded in foreign currency, corrected for the Natad rate Bank of Israel computations.

percent Development Bonds during the past 10 years, it can be seen that with a 15 percent annual rate of increase in prices the net yield rate on fresh bonds drops from 2.6 percent to 1.76 percent due to the linkage reduction; an annual inflation rate of 20 percent reduces their net yield rate to 1.67 percent. It may be expected that a fall in the net yield to maturity of new bonds, ceteris paribus, will bring about a similar reduction in the yield rate of old bonds which were issued with full linkage, with an increase in their prices. The reckoning indicates that the values of these bonds are expected to rise by 7.6 percent with an annual inflation rate of 15 percent, and 8.5 percent, with an expected rise of 20 percent annually in the consumer price index. In fact, rises of this order did not materialize in the secondary market. Apparently, the announcement of the levying of the turnover tax contributed to this. Apprehensions of such a tax led to the unloading of bonds (which were bought for a short duration), and thus to a temporary depression in their prices. Another factor contributing to the immediate reduction in prices in December was the widespread fear of the slapping of measures to counteract the concealing of capital: the issue of only "registered" bonds and not "bearer" ones, and the obligation to report cash transactions exceeding IL15,000.

This year trading in bonds outside the Exchange expanded and reached 82 percent of all bond deals. This trade was conducted in part by offsetting buy and sell orders to banks, and in part through bulk transactions between institutional investors. Thus, these investors can assure complete certainty as to the prices of their transactions without being affected by prices on the Stock Exchange.

3. THE SHARE MARKET

1975 was a year of positive developments for the share market, which finds expression in the volume of new issues, in the overall yield rate, in the rise of share prices and the volume of turnover. Share issues were clustered in the second half of the year, while trade in shares grew from quarter to quarter. During the second half of the year share prices rose comparatively. Thus, there was a reversal of the declining trend which characterized the share market after its 1972 peak. This revival occurred despite expectations of an impending decline in economic activity. These issues served as a source of funds for a small number of issue-houses, mostly banks and financial institutions. The available data is not sufficient to conclude that there was a serious change in the public attitude to the share market: institutional investors may have increased the share component in their portfolios.

Table XIX-8

WEIGHTED MONTHLY INDICES OF QUOTED SHARE PRICES, 1972-75

(31 December 1974 = 100)

	General Stock Exchange index	Finance and insurance					Industry	Commerce and service	Land, construction, development	Traded in foreign currency		
		Total	Commercial banks	Mortgage banks	Specialized financial institutions	Investment companies				Price index	Agio index for Natad	Price index corrected for the Natad rate
					Annual average							
1972	85.9	74.5	—	—	—	91.5	—	—	133.2	—	—	—
1973	108.6	103.1	104.4	97.8	111.4	116.3	114.6	86.2	144.5	—	—	—
1974	100.9	97.4	97.7	95.3	104.0	101.9	111.6	85.2	126.0	—	—	—
1975	115.6	112.7	113.6	105.6	107.4	113.1	128.6	135.8	120.4	113.5	109.4	109.4
					End of month							
1975 January	99.9	100.6	100.2	102.1	100.7	98.7	99.0	106.4	95.3	98.3	100.0	98.3
February	103.4	103.3	103.4	101.4	103.8	101.2	106.2	108.2	102.7	98.2	100.0	98.2
March	101.9	102.7	103.3	97.8	102.3	100.6	103.0	96.5	100.1	98.2	100.0	98.2
April	101.3	102.5	103.9	92.1	103.8	99.5	100.7	101.2	96.0	99.7	100.0	99.7
May	105.0	104.9	106.2	95.2	103.7	102.9	110.0	108.1	100.4	98.4	107.2	105.5
June	112.5	110.9	112.0	101.5	104.9	107.6	125.2	126.2	116.8	105.2	107.7	113.3
July	121.7	117.0	117.7	108.8	113.8	117.0	142.0	150.8	137.0	111.5	115.4	128.7
August	121.0	116.0	116.0	107.0	111.8	116.7	143.3	153.6	134.3	112.2	112.8	126.6
September	124.7	117.7	119.0	107.1	110.2	122.8	153.4	169.7	134.3	121.3	110.0	133.4
October	133.1	126.5	127.6	120.9	114.2	128.9	160.8	174.7	147.7	132.1	118.9	157.1
November	130.9	124.8	126.2	117.0	109.3	129.9	151.3	166.2	141.0	137.8	118.3	163.0
December	131.0	125.2	126.7	116.1	111.2	130.9	148.4	167.6	139.5	148.9	122.5	182.4

SOURCE: Monthly Bulletin of Statistics.

Table XIX-9

MONTHLY SHARE TURNOVER ON AND OFF THE TEL AVIV STOCK EXCHANGE,[a] BY SHARE GROUP, 1975
(IL thousand)

Month	Total Stock Exchange share volume	Commercial banks	Mortgage banks[b]	Specialized financial institutions[b]	Insurance	Commerce and services	Land and development	Industry	Investment companies	Shares sold on the floor[c]
January	66,083	30,994	8,386	3,335	1,759	2,675	2,331	6,293	9,412	898
February	72,138	33,369	6,022	945	3,141	3,623	4,673	8,943	11,027	395
March	55,934	31,590	3,653	1,088	1,170	3,388	2,073	4,739	8,062	171
April	47,148	25,571	3,148	2,136	1,271	2,304	1,900	3,931	5,651	236
May	56,252	28,715	2,765	1,327	1,426	4,552	3,179	6,011	7,882	395
June	190,970	114,034	9,909	4,926	4,381	6,666	9,261	17,243	24,233	321
July	182,860	78,476	11,560	5,221	5,605	8,405	14,941	27,227	30,940	485
August	95,055	45,667	4,197	1,574	4,823	4,418	6,970	13,026	13,055	1,325
September	110,822	45,653	4,419	1,129	6,205	6,842	5,858	15,035	22,858	2,823
October	179,741	64,329	13,195	3,758	6,063	6,248	23,188	29,451	31,179	2,331
November	148,318	69,438	10,947	2,328	4,510	3,871	11,725	19,796	24,597	1,108
December	157,615	93,247	8,130	2,128	3,117	3,580	8,926	16,217	19,922	2,348
Total turnover on the stock exchange	**1,362,936**	**661,083**	**86,331**	**29,895**	**43,471**	**56,572**	**95,025**	**167,912**	**208,818**	**12,835**
Share of the stock exchange in the total trade (percentages)	57.2	44.3	65.1	51.6	72.6	69.9	72.1	69.3	65.8	100.0
Group's share in total trade (percentages)	100.0	48.6	6.3	2.2	3.2	4.2	7.0	12.3	15.3	0.9

[a] Trade off the floor—reported by licenced agents of the Stock Exchange.
[b] Including shares traded in Israeli and in foreign currency.
[c] Securities not registered for trade on the Stock Exchange, but traded there.
SOURCE: Tel Aviv Stock Exchange.

The improvement in the share market this year may be attributed to the moderation in the rate of inflation and to the fluctuations in bond prices, which continued for the second successive year. This situation made bonds a less liquid asset, and the decline in their relative attraction raised the relative weight of shares in the financial asset portfolio from 17 percent last year to 19 percent this year. Additional factors which contributed to giving a fillip to the share market were, apparently, a continuation of last year's uncertainty regarding the possible changes in the terms of bond issues and also the depression in the real estate market. As already stated it is possible that institutional investors increased the ranking of shares in their financial asset portfolio, thereby aiding the success of their issue and stimulating their prices in the market.

The success of the share market this year can be gauged by the large and successful flotations of issues during a trend of rising share prices, not declining prices as in the previous year. This year share values rose by 31 percent as against 11 percent last year. The overall weighted rate of return on shares was 31 percent (13 percent last year), and this against a background of prices rising more moderately than in last year.

This year IL792 million were mobilized by the issue of shares and capital conversion notes. Of this, capital conversion notes constituted 41 percent as compared with 29 percent last year. Turnover, both on and off the Exchange, amounted to IL1363 million this year, 42 percent up on the previous year (following its decline in 1973 and 1974).

Though these are positive features, the boom in the share market should not be overrated. Of total net capital raised - only 16 percent was mobilized through shares: moreover, only a very few financial houses used the market as a means to enlist capital. Share turnover was only 6 percent of the total trading turnover on and off the Exchange, while its weight in the total financial asset portfolio was 19 percent. Conditions were not as yet ripe for any meaningful change in the share market's standing within Israel's capital market.

(a) *The Primary Market*

The volume of share issues reached IL467 million this year,[8] as compared to IL304 million last year. The issue of conversion shares also rose sharply to IL325 million this year against IL127 million pounds last year. In all IL792 million worth of shares were

8. This sum is arrived at after deducting IL72 million. The parent company of one of the banks underwrote the bank's issue to this extent. Since the company issued shares in excess of IL72 million, and to avoid double counting, the amount is deducted from this year's issues.

Table XIX-10

TURNOVER ON TEL AVIV STOCK EXCHANGE AND OVER-THE-COUNTER MARKET,[a] ANNUAL AND QUARTERLY DATA, 1972-75

(IL million)

	Shares				Bonds			
	Over-the-counter market	On the Exchange	Total	Ratio (1)÷(3)	Over-the-counter market	On the Exchange	Total	Ratio (5)÷(7)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1972	349.9	762.9	1,112.8	0.31	2,791.1	691.0	3,484.1	0.80
1973	384.2	633.0	1,017.2	0.38	3,685.3	1,138.2	4,823.5	0.76
1974	426.9	532.3	959.2	0.45	7,076.3	3,056.7	10,133.0	0.70
1975	582.5	780.5	1,363.0	0.43	16,057.0	3,620.3	19,677.3	0.82
			Percent increase					
1973	9.8	-17.0	-8.6		31.9	64.7	38.4	
1974	11.1	-15.9	-5.7		92.0	168.6	110.1	
1975	36.4	46.7	42.1		126.9	18.4	94.2	
1975 Quarterly								
I	76.6	117.6	194.2	0.39	1,890.0	715.0	2,605.0	0.73
II	134.2	160.1	294.3	0.46	3,783.0	930.4	4,713.4	0.80
III	151.4	237.4	388.8	0.39	4,455.0	807.7	5,262.7	0.84
IV	220.3	265.4	485.7	0.45	5,929.0	1,167.2	7,096.2	0.84

[a] Over-the-counter market—as reported by licenced agents of the Stock Exchange.

issued in this market, constituting an increase of 84 percent in the total capital raised. The volume of new issues relative to the market value of share capital at the end of 1974 was quite large - 19 percent.

As in previous years, the mobilization of capital in the share market was undertaken largely by banks and financial intermediaries; the reasons for this have been analyzed in previous Bank of Israel Reports.[9] To a certain extent this is the result of the easy access of banks to the market, low flotation charges, the high profitability of banks in recent years, and the lower risk associated with their share prices. Moreover, banks can raise equity capital only through the market, whereas industrial companies, for example, have more recourse to low-interest development loans for their investments needs.

Table XIX-12 shows the market value of shares at the end of years 1974 and 1975, and also the distribution of the issue-houses by sector in 1975. The table reveals that 51 percent of the value of the share market at the end of 1975 was attributed to commercial banks, 32 percent to financial intermediaries, while 17 percent went to the "real" sector. In the year 1975 these trends accentuated: banks 85 percent of the year's total issues, financial intermediaries - 9 percent, and the real sector - 6 percent only.

9. See Bank of Israel Report, 1973, page 428.

Table XIX-11

NET OVERALL RATES OF RETURN ON LISTED ORDINARY STOCKS, SELECTED PERIODS, 1973–75

(percentages)

Period	Overall rate of return: Arithmetic average rate of return	Overall rate of return: Weighted by total listed capital[a]	Overall rate of return: Weighted by annual volume of trade	Highest overall rate of return	Lowest overall rate of return	Distribution of shares by rate of return — ascending order: 10	25	50	75	90	No. of stocks	No. of companies
1. Banking, finance, insurance												
31.12.73–31.12.74	24.8	24.2	37.0	65.2	3.4	5.1	13.3	20.0	35.4	56.3		
31.12.74–30.6.75	10.8	10.9	14.8	34.5	–4.4	–1.5	2.7	8.4	16.6	22.0		
30.6.75–31.12.75	11.6	12.6	12.2	34.4	–35.1	0.3	4.5	11.4	20.2	22.3	32	20
31.12.74–31.12.75	21.8	24.2	27.7	70.5	–35.1	0.3	7.7	18.4	32.9	40.1		
2. Land and development												
31.12.73–31.12.74	2.5	–9.8	–7.1	73.3	–34.4	–28.1	–13.2	–3.5	9.9	30.4		
31.12.74–30.6.75	21.4	17.2	18.3	30.2	–4.6	–3.6	–0.9	18.7	30.2	51.5		
30.6.75–31.12.75	24.3	25.4	27.4	64.3	–13.6	–12.7	5.6	19.5	37.9	45.2	18	13
31.12.74–31.12.75	50.1	46.1	49.6	110.7	–16.7	4.2	28.1	49.7	72.5	78.0		
3. Industry and commerce												
31.12.73–31.12.74	13.7	21.3	17.3	174.9	–41.1	–25.1	–20.9	–5.7	37.6	55.0		
31.12.74–30.6.75	18.8	23.0	21.3	49.8	–6.1	–2.1	4.2	15.3	30.1	38.1		
30.6.75–31.12.75	26.7	26.7	27.9	122.3	–15.1	4.3	14.3	19.7	35.4	51.8	35	25
31.12.74–31.12.75	50.3	55.6	54.6	167.0	–8.4	16.3	23.3	47.0	73.7	84.2		
4. Investment companies												
31.12.73–30.12.74	6.8	–0.7	12.6	46.4	–31.4	–22.7	–7.0	7.6	16.1	21.4		
31.12.74–30.6.75	16.2	1.4	13.8	52.7	–17.0	–8.4	4.4	19.0	23.2	29.8		
30.6.75–31.12.75	42.2	36.1	35.7	163.2	–11.3	8.4	24.9	27.0	48.9	80.4	23	18
31.12.74–31.12.75	64.9	37.6	54.2	174.7	3.0	5.5	35.5	53.0	74.0	126.1		
5. Total companies listed												
30.12.73–31.12.74	13.6	13.4	25.7	174.9	–41.1	–20.9	–7.0	8.8	22.0	38.0		
31.12.74–30.6.75	16.4	11.2	15.9	52.7	–17.0	–3.6	4.2	14.5	24.7	38.1		
30.6.75–31.12.75	25.4	18.7	20.7	163.2	–35.1	1.5	9.2	20.2	34.4	56.7	108	76
31.12.74–13.12.75	45.4	31.4	39.1	174.7	–35.1	8.2	18.8	42.5	64.5	84.2		

[a] Weighted by listed capital at end-year market prices.
SOURCE: Tel Aviv Stock Exchange.

Public subscriptions this year rose handsomely. Many issues were oversubscribed, and they were not accompanied by falling prices (as was the case last year). Share prices rose during a period of very large issues and did not drop significantly after the issues. However, prices of bank shares rose less than average, which is related to the fact that this group had the largest share issues this year.

1975 saw the continued growth of a relatively new source of financing: capital notes and bonds convertible to shares. The latter class is a cross between a bond and a share and reduces the investor's risk in that while being an obligation for the issuing-house, the investor is enabled to participate in the dividends upon conversion to share. This is also convenient for the issuing company from the tax payment point of view[10] (interest paid to holders of bonds convertible to shares is an expense item for tax purposes, unlike dividends on shares). In the issue of capital notes, one of the banks introduced an innovation: if the investor retains his capital note, he earns the right to link 60 percent of the capital to the consumer price index.

As in previous years part of the issues was by means of rights' issues, proportional to the number of shares on the eve of the issue ("options"). The reasons for this are: some companies are bound by their articles of association to float equity issues only in the form of stock rights, secondly, to enable existing stockholders to retain their share in the total capital, and thirdly, to ensure the success of the issue.[11]

(b) *The Secondary Market*

After two years of declining trade in shares, trading recovered 42 percent relative to the previous year (see Table XIX-10). The volume even exceeded by 22 percent the peak year, 1972. A considerable proportion of the trade in shares (43 percent) was conducted outside the market (bonds - 82 percent were traded off the Exchange). This was done by pairing off buying and selling orders (self-balancing) before the opening of the Exchange. Institutional and other large investors may prefer to conduct their own large transactions in private so as not to affect share prices by the mere size of transactions. Conducting transactions outside the Exchange is bound to detract from the validity of share prices established on the market. From this point of view there was an improvement this year: trading within the Exchange rose by 47 percent, while trading outside grew by only 36 percent.

The overall net yields on ordinary shares (see Table XIX-11) improved this year. The

10. See Bank of Israel Report, 1972, page 444.
11. See Bank of Israel Report, 1973, page 428.

Table XIX-12

MARKET VALUES OF SHARES ISSUED, BY ISSUING GROUP, 1974–75, AND NEW ISSUES OF SHARES AND CONVERTIBLE SECURITIES, 1975

(IL million)

	Market value of shares and convertible securities listed on the Stock Exchange					Issue of new shares for cash[a] of shares and convertible securities, 1975				
	Share of group in total market value (end of year)				Rise in market value of shares in 1975					
	1974		1975			Shares	Convertible promissory notes and bonds	Total	Share of the group in total issue	Share of new issue in total market value of the group's shares at end 1974
		(percent)		(percent)	(percent)				(percent)	
Commercial banks and companies	2,119.4	50.6	3,470.6	51.2	63.8	404.3[b]	270.0	674.3[b]	85.2	31.8
Mortgage banks	344.4	8.2	437.5	6.4	27.0	16.5	20.0	36.5	4.6	10.6
Specialized financial institutions	333.5	8.0	777.6	11.5	133.2	4.5	0.0	4.5	0.6	1.3
Insurance	46.0	1.1	81.4	1.2	77.0	28.7	0.0	28.7	3.6	62.4
Commerce and services	107.3	2.6	183.2	2.7	70.7	0.0	0.0	0.0	0.0	0.0
Land, building, development, and citrus	217.8	5.2	317.8	4.7	45.9	0.0	15.0	15.0	2.1	6.9
Industry	376.4	9.0	656.1	9.7	74.3	12.7	20.0	32.7	4.1	8.7
Investment and companies	647.3	15.4	858.3	12.7	32.6	0.0	0.0	0.0	0.0	0.0
Total	**4,192.0**	**100.0**	**6,782.4**	**100.0**	**54.7**	**466.7**	**225.0**	**791.7**	**100.0**	**18.9**

[a] Excluding bonus issues, conversion of convertible bonds, issues not for cash and registration for trading of existing shares.
[b] See note g in Table XIX-2. This correction was not made in the calculation of the total shares listed for trade.
SOURCE: Tel Aviv Stock Exchange.

average yield, weighted by registered capital, rose to 31 percent (13 last year). The average yield, weighted by turnover, also amounts to 31 percent this year (26 percent last year); the increase took place mainly in the second half of the year when most of the dividends were distributed. Since the rate of inflation eased (about one half of that of 1974), the real growth in profitability of investment in shares was much faster than is suggested by the nominal data.

As for the total yield of issuing groups, it appears that for the financial group there was no increase this year in the rate of yield, probably because of the large additional registered capital in this group. For the other groups, there was a large rise on the overall yield; principally in the second half of 1975.

In the first five months of the year trading in shares was relatively slack (see Table XIX-9), nor was there a rising trend in the share price indices (see Table XIX-8). In June-July transactions, a peak of IL180 million per month was reached and turnover during the second half of the year remained very much higher than in the first half. Nearly half of the dealing in shares took place in the shares of commercial banks, which accounted for half of the Exchange's stock of capital at market prices (trading in bank shares took place for the most part off the Exchange). Similarly, there was a relatively large turnover in the trading of the shares of investment houses and of industrial companies.

In the first five months of the year, the weakness in the share market was also reflected in their prices. The rise in prices was concentrated in the second half of the year, when most dividends were declared. From the weighted indices of share prices, it transpires that the prices of shares in commerce and services rose 68 percent, which exceeds the rise for other shares traded in Israeli currency (a situation similar to that obtained last year when the group under discussion was slightly trailing the leading group, the commercial banks). The other group whose shares increased in value considerably this year was land, building, and development, which recorded an increase of 39 percent. This seems surprising as this was not a successful year for this group. It needs to be stressed that this group contains few shares and it is not possible to draw conclusions from them as to the state of the property market. An explanation of this enigma can perhaps be found in the large decline that took place in the values of these shares in the preceding years, and it is likely that this year saw a rapid and compensating rise in their values. With average 1972 as the base, the land share index was 105, while the general share index was 153; with average 1973 as the base, the index for this group reached 97, and the general index stood at 121. Industrial shares rose during the year by 48 percent, investment and holding companies by 31 percent, and financial and insurance

shares by 25 percent, (a rate of increase 5 percent smaller than that of all the shares put together). This may also be in accord with the large movements in previous years: according to the share index for end-1972, financial and insurance shares rose 68 percent (21 percent according to the average 1972 index) while the general index rose by 53 percent (11 percent according to the mean 1972 index). The share index of securities traded in foreign currency rose by 82 percent (after correcting for agio of the Natad dollar rate), similar to the rate of increase in the index for bonds linked to the foreign exchange rate.

The daily trading in common stock fluctuated between IL10,000 and IL20,000, as in the previous year; the degree of inequality in the daily buying and selling of various shares moderated slightly.

The index of convertible securities rate rose by 14 percent this year, following a rise of 4 percent last year. The relatively moderate rate of increase in this index was to be expected, since in a depressed share market the index of convertible securities does not decline by the rate of fall in shares (since they carry a feature of bonds). This year there was a reversal of the trend in an upward direction, and once again we find that this index did not rise as fast as the share price index.[12]

The rapid rate of increase in the index of share prices, accompanied by a narrowing of their fluctuations, contributed to an increased conversion of convertible securities to shares: IL57 million was converted as against IL29 million last year (the volume of conversion depends also on its terms, such as the option to convert after a certain period).

4. SECURITIES TRADED IN FOREIGN CURRENCY AND THE NATAD MARKET

The creeping foreign exchange rate policy instituted in June 1975, which did not dampen the expectations of a larger devaluation, left their impression on the market for securities traded in foreign currency, on foreign currency deposits, and on the rate of the Natad dollar.

During the year a brake was put on the decline in the weight of securities traded in foreign currency (see line 19 in Table XIX-1), a decline which characterized to date the

12. The index of bonds should be compared not with the index of share prices in general, but with the price index for shares of the types to which the bonds are convertible. A rough comparison can be made with the index of the prices of the financial group which issued a majority of conversion bonds (80 percent).

1970s. The balance of these securities in Natad dollars grew (in Israeli currency) by 40 percent, however, its dollar value dropped by $11.3 million. In terms of dollars there was a decline in the volume of securities registered abroad and Hollis and a rise in securities registered in Israel (see Table XIX-13). This shrinking of the securities portfolio traded in Natad occurred with a net purchase of these securities to the tune of $19.2 million whereas readjustments of exchange rates reduced the value of the portfolio by $30.5 million. Natad deposits grew by $28.4 million so that the combined Natad-traded securities and Natad itself show a rise of $17.1 million.[13]

Table XIX-13

NET PURCHASES[a] OF FOREIGN SECURITIES FROM TAMAM AND NATAD FUNDS, 1973–75

($ million)

			1975			
End of period	1973	1974	Total	Listed in Israel	Hollis	Listed abroad
Net purchases						
January	3.2	0.2	–2.7	–0.9	0.1	–1.9
February	7.7	3.9	–0.7	0.3	—	–1.0
March	–2.3	8.2	–1.2	2.1	–0.4	–2.9
April	–2.0	4.6	0.9	0.1	0.5	–1.5
May	2.8	1.2	5.8	4.0	2.3	–0.5
June	5.4	1.0	–0.2	1.0	2.3	–3.5
July	3.3	5.0	4.5	2.5	2.5	–0.5
August	–3.4	4.6	1.3	1.1	0.2	—
September	1.8	–0.3	2.0	1.3	0.4	0.3
October	0.2	1.5	1.9	1.1	0.1	0.7
November	–1.0	–3.9	–1.0	1.0	–0.2	–1.8
December	0.9	0.8	10.4	14.8	0.0	–4.4
1. Total net purchases	**16.6**	**26.8**	**19.2**	**28.4**	**7.8**	**–17.0**
2. Revaluation[b] of securities	–27.8	–6.7	–26.9	–22.6	–11.8	7.5
3. Revaluation of currency[c]			–3.6	–0.5	–0.8	–2.3
4. Total increase in holdings (1+2+3)	**–11.2**	**20.1**	**–11.3**	**5.3**	**–4.8**	**–11.8**
5. Holdings at end of period	353.7	373.8	362.5	208.2	89.3	65.0
6. Holdings (5) in IL million	1,613	2,258	3,154	1,811	776	566

[a] Total securities purchased, less total securities sold during the period.
[b] The increment from the revaluation of the portfolio according to the prices of securities at the end of March.
[c] Monthly revaluation.
SOURCE: Foreign Exchange Department, Ministry of Finance.

13. The adjustment to security prices is made only once a year in March which limits the reliability of the data here.

Table XIX-14

NATAD AND FREE-MARKET DOLLAR RATES, NATAD BALANCES, AND HOLDINGS OF SECURITIES TRADED IN FOREIGN CURRENCY, 1974-75

($ million)

End of month	1974							1975						
	Securities traded in foreign currency[a]	Natad balances	Total (1+2)	Natad dollar rate (monthly average,[b] in IL)	Agio on Natad dollar (%)	Free-market dollar rate (monthly average,[b] in IL)	Agio on free-market dollar (%)	Securities traded in foreign currency[a]	Natad balances	Total (8+9)	Natad dollar rate (monthly average,[b] in IL)	Agio on Natad dollar (%)	Free-market dollar rate (monthly average,[b] in IL)	Agio on free-market dollar (%)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)
January	353.8	28.7	382.5	4.87	16.0	5.15	22.6	372.6	26.3	389.9	6.00	—	6.51	8.5
February	357.7	35.0	392.7	5.02	19.5	5.26	25.2	374.9	23.8	398.7	6.00	—	6.57	9.5
March	365.9	41.6	407.5	4.92	17.6	5.06	20.5	370.5	25.5	396.0	6.00	—	6.60	10.0
April	363.8	44.6	408.4	4.79	14.0	4.88	16.2	341.6	24.7	366.3	6.00	—	6.66	11.0
May	365.0	51.0	416.0	4.72	12.4	4.88	16.2	348.5	29.4	377.9	6.26	4.3	7.11	18.5
June	366.0	56.4	422.4	4.96	18.1	5.12	21.9	348.1	37.8	385.9	6.54	5.8	7.40	19.7
July	371.0	56.6	427.6	4.71	12.1	5.00	19.0	347.0	40.1	387.1	6.89	12.6	7.57	23.7
August	375.6	60.1	435.7	4.63	10.2	4.87	15.9	348.8	45.1	393.9	7.07	13.3	7.63	22.3
September	375.3	66.0	441.3	4.57	8.8	4.90	16.7	348.9	48.5	397.4	7.29	14.6	7.81	22.8
October	373.8	30.1	403.9	4.79	14.0	5.15	22.6	353.6	55.8	409.4	8.06	15.1	9.08	29.7
November	373.0	38.1	411.0	6.03[c]	0.5	6.45[c]	7.5	351.1	63.4	414.5	8.38	19.7	9.72	38.9
December	373.8	30.1	403.9	6.04	0.7	6.51	8.5	362.5	58.5	421.0	8.67	22.1	10.02	41.1

[a] Including revaluation increments arising from changes in foreign exchange rates and the adjustment of holdings according to prevailing market prices (in March).
[b] Thursday averages.
[c] Average price after the devaluation.

The moderate growth in dollar terms of the portfolio of securities traded in Natad dollars can be attributed to the rise in the Natad dollar rate, which made it less worthwhile to acquire such securities (Hollis, for example). Another factor constraining the expansion of this portfolio is that the supply is not completely elastic.

The fact that there was a more rapid increase in Natad deposits than in investments in securities traded in foreign currency apparently testifies to a growth in the weight of short-term investments in this market; because a longer-term investment entitles the investor to interest or dividends in addition to the Natad dollar rate differential, it is therefore improbable that a long-term investor would acquire Natad which does not earn interest.

The expectation of devaluations, which did not disappear with the administration of creeping devaluation, brought about a rise in the rate of the Natad dollar, which began to climb above the official rate of the dollar as from May 1975. The agio rate of the Natad dollar has since risen up to 22 percent, the average for the month of December (see Table XIX-14).

As in previous years the agio rate of the black market dollar was higher than the agio for the Natad dollar throughout the year. This difference arises from the activities of other factions in this market (whose trading considerations are not those of the financial world), as well as the risks associated with this illegal market.

The price indices for bonds linked to the exchange rate and bonds traded in dollars (after correcting for the Natad dollar rate) began to rise sharply only from the month of May (see Table XIX-7). During the year the rate of the dollar-linked bond rose by 4.5 percent less than that of the bond traded in foreign currency.[14] The explanation for this lies in the fact that the holder of bonds traded in foreign currency bears the risk that the agio on the Natad dollar may drop when he wishes to unload. Against this risk the market provides a higher maturity yield of the bonds traded in dollars (a real rate of 2.2 percent as compared to 0.1 percent of foreign currency bonds).

14. It is necessary to stress the nature of the bonds discussed. Foreign-exchange linked bonds are no longer issued and their volume is progressively diminishing with the passage of time. Bonds traded in foreign currency are issued from time to time; this year to the amount of IL1,974 million.