

CHAPTER IX

ACTIVITIES OF THE BANK OF ISRAEL

1. SUMMARY OF THE BALANCE SHEET AT THE END OF 1981¹

(a) Main Developments

The Bank of Israel's balance sheet totaled IS115 billion at the end of 1981, compared with IS56 billion the year before—an increase of 104 percent, as against 122 percent in 1980. The smaller rate of growth this year is explained primarily by the slower rise of the consumer price index (101.5 percent as against 133 percent) and the milder devaluation of the sheqel (106.7 percent against the dollar and 79.7 percent against the German mark, compared with 113.5 and 88.9 percent respectively in 1980).

Developments in the various balance sheet items did not display a uniform pattern. The most striking change was a big increase in the government's Israeli currency debt in the form of provisional advances. Foreign exchange reserves expanded, though less rapidly than in 1980, while the Bank's securities portfolio increased in real terms at about the same rate as in 1980. By contrast, foreign currency credit granted by the Bank of Israel for financing exports fell off appreciably. Credit in local currency also declined more sharply in real terms than in 1980. The contraction of foreign currency credit is explained by the reduction of the Diamond Fund, the lowering of the rates of financing in the various funds, and changes in export financing arrangements between the Bank of Israel and the commercial banking system. These developments were consistent with the Bank of Israel's policy of limiting non-directed (free market) and directed credit.

The main item on the liabilities side—foreign currency deposits of banking institutions—declined slightly this year in dollar terms. This mainly reflected the depreciation of DM-denominated deposits due to the weakening of that currency against the dollar, and also to the smaller growth of foreign currency deposits in general. The banks' local currency deposits and banknotes and coins in circulation increased in real terms, following last year's real decline.

¹ Most of this section is from the Bank of Israel's Financial Statements for the Year 1981, published in January 1982.

(b) Foreign Currency Accounts Abroad

Foreign exchange reserves held at the Bank of Israel² amounted to \$2,847 million, compared with \$2,780 million at the end of 1980—an increase of \$67 million, as against \$210 million last year.

The contribution of the private and public sectors to the growth of reserves underwent a change this year: the public sector added only some \$370 million to the holdings, in contrast to \$1,100 million in 1980, while the private sector drew them down by only about \$300 million, as against \$900 million in 1980.

This year's smaller public sector contribution can be mainly attributed to the decrease in foreign currency transfers to Israel by the government and the Jewish Agency—from about \$1 billion last year to some \$260 million. This followed a huge increase in foreign aid in 1980 on account of the military redeployment in the Negev. It was also influenced by the fortuitous timing of

Table IX-1
CLAIMS ON AND LIABILITIES TO FOREIGNERS IN GOLD
AND FOREIGN EXCHANGE, 1980-81
(\$ million)

	1981	1980	Increase
Assets			
Gold, foreign currency, and securities in			
foreign currency	3,542	3,394	148
Other foreign currency assets	7	90	-83
Total claims on foreigners	3,549	3,484	65
Liabilities			
Allocation of Special Drawing Rights	124	109	15
Liabilities to IMF	74	93	-19
Foreign currency deposits of foreign banks	4	5	-1
Other liabilities	13	12	1
Nonresidents' deposits	691	608	83
Total liabilities to foreigners	906	827	79
Net claims on foreigners (foreign currency assets)	2,643	2,657	-14
Net foreign exchange reserves at the Bank of Israel^a	2,854	2,781	73

^a Defined in note 2.

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

end-of-year transfers. The Bank of Israel's income from interest and exchange rate differentials on its gross reserve holdings amounted to about \$112 million, compared with \$210 million last year.³

Most of the growth in foreign exchange reserves was recorded in the first four months of the year, when the level rose by \$220 million. In the next four months it fell \$190 million, and in the last third of the year it again turned up, by \$40 million. In the first four-month period both the public and private sectors contributed to the expansion of reserves. In the next four months the public sector continued to be a source of growth, although less so than before, but this was more than offset by the strong contractionary effect of the private sector's operations. In the last four months the public sector further augmented the reserves, while the private sector had only a marginal effect.

The Bank's gross foreign currency assets held abroad reached \$3,542 million at the end of 1981, compared with \$3,395 million at the end of 1980—an increase of 4 percent, as against 9 percent in 1980.

(c) Government Accounts

Bank of Israel credit to the government increased by IS 19 billion, compared with IS 1.3 billion in 1980, and amounted to IS 24.5 billion at the end of 1981. The government pumped some IS 17 billion into the economy during the year reviewed, as against IS 5 billion in 1980.⁴ The overwhelming share of the injection was financed by the incremental Bank of Israel credit. Other transactions in the government's accounts, which are not included in the calculation of its liquidity injection, were the conversion of foreign currency (about IS 2 billion); the transfer of Bank of Israel profits to the Treasury (IS 4.2 billion), which does not constitute an absorption; and the charging of the government with interest and exchange rate differentials on its debt to the Bank (about IS 8 billion), which does not constitute an injection.

(d) Loans and Discounts

This item totaled approximately IS 22 billion at the end of 1981, as against some IS 19 billion in the previous year. Almost the entire balance represented the Bank of Israel's participation in the export fund—about IS 17 billion (\$1.1 billion) in foreign currency and some IS 5 billion in local currency. The contraction of foreign currency credit reflected the decrease in the Diamond Fund, the reduction of the rates of financing in the export funds, and changes in the funds' financing arrangements between the Bank of Israel and the commercial banking institutions.

³ The decline mainly reflected the downward revaluation of the reserves by some \$293 million following the weakening of the various currencies against the dollar, notably the DM, which retreated 13 percent in relation to the dollar.

⁴ These sums include the liquidity injection by the Jewish Agency. Excluding Jewish Agency operations, the government injected IS 15.3 billion, compared with IS 3.8 billion in 1980.

Table IX-2

STATEMENT OF CHANGES IN ASSETS AND LIABILITIES FOR THE YEAR ENDED DECEMBER 31, 1981

	Total assets and liabilities (IS million)					Assets and liabilities in or linked to foreign currency (in terms of U.S. \$ million)			
	Balance on 31.12.80	Balance on 31.12.81	ISm.	Increase		Balance on 31.12.80	Balance on 31.12.81	Increase	
				Percent				Sm.	%
				Nominal	Real ^a				
Assets									
Foreign assets	26,294	55,376	29,082	110.6	4.5	3,484	3,549	65	1.9
Government debt									
In or linked to foreign currency	4,250	5,516	1,266	29.8	-35.6	563	353	-210	-37.3
In local currency	1,209	19,030	17,821	1,474.0	681.2				
Loans and discounts									
In foreign currency	16,213	17,264	1,051	6.5	-47.2	2,148	1,106	-1,042	-48.5
In local currency	3,070	5,066	1,996	65.0	-18.1				
Securities	3,924	9,558	5,634	143.6	19.9				
Other assets	1,362 ^b	3,154 ^b	1,792	131.5	14.9	139	149	10	7.2
Total assets	56,322	114,964	58,642	104.1	1.3	6,334	5,157	-1,177	-18.6
Liabilities									
Banknotes and coins in circulation	2,537	5,360	2,823	111.3	4.8				
Foreign liabilities	828 ^b	1,417 ^b	589	71.2	-15.1	110	91	-19	-17.3

Foreign currency deposits of the government and National Institutions	2,334	4,281	1,947	83.4	-9.0	309	274	-35	-11.3
Foreign currency deposits of banking institutions in Israel									
Against residents' deposits—restitution	19,635	37,482	17,847	90.9	-5.3	2,602	2,402	-200	-7.7
Against residents' deposits—other	18,062	37,772	19,710	109.1	3.8	2,393	2,421	28	1.2
Against nonresidents' deposits	4,591	10,788	6,197	135.0	16.6	608	691	83	13.7
Deposits of banking and financial institutions in Israel	2,007	4,424	2,417	120.4	9.4				
Capital and general reserve	1,000	1,000	—	—	-50.4				
Other liabilities	5,328 ^b	12,440 ^b	7,112	133.5	15.9	334	410	76	22.7
Total liabilities	56,322	114,964	58,642	104.1	1.3	6,356	6,289	-67	-1.0
Foreign exchange reserves held at the Bank of Israel ^c						2,780	2,847	67	2.4

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

^a The nominal change deflated by the increase in the consumer price index (101.5 percent in December levels), apart from the securities item, which was deflated by the November-to-November increase in the index (103 percent)—see note a.8.

^b Consists of sums in or linked to foreign currency and unlinked sums.

^c Defined as gold, foreign exchange, and foreign securities, less deposits of foreign banks and foreign currency deposits of banking institutions in Israel against nonresidents' deposits (see notes b and h).

The Bank of Israel reduced the Diamond Fund this year by imposing credit quotas. Together with the world crisis facing the diamond industry, this led to a drastic decline in diamond inventories in this country and to the shrinkage of the Fund's financing by \$514 million.

The Imports-for-Export Fund contracted by \$313 million following changes in the financing arrangements between the Bank of Israel and the commercial banks, and the lowering of the rates of financing from 75 to 57 percent per dollar of export in April and from 57 to 42 percent in September. Beginning in May 1981 exporters were allowed to receive credit in various foreign currencies, instead of in dollars only, as was the case before.

The Bank of Israel reduced its participation in the Export Shipments Fund by \$279 million in the year surveyed. This decline also reflected the changes in the financing arrangements between the central bank and the banking institutions and the lowering of the rate of financing in this fund in September 1981 from 80 to 70 percent. In March the interest charged by the Fund was raised from 60 percent of the Euromarket rate to 70 percent. The changes in the Fund were also connected with the transfer of medium- and long-term financing of such shipments to a new fund established at the end of 1980 for this purpose. This fund grew by \$60 million in 1981 to stand at \$97 million at year's end.

Local currency credit granted by the Bank of Israel through the export production funds expanded in 1981 by IS2.3 billion to reach IS4.9 billion. Most of the increment derived from adjustments to the rate of exchange, and in part was offset by the reduction of the rate of financing in September from 57 to 50 percent per export dollar.

The IS253 million balance of the special credit granted by the Bank of Israel to commercial banks last year to reduce their liquid asset shortfalls was repaid in 1981, and was not renewed because of their improved liquidity position.

(e) Securities

The Bank of Israel's securities portfolio consists of government bonds linked to the consumer price index or the dollar, which were acquired by the Bank in its capacity as the government's agent and for regulating secondary market trade in such bonds; and nontradable loan certificates acquired from local firms. The revalued balance of the portfolio came to IS9.6 billion, as opposed to IS3.9 billion at the end of 1980—an increase of 144 percent.

The portfolio of tradable securities expanded from IS2 billion to IS5.8 billion, or by 190 percent. This is explained by the revaluation of the portfolio, Bank of Israel intervention in the secondary market, and bond redemptions. The Bank's open-market operations, which are mainly intended to moderate fluctuations, resulted in a IS1.4 billion net purchase this year, after a IS0.2

billion net sale in 1980; most of the purchases were made in November and December.

The nontradable securities portfolio expanded from IS 1.9 billion at the end of 1980 to IS 3.8 billion at the end of 1981, or by roughly 95 percent. The portfolio consists predominantly of nontradable loan certificates acquired from local firms under special arrangements as a substitute for directed credit; purchases totaled IS 0.7 billion in the year reviewed. The special bonds issued as savings scheme cover, which were acquired from banking institutions in 1979 and 1980, were resold to them at the beginning of 1981 in the amount of IS 0.3 billion.

(f) Banknotes and Coins in Circulation

The value of banknotes and coins in circulation reached IS 5.4 billion at the end of 1981, as against IS 2.5 billion at the end of 1980—an increase of IS 2.8 billion, or 111 percent, compared with 84 percent in 1980. This year's growth exceeded the 78 percent increase in the money supply,⁵ and consequently the proportion of currency in the money supply moved up from 30 percent in 1980 to 34 percent. The growth of currency at a pace slightly eclipsing the rate of inflation, after several years of real decline, probably indicated the stabilization of the public's inflationary expectations.

The proportion of the larger banknotes (IS50 and IS100) in total currency in circulation rose further this year, reaching 94 percent as against 85 percent at the end of 1980; the IS 100 note accounted for 68 percent of the total.

The exchange of old Israeli pound notes continued, and by year's end they amounted to only 1 percent of total notes in circulation. The exchange of coins denominated in Israeli pounds and agorot proceeded more slowly, and at the end of 1981 they still accounted for 15 percent of total coins in circulation, although most of them were apparently not in actual use. On September 10, 1981 a five-sheqel coin was put into circulation.

(g) Israeli Currency Deposits of Banking Institutions

Banking institution deposits in Israeli currency with the Bank of Israel totaled IS 4.4 billion, compared with IS 2 billion at the end of 1980—an increase of 120 percent, compared with 122 percent last year. This year's increment reflected the expansion of the public's local currency deposits—both demand deposits and negotiable certificates of deposit—at roughly the same rate as inflation.

(h) Foreign Currency Deposits of Banking Institutions

The commercial banks' foreign currency deposits with the Bank of Israel represent their required liquidity cover against three types of deposits of the

⁵ Provisional datum.

Table IX-3
BANKNOTES AND COINS IN CIRCULATION BY DENOMINATION, 1980-81^a

End of period	1980		1981	
	IS million	%	IS million	%
Banknotes				
Israeli pound series				
IL1 and IL½	0.4	—	0.4	—
IL5	2.5	—	2.5	—
IL10	8.8	—	6.5	—
IL50	11.4	1	8.8	—
IL100	19.7	1	14.1	—
IL500	169.1	7	22.6	—
Total	211.9	9	54.9	1
Sheqel series				
IS1	30.4	1	23.9	—
IS5	28.7	1	36.8	1
IS10	212.6	9	206.8	4
IS50	1,624.2	66	1,276.8	25
IS100	357.3	14	3,599.8	69
Total	2,253.2	91	5,144.1	99
Total banknotes	2,465.1	100	5,199.0	100
Trade coins				
Israeli pound series				
1-500 prutot	0.2	—	0.2	—
1 agora	0.3	1	0.3	—
5 agorot	0.9	2	0.9	1
10 agorot	3.3	7	3.1	2
25 agorot	1.0	2	0.9	—
IL½	2.7	5	2.4	2
IL1	8.9	18	7.8	6
IL5	6.3	13	5.3	4
Total	23.6	48	20.9	15
Sheqel series				
1 new agora	0.4	1	0.8	1
5 new agorot	0.9	2	2.1	1
10 new agorot	9.6	19	23.0	16
IS½	14.8	30	27.7	20
IS1	—	—	51.3	37
IS5	—	—	14.3	10
Total	25.7	52	119.2	85
Total trade coins	49.3	100	140.1	100
Total banknotes and trade coins	2,514.4		5,339.1	
Commemorative coins				
Israeli pound series	17.6		15.8	
Sheqel series	4.6		4.8	
Total	22.2		20.6	
Total banknotes and coins	2,536.6		5,359.7	

^a Includes Israeli pound banknotes still in circulation.

public: those of German restitution recipients (Patam restitution), other residents' deposits (Patam), and deposits of nonresidents, exporters, and new immigrants (Patach). The balance of these foreign currency accounts in the Bank of Israel at the end of the year stood at IS86 billion (about three-fourths of total liabilities in the Bank's balance sheet); this represented an increase of 104 percent, compared with 117 percent the year before. In dollar terms, these accounts decreased only slightly and amounted to \$5.5 billion, even though the nondollar deposits were revalued downward by more than \$400 million following the weakening of the European currencies against the U.S. dollar.

A breakdown shows that at the end of the year reviewed residents' restitution accounts totaled IS37.5 billion, after rising 91 percent; in dollar terms, however, they fell from \$2.6 billion at the end of 1980 to \$2.4 billion, or by 8 percent. The downturn is mainly explained by the weakening of the German mark against the dollar, a trend which began in 1980 and induced the public to shift some of its holdings from marks to dollars. This new phenomenon was also reflected in the commercial banks' deposits with the Bank of Israel: the weight of DM deposits in total restitution accounts dropped from about 90 percent at the end of 1980 to 70 percent at the end of 1981.

The balance of residents' deposits (Patam) rose by only \$28 million to reach \$2.4 billion. They moved up a bit until the end of October, but with the

Table IX-4

INTEREST RATES PAID BY THE BANK OF ISRAEL ON ISRAELI CURRENCY DEPOSITS OF BANKING AND FINANCIAL INSTITUTIONS^a

(Percentages)

Type of asset	Total liquidity requirement	Breakdown of required liquid cover by interest rates paid			
		Interest rate steps			
		0	29	70	85
Ordinary demand deposits	47	15	32	—	Liquidity surplus
Time deposits					
2-6 months	12	6	6	—	—
6+ months	7	3	4	—	—
Negotiable certificates of deposit					
3+ months	14	6	8	—	—
Nondirected credit in IS	3	—	—	3	—

^a Rates in force on December 31, 1981.

introduction of the dollar-linked savings plan in November, an estimated \$150-200 million was withdrawn from Patam accounts, converted, and placed in the new schemes, in which some \$300 million was accumulated by the end of 1981.

Nonresidents' deposits grew by 14 percent in dollar terms, bringing up their balance to \$691 million.

2. STATEMENT OF INCOME AND EXPENSES FOR 1981⁶

(a) Net Income and Its Appropriation

The Bank of Israel's net income totaled IS4.2 billion, compared with IS3.6 billion in 1980. The slower growth this year was mainly due to a decrease in exchange rate differentials; these amounted to only IS0.2 billion, as against IS2.4 billion in 1980. The downturn can be attributed primarily to the excess of liabilities over assets in foreign currency in the second half of the year, following a surplus of assets, on average, in 1980. Excluding revaluation differentials, the Bank's net profit totaled IS4 billion, compared with IS1.2 billion last year. The net profit, amounting to IS4.2 billion, was transferred to the Treasury.

(b) Income

Total income for the year reviewed was IS62.9 billion, as opposed to IS32.5 billion in 1980—an increase of 94 percent. These figures include the revaluation of assets in or linked to foreign currency. Excluding revaluation differentials, the Bank's income for 1981 came to IS19 billion, as against IS7.3 billion in 1980—an increase of 160 percent. Following is an analysis of the main components.

Interest income from the investment of foreign currency assets abroad totaled approximately IS6 billion (about \$430 million), compared with IS2.3 billion (\$368 million) last year. Most of the growth stemmed from a rise in interest rates on the major world currencies in 1981 and a slightly higher average level of foreign exchange reserves.

Interest income from loans and rediscounts were, at IS3.9 billion, 95 percent up on last year's figure of IS2 billion. The increment was the net result of two contrasting developments: (1) an increase in world interest rates and the upping of the rate charged by the Export Shipments Fund from 60 to 70 percent of the Euromarket rate; and (2) the contraction of the Diamond Fund during 1981 and the cutting of the Bank of Israel's participation in the various credit funds toward the end of the year.

⁶ Most of this section is from the Bank of Israel's Financial Statements for the Year 1981, published in January 1982.

Income earned on the Bank's securities portfolio consists mainly of indexation and dollar-linkage differentials and interest. In 1981 such income added up to IS 3.6 billion, as against IS 2.1 billion the year before. Part of this sum is not included in net income due to the matched timing principle (see note a to the Financial Statements).

Net interest income from the government's debt amounted to IS 4.6 billion, in contrast to IS 0.4 billion last year. This rapid growth is mainly explained by the larger average volume of provisional advances extended to the government this year, and the raising of the interest rate on the government's accounts in the last third of the year. The interest paid by the Bank of Israel on the government's accounts was set off against interest received on the latter's debt to the Bank.

(c) Expenses

The Bank of Israel's expenses totaled IS 56.2 billion in 1981, as against IS 27.2 billion in the previous year—an increase of 107 percent. The increment includes the revaluation of foreign currency liabilities for changes in the relevant exchange rates against the sheqel. Most of the valuation changes were in the foreign currency deposits of banks, which reached some IS 40 billion this year. Excluding revaluation, the Bank's expenses amounted to IS 12.4 billion, compared with IS 4.4 billion in 1980—a growth of 182 percent.

The leading expenditure item is interest paid on the commercial banks' obligatory liquidity deposits in foreign currency; this reached IS 9.7 billion, more than three-fourths of total expenditure for the year. Higher interest rates and the switch from DM deposits to dollar deposits, which offer a higher return, explain the expansion of this item.

Interest paid on the banks' obligatory liquidity deposits in local currency rose from IS 0.5 billion in 1980 to IS 1.4 billion, i.e., by 173 percent. The increase can be chiefly ascribed to the growth of the average balance of these deposits, as well as to the raising of the rates of interest paid thereon.

3. BANK CREDIT

(a) Directed Bank of Israel Credit

The granting of directed credit is the responsibility of the Credit Control Department of the Bank of Israel, which is assisted by committees comprising representatives of the various government ministries. The credit is actually provided by joint funds of the Bank of Israel and the commercial banks, and is intended primarily to meet the working capital requirements of export enterprises. This type of finance is also extended, wherever necessary, to foreign buyers. (For a breakdown of the funds' sources of financing and their interest rates, see Table IX-5.)

Table IX-5
STRUCTURE AND TERMS OF DIRECTED CREDIT FUNDS, 1980-81
 (Percentages)

End of period	Sources of funds in 1980				Sources of funds in 1981			
	Commercial banks	Bank of Israel		Interest rate in 1980	Commercial banks	Bank of Israel		Interest rate in 1981
		Liquidity exemptions	Rediscounts or loans			Liquidity exemptions	Rediscounts or loans	
Export funds in foreign currency								
Imports for export production	5.5	—	94.5	11.7	100.0	—	—	8.6
Regular export shipments	5.5	—	94.5	11.7 ^a	5.5	—	94.5 ^b	10.0 ^a
Special export shipments	5.5	—	94.5	19.5 ^a	5.5	—	94.5	15.7 ^a
Diamonds	—	—	100.0	15.2	—	—	100.0	10.5
Export funds in Israeli currency								
Export production	5.5	19.5	75.0	57.0	5.5	19.5	75.0	34.5
Citrus	5.5	19.5	75.0	57.0	5.5	19.5	75.0	34.5
Indirect exports	5.5	19.5	75.0	66.5	5.5	19.5	75.0	66.5
Working capital funds in Israeli currency								
Supervised farm credit	5.0	—	95.0	55.0	—	—	100.0	72.0
Assistance to agricultural settlements	40.0	—	60.0	57.0	40.0	—	60.0	57.0
Industry and crafts	15.0	—	85.0	55.0	15.0	—	85.0	55.0
Assistance to industrial enterprises	40.0	—	60.0	57.0	40.0	—	60.0	57.0
General fund	15.0	—	85.0	55.0	15.0	—	85.0	55.0
Employers Loan Fund	—	10.0	90.0	^c	—	—	100.0	3.0 ^d

^a The credit is given in various currencies; the interest rate appearing here relates solely to that on dollar credits.

^b Beginning in September the banks were required to deposit foreign currency from their own means against Bank of Israel credit granted through this fund. At the end of the year the deposit requirement reached 50 percent of the balance of the Fund for Financing Export Shipments.

^c The interest rates vary in accordance with the rates specified in the relevant bond issues.

^d 80-90 percent indexation.

The balance of directed credit in Israeli and foreign currency provided by the export and working capital funds came to IS33.7 billion at the end of the year reviewed, compared with IS20.1 billion in 1980—a nominal increase of 68 percent, as against 143 percent in 1980, but a real decline of 17 percent. Outstanding directed export credit in foreign and Israeli currency amounted to IS33.3 billion at the end of 1981, up 69 percent from the previous year. The annual average level rose 99 percent, in contrast to 151 percent during 1980; this represented a slight drop in real terms. Exports eligible for such financing expanded by roughly 8 percent in dollar terms during this period.

The balance of directed export credit in foreign currency grew 63.7 percent, and that in Israeli currency by 93.9 percent; in the previous year both components rose to the same extent—135 percent. The Diamond Fund was mainly responsible for the differential rate of increase in 1981, as it expanded by a mere 15.7 percent in Israeli currency terms. Directed credit for domestic activities rose nominally by only 24 percent, reflecting the continuation of the Bank of Israel's policy of restricting the growth of such credit.

1. Export Funds

These funds finance all stages of export production through the Export Production Fund (in Israeli currency); the import of inputs through the Imports-for-Export Fund (in foreign currency); and shipments through the Export Shipments Fund (in foreign currency). There are also two branch funds: the Diamond Fund (in foreign currency) and the Citrus Fund (in Israeli currency). The Indirect Export Fund assists enterprises supplying intermediates for production for the foreign market. In 1980 the Long- and Medium-Term Export Finance Fund was established to finance export transactions in capital goods sold on medium- or long-term credit. The Export Reorientation Fund, which was set up in the same year by the Bank of Israel and exporters to finance the shifting of production from the domestic to the export market, expanded its activities in the year reviewed.

The IS33.3 billion balance of directed export credit at the end of 1981 consisted of IS6.6 billion in Israeli currency and IS26.7 billion (\$1,708 million) in foreign currency, of which approximately IS10 billion (\$640 million) was in the Diamond Fund. In 1981 the funds granting finance in Israeli and foreign currency, apart from the Diamond Fund, expanded by 110 percent (125 percent on an annual average), following increases of 94 percent in the Israeli currency funds and 118 percent (5.5 percent in dollar terms) in the foreign currency funds.

Foreign currency credit provided by the Long- and Medium-Term Export Finance Fund spurted from approximately \$40 million at the end of 1980 to \$100 million a year later. With this exception, the foreign currency funds did not grow in dollar terms during 1981.

Table IX-6
DIRECTED EXPORT CREDIT, 1980-81
 (IS million)

	1980		1981		Percent increase	
	End-year balance	Average balance	End-year balance	Average balance	End-year balance	Average balance
In Israeli currency						
Export production	2,867	2,105	5,572	4,425	94.3	110.2
Citrus	423	215	809	336	91.3	56.3
Indirect export	87	76	124	110	42.5	44.7
Export reorientation	41	7	122	95	197.6	1,257.0
Total	3,418	2,403	6,627	4,966	93.9	106.7
In foreign currency						
Imports for export production	2,713	1,781	5,196	4,124	91.5	131.6
Export shipments	4,645	3,057	9,909	6,809	113.3	122.7
Long- and medium-term export finance	292	144	1,560	718	434.2	398.6
Total, excl. Diamond Fund	7,650	4,982	16,665	11,651	117.8	133.9
In \$ million	(1,014)	(972)	(1,068)	(1,020)	(5.3)	(4.9)
Diamond Fund	8,634	5,452	9,987	8,866	15.7	62.6
Total foreign currency credit	16,284	10,434	26,652	20,517	63.7	96.6
In \$ million	(2,157)	(2,035)	(1,708)	(1,796)	(-20.8)	(-11.7)
Total credit from export funds	19,702	12,837	33,279	25,483	68.9	98.5

SOURCE: Liquidity report of the banking institutions.

(i) Imports-for-Export Fund

The balance of this fund at the end of 1981 was lower in dollar terms than at the end of the previous year, despite a 12 percent gain in the overseas commodity sales eligible for its assistance. The reduction of the rate of financing during the year—from 70 percent to 48 percent on an annual average (42 percent of the marginal rate of financing from October 1981) was responsible for this drop. The interest charged by the fund remained unchanged at approximately 60 percent of the Eurodollar rate. In April 1981 it began to grant credit in various foreign currencies, instead of only in dollars, and borrowers can now obtain loans in the same currencies they receive for their exports.

(ii) Export Production Fund

In continuation of the policy of reducing the volume of credit granted by this fund, the rate of financing, which had been lowered from 70 percent of the Bank of Israel representative exchange rate to 57 percent at the end of 1980, was cut further, to 50 percent, in September 1981. This brought down the average rate of financing for the year to 53 percent.

(iii) Diamond Fund

During 1981 the balance of this fund shrank from \$1,145 million to \$640 million, mainly because of the imposition of credit quotas with a view to paring the fund by 25 percent during the first quarter of 1981, and also because of the reduction of diamond inventories during the year.

The Diamond Fund accounted for only 30 percent of total outstanding credit granted by all the export funds at the end of 1981, compared with 44 percent the year before.

(iv) Export Shipments Fund

The average balance of this fund rose 123 percent in 1981 (8 percent in dollar terms), while exports eligible for such finance advanced 12 percent. The rate of financing was cut to 70 percent in September 1981, depressing the average level for the year by 8 percent. This was offset primarily by the growth of commodity exports.

(v) Long- and Medium-Term Export Finance Fund

This fund was established in January 1980 to provide credit in the form of Bank of Israel rediscounts for periods of over 18 months, to finance the export of capital goods and equipment. This type of fund is found in many other countries, and the terms offered here are similar to those abroad with respect to repayment period (up to five years), rate of financing (85 percent), and interest rate, which is based primarily on an international export credit consensus. The balance of this fund shot up from \$40 million at the end of 1980 to \$100 million at the end of 1981, mainly due to an increase in the weight of capital goods in total exports.

Table IX-7

DIRECTED CREDIT FOR DOMESTIC PRODUCTION, 1980-81

(IS million)

	1980		1981		Percent increase	
	End-year balance	Average balance	End-year balance	Average balance	End-year balance	Average balance
Industry and crafts	95	69	99	96	4.2	39.1
Assistance to agricultural settlements	72	69	135	95	87.5	37.7
Conversion loans to agriculture	149	112	112	156	-24.8	39.3
Other funds ^a	115	130	85	125	-26.1	-3.8
Total directed credit for domestic production	431	380	431	472	—	242

^a Excludes linkage differentials; includes emergency credit.

SOURCE: Liquidity report of the banking institutions.

2. Working Capital Funds for Domestic Production

Directed credit for domestic production continued downward in real terms, with the balance at the end of 1981 remaining unchanged in nominal terms. The year reviewed saw the completion of the conversion of short-term agricultural credit for financing approved investments into long-term loans for up to seven years and linked 70 percent to the consumer price index, under the government's and Bank of Israel's policy of assisting agricultural settlements in financial straits. The total amount of loans granted by the Bank of Israel in 1981 came to IS120 million, of which IS72 million was transferred to the government's management under its arrangement with the Bank.

(b) Credit Ceilings

The Bank of Israel continued to set ceilings on nondirected (free market) credit provided to Israeli residents in both foreign and local currency. During the initial freeze this year (January 1 - March 4, 1981), the Bank maintained its policy of imposing separate Israeli and foreign currency ceilings for each banking institution, allowing any deviation from the Israeli currency ceiling to be set off against an underutilization of the foreign currency ceiling.

With the extension of this system on March 5, 1981, the basis for calculating the ceiling was revised as follows:

(1) An overall ceiling, expressed in sheqalim, was set for directed credit in

both Israeli and foreign currency, with half the amount being linked to the Bank of Israel representative exchange rate (in relation to the dollar) during the period of the freeze.

(2) The foreign currency ceiling was limited to the average level of credit granted during the three weeks ending March 4, 1981.

(3) Accrued indexation increments on Israeli currency credit provided by the directed credit funds were included in the overall ceiling.

(4) Foreign currency credit granted to Israeli residents by overseas offices of local banks was also included. For purposes of checking compliance with the quotas the year was divided into the following subperiods: March 5–May 13, May 14–August 12, August 13–November 4, and November 5–February 10, 1982. A separate calculation was made for each of the first two periods, and a combined calculation for the last two.

Until the end of the first period the fine for exceeding the credit limit was 30 percent p.a.; thereafter it was raised to 70 percent p.a.

4. FOREIGN EXCHANGE CONTROL

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

Foreign exchange control is exercised at the Bank of Israel by three units: the Economic Unit, the Companies Unit, and the Permits Unit—Individuals (until recently the last two operated as a single unit—the Permits Unit).

The Economic Unit deals with changes in the General Permit, procedures for authorized dealers, informational activity, and the conducting of economic surveys and studies in relevant areas. The Companies Unit deals with foreign investment in Israel, the approval of overseas investments by Israeli residents, and especially applications to establish companies abroad and the monitoring of their operations. The Permits Unit—Individuals grants specific permits to Israeli noncompany residents, and deals with requests of Israeli residents to receive foreign currency loans from abroad. In addition, the Controller of Foreign Exchange maintains the Administrative Fines Committee in cooperation with the government's legal adviser and in coordination with the police.

(a) General Permit

The General Permit defines those activities which Israeli residents are permitted to undertake in foreign currency and with foreign residents. From time to time the Permit is revised in the light of general economic and monetary developments and in accordance with the policy of the government and Bank

of Israel. In 1981 and the first quarter of 1982 the following changes were introduced:

1. Directives were issued defining which foreign securities sold in the U.S. over-the-counter market may be purchased by Israeli residents.

2. Under the General Permit it was formerly possible to acquire a controlling interest in a foreign corporation by purchasing its stock on a foreign stock exchange or in the U.S. over-the-counter market. The Permit was amended to prohibit an Israeli resident from acquiring more than 5 percent of the stock or voting rights of a foreign corporation in this manner. Such acquisitions now require a specific permit from the Controller of Foreign Exchange.

(b) Circulars of the Controller of Foreign Exchange

In addition to amendments to the General Permit, the Controller of Foreign Exchange from time to time issues circulars to banks and authorized dealers. These clarify and explain the rules pertaining to the General Permit as well as the policy and activities of the Controller of Foreign Exchange. They contain operating procedures for authorized dealers and prescribe the examinations, records, and reports required of them.

(c) Informational Activity

Following the publication of the pamphlet *Foreign Exchange Control—Explanatory Guide* in 1980, two leaflets were published in 1981 and widely distributed: one clarifies what is permitted and prohibited in connection with the holding of foreign currency and its use in Israel, and the other is intended for Israeli residents traveling abroad.

5. ADMINISTRATION OF STATE LOANS

(a) Issue and Redemption of Noncompulsory Government Bonds

The State Loans Administration of the Bank of Israel is responsible for the issue and redemption of tradable bonds sold to the general public, special bonds for institutional investors (savings schemes and provident and pension funds), and bonds issued against insurance company and National Insurance Institute deposits. It maintains the record of registered bond owners and handles current payments and receipts in connection with the government's bond issues. In addition, it transfers to the Accountant General the proceeds of bank and financial institution issues that must be deposited with him; in 1981 these transfers amounted to IS34.1 billion, as against IS10.3 billion in the previous year.

**LOAN AND OTHER ISSUE PROCEEDS AND DEPOSITS^a TRANSFERRED BY
STATE LOANS ADMINISTRATION TO THE ACCOUNTANT GENERAL, 1980-81**

(IS million)

	1980	1981
Managed by the State Loans Administration	5,232	15,327
State loans	4,739	3,235
Bonds issued against National Insurance		
Institute deposits	—	6,491
Bonds issued against insurance company deposits	493	1,011
Deposits against dollar-linked savings schemes	—	4,590
Transfers to the Treasury	5,052	18,783
Bond issue proceeds	4,253	17,253
Voluntary deposits	799	1,530
Total	10,284	34,110

^a For details of these loans and their terms see Table IX-8.

Capital mobilization (issues less redemptions) through the sale of government bonds to institutional investors and the general public plunged from IS8.3 billion in 1980 to IS0.7 billion, owing to a sharp drop in new issues and the flattening of redemptions. Direct holdings of indexed bonds shrank further in 1981, when a decrease in issues of tradable bonds outweighed an increase in nontradable bond sales to institutional investors. The public's demand for indexed financial assets was directed overwhelmingly to institutional savings—bank savings schemes and provident, pension, and advanced study funds.

The general public took only 21 percent of total government loan issues in 1981, compared with 77 percent the year before. Concurrently there was a much larger deposit of bank and financial institution issue proceeds for covering the accumulation in savings schemes and social insurance funds. These deposits, which were transferred to the Accountant General by the State Loans Administration, jumped 113 percent in real terms.

The bulk of the tradable bonds sold to the public (IS1 billion) were fully indexed issues with a 3 percent coupon. In addition, IS60 million of bonds were sold of a new type of issue, which is linked to the dollar and carries a variable rate of interest calculated half yearly at 1.5 points higher than the rate payable on commercial bank six-month dollar deposits with the Bank of Israel.

The growth of the savings schemes in 1981 was concentrated in the first and last quarters of the year. In February the required cover was changed, whereupon purchases of the special savings scheme bond issues rose precipitately. The Bank of Israel sold IS200 million of these issues, but the

Table
STATE LOAN ISSUES

(IS			
1980			
	Interest rate (%)	Gross issues (1)	Redemption of principal (2)
A. Medium- and long-term			
1. To the public and for savings schemes ^b			
For 10 years, 80%indexation	4, 6, 7	1,246.3	—
For 10 years, 90% indexation	4	—	—
For 10 years, full indexation	3, 4	2,777.4	0.1
For 10 years, double-linkage option	5	27.3	—
For 6 years, full linkage to dollar	5.5	—	—
For 8 years, 70% linkage to dollar	6	—	—
For 7 years, full linkage to dollar	variable	—	—
For 5 years, option-type	4.84	—	14.7
For 7 years, full indexation ^c	3.25, 6.5	—	41.3
Absorption Loan ^d	4	—	3.0
Other ^e	—	—	0.5
2. For savings schemes			
For 6 years, linked option	4.25	44.8	—
For 6 years, dollar option	5	1.9	—
3. For financial institutions			
For 17, 20 years for provident and pension funds	5, 6.5	651.6	2.8
Insurance Companies Loan	8.2, 5.8, 6.2	482.5	0.7
Bank Defense Loan	7.5	—	3.3
4. For National Insurance Institute		—	—
Total medium- and long-term loans		5,231.8	66.4
B. Deposits with Accountant General			
1. Issue proceeds deposited with the Treasury		4,253.4	
2. Deposits against dollar-linked savings schemes		—	
3. Voluntary deposits		799.3	

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

^b Includes sales and redemptions of issues for the Bank of Israel's portfolio.

IX-8

AND REDEMPTIONS, 1980-81^a

million)

Interest and linkage increments (3)	Net issue (1-2-3) (4)	Gross issues (5)	1981		
			Redemption of principal (6)	Interest and linkage increments (7)	Net issue (5-6-7) (8)
447.7	798.6	—	—	1,103.9	-1,103.9
36.6	-36.6	—	—	78.5	-78.5
111.5	2,665.8	890.6	—	404.8	485.8
45.6	-18.3	—	—	100.1	-100.1
0.7	-0.7	—	—	8.3	-8.3
1.2	-1.2	—	—	2.6	-2.6
—	—	60.0	—	—	60.0
148.8	-163.5	—	1.3	19.4	-20.7
757.9	-799.2	—	19.2	533.5	-552.7
89.5	-92.5	—	2.8	211.2	-214.0
1.7	2.2	—	—	—	—
—	44.8	172.7	—	—	172.7
—	1.9	0.1	—	—	0.1
136.0	512.8	2,111.9	2.4	291.5	1,818.0
176.9	304.9	1,010.9	4.8	450.9	555.2
89.8	-93.1	—	9.0	305.7	-314.7
2,518.3	-2,518.3	6,491.0	—	2,518.3	3,972.7
4,562.2	603.2	10,737.2	39.5	6,028.7	4,669.0
		17,253.0			
		4,589.5			
		1,530.0			

^c With an option for final redemption after 10 years.^d Includes payments under the Compensation Interest on Compulsory Loans Law.^e Includes loans under the Absentees' Property Law, unlinked loans, and other loans.

commercial banks acquired most of their bonds—IS3.9 billion as against IS0.1 billion in 1980—from issues of affiliated financial institutions. The banks also purchased some tradable government bonds, but in the secondary rather than the primary market. During the first quarter most of the purchases were for covering the new two-year savings schemes; in the last quarter the banks began to market dollar-linked schemes, and the entire IS4.6 billion accumulation was deposited with the Treasury through the Bank of Israel.

There was an increase this year in contributions to provident, pension, and advanced study funds and in life insurance premium payments. As a result, purchases of government issues to cover the incremental accumulation rose from IS1.1 billion in 1980 to IS3.1 billion. The expansion of such contractual saving was reflected primarily by the purchase of bond issues of bank subsidiaries to the tune of IS13.4 billion, which was deposited with the Treasury through the Bank of Israel. The funds concerned also bought IS1.4 billion of bonds whose proceeds were freely usable.

The National Insurance Institute deposited IS6.5 billion with the Treasury, in exchange for which it received bonds from a special issue in this amount. Redemption of bonds received in earlier years totaled IS2.5 billion.

(b) Distribution and Redemption of Compulsory Loans

In August 1981 the final redemption was begun of the last third of the 1975 Savings Loan series, the second third of the 1976 Loan, and the first third of the 1977 Loan. All 1977 Savings Loan certificates with a face value of up to IS100 also reached maturity. Total redemption in 1981 of the 1970-77 series amounted to IS49.5 million face value, or IS835.9 million redemption value (including indexation increments; accrued interest, and interest on late redemptions). In 1980 the figures were IS36.6 million and IS400.3 million respectively; there was thus a 35 percent increase in redemptions at face value.

In September the first interest coupon of the 1975 Land Appreciation War Loan fell due, and in October the second coupon of the 1971 Defense Loan. The redemption value of all compulsory loan coupons cashed in during 1981 totaled IS14.1 million.

The Defense and War Loan Laws provide for the early redemption of bonds in the case of the elderly, needy disabled persons, and heirs upon the death of the registered owners. The regulations also permit companies and other enterprises experiencing financial difficulties to cash in their bonds ahead of maturity as compensation for waiving receipt of development loans, with the approval of the Ministries of Trade and Industry, Agriculture, Housing, and Transport. Early redemption is also permitted in the case of the Voluntary War Loan, with the approval of the Minister of Finance. In 1981 early redemptions amounted to IS18.7 million face value, or IS570.3 million

Table IX-9
REDEMPTION OF COMPULSORY STATE LOANS, 1980-81^a
 (IS million)

	1981			1980		
	Redemp- tion of principal	Interest and in- dexation incre- ments	Total	Redemp- tion of principal	Interest and in- dexation incre- ments	Total
Defense Loan, 1970-74	9.7	366.7	376.4	9.8	179.6	189.4
Savings Loan, 1970-77	49.5	786.4	835.9	36.6	363.7	400.3
War Loan, 1973-75 ^b	9.0	184.9	193.9	11.5	140.4	151.9
Cost-of-Living Allow- ance Loan	0.8	4.8	5.6	16.7	103.5	120.2

^a Includes extra interest paid on late redemptions.

^b Includes the Voluntary War Loan.

redemption value, compared with IS21.3 million and IS341.3 million respectively in 1980.

In July 1981 the interest on late compulsory loan redemptions, which is calculated four times annually, was raised to 102 percent. Total interest paid reached IS39.2 million, as against IS17.5 million in 1980.

The face value of compulsory loan certificates (Savings, Defense, War, and Cost-of-Living Allowance Loans) distributed in 1981 came to only IS100 million, down from IS201 million the year before. Delivery was continued this year of Defense Loan certificates for 1970-75, War Loan certificates for 1973-75, and Cost-of-Living Allowance Loan certificates. Approximately 63,000 certificates, including 40,000 of the 1977 Employers' Savings Loan, were mailed, compared with 370,000 in 1980.

The Bank of Israel continued its efforts to locate those whose certificates had been returned in previous years. In the first quarter of 1981 it concentrated on certificates which reached maturity. Some 45,000 certificates were remailed during the year reviewed, as against 83,000 in 1980. For the public's convenience the Bank of Israel operates a computer terminal system which provides up-to-date information on compulsory loan holdings of individuals and companies.

(c) Bank of Israel Open-Market Operations

The Bank of Israel operates in the secondary bond market to stabilize trade in government bonds and thereby promote private saving through the purchase of such paper. The Bank's open-market transactions soared 232 per-

Table IX-10
BANK OF ISRAEL OPEN-MARKET OPERATIONS, 1978-81
 (IS million at current prices)

	Net purchases (sales-) on the Stock Exchange								Total Bank transactions on Stock Exchange (sales + purchases)	Percent of total Stock Exchange trade ^a	Total open-market operations ^b
	Index-linked					Double-option	Dollar-linked	Total			
	(3% int.) 100%	80%	90%	(4% int.) 100%	Others						
1978	—	11.8	11.3	-21.9	-2.3	10.4	0.4	9.7	179.3	24.5	-25.8
1979	—	192.1	4.0	-22.9	-2.9	-9.7	-0.1	160.5	610.4	32.7	218.1
1980	-24.1	-97.5	-5.3	-86.1	-7.3	-11.0	-0.4	-231.7	347.5	9.5	-249.2
1981	926.2	585.7	15.3	-114.8	-0.2	-2.6	5.8	1,415.4	3,995.5	37.6	1,530.6
January	-22.0	0.4	—	-9.9	-0.2	-0.5	—	-33.0	34.3	7.2	-23.3
February	27.9	-4.1	-1.4	-10.7	—	-1.0	—	10.7	90.4	13.0	3.9
March	63.4	1.2	-0.4	-10.7	—	—	—	53.5	79.6	9.3	45.0
April	10.6	-1.5	0.1	-6.1	—	-0.3	—	2.8	21.4	3.8	3.6
May	18.4	2.8	—	0.1	—	0.1	—	21.4	33.2	7.5	40.4
June	78.7	4.4	—	-1.7	—	—	-0.5	80.9	98.9	16.2	107.7
July	65.7	-5.0	0.3	-17.3	—	-1.6	5.5	47.6	256.6	31.9	40.2
August	81.0	-14.6	0.3	-25.6	—	-1.2	5.1	45.0	349.7	36.6	39.3
September	-237.2	-14.2	-2.3	-26.8	—	-1.8	0.2	-282.1	439.8	43.7	-251.1
October	63.6	5.0	3.9	5.6	—	0.8	1.9	80.8	244.7	28.6	114.4
November	393.1	96.5	8.8	16.3	—	0.9	3.3	518.9	746.5	49.1	560.8
December	383.0	515.6	6.0	-28.0	—	2.0	-9.7	868.9	1,600.4	71.8	849.7

^a This series was calculated by a different method from that used in previous years; see note to Table VIII-B10.

^b Bank of Israel Stock Exchange purchases less sales, plus holdings of original-issue bonds, less redemptions of tradable bonds in the Bank's portfolio.

cent in real terms over last year's figure as the result of a change in policy in the second half of the year. In the first half of 1981 the Bank continued its previous year's policy, preventing sharp fluctuations in bond prices with only a limited effect on market trends. In the second half of the year the Bank stepped up its intervention, increasing its operations from IS0.4 billion during the first half to IS3.5 billion. Since mid-July the Bank has initiated transactions in bonds by submitting buy orders before the start of the daily trading session on the Stock Exchange, and its share in total Stock Exchange trade moved up from 5 percent before the change of policy to 25 percent. This high degree of intervention reduced fluctuations in index-linked bond prices.

During the year reviewed the Bank of Israel was a heavy net buyer of bonds—IS1.4 billion as against a mere IS0.2 billion in 1980. Most of the net purchases (IS1.2 billion) were made in the last two months of the year, after the introduction of the dollar-linked savings schemes. The Bank wound up with a net sale in only two months—January and September; the rest of the year purchases exceeded sales.

The Bank of Israel's regulatory activities were mainly concentrated on the fully indexed bond with a 3 percent interest coupon and the 80 percent indexed issues with a 7 percent coupon; its intervention helped to arrest the real decline in their prices, which began in early 1981. Prices of the fully linked bonds sank 10.7 percent in real terms in the first half of the year, but turned up 3.8 percent during the second half, thanks largely to the Bank's intervention. The 80 percent indexed bonds fell 10 percent by the middle of July, but rose 1.3 percent thereafter.

(d) Redemption of Israel Bonds

The Bank of Israel handles the redemption and conversion (early redemption in local currency) of the Independence and Development Loans (Israel Bonds). These bonds, which are issued abroad, can be cashed in ahead of maturity in this country by Israeli public institutions, foreign investors, tourists, and returning Israeli residents, in accordance with the conditions prescribed by the Controller of Foreign Exchange and the relevant regulations.

The volume of Israel Bonds redeemed and converted during 1981 went up 31 percent to reach \$214 million (\$198 million principal and \$16 million interest), compared with \$164 million in 1980. In current Israeli currency terms the figure was roughly IS2.5 billion.

A breakdown of conversions by holder shows a continued rise in the share of tourists from 38 percent (\$62 million) in 1980 to 41 percent (\$87 million). Public institutions also increased their share appreciably, from 25 percent in 1980 to 35 percent.

6. ISSUE OF CURRENCY AND COMMEMORATIVE COINS AND MEDALS

(a) Trade Coins

On September 10, 1981 a new IS5 bronze coin was put into circulation. It weighs 6.1 grams, is 24 mm. in diameter, and has a milled edge. On the obverse is a double cornucopia with pendant ribbons—a stylized design of the motif which appeared on Jewish coins from the period of John Hyrcanus I (ca. 128 B.C.E.).

A cupronickel IS10 coin was introduced into circulation on February 25, 1982. It weighs 8 grams, is 26 mm. in diameter, and has a smooth edge. The obverse features a galley from the period of Herod Archelaus (4 B.C.E.); this is in keeping with the Bank's tradition of selecting motifs and symbols of ancient Jewish coins.

In 1982 the Bank will put into circulation a new 500 sheqel banknote bearing the portrait of Baron Edmond de Rothschild, father of modern Jewish settlement in Israel.

Table IX-11

COMMEMORATIVE COINS ISSUED BY THE BANK OF ISRAEL, 1980/81-1981/82

Coin	Face value (in IS)	Weight (grams)	Diameter (mm.)	Number issued ^a		
				B.U.	Proof	Total
Independence Day, 5741-1981						
(silver)	2	28.8	37	20,000	13,000	33,000
(gold)	10	17.28	30	—	7,500	7,500
Hanukka, 5742-1981	1	14.4	30	25,000	15,000	40,000

^a Includes coins which remained unsold by the Israel Government Coins and Medals Corporation.

Table IX-12

COINS MINTED IN 1980/81

Coin	Minted abroad	Minted in Israel	Total
1 new agora	1,000,000 (Canada)	—	1,000,000
5 new agorot	1,000,000 (Canada)	—	1,000,000
10 new agorot	123,000,000 (Germany)	28,160,000	151,160,000
IS ½	15,296,000 (France)	37,976,000	53,272,000
IS 1	99,000,000 (France)	39,970,000	138,970,000

Table IX-13
COMMEMORATIVE AND SPECIAL COINS ISSUED BY THE BANK OF ISRAEL,
1974/75^a TO 1980/81 (UPDATE)

Coin	Mint	B.U./ proof	No. minted— previous figures	No. de- stroyed	Updated mintage
Independence Day coins					
1966/67 (Eilat)	Utrecht	B.U.	30,250	54	30,196
	Utrecht	Proof	7,755	35	7,720
1967/68 (Jerusalem)	Bern	B.U.	50,000	—	50,000
	Bern	Proof	20,501	—	20,501
1968/69 (Peace)	Kreshmer, Jm.	B.U.	20,199	—	20,199
	San Francisco	B.U.	40,000	76	39,924
	San Francisco	Proof	20,000	122	19,878
1969/70 (Mikve Israel Centenary)	Kreshmer, Jm.	B.U.	47,604	57	47,547
	Bern	Proof	22,500	26	22,474
1970/71 (Science-Based Industries)	Jerusalem	B.U.	22,700	—	22,700
	Utrecht	B.U.	30,000	18	29,982
	Utrecht	Proof	17,501	—	17,501
1971/72 (Israel Aviation)	Jerusalem	B.U.	50,000	130	49,870
	Jerusalem	Proof	15,000	—	15,000
1972/73 (Proclamation of Independence)	Jerusalem	B.U.	124,050	59	123,991
	Jerusalem	Proof	41,500	—	41,500
1973/74 (Revival of Hebrew)	Jerusalem	B.U.	127,300	67	127,233
	Jerusalem	Proof	49,750	53	49,697
	Jerusalem	B.U.	49,200	22	49,178
1974/75 (Israel Bonds)	Jerusalem	Proof	39,980	93	39,887
1975/76 (Israel's 28th Anniversary)	Jerusalem	B.U.	40,000	2,150	37,850
	Jerusalem	Proof	35,000	7,500	27,500
1976/77 (Brotherhood in Jerusalem)	Jerusalem	B.U.	37,300	290	37,010
	Jerusalem	Proof	27,200	425	26,775
1977/78 (Israel's 30th Anniversary)	Jerusalem	B.U.	40,500	60	40,440
	Bern	Proof	22,000	158	21,842
1978/79 (Mother and Child)	Jerusalem	B.U.	30,000	5,850	24,150
	Ottawa	Proof	25,000	8,860	16,140
1979/80 (Israel-Egypt Peace Treaty)	Bern	B.U.	30,000	9,795	20,205
	Bern	Proof	20,000	7,082	12,918
1980/81 (People of the Book)	Ottawa	B.U.	20,000	3,644	16,356
	Ottawa	Proof	13,000	1,642	11,358
Hanukka coins					
1974/75 (Hanukka lamp from Damascus)	Jerusalem	B.U.	74,375	224	74,151
	Jerusalem	Proof	58,900	218	58,682

Table IX-13 (cont.)

Coin	Mint	B.U./ proof	No. minted— previous figures	No. de- stroyed	Updated mintage
1975/76 (Hanukka lamp from Holland)	Jerusalem	B.U.	44,400	146	44,254
	Jerusalem	Proof	33,650	73	33,577
1976/77 (Hanukka lamp from U.S.A.)	Jerusalem	B.U.	25,000	116	24,884
	Jerusalem	Proof	20,000	—	20,000
1977/78 (Hanukka lamp from Jerusalem)	Jerusalem	B.U.	46,302	166	46,136
	Jerusalem	Proof	29,689	140	29,549
1978/79 (Hanukka lamp from France)	Jerusalem	B.U.	36,200	—	36,200
	Ottawa	Proof	22,300	—	22,300
1979/80 (Hanukka lamp from Egypt)	Bern	B.U.	33,000	1,365	31,635
	Bern	Proof	20,000	938	19,062
1980/81 (Hanukka lamp from Corfu)	Ottawa	B.U.	23,800	—	23,800
	Ottawa	Proof	15,490	—	15,490
1981/82 (Hanukka lamp from Poland)	Paris	B.U.	25,000	—	25,000
	Stuttgart	Proof	15,000	—	15,000
Pidyon Haben (Redemption of the Firstborn)					
1974/75	Jerusalem	B.U.	63,000	775	62,225
	Jerusalem	Proof	49,450	218	49,232
1975/76	Jerusalem	B.U.	50,000	12,620	37,380
	Jerusalem	Proof	29,600	130	29,470
1976/77	Jerusalem	B.U.	32,100	—	32,100
	Jerusalem	Proof	19,296	720	18,576
Special coins					
1974/75 (Ben-Gurion)	Jerusalem	B.U.	100,250	921	99,329
	Bern	Proof	64,600	407	64,193
1980/81 (Jabotinsky)	Ottawa	B.U.	20,000	5,500	14,500
	Ottawa	Proof	12,300	50	12,250
Half-sheqel coins (Purim)					
1960/61	Utrecht	B.U.	20,004	27	19,977
	Utrecht	Proof	5,000	59	4,941
1961/62	Utrecht	B.U.	20,000	72	19,928
	Utrecht	Proof	10,000	66	9,934
Gold coins					
1974/75 (Israel Bonds)	Utrecht	Proof	31,775	44	31,731
1974/75 (Ben-Gurion)	Bern	Proof	47,847	281	47,566
1977/78 (Israel's 30th Anniversary)	Bern	Proof	12,100	20	12,080
1979/80 (Israel-Egypt Peace Treaty)	Ottawa	Proof	10,000	3,593	6,407
1980/81 (People of the Book)	Ottawa	Proof	7,500	1,827	5,673
1980/81 (Jabotinsky)	Ottawa	Proof	7,500	—	7,500

^a Data on the Independence Day coins are for 1966/67 to 1980/81.

SOURCE: Annual Survey of the Bank of Israel Currency Department, May 1982 (Hebrew).

(b) Commemorative and Special Coins

The theme of the 1981 commemorative Independence Day coin is the State's achievements in the field of the Hebrew book and the Hebrew letter. The silver series was minted in B.U. (smooth edge) and proof (milled edge) form, with a silver and copper content (850/150), while the gold series was issued only in proof form, and is made of gold and copper (900/100).

In 1981 the Bank issued another in the series of Hanukka coins. It features a Hanukka lamp from Poland and was minted in B.U. and proof form.

The first special mint set (piefort) to be denominated in IS and new agorot was issued during 1981. Comprising five coins (ranging from one agora to one sheqel), the series is identical to the trade coins in circulation, but twice their thickness and made of cupronickel. The series of 35,000 pieces per denomination bears a special mintmark in the form of a tiny Star of David and the Hebrew date 5741.

(c) Withdrawal of Coins in the Israeli Pound Series

Table IX-14 lists the number of coins in the Israeli pound series which have been withdrawn from circulation and melted down since the introduction of the sheqel.

(d) Committee for the Planning of Currency and Commemorative Coins

This committee assists the Bank in planning banknotes and trade and commemorative coins to be issued, and recommends to the Governor of the Bank the designs which it has chosen from among those submitted by competing artists. Professor Y. Yadin was appointed chairman of the committee in May 1982, replacing Supreme Court Justice Dr. A. Witkon (the members of the committee are listed at the end of this chapter).

Table IX-14

COINS WITHDRAWN FROM CIRCULATION AND MELTED, FEB. 22, 1980 TO DEC. 31, 1981

Denomination	Number in circulation on Feb. 22, 1980	Number in circulation on Dec. 31, 1981	Number withdrawn during the period
1 agora	312,642,438	309,526,220	3,116,218
5 agorot	209,070,574	185,603,544	23,467,030
10 agorot	389,336,445	310,799,232	78,537,213
25 agorot	47,734,537	36,637,824	11,096,713
IL ½	75,462,990	47,026,523	28,436,467
IL 1	151,203,315	76,695,674	74,507,641
IL 5	30,597,362	10,440,350	20,157,012

NOTE : Does not include special series (with small Star of David mintmark).

Table IX-15

NUMBER OF BANKNOTES AND TRADE COINS IN SHEQEL SERIES IN CIRCULATION, 1981

(In millions)

Banknotes		Trade coins	
Denomination	Number	Denomination	Number
IS 1	23.9	1 new agora	82.9
IS 5	7.3	5 new agorot	42.8
IS 10	20.7	10 new agorot	229.8
IS 50	25.5	IS ½	55.5
IS 100	36.0	IS 1	51.3
Total	113.4	IS 5	2.9
		Total	465.2

(e) Banknotes and Coins in Circulation

At the end of 1981 there were 113.4 million banknotes and 465.2 million trade coins in the sheqel series in circulation, as detailed in Table IX-15.

The most striking feature was the weight of IS 100 banknotes in total currency in circulation. Issued in December 1980, it accounted for 67.5 percent of the value of all notes and coins in circulation by the end of 1981. (It took the IL500 banknote almost two years to reach a similar figure.)

(f) Deposits and Withdrawals

In 1981, 223 million banknotes were deposited in Bank of Israel branches and 234 million notes were withdrawn.

(g) Unfit Banknotes and Total Supply

In the year reviewed 55.3 million unfit banknotes denominated in IS were replaced. The number of banknotes in the sheqel series in circulation grew by 20 million; the total supply—defined as the number of unfit notes replaced plus the increase in the number of notes in circulation—therefore came to 75.3 million.

7. SUPERVISION OF BANKING CORPORATIONS

(a) General

In 1981 special emphasis was placed on implementation of the banking legislation which went into force during the year. The Banking Law (Licensing) made it necessary for the Department of the Examiner of Banks to redefine the various categories of banking corporations and the requisite reporting and supervision applicable to them. The Bank (Checks without Cover) Law made it necessary to prepare lists of offenders and to explain to

Table IX-16

**BANKING CORPORATIONS UNDER BANK OF ISRAEL
SUPERVISION,^a DEC. 31, 1981**

Ordinary banking institutions	
Banks ^b	28
Investment banks	1
Special banking institutions	
Mortgage banks	15
Investment finance banks ^c	9
Financial institutions	8
Joint services company	1
Total	62

^a Classified in accordance with the Banking Law (Licensing). Because of definitional changes no comparison can be made with previous years.

^b Excludes four inactive banks and the Israel Bank of Agriculture, which has a bank license but operates mainly as an investment bank; includes the Maritime Bank, which has a restricted license, the Bank of Palestine in Gaza, and one foreign-owned bank in Israel.

^c Includes the Israel Bank of Agriculture.

the public the law and its implications. The Banking Law (Customers' Services) gave a statutory basis to the procedures for protecting the banking corporations' customers. In 1981 the corporations, for the first time, had to publish their financial statements adjusted for inflation, in conformity with detailed directives issued by the Examiner of Banks Department.

The Bank of Israel and the commercial banks, with the Examiner of Banks' encouragement, entered into an international agreement which will link them up with the international clearing system SWIFT. This will expedite international interbank transfers and clearings between Israeli and foreign banks. At the Examiner of Banks' initiative, a joint steering committee representing the commercial banks and the Bank of Israel took steps to establish an automated central clearinghouse which will serve the banks and their customers. The automation of banking operations was stepped up during the year reviewed.

At the end of 1981 the number of banking corporations operating in Israel (including the Gaza Strip) under the supervision of the Department of the Examiner of Banks stood at 62. The regular banking corporations operated 1,062 branches in Israel (including main offices) and 33 branches in Judea, Samaria, the Gaza Strip, and Golan Heights. In addition, one branch of a local bank operated in the Gaza Strip, under the supervision of the Examiner of Banks as representative of the military government.

Total assets of the branches of regular banking corporations in Israel reached IS675 billion at the end of 1981.

The number of foreign branches of Israeli banks rose to 115 by the end of the year surveyed. These included 13 subsidiaries (53 offices), 32 branches and agencies, and 30 representative offices. Total assets of these subsidiaries and branches came to \$15,260 million at the end of 1981.

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

1. *Legislation*

a. The Banking Law (Licensing), 5741-1981 took effect in April 1981 and is presently being implemented.

b. The Banking Law (Customers' Services), 5741-1981 went into force in July 1981.

c. The Bank (Checks without Cover) Law, 5741-1981 went into force in December 1981, at which point special regulations were issued for implementing the law.

d. An amendment to the Banking Ordinance laid down the procedures for early repayment of mortgage loans from banking corporations.

e. An amendment to the Banking Order (Guarantees and Other Customers' Liabilities), 5735-1975 broadened its scope to include guarantees provided by foreign branches of Israeli banks.

2. *Licensing*

In conformity with the transitional provisions of the Banking Law (Licensing), new licenses were granted to all banking corporations. They were also granted permits to hold a controlling interest in all nonbanking companies which were under their control when the law went into force. Information on such companies is being gathered with the aim of classifying them and establishing criteria for the reporting required from the various types of companies.

3. *Branching*

During 1981 the Department of the Examiner of Banks dealt with the licensing of branches in conformity with the Banking Law (Licensing), especially in the case of mortgage banks, which previously had not been obliged to obtain a license before opening a branch. The various types of mortgage bank branches were defined, procedures were prepared for dealing with applications for the opening and transfer of branches, and criteria were established for licensing new bank counters in hotels and for opening branches in Arab villages.

4. *Customer Protection*

The Banking Law (Customers' Services), which took effect in July 1981,

gave the Department of the Examiner of Banks explicit legal authority to investigate complaints from the public concerning the banking corporations.

5. *Audits of Ordinary Banking Corporations*

During the year 200 general audits were conducted in the country's banks, and 130 audit reports were sent to the banks examined. The main subjects dealt with this year were the banks' capital, fixed investments, and the real profitability of both the individual bank and the banking groups in the light of the taxation of inflationary profits and the erosion of bank capital. The expansion of foreign branch operations prompted a study on the feasibility of establishing new branches and of investing in new and existing ones.

6. *Audits of Specialized Banking Corporations*

In the current audits of such banking corporations special attention was devoted to verifying their statements of sources and uses of funds. Procedural directives were issued on the following subjects: refund of mortgage registration fees to customers, early redemption of housing loans, and insuring of borrowers' assets. Criteria were laid down with respect to the structure of the mortgage banks' branch network. In 1981 the Bank of Israel teams dealing with investment finance banks, cooperative credit societies, and financial institutions concentrated on the preparation of manuals for auditing specialized credit and a uniform format for financial institution reports, as well as on the revision of reporting procedures for investment finance banks.

7. *Research and Publications*

During the year reviewed the Department published the 1980 Annual Survey of Israel's Banking System in Hebrew and a digest in English, a survey of the system's development in the first half of 1981, and *Banking Topics* No. 3 (three articles).

It also investigated other subjects, among them:

- a. Productivity of the banking industry in Israel.
- b. Establishment and opening of bank branches abroad.
- c. Production costs function of Israel's banking institutions—economies of scale.
- d. Estimating the expenses of the commercial bank in Israel as a multifunctional firm.
- e. A comparison of mutual funds by yield, risk, and management efficiency.

The first four studies in this list will be published shortly in *Banking Topics*.

8. *Banks in Judea, Samaria, and the Gaza Strip*

On April 1, 1981 the Bank of Palestine was opened in Gaza for a period of three months, for debt collecting purposes only. At the beginning of August it

was granted a license to conduct regular banking operations in Israeli currency. To ensure orderly banking operations in the region, the military government, at the initiative of the Department of the Examiner of Banks, issued a number of administrative orders based on corresponding Israeli banking legislation. The bank is subject to the Bank of Israel's liquidity requirements.

9. Advisory Committee on Matters Relating to Banking Business

The committee discussed various subjects relating to the banking system, including the Annual Survey of Israel's Banking System by the Examiner of Banks, the amending of the Banking Order concerning customers' guarantees and other liabilities, the adjustment of financial statements for inflation, and the early repayment of mortgage bank loans.

10. Financial Reports to the Public

In September 1981 all banking corporations were provided with guidelines on how to show the effect of inflation in their financial statements. Specimens of the profit and loss statement, balance sheet, and statement of changes in equity capital were included to illustrate the adjustment for changes in the consumer price index.

11. Payments System

The steering committee for the automation of the payments system, which includes representatives of the five biggest banks and the Bank of Israel, decided to establish an automated clearinghouse, and initial planning was begun. The committee also decided that the Bank of Israel and the large commercial banks should join SWIFT, an international interbank communications network. SWIFT approved their membership, and it is due to go into effect by mid-1983.

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

The Bank of Israel represents the State in all matters connected with its membership in the International Monetary Fund, the World Bank Group, and the Inter-American Development Bank.

(a) International Monetary Fund (IMF)

In 1981 Israel did not submit any applications for IMF assistance.

In February an IMF mission visited the country for routine consultations on economic policy with Israeli authorities, in the course of which it met with Bank of Israel and Finance Ministry economists. On the basis of these discussions the mission drew up a report on the state of Israel's economy and the

Table IX-17
ISRAEL'S FINANCIAL RELATIONS WITH THE INTERNATIONAL MONETARY FUND, 1954-81
(Millions of SDRs) ^a

	1954	1957	1959	1964	1966	1969	1970	1971	1974	1975	1976	1978	1979	1980	1981
General Resources Account															
1. Israel's quota in IMF	4.5	7.5	25.5	50.0	90.0	90.0	130.0	130.0	130.0	130.0	130.0	205.0	205.0	307.5	307.5
2. Use of IMF resources	—	1.9	—	12.5	—	45.0	—	20.0	65.0	175.8	77.0	72.4	—	31.6	25.6
Credit tranches ^b	—	1.9	—	12.5	—	45.0	—	20.0	65.0	32.5	12.0	—	—	31.6	25.6
Special facilities	—	—	—	—	—	—	—	—	—	143.3	65.0	72.4	—	—	—
Special Drawing Rights Department															
1. Net cumulative allocation of SDRs	—	—	—	—	—	—	15.1	29.0	42.8	42.8	42.8	42.8	64.1	85.4	106.4
2. Net cumulative use of SDRs	—	—	—	—	—	—	15.1	15.9	40.3	40.8	34.2	21.8	59.3	76.7	106.0

^a Until 1969 all amounts are quoted in dollars.

^b Includes the reserve tranche (until 1978 the gold tranche).

economic policies pursued, and submitted it to the IMF Board of Directors. In May 1981 the latter discussed the mission's report and approved the conclusions.

In January 1981 Israel received a new allocation of SDR 21.3 million⁷ under the IMF policy of expanding the international liquidity of all member nations; this brought Israel's net cumulative allocation of SDRs to 106.4 million.

(b) World Bank Group

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

Israel is no longer eligible for direct aid from the World Bank. In the mid-1970s the Bank began to "phase out" developing member nations with a relatively high per capita national income from the list of countries eligible for its aid. Israel was struck off the list in 1975, but continues to receive disbursements of loans approved in earlier years. In 1981 this amounted to \$13 million, reducing the undisbursed balance to only \$3.4 million, out of a total loan allocation of \$284 million since 1960. The outstanding balance consists of 11 loans earmarked for various agricultural, industrial, and infrastructure projects, such as ports, phosphate production, highway construction, and sewerage, as well as industrial and agricultural investment credit (channeled through designated banks).

2. *International Development Association (IDA)*

This World Bank affiliate extends aid only to the poorest nations and on far softer terms (for periods of up to 30 years and with hardly any interest) than those of the World Bank.

The current Sixth Replenishment of IDA resources is intended to enlarge the scope of its activities. Israel decided to participate in this replenishment in an amount required to maintain its relative share in the Association.

3. *International Finance Corporation (IFC)*

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

The IFC is presently increasing its capital to a target level of approximately \$0.5 billion. Israel decided to increase its share in the Corporation by \$500,000; it purchased \$400,000 of capital stock in August 1981, and will complete its participation in 1982.

⁷ The average value of a Special Drawing Right in 1981 was \$1.00, compared with \$1.30 in 1980.

4. *Inter-American Development Bank (BID)*⁸

This institution, second only to the World Bank in the scope of financing socio-economic development, limits its operations to Latin America and the Caribbean. Its current lending exceeds \$2.5 billion per annum; this is given in grants and in loans for the development of infrastructure, agriculture, industry, communications, transport, and energy. Israel became a nonregional member of the BID in 1976, in order to strengthen its economic ties with the region and to enable Israeli companies to expand their activities there through BID-financed projects.

The Bank of Israel provides current information on BID projects to hundreds of Israeli companies interested in participating in bidding for procurement. It also serves as a liaison between firms interested in expanding their activities in Latin America through the BID and development institutions (such as National Financera of Mexico) which the BID supports.

In recent years Israeli firms have procured contracts with BID projects primarily in irrigation, extension services, education, communications, electronics, agricultural services, and equipment.

9. ECONOMIC RESEARCH

As usual the Bank of Israel's Annual Report includes much of the current research on the Israeli economy conducted by the Bank's Research Department. Among the other current research carried out by the Department's economists in 1981 were the following:

(a) *Recent Economic Developments*, Nos. 32 and 33.

(b) The Governor's report on the increase in the money supply for the period between November 30, 1980 and January 31, 1981.

(c) The Governor's report on the increase in the money supply for the period between January 31, 1981 and March 31, 1981.

(d) The Governor's report on the increase in the money supply for the period between April 30, 1981 and July 31, 1981.

(e) The Governor's report on the increase in the money supply in August 1981.

(f) Periodic internal surveys of monetary developments and macroeconomic policy.

(g) *Economic Indicators*—a weekly publication.

In addition to current research, the Department carried out a number of basic studies of specific subjects, of which the following were published:

(a) "A Wage Restraint Policy in the Public Service during a Period of Inflation, 1974-1978" (prepared in cooperation with the committee for ex-

⁸ Banco Interamericano de Desarrollo.

amining the wage structure in the public service—in Hebrew).

(b) "The Distribution of Israel's Imports by Final Uses, 1971-80" (in Hebrew).

(c) *Economic Review*, No. 54, which includes the following studies:

(1) "Grant Equivalent of Subsidized Investment in Israel".

(2) "Financial Saving of the Private Sector in Israel, 1972-77".

(d) Articles in periodicals published by other Israeli and foreign institutions:

(1) "The Welfare of the Israeli and World Price Increases" (Hebrew).

(2) "What Went Wrong?—The Record of Macroeconomic Policy" (Hebrew).

(3) "Monetary Developments and Bank of Israel Policy—The Lessons of the 1970s".

(4) "The Effects of Changes in the Business Cycle on Small Firms".

(5) "The Financial Structure of the Small Firm—An International Comparison of Corporate Accounts in the U.S.A., France, U.K., Israel, and Japan".

(6) "A Macroeconomic Approach for Estimating the Foreign Debt Burden" (forthcoming).

(7) "Disinflation with and without Incomes Policy".

(e) The following studies will be published in *Economic Review*, No. 55 (English titles are provisional):

(1) "Inflation and Monetary Aggregates in Israel".

(2) "Congestion Charges and Vehicle Taxes in Israel".

(3) "Demand for Commodity Imports in Israel, 1968-76".

(f) The Research Department has recently initiated a Discussion Paper Series (mostly in Hebrew), which presents to Israeli economists the drafts of studies before their final publication. The series has two main purposes: to make this research on the Israeli economy available to economists sooner than would be possible where final publication is involved; and to stimulate, prior to final publication of the articles, fruitful discussion by non-Bank economists, thereby helping to improve the articles concerned.

The first articles in the series appeared in April, and further articles will appear shortly. Following is a list of papers that have already been completed and those that are due to appear in the near future (all papers are in Hebrew unless otherwise indicated):

(1) "Inflationary Expectations in Israel, 1965-80".

(2) "Evaluating Israel's Balance of Payments Problem—Alternative Points of View".

(3) "The Government's Revenue from Money Creation and the Inflationary Effects of a Decline in the Rate of Growth of GNP" (English).

- (4) "An Annual Model of Israel's Consumption Sector".
- (5) "The Slowing of Industrial Productivity Growth".
- (6) "Effect of Raw Material Price Rises on Industrial Productivity and Profitability, 1965-68".
- (7) "Estimating Inflationary Expectations Using a Simultaneous Model".
- (8) "Excess Labor Demand, Inflationary Expectations, and the Nonsubstitution Hypothesis".
- (9) "Neutrality of the Government Deficit and Its Test in Israel".
- (10) "Composition of Foreign Exchange Reserves in Developing and Industrialized Nations and the Substitution Account".
- (11) "The Balance of Payments Problem: An Evaluation from Several Standpoints".

10. ADVISORY COMMITTEE AND ADVISORY COUNCIL

The Bank of Israel's Advisory Committee and Advisory Council devoted their deliberations this year mainly to the measures taken by the Bank to restrict the volume of bank credit and the extent of such restraint following the curbing of nondirected (free market) credit at the end of 1979. The Committee several times weighed the value of a tight credit policy as a monetary policy instrument against its negative implications: inhibition of the growth of industry and other sectors of the economy, and the devising of ways to indirectly supply credit. The Committee approved the continuation of credit restraint, and at its recommendation this policy was applied in 1981 to both nondirected bank credit and directed export credit.

As usual, most of the sessions of the Committee and the Council were devoted to assessing economic and monetary developments during the year. Several ways were examined of expanding the commercial banking system's volume of Israeli currency business in unlinked deposits and credit supply. To this end it was decided in January to lower the required liquidity ratios on deposits. The Committee also discussed, mainly toward the end of the year, ways of encouraging the holding of unlinked Israeli currency deposits.

Following the Advisory Committee's deliberations on the capital market, it was decided in the middle of the year to increase the Bank of Israel's flexibility in selling linked bonds to the public.

The Advisory Council approved the planned issue of coins and banknotes during the year, as described in section 6 of this chapter.

11. THE GOVERNOR AND DEPUTY GOVERNORS OF THE BANK OF ISRAEL

Mr. Arnon Gafny, who served as Governor of the Bank for five years, completed his term of office on October 31, 1981. Dr. Eliezer Sheffer and

Professor Zvi Sussman, who served as Deputy Governors of the Bank, completed their term of office on July 31, 1981.

On August 30, 1981 the government approved the appointment of Dr. Moshe Mandelbaum to the post of Deputy Governor of the Bank, commencing September 15. On January 15, 1982 he was appointed fourth Governor of the Bank of Israel by the President of the State, Mr. Yitzhak Navon, at an official ceremony in the President's residence.

Professor Yakir Plessner began to serve as Deputy Governor of the Bank on April 25, 1982.

BALANCE SHEET AS AT DECEMBER 31, 1981
AND
STATEMENT OF INCOME AND EXPENSES FOR THE YEAR ENDED
DECEMBER 31, 1981

BANK OF
BALANCE SHEET AS

(Millions of

Assets	Notes	Dec. 31, 1981	Dec. 31, 1980
Foreign assets			
Gold, foreign exchange, and foreign securities	b	55,272	25,618
Other foreign assets		104	676
		55,376	26,294
Government debt			
Long-term debt	c	5,566	4,300
Provisional advances		18,980	1,159
		24,546	5,459
Loans and discounts			
In foreign currency	d	17,264	16,213
In local currency		5,066	3,070
		22,330	19,283
Securities	e		
Tradable		5,802	2,000
Nontradable		3,756	1,924
		9,558	3,924
Other accounts	f	3,154	1,362
Total		114,964	56,322

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

ISRAEL

AT DECEMBER 31, 1981

sheqalim)

Liabilities	Notes	Dec. 31, 1981	Dec. 31, 1980
Banknotes and coins in circulation		5,360	2,537
Allocations of Special Drawing Rights	g	1,928	823
Foreign liabilities			
Liabilities to the IMF	b	1,149	698
Other liabilities	h	268	130
		1,417	828
Foreign currency deposits of the govt. and National Institutions		4,281	2,334
Foreign currency deposits of banking institutions in Israel			
Against residents' deposits—restitution		37,482	19,635
Against residents' deposits—other		37,772	18,062
Against nonresidents' deposits		10,788	4,591
		86,042	42,288
Deposits of banking and financial institutions in Israel		4,424	2,007
Other deposits	i	684	405
Other accounts	j	9,828	4,100
Capital and general reserve	k	1,000	1,000
Total		114,964	56,322

**STATEMENT OF INCOME AND EXPENSES FOR THE YEAR ENDED
DECEMBER 31, 1981**

(Millions of sheqalim)

	Notes	1981	1980
Income	m		
From investments abroad	n	32,929	15,187
From the government		8,753	4,442
From loans and discounts		16,599	10,128
From "liquidity loans" to banking institutions		68	110
From banking institutions in respect of liquidity deficiencies		174	66
From securities	o	3,646	2,066
Interest on foreign currency loans to the public from local banks and from abroad	p	618	381
Other income		138	95
Total income		62,925	32,475
Expenses	m		
On foreign currency deposits of banking institutions in Israel		49,234	23,867
On local currency deposits of banking and financial institutions in Israel		1,390	509
On foreign currency deposits of the government and National Institutions		2,694	1,374
On other deposits and liabilities		2,353	1,192
Administrative and general expenses	q	361	157
Printing banknotes and minting coins		170	59
Total expenses		56,202	27,158
Surplus of income over expenses		6,723	5,317
Less: Income from the government subject to matched timing	a.1	2,522	1,726
Net income		4,201	3,591
Appropriation statement			
Transfer to general reserve			500
Transfer to the government		4,201	3,091
Total		4,201	3,591

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

NOTES TO THE FINANCIAL STATEMENTS, DECEMBER 31, 1981

(a) Accounting Policies

1. *Income and Expenses*

Income and expenses are recorded on the accrual basis. Income from the government is recorded on the accrual basis, but is included in the net income of the Bank on a matched timing basis; i.e. the Bank includes in its net income for the financial year sums due from the government only when they are budgeted and paid by the latter in the fiscal year ending the following March 31. Income receivable from the government after March 31 of the following year is deducted in the Statement of Income and Expenses as "Income from the government subject to matched timing", and is included in the balance sheet in "Other accounts (liabilities)" (see also note a.8).

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

2. *Foreign Currency Accounts*

Assets and liabilities in foreign currency are translated into sheqalim at the representative rates published by the Bank of Israel. The rate for the U.S. dollar on December 31, 1981 was IS15.6041 and on December 31, 1980—IS7.5480. Special Drawing Rights (SDR) are translated into sheqalim on the basis of the SDR-U.S. dollar rate, i.e. IS18.1273 per SDR on December 31, 1981 and IS9.6343 on December 31, 1980.

3. *Gold*

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

4. *Foreign Securities*

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

5. *Securities Denominated in Local Currency*

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

6. *Premises and Equipment*

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

7. *Participation in International Financial Institutions*

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

8. *Employee Pensions and Severance Pay*

Provision for employee pensions and severance pay, actuarially computed and adjusted at

the balance sheet date, is included in "Other accounts (liabilities)". Part of the domestic securities has been earmarked against the employee pensions and severance pay liability. Income from these securities is not subject to matched timing, and is set off in the Statement of Income and Expenses against the increase in the above liability.

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

"Gold, foreign exchange, and foreign securities" include IS 10 million of holdings of Special Drawing Rights (SDR) in the IMF (on December 31, 1980: IS85 million). On December 31, 1980 this item included the Reserve Position in the IMF, amounting to IS247 million, which was withdrawn in 1981. Accounts with the Fund also include the liability on account of the Compensatory Financing Facility (appearing in "Liabilities to the IMF").

Accounts with the Fund are as follows:

	IS million		SDR million	
	Dec. 31 1981	Dec. 31 1980	Dec. 31 1981	Dec. 1980
General Account:				
Quota	5,574	2,963	308	308
Less: Liability	5,574	2,716	308	282
Reserve	0	247	0	26
Liability o/a Compensatory Financing Facility	1,148	698	63	72

The government's liability to the Fund, amounting to SDR 24 million in respect of the Oil Facility (on December 31, 1980: SDR 84 million in respect of the Oil Facility and Compensatory Financing Facility), is not included in the accounts of the Bank.

(c) Government Debt—Long-Term

This item consists mainly of (1) IS5 billion linked to the basket of foreign currencies, bearing unlinked interest of 5 percent per annum and repayable over the years 1983–2005, with interest and linkage differentials payable on December 31 of each year (balance of the debt on December 31, 1980: IS4 billion); and (2) U.S. \$33 million (on December 31, 1980: same amount).

(d) Loans and Discounts in Foreign Currency

This item is presented net of IS5,048 million—the participation of banking institutions in the fund for financing export shipments; this participation commenced this year.

(e) Securities

"Tradable securities" consist of government bonds, most of them linked to the consumer price index; their market value is IS6,181 million (on December 31, 1980: IS2,275 million).

"Nontradable securities" consist mainly of compulsory government bonds purchased from firms in accordance with the Government Loans (Sundry Provisions) Law, 5738–1977. In 1980 this item also included bonds acquired from banking institutions, under repurchase agreements, from their frozen savings scheme portfolios.

(f) Other Accounts (Assets)

This item consists mainly of (1) accrued interest and other income; (2) premises and equip-

ment net of accumulated depreciation; (3) participation in the following international financial institutions: International Bank for Reconstruction and Development (IBRD), International Development Association (IDA), International Finance Corporation (IFC), and Inter-American Development Bank (IDB).

(g) Allocations of Special Drawing Rights

In 1981 Israel received some SDR 21 million from the IMF; this was the third and last installment of the approximately SDR 64 million allocation of 1979. On December 31, 1981 the balance amounted to SDR 106 million (on December 31, 1980: SDR 85 million).

(h) Other Foreign Liabilities

This item includes liabilities to international financial institutions amounting to IS206 million (on December 31, 1980: IS90 million), and deposits of foreign banks amounting to IS62 million (on December 31, 1980: IS40 million).

(i) Other Deposits

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

(j) Other Accounts (Liabilities)

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

(k) Capital and General Reserve

The Bank's capital at the balance sheet date was IS200 million, and the general reserve IS800 million (on December 31, 1980: same amounts).

(l) Contingent Liabilities

The contingent liabilities are as follows: (1) uncalled amounts on account of shares and participations subscribed to international financial institutions—IS2,073 million (on December 31, 1980: IS1,114 million); (2) documentary credits—IS1,105 million (on December 31, 1980: IS295 million); (3) other liabilities—IS95 million (on December 31, 1980: IS59 million).

(m) Exchange Rate Differentials

Income and expenses include differentials resulting from changes in the exchange rates of foreign currencies against the sheqel. Net income includes differentials amounting to IS184 million (in 1980: IS2,434 million).

(n) Income from Investments Abroad

In terms of U.S. dollars this amounted to \$137 million (in 1980: \$230 million).

(o) Income from Securities

This item does not include income from securities held against the employee pensions and severance pay liability, and which partly covered the increase in the liability (see note a.8). This item includes IS2,522 million income subject to matched timing (in 1980: IS1,726 million); this is deducted from the excess of income over expenses (see note a.1). The accumulated income subject to matched timing is IS4,751 million (on December 31, 1980: IS2,229 million).

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

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

(q) Administrative and General Expenses

In 1981 this item increased by about 130 percent in nominal terms, but after adjusting for the average rise in the consumer price index, the increase was about 6 percent.

(r) Adjustment for Changes in the Purchasing Power of the Sheqel

The Statement of Changes in Assets and Liabilities and the notes to the financial statements include information which permits a comparison of data adjusted for changes in the purchasing power of the Israeli currency either by deflating by the rise in the consumer price index or by presenting the data in U.S. dollar terms).

BANK OF ISRAEL

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MAY 31, 1981

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Deputy Governor

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