CHAPTER VI

CAPITAL IMPORTS, THE FOREIGN CURRENCY BALANCE AND THE FOREIGN DEBT

1. Main Developments

In 1977 long- and medium-term capital imports decreased to $2.6 billion, from about $3.3 billion in the previous two years. This decline in capital imports is explained mainly by a reduction of the current deficit in the balance of payments; the steep drop in the deficit to a level lower than annual capital imports enabled the economy to increase its foreign currency balance and to reduce its short-term liabilities. Along with this positive development, there was an additional positive change: the weight of loans in capital import items decreased while the weight of unilateral transfers increased. The reform in the exchange rate in October 1977 did not bring about any exceptional changes in the flow of capital to and from the economy through the end of the year.

Positive trends in the current deficit and its financing had already appeared the previous year, after the pressure on short-term credit sources had reached its peak in 1975, but this year these trends bore a different character and significance: there was a change in the direction of development of most capital import items to the private sector. An additional phenomenon was the decline in capital flow to the public sector and the reduction of its weight in general capital imports, after it had reached an unprecedentedly high level last year.

The basis of the development in capital imports in the public sector was the decrease of capital flow from all sources: U.S. government assistance shrank considerably this year, following a steep decrease in direct defense imports, most of which originate in the United States; the flow of capital from Jewish sources was also reduced with a decline in the revenues from the United Jewish Appeal and only a slight increase in net sales of Development Loans ("Israel Bonds").

The development of the capital items to the private sector was fundamentally different from last year: first, there was slow growth in a number of items which had decreased last year, among them personal restitutions, transfers by new immigrants and local residents, and net investments from abroad; second long- and medium-term loans from abroad to the private sector, which increased sharply last year, shrank considerably this year, to the

TABLE

FINANCING OF THE CURRENT
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	1974	1975	1976	1977
A. Current accounts and long-term capital movements				
Balance on current account[b]	–3,397	–4,061	–3,316	–2,560
of which: defense imports	(–1,225)	(–1,846)	(–1,496)	(–942)
Unilateral transfers	1,718	1,770	2,224	2,005
Balance on current account and transfers	–1,679	–2,291	–1,092	–555
Long-term capital movements				
Investments from abroad, net	97	67	58	90
Independence and Development Loans	165	138	163	172
U.S. government loans	142	1,197	665	405
Other loans	253	143	172	–73
Total long-term capital movements	639	1,545	1,058	594
Total capital imports (including transfers)	2,357	3,315	3,282	2,599
Surplus of capital imports over deficit	–1,040	–746	–34	39
B. Israeli investment abroad	–10	17	–12	–7
C. Short-term credit, net (nonfinancial)	79	236	104	–54
D. Financial sectors				
Deposits and loans from foreign banks in commercial banks	350	565	243	540
Deposits in Bank of Israel	0	2	5	–
Total (a)	350	567	248	540
Loans by commercial banks to foreigners	–80	–185	64	193
Loans by Bank of Israel	24	12	–171	13
Loans by IMF	39	215	89	–
Total (b)	–17	42	–18	206
Foreign exchange reserves of central monetary institutions[a]	720	–31	–174	–307
Reserves of other monetary institutions[a]	82	–29	–143	–628
Total (c)	802	–60	–317	–935
Foreign currency valuation adjustments	87	–46	53	127
Total change in reserves due to economic transactions (d)[a]	889	–106	–264	–808
Total financial sectors (a) + (b) + (c)	1,222	503	–34	–62
E. Errors and omissions	–250	–7	–27	87

a Minus sign indicates growth of balances.

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ACCOUNT DEFICIT, 1974–1977
million)

1976				1977			
I	II	III	IV	I	II	III	IV
–739	–919	–776	–882	–498	–745	–730	–587
(–364)	(–366)	(–321)	(–445)	(–194)	(–271)	(–189)	(–288)
511	490	661	562	433	475	491	606
–228	–429	–115	–320	–65	–270	–239	19
8	18	17	15	22	21	16	30
34	37	28	64	62	37	30	43
117	117	98	333	70	92	57	187
38	33	60	41	33	–17	–37	–52
197	205	203	453	187	133	66	208
708	695	864	1,015	620	608	557	814
–31	–224	88	133	122	–137	–173	227
–8	–2	6	–9	–4	–12	–3	11
–51	147	34	–26	–32	–8	–22	8
–257	81	79	340	–207	153	48	546
2	4	–1	–	–	–	15	–15
–255	85	78	340	–207	153	63	531
133	55	–68	–56	37	33	87	36
–1	–109	–34	–27	–59	103	15	–46
–	–	75	14	–	–	–	–
132	–54	–27	–69	–22	136	102	–10
45	–64	–94	–62	–136	–39	–17	–114
136	–43	–35	–201	145	–152	–44	–578
181	–107	–129	–263	9	–191	–61	–692
15	–1	23	16	–10	19	14	104
196	–108	–106	–247	1	–172	–47	–588
73	–77	–55	24	–228	117	118	–67
17	155	–75	–124	145	38	80	–181

b Excluding administered areas.

point where their volume of repayment for the first time exceeded gross revenues, and the net balance of debts in regard to these loans decreased.

The deficit in the current account of the private sector decreased this year, and, at the same time, long- and medium-term capital imports were reduced, although to a lesser extent. These developments led to a $100 million decline in the deficit balance, which is not covered by long- and medium-term capital movements, so that it totalled about $638 million. At the same time, the extent of financing required by the private sector from the entire banking system remained unchanged, because this decrease of the unfinanced deficit balance was offset by a flow of short-term capital to foreign countries (see Table VI-12). Short-term assets of the non-financial private sector increased this year by about $130 million, as it had the previous year. This took place against an increase of only about $10 million in short-term liabilities, which contrasts with an increase of about $153 million in 1976.

The improvement in current deficit financing was expressed in a significant growth of total net assets of the Israeli monetary institutions for the first time in a number of years. The net foreign currency balance of the central monetary institutions increased this year by about $300 million, and at the same time there was no significant change in net liquid liabilities of commercial banks in foreign currency.

The foreign debt continued to grow this year, but more moderately than in preceding years, reaching about $10.7 billion at the end of 1977. Average interest rates on long- and medium-term debts remained stable, as did the composition of these debts by original repayment dates. At the same time, the weight of debts repayable during the coming year increased, reaching about $1.8 billion. The increase in the debt services of the economy was accompanied this year by an even steeper rise in revenues from exports and unilateral transfers; these developments point to a reduction in the burden of debt service repayment.

2. Background to Capital Import Developments

There were changes in the volume of capital imports and their composition during the year: capital flow decreased significantly for the first time in a long while (except 1974, when capital flow dropped, after its exceptional rise following the Yom Kippur War). Capital imports to the public sector, from most of its sources, declined steeply; the decline in transfers of individuals and investments which had characterized the preceding years was halted.

The weight of capital imports to the public sector, influenced mainly by noneconomic considerations, decreased this year in general capital flow from abroad, but its weight was still about 68 percent of all capital imports, compared to about 74 percent last year. Such a weight of capital flow to the public sector as has been prevalent in the last three years has a precedent only in the first years of the existence of the State, but at that time capital imports were mostly from Jewish sources, while now their bulk stems from aid granted by the government of the United States. This year United States government aid was reduced, both in grants and in loans. This development can be explained by the decrease of defense imports almost all of which are from the United States, since most of the assistance from this country is linked to imports of this type. Capital imports from Jewish sources also declined this year; this may be partly connected with the drop of the prices on the stock market and the rise of interest rates during the year in the United States[1].

Capital imports to the private sector remained stable this year for the most part, but the trends prevalent in most of the items of these imports changed course during recent years. On the one hand, the steep declines in investments from abroad and in transfers of immigrants to Israel halted; but there was also a sharp drop in private loans from abroad, which decreased considerably in the previous year. These developments in capital imports to the private sector stem from two basic factors: the easing of the problem of current deficit financing, accompanied by an increase of the domestic foreign currency balance – a factor that mainly affects the composition of private capital imports; and the continued standstill in product growth in the economy for the second consecutive year – a factor whose main effect is also on the volume of private capital imports.

The first factor has contradictory effects on capital flow to the private sector: the decrease of the current deficit together with the easing of its financing problem, reduce the risk factor involved in the transfer of currency to Israel, thus contributing to the growth of capital flow. A rise in the current deficit enhances expectations of drastic policy measures aimed at solving the balance of payments problem and therefore deters potential currency transferers whose considerations are purely economic. At the same time, the easing of the deficit financing problem and the growth of balances have opposite effects on the scope of private sector loans; the intensification of the problem prompts the authorities to take various steps to encourage loans from abroad (such as the granting of exchange rate insurance with subsidized premiums, guaranteeing repayment, etc.). The growth of the foreign currency balances of the economy is generally connected with the cancellation of some of the steps intended as encouragement, and this is in line with the sharp decrease in loans of the private sector over the course of the year.

1 These two factors reduce capital transfers to Israel through their effect on incomes (losses on the Stock Market) and the effect of exchangeability (the rise of alternative interest rates to potential currency transferers).

TABLE

CAPITAL IMPORTS BY SOURCE

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	1971	1972	1973	1974
1. Private sector				
a. Unilateral transfers[a]	626.6	796.7	797.4	742.4
b. Investments from abroad, net	76.2	148.7	185.2	97.0
c. Net long-term loans	123.0	178.0	197.0	83.0
Total private sector	825.8	1,123.4	1,179.6	922.4
2. Public sector				
a. Unilateral transfers	162.3	261.4	1,393.4	975.6
b. Long-term loans (net)	447.0	410.0	633.7	459.1
Total public sector	609.3	671.4	2,027.1	1,434.7
3. Total capital imports	1,435.1	1,794.8	3,206.7	1,357.1
Less: Israeli investments abroad	10.9	0.6	12.5	9.5
Total net capital imports	1,424.2	1,794.2	3,194.2	1,347.6

[a] Including nonprofit institutions.

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AND BY SECTOR, 1971–1977
million)

1975	1976	1977	1977 I	II	III	IV
731.9	683.4	749.2	170.9	177.7	195.5	205.1
67.3	57.8	90.0	21.9	21.3	16.4	30.4
73.0	119.0	–26.0	23.0	–16.0	–26.0	–7.0
872.2	860.0	813.2	215.8	183.0	185.9	228.5
1,039.7	1,540.6	1,254.7	262.2	296.1	295.8	400.6
1,403.5	882.6	530.5	141.4	129.0	76.0	184.1
2,443.2	2,423.2	1,785.2	403.6	425.1	371.8	584.7
3,315.4	3,283.2	2,598.4	619.4	608.1	557.7	813.2
–16.8	12.0	6.8	3.6	11.5	3.0	–11.3
3,332.2	3,271.2	2,591.6	615.8	596.6	554.7	824.5

TABLE VI-3

U.S. GOVERNMENT AID AND DEFENSE IMPORTS, 1972–1977
($ million)

	Grants	Revenues from loans	Repayment of loans	Total aid gross	Total aid net	Direct defense imports[a]
1972	71	330	125	401	276	–490
1973	820	369	118	1,189	1,071	–1,253
1974	672	301	155	973	818	–1,225
1975	642	1,361	148	2,003	1,855	–1,846
1976	1,176	892	215	2,068	1,853	–1,496
1977	977	656	253	1,633	1,380	–942

[a] In comparing direct defense imports with U.S. government aid, it should be remembered that there are also indirect imports, which amounted to $ 310 million in 1977.

The continued standstill of the Gross National Product has a stabilizing effect on the volume of capital imports to the private sector; the freeze of the product at its 1976 level in fact fixed the volume of capital flow at the low level of last year. This level is the "hard core" of capital import flowing to the economy despite the standstill of the product.

There was apparently no essential change in the level of expectations for devaluation nor in the change of interest differentials between the economy and the rest of the world, so that they had no special effect on the capital movements of the economy.

Toward the end of 1977[2], liberalization was introduced into the control of foreign currency, mainly by cancelling most restrictions on foreign exchange transactions of local residents, as well as by abolishing the few remaining restrictions in the field of money transfers of foreign residents. This liberalization in itself does not affect institutional currency transfers abroad; it also has a relatively weak effect on foreign residents, because the changes applying to them were insignificant, mainly the cancellation of restrictions on the timing of withdrawal of funds and revenue from investments made in Israel. The strongest effect was on foreign currency transactions of local residents, for whom the liberalization covers a great variety of subjects, among them the abolition of rationing and

2 On 28.10.1977.

control of loans from abroad, the sharp rise in the ceiling on foreign currency allocations for various purposes and the expansion of the general framework of licences to include additional transactions, such as the purchase of foreign securities, the purchase of various services abroad, and covering of various expenditures in foreign currency.

Liberalization in fact led to a lowering of the barrier intended to prevent the flight of domestic capital. At the time, during the first two months following the reform, i.e. until the end of the year, the exit of capital from the economy did not rise, mainly due to the devaluation of the pound effected at the same time as the reform went into effect; this devaluation has been estimated at about 47 percent for those transfering currency to Israel. The sharp drop in the exchange rate of the pound created two effects that provided an important contribution toward checking short-range outflow of domestic capital. The first effect was through the adjustment of asset portfolios of various bodies in the economy holding foreign currency, who reduced the share of the foreign currency component, which had increased in price following the devaluation; the second effect is related to expectations of an adjustment of domestic price levels to the increase of foreign currency price; these expectations enhanced demand for assets linked to the Israeli pound.

3. Unilateral Transfers

Following the sharp rise of unilateral transfers in 1976, they decreased this year to about \$2 billion, compared with about \$2.2 billion in 1976 and about \$1.7 billion in the preceding two years. The reduction of transfers this year is the result of a drop in the flow of public sector transfers, mainly grants from the government of the United States, which was offset by the slow increase of private sector transfers.

Transfers of the private sector increased gradually over the course of the year, after having declined for three consecutive years, and they amounted to about \$750 million. Among the transfers of the private sector, the direction change in transfers of immigrants stands out, despite the fact that the absolute size of the change has no great effect on total transfers. In 1972 immigrant transfers constituted about one quarter of all private sector transfers, and since then they have been decreasing at a rapid and continuous rate, to about 6 percent of the total transfers of the private sector in 1976, or only about \$40 million. In 1977, transfers of immigrants increased for the first time, reaching about \$50 million, their level remaining stable throughout the year. The development of immigrant transfers has gone hand-in-hand with the development of the scope of immigration to Israel from prosperous countries, which had decreased at a rapid pace between 1973 and 1976. In 1977 this decrease stopped, and a certain increase appeared in the number of immigrants.

TABLE

UNILATERAL

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	1974	1975	1976	1977
Personal restitution from West Germany				
Lump-sum	117.9	121.7	57.7	46.5
Pensions	199.2	236.9	256.2	297.9
Total	317.1	358.6	313.7	344.4
Personal transfers in cash	337.8	274.8	261.7	309.5
Immigrants	(99.8)	(62.9)	(39.7)	(50.1)
Others	(238.0)	(211.9)	(222.0)	(259.4)
Personal transfers in kind	11.9	9.3	14.0	15.3
Total personal transfers	666.8	642.7	589.4	669.2
Personal transfers to foreign countries	34.0	23.0	29.0	52.0
Total net personal transfers (a)	632.8	619.7	560.4	617.2
Nonprofit institution transfers	109.6	112.2	122.8	132.0
National institution transfers	300.8	394.6	416.0	327.8
Transfers in kind	2.8	3.1	2.6	5.9
Total institutional transfers (b)	413.2	509.9	541.4	465.7
Intergovernmental transfers (c)	672.0	642.0	1,122.0	921.0
Total transfers (a) + (b) + (c)	1,718.0	1,771.6	2,223.8	2,003.9

* Estimate.

VI-4

TRANSFERS, 1973–1977
million)

1976				1977			
I	II	III	IV	I	II	III	IV
13.0	15.5	14.9	14.1	10.8	12.8	11.4	11.5
64.6	61.3	63.2	67.1	72.3	74.7	71.4	79.5
77.6	76.8	78.1	81.2	83.1	87.5	82.8	91.0
52.0	56.8	72.2	80.7	68.3	73.5	85.7	82.0
(5.9)	(5.7)	(11.4)	(16.7)	(14.5)	(10.2)	(14.4)	(11.0)
(46.1)	(51.1)	(60.8)	(64.0)	(53.8)	(63.3)	(71.3)	(71.0)
3.6	3.6	3.3	3.5	3.6	3.8	3.8	4.1
133.2	137.2	153.6	165.4	155.0	164.8	172.3	177.1
10.0	10.0	4.0	5.0	18.0	14.0	8.0	12.0
123.2	127.2	149.6	160.4	137.0	150.8	164.3	165.1
27.3	26.6	40.4	28.5	33.9	26.9	31.2	40.0*
86.0	122.7	93.6	113.7	92.9	81.7	63.2	90.0
0.3	1.7	0.3	0.3	1.3	3.4	0.5	0.6
113.6	151.0	134.3	142.5	128.1	112.0	95.0	130.6
274.0	212.0	377.0	259.0	168.0	211.0	232.0	310.0
510.8	490.2	660.9	561.9	433.1	473.8	491.3	605.7

Transfers of Israeli residents also increased over the course of the year, amounting to about $260 million, as against about $222 million in the same period last year.

The volume of personal restitutions also increased this year, after having fallen last year: total restitutions during this period amounted to about $344 million, as against $314 million in the parallel period last year. Two items can be discerned among the components of restitutions: the first, one-time restitutions arising from single payment arrangements between the German government and Nazi victims living in Israel; the second, annuities and pensions, which are periodic payment arrangements from Germany, that are adjusted each year to price rises in Germany and the increase of the value of the German mark in relation to the dollar rate. There was an increase in the scope of pensions this year, explained in its entirety by the rise in the exchange rate of the mark in relation to the dollar and the adjustment of pensions according to price increases in Germany. This increase was partially offset by the decline of one-time restitutions to a level lower than last year.

In summing up it can be said that there were no exceptional developments in transfers of the private sector to Israel following the liberalization.

The volume of institutional transfers shrank this year, after a considerable decrease in transfers of national institutions to Israel, which was offset to a certain degree by the slow increase of transfers of nonprofit institutions.

U.S. government grants were reduced this year to approximately one billion dollars, from about $1.2 billion in 1976. This development is related to the decrease of military aid from the American government and the lack of any change in the economic aid grant, which amounted to about half a billion dollars.

4. Foreign Investments

The decline of gross cash foreign investments was halted in 1977, and they stabilized at about $58 million, an amount equal to their level last year. At the same time, the extent of liquidation of investments was reduced to about one third of its volume in 1976. These developments led to an increase in net investments, for the first time since 1973.

These trends occurred against a backdrop of continued economic standstill together with a continuing steep decline in investments in fixed assets and low activity on the land and housing markets, all having a detrimental effect on investments from abroad. In addition, the pause in world economic recovery – against the background of greately increased liquidity – apparently brought about a delay in the liquidation of foreign investments that had been made in Israel in the past, and these were considerably lower than in previous years. It should be pointed out that despite the boom on the local stock exchange in the first three quarters of the year, there was no outstanding change in the quantity of securities purchased by foreigners.

Investments of Israeli banks in foreign securities, which had risen steeply in the first three quarters of the year, reaching $17 million, showed the opposite trend in the last quarter of the year, about $14 million being liquidated during this period. It seems that the general expansion of bank activity abroad this year was also expressed in the purchase of foreign securities up to the time of the reform in the foreign currency market. Afterwards, following expectations of domestic price increases, investments abroad were liquidated and converted to investments in the domestic market.

Total net investments, after deduction of Israeli investments abroad, almost doubled this year from last; nevertheless, their level still remains very low in comparison to the level reached at the beginning of the seventies and to price increases abroad.

5. Long- and Medium-Term Loans from Abroad

The sharp decrease in the volume of long- and medium-term loans raised by the economy abroad continued this year, and they amounted to only half a billion dollars, which is about half the amount received last year and a third of the amount received in 1975. This development is the result of a decline in the gross volume of loans and an increase in the volume of repayments, in both the private and the public sectors.

Gross U.S. government loans decreased over the course of the year to $656 million, as against $900 million in 1976 and about $1.4 billion in 1975. The weight of loans in the general aid received from the U.S. government remained similar to that of last year, about 40 percent, after a parallel decrease in grants. Sales of "Israel Bonds" increased this year, as they had in 1976, their net total being about $165 million. The volume of redemptions of these bonds remained stable this year after having increased continuously since 1973, when there was an exceptional volume of sales of this loan.

The redemption of old loans of other bodies remained constant this year, at a level of about $220 million, but a sharp decrease in the volume of gross receipts of loans, below the level of annual repayment, caused the net volume of loans of other bodies to remain negative, i.e. the debt balance for these loans decreased.

The decline of the volume of loans of the public and private sectors is the result of developments in the current account of the balance of payments.

A considerable portion of the loans of the public sector is directly linked to specific

TABLE

FOREIGN INVESTMENT IN ISRAEL AND

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	1971	1972	1973
INVESTMENT IN ISRAEL BY NONRESIDENTS			
A. Investment in cash	85.9	171.8	234.5
Investment repatriated	–23.4	–47.5	–78.5
Net investments in cash	62.5	124.3	156.0
B. In Israeli currency from blocked accounts	–0.7	3.0	–8.2
C. In Independence and Development Bonds	5.3	7.3	12.5
D. In kind	3.5	6.7	8.6
Total	70.6	141.3	168.9
E. Reinvestment of profits	5.6	7.4	16.3
Total, net	76.2	148.7	185.2
ISRAELI INVESTMENT ABROAD			
A. Direct	4.2	–0.5	–0.5
B. Portfolio			
Private individuals	9.6	2.5	6.4
Banks	–2.9	–1.4	6.6
Total Israeli investment abroad	10.9	0.6	12.5
NET FOREIGN INVESTMENT IN ISRAEL	65.3	148.1	172.7

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ISRAELI INVESTMENT ABROAD, 1971–1977
million)

				1977			
1974	1975	1976	1977	I	II	III	IV
127.5	91.0	57.1	58.1	12.9	12.9	16.4	15.9
–55.9	–22.6	–31.6	–11.7	–1.2	–2.0	–3.3	–5.2
71.6	68.4	25.5	46.4	11.7	10.9	13.1	10.7
–12.6	–28.9	–14.2	–13.2	–2.4	–5.4	–5.4	–
10.6	10.7	10.2	12.8	2.9	2.6	4.4	2.9
9.0	9.1	28.3	36.0	7.7	11.2	2.3	14.8
78.6	59.3	49.8	82.0	19.9	19.3	14.4	28.4
18.4	8.0	8.0	8.0	2.0	2.0	2.0	2.0
97.0	67.3	57.8	90.0	21.9	21.3	16.4	30.4
–0.2	–1.9	5.7	3.0	–0.2	2.1	–0.2	1.3
5.1	–9.2	–2.2	0.2	1.5	1.2	–3.5	1.0
4.6	–5.7	8.5	3.6	2.3	8.2	6.7	–13.6
9.5	–16.8	12.0	6.8	3.6	11.5	3.0	–11.3
87.5	84.1	45.8	83.2	18.3	9.8	13.4	41.7

TABLE VI-6

LONG AND MEDIUM-TERM FOREIGN LOANS, 1972–1977
($ million)

	1972	1973	1974	1975	1976	1977			
						I	II	III	IV
LOANS RECEIVED									
Government	701	910	792	1,763	1,284	240	260	186	348
Independence Loan	(300)	(502)	(326)	(310)	(347)	(94)	(84)	(77)	(100)
U.S. government	(330)	(341)	(291)	(1,319)	(828)	(132)	(158)	(107)	(236)
Other	311	342	218	247	340	72	35	40	50
Total	1,012	1,252	1,010	2,010	1,624	312	295	226	398
LOANS REPAID									
Government	291	275	334	360	401	99	132	110	164
Independence Loan	(116)	(143)	(161)	(172)	(184)	(32)	(47)	(47)	(57)
U.S. government	(111)	(105)	(141)	(129)	(165)	(62)	(63)	(59)	(49)
Other	141	145	135	174	221	49	51	66	57
Total	432	420	469	534	622	148	183	176	221
NET LOANS RECEIVED									
Government	410	635	458	1,403	883	141	128	76	184
Independence Loan	(184)	(359)	(165)	(138)	(163)	(62)	(37)	(30)	(43)
U.S. Government	(219)	(236)	(150)	(1,190)	(663)	(70)	(95)	(48)	(187)
Other	170	197	83	73	119	23	–16	–26	–7
Total	580	832	510	1,476	1,002	164	112	50	177

TABLE VI-7

FOREIGN LOAN PERMITS, 1973–1977

($ million)

	1973		1974		1975		1976		1977	
	Value	No.	Value	No.	Value	No.	Value	No.	Value	No.
I	69	60	114	36	76	47	113	34	133	47
II	9	49	90	57	127	42	69	39	206	61
III	38	80	351	70	105	40	172	43	85	44
IV	51	36	120	47	408	50	104	46		
Total	167	225	675	210	716	179	458	162		

1) With the October reform in foreign currency policy; distribution of foreign loan permits ceased.

imports, and its decrease is connected with the decline of loans obtained for its financing (defense imports are the central items in this category). At the same time, the shrinking of the current deficit, accompanied by a smaller decrease in other capital import items, had a positive effect on the problem of deficit financing, and thus, the pressure for raising loans, which is a less convenient source than the other capital items, decreased considerably. These developments apparently led to the reduction of special measures[3] taken by the authorities to encourage receipt of loans by other bodies apart from the government, thus contributing to the decrease of their volume.

During the first three quarters of the year, there was an increase in the value of loan approvals accorded by the Treasury to various bodies in the economy; at the same time, the value of utilization of loans decreased, as previously mentioned. An additional reason for this is apparently the increase of interest rates in the United States and a rise in the value of the Eurodollar in Europe, to which a considerable part of the loans raised abroad by this sector is linked. These developments on the foreign credit markets apparently contributed to a reduction in the quantity of requested long- and medium-term loans.

3 The most effective means of encouraging borrowers is through exchange rate insurance on loans with subsidized premiums. We have no data on the size of this component and its variations.

6. Foreign Currency Assets and Liabilities of Monetary Institutions

The considerable improvement in the financing of the balance of payments current deficit this year found its expression in the growth of net foreign currency assets of monetary institutions. The increase of these assets resulting from transactions reached about $267 million this year, following stability in 1976 and a steep decline in 1974 and 1975. A considerable increase in net foreign currency assets occurred this year in the central monetary institutions, i.e. the Bank of Israel and the Treasury, while the volume of assets of commercial banks remained similar to that of last year.

At the end of 1977 gross balances of the Bank of Israel amounted to about $1,571 million, and net balances to about $1,156 million in 1976. Deposits of other central monetary institutions, which had increased sharply in the first half of the year, remained stable in the second half, and amounted at the end of the year to about $200 million, as against $90 million at the end of 1976.

The growth of balances, together with the slower increase of imports of commodities and services during the year, raised the ratio between net balances and the value of imports. The net inventory of balances at the Bank of Israel was sufficient this year to cover about two months of imports, as against 1.8 months in 1976 and about 1.5 months of imports in 1975. Despite the fact that this is the second year in which the share of the foreign currency inventory in the hands of the Bank of Israel for covering annual imports increased, this level of coverage is still considered low, in comparison both with other countries and with previous years in Israel.

The increase in the balances of the Bank of Israel occurred this year in the first quarter and the last two months of the year. During the rest of the year, the level of balances at the Bank of Israel remained stable. Like last year, the value of European currencies again increased in comparison to the dollar, and this contributed an increase of foreign currency balances of the Bank in dollar terms; about half of the growth of balances this year can be attributed to these revaluation differentials, which were mainly concentrated in the last quarter of the year, with the steep decline of the dollar in relation to other currencies.

Deposits of Israeli commercial banks abroad were estimated at about $2 billion at the end of the year, after an annual increase of more than $600 million concentrated entirely in the last quarter of the year. Together with the increase of these deposits, there was a similar increase in liquid liabilities of the banks this year, including deposits and loans of the banks, as well as deposits of foreign residents. Thus the liquid liability of commercial banks, amounting to about $1.4 billion, remained stable compared with the previous year, after continuously increasing since 1972.

TABLE VI-8

FOREIGN EXCHANGE RESERVES HELD AT BANK OF ISRAEL, 1977

($ million)

End of month	Gross reserves	Less foreign bank deposits	Less Patach deposits	Net reserves	Change in net reserves	Derived change of exchange rate differentials	Change in net reserves adjusted for differentials
December 1976	1,373.2	10.0	206.8	1,156.3	12.4	8.1	4.3
January 1977	1,396.8	10.0	205.9	1,180.9	24.6	–18.6	43.2
February	1,413.9	10.0	203.8	1,200.1	19.2	4.3	14.9
March	1,433.1	10.0	199.2	1,223.9	23.8	6.5	17.3
April	1,446.1	10.0	205.8	1,230.3	6.4	4.5	1.9
May	1,440.4	10.0	201.6	1,228.8	–1.5	4.3	–5.8
June	1,437.3	10.0	206.6	1,220.7	–8.1	2.9	–11.0
July	1,477.2	10.0	211.9	1,255.3	34.6	33.2	1.4
August	1,447.1	10.0	208.2	1,228.9	–26.4	–16.7	–9.7
September	1,457.1	25.0	205.6	1,226.5	–2.4	–3.7	1.3
October	1,454.4	10.0	212.5	1,231.9	5.4	30.7	–25.3
November	1,496.0	10.0	208.0	1,278.0	46.1	11.0	35.1
December	1,571.0	10.0	202.0	1,359.0	81.0	55.0	26.0
Total					202.7	113.4	89.3

7. Foreign Currency Debt [5]

For the first time in a long period, the pace of nominal growth of Israeli foreign currency debts decelerated to a significant extent this year. The balance of debts at the end of 1977 totalled $10.7 billion, compared to about $9.4 billion in 1976, and about $7.6 billion in 1975. The significance of the increase of debts is reduced even more against the backdrop of world price increases: after deducting the increase of export prices of commodities and services, the annual growth of debts amounts to only about 2 percent. Like last year, most of the increase in the debt[6] occurred in the last quarter, while at the same time, some of the positive trends that have characterized the development of debts since 1975 were blunted.

The growth of the debt encompassed all categories of debts, so that debt composition by repayment dates remained stable: about 82 percent of the debt were long-term debts; about 10 percent, from 9 percent last year, were medium-term debts and about 8 percent, as against 9 percent last year, were short-term.

At the same time, the repayment schedule points to an increase in the weight of debts the economy will have to pay within the coming year, after these increased to $1.8 billion as against $1.5 billion last year, and their weight in total indebtedness amounted to about 17 percent. This development in itself is responsible for a slight increase in the pressure of repayment on the balance of payments in the coming year.

Despite the increase in the volume of debts, interest payments to foreign countries increased by only about $8 million, and amounted to about $560 million. This development can be explained by the decrease of interest rates on short-term debts (we have no direct data on this). At the same time, it is possible that the increase in liabilities that occurred in the last quarter of the year was not yet reflected in interest payments in 1977. Average interest on long-term debts remained constant this year and was estimated, like last year, at about 5.1 percent. a comparison of this rate to other interst rates prevalent in the world credit market[7], which were in the vicinity of 7 percent this year, points to a

5 The foreign currency debt is not identical with the external debt of the economy, which also includes, in addition to items recorded in the debt, Israeli currency liabilities abroad, balances in clearing accounts, foreign investments in Israel, deposits of foreign residents in Israeli banks, and loans whose maturity date is less than ninety days.

6 Changes in the total debt include revaluations, but are not otherwise adjusted; they therefore do not accurately represent the change in loans as registered in the balance of payments.

7 Such as the Eurodollar in Europe and the primary interest rate in the United States.

considerable grant-base inherent in long-term debts of the economy. Average interest on medium-term debts remained stable as well, and stood at about 8.7 percent, as against 8.6 percent in 1976.

An accepted criterion for assessing the debt payment burden on the economy is the measurement of the weight of foreign currency revenues of the economy in the current account dedicated to the financing of debt services. A downward trend in the ratio of debt services to export revenues has been noted since 1970, pointing to a decrease of the debt payment burden on the balance of payments. This trend stopped in 1975, and the ratio rose considerably; in the last two years, following the considerable growth of exports and the moderate increase in debt services, the ratio again decreased gradually, reaching 23.2 percent this year, which is the lowest rate in the past decade. In respect to the Israeli economy, enjoying a continuously high level of unilateral transfers, it is customary to use an additional indicator for the measurement of the debt service burden, i.e. the ratio of debt services to revenue, including exports and unilateral transfers. This indicator also points to an easing in the burden of external debt repayment on the Israeli balance of payments in 1977.

Direct debts of the government amounted to about $8.0 billion this year, as against about $6.9 billion in 1976 and about $5.6 billion in 1975. Debts of other bodies amounted to about $2.4 billion this year, and its weight in the total debt decreased to 22 percent, as against about 23 percent in 1976 and about 27 percent in 1975. In fact, there is a long-term downward trend in the weight of the development loan, due to an increase in the weight of the Defense Loan, which grew this year by about $667 million, and amounted to about $3.2 billion. In the course of recent years, the development loan and the Defense Loan together constitute about half of the total debt, but in review of the recent extension of repayment dates, their weight in annual repayment of the principal is on the decline.

TABLE

FOREIGN CURRENCY ASSETS

($

	1974	1975	1976	1977
1. Foreign currency assets in Bank of Israel				
A. Foreign currency assets				
Foreign currency reserves	1,150.3	1,134.5	1,318.4	1,494.4
Gold	46.4	46.5	44.8	49.5
Gold quota in IMF	–	–	–	–
Special drawing rights	3.0	2.6	10.0	27.0
Total (1)	1,199.7	1,183.6	1,373.2	1,570.9
B. Liabilities				
Foreign banks	–	2.0	10.1	9.8
Patach[a]	129.1	142.1	206.8	202.0
Total (2)	129.1	144.1	216.9	211.8
C. Net balance with Bank of Israel	1,070.6	1,039.5	1,156.3	1,359.1
2. Other monetary organizations				
A. Assets				
Deposits abroad of other central monetary organizations[b]	58.4	105.0	89.8	198.9
Commercial bank deposits	1,224.0	1,211.0	1,351.4	1,975.4
Other	21.6	13.9	16.1	19.9
Total, net (A)	1,304.0	1,329.9	1,457.3	2,194.2
B. Liabilities				
Foreign bank deposits and loans	1,101.7	1,391.2	1,571.5	1,938.3
Patach in commercial banks	1,071.3	1,303.7	1,372.6	1,657.1
Total (B)	2,173.0	2,694.9	2,944.1	3,595.4
3. Assets in banking system				
A. Assets (A1+B1)	2,503.7	2,513.5	2,830.5	3,765.1
B. Liabilities (B2+ foreign banks)	2,173.0	2,696.9	2,954.2	3,605.2
C. Net assets	330.7	−183.4	−123.7	159.9
D. Change in net assets	−1,224.1	−514.1	59.7	283.6
(−) rate adjustments	−16.0	2.1	−43.8	−16.7
E. Change in net assets due to transactions	−1,240.1	−512.0	15.9	266.9

[a] The source is the daily balance of the Bank of Israel.

IN BANKING INSTITUTIONS, 1974–1977
million)

1976				1977			
I	II	III	IV	I	II	III	IV
1,101.9	1,166.2	1,260.2	1,318.4	1,376.2	1,380.8	1,394.2	1,494.4
46.5	46.5	46.5	44.8	45.9	46.1	46.0	49.5
–	–	–	–	–	–	–	–
1.5	1.6	9.3	10.0	11.0	10.4	16.9	27.0
1,149.9	1,214.3	1,316.0	1,373.2	1,433.1	1,437.3	1,457.1	1,570.9
4.0	8.0	10.6	10.1	10.0	10.0	25.0	9.8
142.7	172.2	185.3	206.8	199.2	206.6	205.6	202.0
146.7	180.2	195.9	216.9	209.2	216.6	230.6	211.8
1,003.2	1,034.1	1,120.1	1,156.3	1,223.9	1,220.7	1,226.5	1,359.1
93.8	93.5	85.5	89.8	166.0	201.1	198.7	198.9
1,069.9	1,117.4	1,143.8	1,351.4	1,214.0	1,366.1	1,396.8	1,975.4
18.8	14.0	23.0	16.1	8.4	8.0	20.9	19.9
1,182.5	1,224.9	1,252.3	1,457.3	1,388.4	1,575.2	1,616.4	2,194.2
1,234.4	1,223.9	1,342.7	1,571.5	1,383.8	1,480.1	1,489.0	1,938.3
1,184.5	1,274.7	1,252.0	1,372.6	1,362.6	1,434.1	1,480.2	1,657.1
2,418.9	2,498.6	2,594.7	2,944.1	2,746.4	2,914.2	2,969.2	3,595.4
2,332.4	2,439.2	2,568.3	2,830.5	2,821.5	3,012.5	3,073.5	3,765.1
2,422.9	2,506.6	2,605.3	2,954.2	2,756.4	2,924.2	2,994.2	3,605.2
–90.5	–67.4	–37.0	–123.7	65.1	88.3	79.3	159.9
92.9	23.1	30.4	–86.7	188.8	23.2	–9.0	80.6
–33.0	–0.7	–2.4	–7.7	19.6	–4.5	–7.4	–24.4
59.9	22.4	28.0	–94.4	208.4	18.7	–16.4	56.2

b According to the definition of the balance of payments.

TABLE

END OF YEAR FORECAST OF ISRAEL'S FOREIGN

($

	1969	1970	1971
Up to one year	244	398	475
Thereof: short-term loans	(82)	(115)	(183)
One to two years	195	195	224
Two to three years	135	174	202
Three to four years	122	136	159
Four to five years	109	117	192
Five years or more	1,316	1,602	2,178
Total	2,121	2,622	3,430
		Percentage distribution	
Up to one year	11.5	15.2	13.9
Thereof: short-term loans	(34)	(39)	(39)
One to two years	9.2	7.4	6.5
Two to three years	6.4	6.6	5.9
Three to four years	5.7	5.2	4.6
Four to five years	5.1	4.5	5.6
Five years or more	62.0	61.1	63.5
Total	100.0	100.0	100.0
		Cumulative percentage	
Up to one year	11.5	15.2	13.9
Up to two years	20.7	22.6	20.4
Up to three years	27.1	29.2	26.3
Up to four years	32.8	34.4	30.9
Up to five years	37.9	38.9	36.5
Five years or more	100.0	100.0	100.0

VI-10

CURRENCY DEBT, BY REPAYMENT DATE, 1969–1977
million)

1972	1973	1974	1975	1976	1977
434	549	968	1,414	1,480	1,826
(187)	(187)	(564)	(927)	(805)	(873)
263	329	504	490	785	950
241	351	423	511	850	1,165
268	327	439	628	725	1,071
238	369	481	530	813	777
2,637	3,168	3,435	4,044	4,718	4,926
4,081	5,093	6,250	7,617	9,371	10,715
by repayment date					
10.6	10.8	15.5	18.6	15.8	17.0
(43)	(34)	(58)	(66)	(54)	(48)
6.4	6.5	8.1	6.4	8.4	8.9
5.9	6.9	6.8	6.7	9.1	10.9
6.6	6.4	7.0	8.2	7.7	10.0
5.8	7.3	7.7	7.0	8.7	7.2
64.6	62.1	55.0	53.1	50.3	46.0
100.0	100.0	100.0	100.0	100.0	100.0
distribution					
10.6	10.8	15.5	18.6	15.8	17.0
17.0	17.3	23.6	25.0	24.2	25.9
22.9	24.2	30.4	31.7	33.3	36.8
29.9	30.6	37.4	39.9	41.0	46.8
35.3	37.9	45.1	46.9	49.7	54.0
100.0	100.0	100.0	100.0	100.0	100.0

TABLE

FOREIGN CURRENCY TRANSACTIONS

($

	1974	1975	1976	1977
1. Current account deficit	–3,397	–4,061	–3,316	–2,560
A. Government deficit[a]	–1,345	–2,046	–1,725	–1,116
B. Private sector deficit	–2,052	–2,004	–1,591	–1,444
2. Private sector capital import[b]	913	912	848	806
Capital import surplus over private sector deficit (2–1B)	–1,139	–1,092	–743	–638
3. Commercial banking system and short-term capital flows				
A. Short-term non-financial private capital	20	316	35	–116
B. Reduction of commercial bank balances	–113	–37	–131	–569
C. Loans received by banks from abroad and Patach	350	565	243	540
D. Loans given to banks abroad	–80	–185	64	193
E. Less transfers of public sector to banks	–350	–282	101	–143
Total financing given by commercial bank and short-term capital flows	–173	377	302	–95
Total computed sales to Bank of Israel (2+3–1B)	–1,312	–715	–441	–733
5. Errors and omissions	–250	–7	–27	82
6. Actual sales to Bank of Israel[c]	–1,244	–770	–559	–754

a Including defense imports, public sector interest and additional items of insignificant scope.

b Less Israeli investments abroad.

OF THE PRIVATE SECTOR, 1974–1977
million)

1976				1977			
I	II	III	IV	I	II	III	IV
–739	–919	–776	–882	–498	–745	–730	–587
–418	–415	–373	–518	–237	–278	–246	–354
–321	–504	–403	–364	–261	–467	–484	–233
194	180	210	264	211	172	183	240
–127	–324	–193	–100	–50	–295	–301	7
–69	147	–33	–10	–47	–4	–40	–25
137	–44	–34	–199	141	–146	–40	–524
–257	81	79	340	–207	153	48	546
133	55	–68	–56	37	33	87	36
3	91	57	–50	–45	–23	–25	–50
–53	330	1	52	–121	13	30	–17
–180	6	–192	–75	–171	–282	–271	–10
17	155	–75	–124	145	38	80	–181
–188	–49	–189	–133	–74	–264	–253	–154

c This datum is not derived from the balance of payments but is received directly from the Bank of Israel.
SOURCE: Balance of payments.

TABLE VI-12

INDICATORS OF THE SERVICING BURDEN, 1968–1977

($ million)

	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
1. Interest payments	92	109	133	141	179	262	389	530	552	560
2. Principal payments (long- and medium-term)	229	252	292	330	432	420	469	534	622	728
3. Total debt servicing (1)+(2)	321	361	425	471	611	682	858	1,064	1,174	1,288
4. Exports of goods and services	1,150	1,290	1,402	1,875	2,222	2,784	3,634	3,766	4,430	5,560
5. Unilateral transfers	438	464	650	792	1,059	2,190	1,718	1,772	2,224	2,004
6. Ratio (3/4)	27.9	28.0	30.3	25.1	27.5	24.5	23.6	28.3	26.5	23.2
7. Ratio 3/(4+5)	20.2	20.6	20.7	17.7	18.6	13.7	16.0	19.2	17.6	17.0