CHAPTER XVII

SOCIAL INSURANCE FUNDS AND INSURANCE COMPANIES

I. SOCIAL INSURANCE FUNDS

1. Main Developments

Social insurance fund receipts rose 31 percent in 1971, as contrasted with 16 percent the year before, and totalled IL 1,185 million. The faster growth in the year reviewed was due mainly to the larger contributions to both provident schemes (especially those administered by commercial banks) and pension schemes.

Household saving through the funds – i.e. the nominal growth of the household sector's assets in the funds during the year – soared from IL 669 million in 1970 to IL 1,016 million. But the amount of liquidity absorbed by the funds from households and employers also rose steeply, from IL 478 million in 1970 to IL 722 million. This represented 4 percent of gross disposable private income from domestic sources (less compulsory loans), compared with only 3.2 percent in 1970.

The striking growth in provident scheme contributions stemmed from several factors: (a) the raising of the ceiling on tax deductions and credits recognized by the income tax authorities with regard to payments to the social insurance funds; (b) the growing tendency to purchase financial assets through the provident funds because of the greater return that can be earned by savers, whose marginal income tax rates have been rising along with nominal wages; (c) the more rapid increase in 1971 in wages and in the number of wage and salary earners in the economy.

The last development, together with the inclusion in 1971 of the 4 percent wage and salary hike awarded at the beginning of the previous year for the purpose of calculating the contribution rate, goes a long way to explain the accelerated growth of pension scheme contributions in 1971.

Another factor in the more vigorous growth of the funds' receipts was the larger income – interest, dividends, and especially realized capital gains – earned on their financial asset holdings. There was a particularly notable rise in realized capital gains – 31 percent as against 16 percent in 1970 – due to the sharpening of the inflation in 1971 and the expansion of the asset portfolio.

Payments to members were, at IL 373 million, up 28 percent from 1970, when the increment came to 23 percent. The higher 1971 growth rate was the resultant of an

Table XVII–1

FLOW-OF-FUNDS STATEMENT OF SOCIAL INSURANCE FUNDS,[a] 1969–71

(IL million)

Receipts	1969[b]	1970[b]	1971	Percent annual increase 1970	Percent annual increase 1971
Contributions to funds	536	620	820	16.7	32.3
Pension	259	294	354	13.5	20.4
Provident	150	158	260	5.3	64.6
Severance pay	75	95	106	26.7	12.0
Social benefits	52	73	100	40.4	37.0
Current income (interest, dividends, linkage increments, etc.)	180	227	280	26.1	23.3
Realized capital gains (incl. realized linkage increments)	39	51	82	30.8	60.8
Other income	22	4	3	–	–
Total receipts	777	902	1,185	16.1	31.4

Payments	1969[b]	1970[b]	1971	Percent annual increase 1970	Percent annual increase 1971
		Nonfinancial transactions			
Social insurance benefits	238	292	373	22.7	27.7
Pension	118	141	181	19.5	28.4
Provident	41	47	61	14.6	29.8
Severance pay	33	47	61	42.4	29.8
Social benefits	46	57	70	23.9	22.8
Mutual insurance benefit payments	11	18	18	63.6	0.0
Current expenditure	31	33	42	6.5	27.3
Expenditure on capital account	8	10	6	25.0	–40.0
Total payments on real account	288	353	439	22.6	24.4
		Financial transactions			
Net purchases of bonds and other securities (mostly financial institution issues)		455	693		
Loans to members		34	62		
Employer debt		0	5		
Deposits in banks		35	17		
Other transactions		–18	1		
Total		506	778		
Errors and omissions		43	–32		
Total payments		902	1,185		

[a] In order to reconcile the data in this table with those in the economy's flow-of-funds set of accounts (see Chapter XVI), both receipts and payments on financial account have to be increased by IL 145 million for 1971 and IL 78 million for 1970, as in the flow-of-funds structure of the economy Gmul Ltd., Bitzur Ltd., and Teudah Ltd. are by definition included in the social insurance funds and insurance companies sector but are excluded here.

[b] Data have been revised after reclassification of items.

SOURCE: Central Bureau of Statistics.

accelerated increase in pension and provident payments and a more sluggish increase in severance and social benefit payments as compared with the previous year. Pension payments grew faster than in 1970 because of the more rapid rise in earnings per employee, the continued upswing in the number of pensioners, and the deduction of a smaller sum in 1971 from payments made to those who also receive a pension from the National Insurance Institute. Provident scheme payments, most of which are meanwhile being made by company rather than bank-administered funds, again increased at a stronger rate after a temporary slackening in 1970. Total payments to members amounted to 83 percent of total profits plus realized linkage differentials, indicating that the social insurance funds are still at the stage where they accumulate the whole of employee and employer contributions. But this has no significance whatsoever as far as the actuarial position of the funds is concerned, nor does it indicate the extent to which the funds have consolidated their position; it merely points to the stage which the subsector has reached in its development.

The combined balance sheet of the social insurance funds shows a 22 percent increase, compared with 17 percent in 1970. Bank-administered and other provident funds were mainly responsible for the accelerated growth; pension scheme assets expanded at about the same rate as in 1970. Total assets of the subsector at the end of 1971 amounted to about IL 5,600 million (after revaluation).

Purchases of newly issued bonds totalled IL 870 million, as against IL 610 million in 1970. There were a number of reasons for this rise: (a) a heavier redemption of securities from the funds' portfolio; (b) the accelerated accumulation in 1971; (c) continued portfolio adjustment in compliance with the regulation raising the proportion of recognized investments from 80 to 85 percent; and (d) some advancing of purchases in the final part of the year in anticipation of a further rise in prices. In 1971 interest on long-term bonds held by the funds was upped from 5.5 percent plus linkage (to the consumer price index) to 6 and 6.5 percent plus linkage.

2. Structure of the Social Insurance Funds and Their Investments

In Israel there are approximately 230 social insurance funds administering pension, provident, severance pay, or some other type of scheme, with a few administering more than one type.[1] Numerically, the 14 pension funds constitute the smallest group, but from the financial standpoint they are the most important, accounting at the end of 1971 for 68 percent of the subsector's total assets (after revaluation). The next most important group is the provident funds, some of which serve the employees of individual firms (these will hereinafter be referred to as company funds), while the remainder are central funds, operated mostly by commercial banks and open to the general public. Membership in the latter is available both to individuals and to employees of firms on a collective basis. The third group comprises severance pay funds, which are also administered either

1. Apart from the fact that most of the pension funds also provide social and mutual insurance (see section 3[b] below).

Table XVII–2

HOUSEHOLD SAVING THROUGH SOCIAL INSURANCE FUNDS, 1970–71

(IL million)

	1970[a]	1971
1. Total accumulation[b]	533	821
2. Increase in unrealized revaluation increments	233	379
3. Total accumulation after revaluation (1 + 2)	766	1,200
4. Less: Accumulation in severance pay funds[c]	63	122
5. Total accumulation of households (3 – 4)	703	1,078
6. Less: Increase in loans to households	34	62
7. Household saving through social insurance funds	669	1,016

[a] Revised data.
[b] See Table XVII-4.
[c] This is employers' and not household saving. Includes the share of the central and other severance pay funds in unrealized revaluation increments.
SOURCE: Central Bureau of Statistics.

by individual firms or by commercial banks. Besides these, there are a number of schemes covering holiday leave and advanced study, but they account for only a small fraction of the subsector's assets.

Membership in pension and provident funds generally follows automatically upon employment in any firm or other enterprise, being provided for as an integral part of the relevant collective labor agreement, which stipulates the fund and the type of insurance to be provided for all employees. In contrast, the central provident funds administered by commercial banks also enroll members on an individual basis. Contributions to the severance pay funds – as distinct from the severance pay schemes incorporated into some of the pension and provident funds – are made only by the employer, this being the means whereby he builds up a reserve for providing severance and retirement payments to his employees.

Social insurance funds are by and large primary financial intermediaries, mobilizing funds which are not poured directly into the economy but are used, in accordance with Treasury regulations, mainly for purchasing the securities of secondary financial intermediaries (see Bank of Israel, *Annual Report, 1970,* p. 368). The regulations prescribe that the social insurance funds may not place more than 5 percent of their recognized investments in equities; but in practice neither the subsector as a whole nor the bank-administered funds (which have the benefit of a thorough knowledge of the securities' market) reach this ceiling, and in most cases fall far short of it. This is explained by the fact that the funds can now obtain a yield of 6-6.5 percent (plus linkage) on long-term bonds, which exceeds the average overall return earned hitherto on a long-term investment in shares quoted on the Tel Aviv Stock Exchange (short-term speculative investments have at times been highly lucrative, but the social insurance funds are obviously precluded from anything smacking of speculation).

The investment policy of the social insurance funds, as regards the type of approved bonds they acquire, is decisively influenced by the Government. In fact, it makes no difference to the funds which approved bonds they purchase under their obligation to invest in original-issue long-term or optional bonds,[2] since interest rates, the soundness of the issuing institution, and other conditions are about the same for all issues. Under a 1960 agreement between the Treasury and Hevrat Ovdim,[3] the latter is able to allocate to its own projects half of the recognized investments of the Histadrut-affiliated social insurance funds, which purchase their approved bonds through Gmul Ltd.[4] This allocation is effected through the issues of Histadrut-controlled financial institutions, which put most of the proceeds at the disposal of Hevrat Ovdim. Since 1966 the Treasury guarantees the linkage differentials on part of the credit received by Hevrat Ovdim under this arrangement. In return Hevrat Ovdim pays a premium of 4-4.5 percent and has undertaken to reduce its share in the funds' recognized investments, with a corresponding increase in the proportion allocated by the Government.

It must be emphasized that the funds' freedom of action in managing their asset portfolios is limited and therefore no great differences in yield are to be expected. There is, however, a difference in managerial performance, with some of the funds earning a somewhat higher yield than others (this does not necessarily ensure a higher return to the saver, since the higher yield sometimes stems from the fact that the fund does not provide cheap loans to its members but instead places its moneys in more profitable investments).

3. Receipts and Payments

(a) *Receipts*

Social insurance fund receipts on real account derive from two main sources: employer and employee contributions and profits from investments – dividends, interest, linkage differentials on interest, and realized capital gains (see Table XVII-1).

Employer and employee contributions are made to four different types of schemes. Foremost among them are the pension schemes, whose receipts in 1971 added up to IL 354 million. Next come the provident schemes (IL 260 million), and trailing far behind are the severance pay (IL 106 million) and social benefit schemes (IL 100 million). The provident schemes posted the biggest growth in contributions – IL 100 million; this compares with only IL 60 million for the pension funds and IL 10 million for each of the other two types of schemes.

Contributions to pension schemes went up 20.4 percent in 1971, as against 13.5 percent the year before, and reached IL 354 million. The higher growth rate was due mainly to the faster increase in earnings per employee (15.3 as against 9 percent in 1970)

2. For a description of such bonds see Chapter XVIII, note 1. p. 395.
3. The holding company of the Histadrut (General Federation of Labor in Israel).
4. Gmul Ltd. serves as the investment agent for some of the social insurance funds. In 1971 about 63 percent of the total recognized investments were placed through this concern, compared with 76 percent in 1970.

and the inclusion in 1971 of the 4 percent increment awarded all employees in the previous year in the total wage or salary on which the contribution rate is calculated.[5] Another factor influencing receipts was the sharper rise in 1971 in the number of employees – 5 percent compared with 2.9 percent in 1970 (there are no direct data on the change in the number of insured in the pension schemes). In the year under review the transition from a system of provident to pension benefits was arrested, not a single instance of a group changeover being recorded.

Provident scheme contributions soared 65 percent in 1971, compared with only 5.3 percent in the previous year. This marked acceleration resulted from a number of developments.

First was the raising of the maximum tax deduction and credit allowed by the income tax authorities on contributions. For the self-employed the deduction was increased from IL 900 to IL 1,500 and the credit from IL 1,500 to IL 1,900, while the credit ceiling for wage and salary earners was upped from IL 1,500 to IL 1,700. These concessions mainly affected the volume of contributions to provident schemes which insure the self-employed and to which employees, too, can voluntarily increase their contributions (pension fund contributions are calculated as a fixed percentage of the employee's wage or salary). It should be borne in mind that as wages and incomes rose, so did marginal income tax rates. Therefore, it increasingly paid to take advantage of the tax deductions and credits allowed on saving through the social insurance funds (even though this saving is illiquid – it is virtually impossible to withdraw it until 10 years after the initial payment, which means an average saving period of approximately five years for the total sum put into a fund). The increased yield of this asset – as opposed to that of other financial assets where no income tax concessions are granted with respect to contributions and profits – has apparently enhanced the attraction of the social insurance funds, especially for the self-employed and wage and salary earners covered by noncontributory pension schemes. However, no conclusions should be drawn from this concerning the marginal propensity to save in the economy; it merely indicates the position of the provident funds in the whole gamut of savings instruments. In this context mention should be made of the tendency to award wage and salary increments in the form of higher provident fund contributions.

A second reason for the accelerated expansion of provident scheme contributions is, as in the case of the pension schemes, the faster 1971 rise in the number of employees and in earnings per employee. This applies especially to those provident schemes where the employer's contribution is matched by the employee, and it is connected with the total wage bill of the enterprise (the reference is to provident schemes administered by pension funds and company provident funds). The cessation of the changeover from a system of provident to pension benefits was another reason for the faster increase in contributions to the former.

Contributions to severance pay schemes were, at IL 106 million, up 12 percent. This

5. It should be stressed that the growth of "earnings per employee" is not identical with the growth of the employee's earnings on which the contribution rate is calculated, as the latter aggregate does not include all the wage or salary components (e.g. premiums and overtime payments).

compares with an exceptionally high 27 percent in 1970, but as the latter gain followed a decline in 1969, the deceleration in the year reviewed can be regarded as of a compensatory nature. Severance pay schemes fall into two categories: those in which the employer is insured, he and not the employee making contributions and withdrawals according to his needs; and those set up within a pension fund in which the employee is insured (here the contributions and their rates reveal a much greater regularity). The former type of scheme accounts for about 70 percent of all contributions to severance pay schemes.

Contributions to social benefit schemes increased by 37 percent, a shade less than the 40.4 percent recorded in 1970, and reached some IL 100 million. The social benefits are actually paid by employers through central pension funds for such purposes as convalescence, holidays, etc. This arrangement is found in sectors with a high degree of labor mobility (notably construction and agriculture), and its object is to safeguard the social benefit rights of workers changing their place of employment. The funds in effect act merely as agents for the transfer of contributions; but since part of the sums collected is not paid out to employees for various reasons – chiefly because of difficulties in tracking them down or because they have waived their rights – and is not returned to employers, the funds' assets are augmented accordingly.

The other component of the subsector's receipts – current income and capital gains – was up 29.4 percent, compared with 17 percent in 1970. The faster growth rate stemmed entirely from the realization of capital gains, as the continued rapid advance of prices resulted in larger linkage differentials.

The growth of current income (mainly interest from securities, deposits, and loans) was a little less than in 1970 – 23.3 as against 26.1 percent; the effect of the hiking of interest rates on bonds purchased by the funds was not yet felt in 1971. The deceleration in the year reviewed is largely attributable to the increase in "interest and linkage differentials due", which means there was some lag in the realization of such income.

(b) *Payments*

Payments to members of the social insurance funds fall into three categories: monthly pensions, payments to members withdrawing from the funds (in the main after leaving their jobs), and social benefits (a detailed description of the three categories appears in the *Annual Report* for 1970, p. 370).

Total payments to members rose from IL 292 million in 1970 to IL 373 million – i.e. by 27.7 percent, compared with 22.7 percent in 1970. The pension and provident schemes accounted for the steeper 1971 increase, the figures for the other funds either remaining static or falling off.

Pension payments were up 28.4 percent, as contrasted with 19.5 percent in 1970. There were three principal reasons for the faster rise in the year reviewed: first was the more rapid growth of earnings per employee (pension payments are linked to changes in the wage level); secondly, there was a further increase in the number of pensioners;[6] and

6. Although there are no precise data on the number of pensioners, it is reasonable to assume that the figure is moving up at an accelerated pace.

thirdly, the sum deducted from payments to those also receiving a pension from the National Insurance Institute was halved.[7]

Provident scheme payments rose 30 percent (exactly double the 1970 rise) to reach IL 61 million. It should be noted that the majority of bank-affiliated provident funds are still accumulating all their receipts, since very few members have participated long enough to be entitled to withdraw their money. Hence these funds are presently contributing to the sector's receipts but not to its payments, most of which are made by the company funds. The higher percentage rise in payments in 1971 followed a sharp deceleration the year before.

Severance payments were, at IL 61 million, also up 30 percent in 1971; but in this case the increase was 12.4 percent lower than in 1970. The growth in social benefit payments, which totalled approximately IL 70 million, was virtually the same as in 1970, the percentages being 22.8 and 23.9 respectively. As mentioned above, changes here are mainly connected with changes in wages and fringe benefits and not with the activities of the social insurance funds. In the sectors mainly concerned – construction and agriculture – the rise in employment was smaller than in the preceding year, while wages (and particularly fringe benefits) moved up faster, the net result being a slightly faster growth of social benefit payments.

(c) *Household saving through the funds*

Household saving through the social insurance funds may be defined as the total accumulation of the funds, plus the increase in unrealized revaluation increments, less the accumulation in the central severance pay funds[8] (which represents employers' saving) and the growth of outstanding loans to households. Calculated on this basis, household saving in 1971 amounted to IL 1,016 million, as against IL 669 million a year earlier. The increase is attributable to the more rapid accumulation of the provident funds, especially those administered by banks, as well as to the mounting inflation (which affected the growth of unrealized revaluation increments), though the influence of the latter was offset by heavier household borrowing.

The above definition of household saving through the funds reflects the nominal increase in household assets in the funds during the year reviewed. To estimate the amount of liquidity absorbed by the funds from households and employers, it is necessary to deduct from the total accumulation the year's growth in outstanding loans to households and in interest and linkage differentials due. In 1971 absorption amounted to IL 722 million, compared with IL 478 million the year before. The ratio between this magnitude and gross nominal disposable income from domestic sources (less compulsory loans) edged up from 3.2 percent in 1970 to 4 percent, signifying an increase in the contribution of this sector to the absorption of purchasing power in the year reviewed. Household saving through the funds is contractual saving and is determined mainly by labor agreements; hence it is not affected in the short run by changes in the propensity to save. It is

7. This deduction was abolished altogether on April 1, 1972.

8. Central and company severance pay funds.

only in the few social insurance funds where membership is voluntary (mainly the provident funds administered by commercial banks) that saving takes on a somewhat different character, but even here members display a strong tendency to keep up their contributions.[9]

As in 1970, the sum total of pension, provident, and severence payments amounted to 83 percent of the funds' receipts from profits and realized linkage increments. This indicates that the subsector is still at the stage of accumulating the whole of employee and employer contributions, with payments to members being made entirely from current income. This has no actuarial significance whatsoever, nor is it evidence of the soundness of the funds; it does, however, give an idea of the volume of saving and accumulation through the social insurance funds, as well as of their present stage of development and the prospects for their future growth.

4. Balance Sheet Developments

Total assets of the social insurance funds rose in 1971 by 21.8 percent at current prices, compared with 16.5 percent in 1970, and reached approximately IL 4,600 million. The addition of IL 1,000 million of unrealized revaluation increments on the subsector's assets (see Tables XVII-3 and 4) brings the figure up to IL 5,600 million, which represents the nominal saving through the funds.

(a) *Assets by type of fund*

An analysis of the asset growth by type of fund reveals that the highest rate was achieved by bank-administered funds, especially the provident schemes. Here the gain came to a respectable 44.7 percent, as against last year's 30.6 percent, bringing the level up to IL 964 million. This sum represents 21 percent of the subsector's total assets, but the weight of the bank-administered funds in the total increment for the year was much greater – 36 percent. There are three main reasons for this notable expansion:

(1) The bank-administered funds answer the growing demand for financial assets in the form of provident scheme rights both by wage and salary earners covered by noncontributory pension plans (see below) and by the self-employed. This is because they insure both categories regardless of place of work, whereas the others are company funds.

(2) The accumulation in pension funds is not subject to drastic fluctuations stemming from changes in the capital market or in the propensity to save through this instrument, since it is a function of fixed contribution rates, the number of members, and the actuarial structure of the funds. Thus the accumulation here is much more stable and predictable than that of the bank-administered provident funds.

9. A central question with regard to the importance of saving through the social insurance funds is whether this constitutes a net addition to saving or whether it merely represents a shift in savings instruments. There is no precise answer as far as Israel is concerned; a Canadian study of the subject came to the conclusion that, in general, social insurance funds are an additional and not an alternative instrument of savings.

Table XVII–3

GROWTH OF SOCIAL INSURANCE FUND ASSETS,[a] BY TYPE OF FUND, 1969-71

(IL million)

	1969[b]	1970	1971	Percent annual increase 1970	Percent annual increase 1971
Pension funds	2,227	2,596	3,031	16.6	16.8
Funds administered by banks and insurance companies[c]	510	666	964	30.6	44.7
Central severance pay funds	225	287	369	27.6	28.6
Provident funds	285	379	595	33.0	57.0
Other funds[d]	495	503	591	1.6	17.5
Total	3,232	3,765	4,586	16.5	21.8

[a] Excluding unrealized revaluation increments.
[b] Revised data.
[c] The big majority are run by commercial banks.
[d] Mainly company provident funds and schemes for self-employed operated other than by banks and insurance companies.
SOURCE: Central Bureau of Statistics.

(3) Company provident and severance pay funds continued to merge with bank-administered funds so as to benefit from administrative economies of scale. In the year reviewed 19 funds, with assets totalling IL 9.5 million, took this step. Though the sum involved is small, the cumulative effect of this tendency is not insignificant.

(b) *The combined balance sheet*

1. *Assets*

The relative shares of the various social insurance fund assets are determined by Treasury regulations, and funds wishing to enjoy income tax concessions and exemptions must adhere to them. In 1970 the proportion of its assets that a fund was required to hold in recognized investments was raised from 80 to 85 percent (except for the social benefit schemes), and by the end of 1971 fully 84 percent of the funds' total assets that had to be invested[10] were already placed in this way. The process of portfolio adjustment has therefore been virtually completed (since social benefit funds are required to invest only 50 percent of their assets); however, there are probably some funds that exceed and others that have not yet reached this ceiling, especially considering the heavy advance purchases made in 1971 (see section 5).

10. Total accumulation, less loans granted from the auxiliary fund, mutual insurance benefit payments, and employer debt.

Table XVII–4

COMBINED BALANCE SHEET OF SOCIAL INSURANCE FUNDS, 1969-71

(IL million)

	1969[a]	1970[a]	1971	Increase or decrease (–)		Percentage distribution		
				1970	1971	1969	1970	1971
Assets[b]								
Securities	2,548	3,003	3,696	455	693	78.8	79.8	80.6
Loans to members	294	328	390	34	62	9.1	8.7	8.5
Employer debt	73	73	78	0	5	2.3	1.9	1.7
Deposits	75	113	119	38	6	2.3	3.0	2.6
Loans to others	39	18	17	–21	–1	1.2	0.5	0.4
Real estate	81	87	93	6	6	2.5	2.3	2.0
Accrued interest and linkage increments receivable	74	95	132	21	37	2.3	2.5	2.9
Demand deposits and cash	18	15	26	–3	11	0.6	0.4	0.6
Other assets	30	33	35	3	2	0.9	0.9	0.7
Total	3,232	3,765	4,586	533	821	100.0	100.0	100.0
Liabilities[b]								
Pension reserve	1,613	2,074	2,410	461	336	49.8	55.0	52.6
Provident reserve	852	895	1,199	43	304	26.4	23.8	26.1
Severance pay reserve	439	454	552	15	98	13.6	12.1	12.0
Social benefit and mutual insurance reserves	124	127	153	3	26	3.8	3.4	3.3
Paid-up share capital and general reserve	18	21	25	3	4	0.6	0.6	0.6
Auxiliary reserve and undistributed profits	99	118	140	19	22	3.1	3.1	3.1
Deposits earmarked for loans and sundry creditors	87	76	107	–11	31	2.7	2.0	2.3
Total	3,232	3,765	4,586	533	821	100.0	100.0	100.0

[a] Data have been revised after reclassification of items.
[b] Excluding revaluation increments of IL 370 million in 1969, IL 603 million in 1970, and IL 982 million in 1971.
SOURCE: Central Bureau of Statistics.

Security holdings accounted for 80.6 percent of the funds' aggregate assets at the end of 1971, compared with 79.8 percent the year before. This high proportion is explained by the aforementioned requirement regarding recognized investments, which consist overwhelmingly of securities and only to a small degree of deposits and real estate.[11] Loans to members[12] were up 18.9 percent in 1971, as against 11.6 percent in 1970, but their weight fell to 8.5 percent of total assets. The higher growth rate in 1971 is apparently attributable to two factors: an increase in the average size of the loans, and the fact that because of the strong inflation members found it paid to borrow at a comparatively low, fixed rate of interest. The further drop in the weight of this item was due to the raising of the recognized investment requirement.

Employer debt was down a fraction – from 1.9 percent of total assets in 1970 to 1.7 percent. Other items, including approved deposits, interest and linkage differentials due, real estate, etc., accounted for about 9.2 percent of the total.

2. *Liabilities*

The liabilities of social insurance funds consist predominantly of three reserves: pension, provident, and severance pay.[13]

The stronger growth of provident fund contributions relative to those to the pension and severance pay funds brought up the weight of the provident reserve in total liabilities from 23.8 percent in 1970 to 26.1 percent. The weight of the pension reserve fell from 55 percent to 52.6 percent, while the severance pay reserve held steady at 12 percent.

5. Financial Transactions

Because of the Treasury regulations which require them to place most of their assets in recognized investments and the consequent large size of their securities portfolio, which results in a great deal of reinvestment of securities reaching maturity, the social insurance funds have become the principal customer for new domestic issues. In 1971 they purchased original issues to the tune of IL 870 million (IL 610 million in 1970); these consisted mainly of long-term bonds, with only IL 14 million being in option-type paper. In August 1971 the rate of interest on the long-term bonds was raised from 5.5 percent, with linkage to the cost-of-living index, to 6 percent with linkage for the provident and severance pay funds and 6.5 percent with linkage for the pension funds (the life of the higher interest bonds was increased on the average by about 1.5 years).

The fact that purchases of option-type bonds were below the maximum allowed (i.e. 10 percent of the total required investment in bonds) was probably due to the diminishing attraction of this paper in view of the improved interest terms offered on long-term bonds. However, it is hardly likely that these higher rates of interest affected contri-

11. In the past the regulations allowed a certain percentage of the funds' real estate to be treated as part of their recognized investment, but this clause has since been repealed.
12. Some of the bank-administered provident funds extend such loans in the form of ordinary bank credit rather than from their own resources; these are excluded from the data cited here.
13. For a description of the various reserves see Bank of Israel, *Annual Report 1970*, p. 373.

butions to the funds in 1971, though they may affect future enrollment in the voluntary bank-administered provident schemes. The expectation of such a change in interest rates depressed sales of long-term bonds during the first seven months of the year, with a compensatory jump in the last five months. The upswing was also due in part to the advancing of purchases, prompted by the strong expectations of a price rise which prevailed after the August devaluation and especially in the first part of 1972 (for a monthly breakdown of long-term bond purchases see Table XVIII-2).

It is difficult to estimate precisely the volume of advance buying by the social insurance funds and the central institutions which act as their agents. The bond portfolio of one of the latter grew by about IL 40 million during the last five months of 1971, and advance buying appears to have been mainly responsible; but it is impossible to determine the extent of this phenomenon for the subsector as a whole. It was probably facilitated in some measure by the liquidity surpluses possessed by the banking institutions (the reference is to the central institutions acting as agents), whereas the funds probably financed their advance purchases by reducing their loan and deposit portfolio.

The funds continued to place most of their bond investments in financial institution issues (96 percent of total purchases) and only a small fraction in issues of other firms or the Government (for details of the allocation of the subsector's funds see section 2). Despite the strong recovery of the Tel Aviv Stock Exchange, the social insurance funds continued to avoid stocks, and their equity portfolio remained insignificant, much below the permitted ceiling.[14]

If we deduct from total purchases of original-issue securities the amount reaching maturity and therefore requiring reinvestment, we find that net bond purchases reached IL 693 million in 1971, compared with IL 455 million in the previous year (see Table XVII-1). Since most of the bonds were from financial institution issues, this precludes the tracing of the final uses to which the proceeds were allocated (this is presented in the flow-of-funds analysis of the economy in Chapter XV). In addition to their securities transactions, the funds lent their members IL 62 million more (net) in the year reviewed than in 1970, recorded a IL 5 million increase in employer debt for arrears in contributions, and deposited IL 17 million with banks in the form of recognized investments and liquid assets.

II. INSURANCE COMPANIES[15]

The year reviewed saw a rapid expansion of insurance business, in contrast to the slight slackening of growth in 1970. The gain, which was impressive even in comparison with previous years, was concentrated mainly in the life insurance branch.

14. A large percentage of the social insurance funds' equity portfolio consists of shares of Gmul Ltd., but these differ essentially from an ordinary investment in shares traded on the Stock Exchange or in the over-the-counter market, being more akin to an investment in approved bonds.
15. Israeli insurance companies, branches of foreign insurance firms, and Lloyd's agents operating in Israel.

Following the vigorous growth of economic activity and the rapid advance of prices, the value of life insurance in force and premium receipts[16] increased markedly, the former by 45 percent (21 percent in 1970) and the latter by 28 percent (21 percent in 1970). The life insurance reserve also expanded appreciably, from IL 75.3 million in 1970 to IL 118 million. Life insurance premium rates were trimmed in the year reviewed, self-retention[17] of the Israeli companies continued to increase, and the weight of foreign insurers dropped further. General insurance business developed similarly, with premiums rising by about 24 percent (19 percent in 1970), self-retention continuing upward, and the share of foreign companies declining.

The combined balance sheet of Israeli insurance companies rose by IL 159 million, compared with IL 148 million in 1970. The life insurance reserve, which represents the accumulated savings of households through the insurance companies, accounted for two-thirds of the incremental liabilities, while Government and Government-guaranteed bonds accounted for 72 percent of the asset growth. On the liabilities side, the upward trend in reinsurers' deposits was sharply reversed, a development partly related to the increase in self-retention. Among the assets, outstanding loans and deposits were up 19 percent, as against 12 percent in 1970, apparently signifying a heavier demand for insurance company credit.

1. Life Insurance

(a) *General developments*

The life insurance portfolio[18] of Israeli companies expanded enormously in 1971 – by over IL 2,500 million, as against IL 1,000 million in each of the two preceding years – and reached IL 8,350 million. This can be credited chiefly to the intensification of economic activity, which resulted *inter alia* in an accelerated growth of private income and saving and a rapid rise of prices. Another factor was the reduction of life insurance rates and the introduction by a number of local firms of new schemes, some of which actually constituted a means of lowering rates.

Unlinked insurance, which has a very low saving element, rose 30 percent (20 percent in 1970), while insurance linked to the consumer price index – where the saving element is higher – soared 64 percent, twice as fast as in 1970. Even after deducting the linkage increments due to the rise in the index, the expansion of the portfolio came to a respectable 44 percent. This contributed to the accelerated growth of saving in 1971 and supports the hypothesis that at a time of strong inflation the public prefers linked to unlinked life insurance.

As regards dollar-linked life insurance, the portfolio rose to IL 92 million in 1971, but if the increments arising from the 1971 devaluation of the Israeli pound are deducted, there was a further drop in the year reviewed. No such policies have been issued since 1962, and meanwhile many have either matured or have lapsed or been surrendered.

16. Less reinsurance in Israel. The data for 1970 are estimates based on reports received from only part of the insurance companies subsector and hence they are liable to change.
17. That portion of total insurance transactions not reinsured abroad.
18. Including severance pay insurance and excluding pension insurance.

Table XVII–5

LIFE INSURANCE IN FORCE,[a] 1962-71

(IL million)

	Total amount at end of year	Linked insurance: Linked to consumer price index	Linked insurance: Linked to the dollar	Unlinked insurance	Share of linked insurance (%)
1962	632.3	201.0	119.3	312.0	50.7
1963	1,048.5	375.7	109.8	563.0	46.3
1964	1,489.6	586.3	101.8	801.5	46.2
1965	1,888.9	863.4	96.1	929.4	50.8
1966	2,524.4	1,093.9	90.8	1,339.7	46.9
1967	3,026.9	1,225.5	99.0	1,672.4	44.7
1968	3,749.6	1,553.5	93.0	2,103.1	43.9
1969	4,758.0	1,979.6	90.7	2,569.8	44.6
1970[b]	5,772.0	2,591.2	83.3	3,097.5	46.3
1971[c]	8,350.0	4,241.3	92.4	4,016.3	51.9

[a] Excluding pension and retirement plans.
[b] Revised data.
[c] Estimate.
SOURCE: Commissioner of Insurance, Ministry of Finance.

(b) *Investment of linked and unlinked funds*

Under existing regulations insurance companies must hold assets with matching terms against their liabilities on account of linked life insurance, with the exception of (1) 5 percent, which they may hold in cash; (2) their outstanding premiums; and (3) other current assets, in accordance with their balance sheet position.

As to the composition of assets subject to linkage, insurance companies may grant policyholders loans up to the cash surrender value of the policies without any limitation; of the balance, they may invest up to 20 percent in securities approved by the Commissioner of Insurance and up to 20 percent in linked loans against bank guarantees. The remainder must be invested in Government or Government-guaranteed bonds.[19] Because of the relative profitability of this type of investment, the companies actually purchase more bonds than legally required. The agreements they have signed with the Israel Electric Corporation and the Government assure the purchase by insurance companies of index-linked long-term bonds with maturities of up to 40 years.

The regulations governing the investment of unlinked insurance premium receipts differ from those for linked insurance: they allow the companies to invest 10 percent of their

19. As in 1970, the insurance companies received 6 percent interest on their investments in Israel Electric Corporation bonds and 5.8 percent on deposits with the Accountant General.

assets in shares (such investment is prohibited in the case of linked insurance); 35 percent (instead of the 20 percent for linked insurance) in securities approved by the Commissioner of Insurance; and 50 percent (instead of 20 percent) in loans and bank deposits. They are also permitted to invest up to 20 percent in immovable assets and in subsidiaries, and they may hold 7.5 percent (instead of 5 percent) in cash.

In 1971 the insurance companies acquired, under the linked insurance regulations, IL 29 million worth of newly issued Government bonds, compared with IL 24 million in 1970, and IL 42 million of Electric Corporation bonds, as against the previous year's IL 31 million.

(c) *Income and outgo of the life insurance branch*

Income of the companies operating in Israel from life insurance business increased in 1971 by 32 percent, as against 22 percent in 1970, and totalled IL 195 million.

Premium receipts, the leading income item, rose 28 percent, as against 21 percent in 1971, to reach IL 159 million. The higher 1971 growth rate may be largely ascribed to the notable increase in private incomes and to the strong rise in the consumer price index (to which the premiums are pegged) since the middle of 1970.[20] Devaluation augmented

Table XVII–6

INCOME, OUTGO, AND ACCUMULATION OF LIFE INSURANCE COMPANIES IN ISRAEL,[a] 1967-71

(IL million)

	1967	1968	1969	1970[b]	1971[c]
Income					
Premiums	68.7	78.3	102.2	124.3	159.0
Interest	12.8	15.3	18.6	23.3	36.3
Total	**81.5**	**93.6**	**120.8**	**147.6**	**195.3**
Outgo					
Benefits to policyholders	24.0	25.3	33.6	41.2	51.0
Operating expenses	17.8	20.7	26.3	33.9	45.3
Gross profit[d]	3.1	5.9	5.8	6.5	7.9
Total	**44.9**	**51.9**	**65.7**	**81.6**	**104.2**
Balance of income over outgo	36.6	41.7	55.1	66.0	91.1
Income from investment of life insurance funds	7.8	2.6	6.6	9.3	27.0
Annual accumulation (growth of the life insurance reserve)	44.4	44.3	61.7	75.3	118.1

[a] Israeli and foreign insurance companies operating in Israel; before deducting reinsurance abroad.
[b] Revised data.
[c] Estimate.
[d] Including profits of reinsurers abroad.
SOURCE: Central Bureau of Statistics.

20. The rate of premium linkage is adjusted twice a year for changes in the consumer price index – in February and in July. Therefore, the increase in the rate of linkage in 1971 was calculated on the basis of the rate prevailing in August 1970.

dollar-linked premium receipts, but this was of little import because of their small weight in total premium income. In addition to premiums, the life insurance business account was credited with IL 36 million in interest income and IL 27 million in capital gains on investments.

Claims paid to policyholders went up by IL 10 million to IL 51 million; this amounted to 22 percent of total receipts, and compares with 28 percent in 1970. The decline in the ratio[21] stemmed primarily from the much heavier volume of premium receipts in 1971. Current expenses in the life insurance branch rose proportionately to the growth of receipts and amounted to IL 45 million.

The net increase in the life insurance reserve, including the appreciation of investments, came to IL 118 million (57 percent), as contrasted with IL 75 million in 1970 and IL 62 million in 1969.

2. General Insurance

General insurance business continued to expand: premium receipts were, at IL 486 million, up 24 percent, as against 19 percent in 1970.

The stronger growth of this class of insurance was due to a number of factors, the most significant being the surging economy, the rapid mounting of prices since the middle of 1970,[22] and the upward revision of premium rates.

Table XVII–7

PREMIUM RECEIPTS FROM GENERAL INSURANCE,[a] 1965-71

(IL million)

	Total	Annual increase	
		IL m.	%
1965	172.4	33.6	24.2
1966	202.7	30.3	17.5
1967	204.8	2.1	1.0
1968	258.3	53.5	26.1
1969	329.1	70.8	27.4
1970[b]	390.3	61.2	18.6
1971[c]	485.7	95.4	24.4

[a] Israeli and foreign companies and Lloyds' agents; including registration fees and marine insurance; excluding reinsurance in Israel and receipts from abroad.
[b] Revised data.
[c] Estimate.
SOURCE: Central Bureau of Statistics.

21. In contrast to other countries, the ratio of claim payments to total receipts is low in Israel, owing to the comparatively young age structure of the population and the notable expansion of life insurance business.
22. In general insurance a change in the price level does not have an immediate effect, since there is usually a lag between the appreciation of a given asset and the adjustment of the policy to the new value.

Premium rates rose appreciably in two branches of general insurance. The devaluation of the Israeli pound automatically increased cargo insurance rates, while those for motor vehicles were raised by more than 20 percent. Premium receipts from motor vehicle insurance, which accounted for 32 percent of total general insurance premiums in 1971, rose from IL 106 million in 1970 to IL 133 million, or by 26 percent. Part of this gain is explained by the larger number of private cars on the roads in the year reviewed.

The advancing trend in the share of Israeli companies in general insurance business carried over through 1971, although their share in the motor vehicle branch remained unchanged. The proportion of transactions reinsured abroad declined from 48 percent of total premiums in 1970 to 42 percent. In vehicle insurance there was even an absolute drop, from IL 36 million in 1970 to IL 34 million. These figures point to a strengthening of the position of domestic firms in general insurance business.

3. Balance Sheet Growth of Israeli Companies

The combined balance sheet of Israeli insurance companies expanded in 1971 by IL 159 million, as against IL 148 million in 1970 and IL 145 million in 1969, and totalled IL 1,018 million. The growth of the life and general insurance reserves accounted for 80 percent of the incremental liabilities (including stockholders' equity), compared with 56 percent in 1970, while the expansion of the securities portfolio accounted for 63 percent of the incremental assets (53 percent in 1970).

The life insurance reserve, which is determined according to actuarial calculations and represents the accumulated savings of households through insurance companies, grew by IL 105 million,[23] as against IL 66 million in 1970, and its weight in total liabilities moved up from 41 percent in the three preceding years to 45 percent in 1971.

The general insurance reserve, allocations to which are based on the estimated outstanding risk assumed by insurance companies in connection with such business, increased by IL 23 million, compared with IL 16 million in 1970, and totalled IL 90 million. The upward trend in the weight of this reserve in total liabilities carried over through 1971, when it reached 8.8 percent – a development connected with the increase in self-retention.

Among the other liabilities, the outstanding change was a sharp decline in deposits of reinsurers, in contrast to their growth in previous years; this, too, can be ascribed to the greater self-retention in 1971.

The weight of stockholders' equity (paid-up share capital and the general and other reserves) in total liabilities continued downward, standing at 12.2 percent as against 13.1 percent in 1970 and 14.8 percent in 1969.

On the assets side, the weight of the securities portfolio moved up from 46 to 49 percent of total assets. Purchases of Government and Government-guaranteed bonds rose from IL 71 million in 1970 to IL 115 million, but holdings of other securities contracted.

23. This reserve is theoretically equal to the present value of all claims that will have to be paid to policyholders in the future, less the present value of premium receipts and other anticipated income.

Outstanding loans and deposits expanded by IL 31 million to account for 19 percent of the total asset growth, as against 12 percent in 1970; this probably reflected a heavier demand for insurance company credit in the year reviewed.

Outstanding premiums went up by IL 16 million to IL 127.4 million. Most of this represented sums collected by agents and not yet transmitted, but some was still owing by households.

Table XVII–8

ASSETS AND LIABILITIES OF ISRAELI INSURANCE COMPANIES, 1968-71

	IL million				Percent			
	1968	1969	1970[a]	1971[b]	1968	1969	1970[a]	1971[b]
Assets								
Government or Government-guaranteed bonds	241.0	291.5	362.5	477.5	42.6	40.9	42.2	46.9
Other securities	19.9	27.6	35.9	21.3	3.5	3.9	4.2	2.1
Loans on policies	15.7	17.7	22.0	23.1	2.8	2.5	2.5	2.3
Other loans	31.9	43.5	62.9	84.3	5.6	6.1	7.3	8.3
Long-term deposits	24.8	34.5	29.2	37.2	4.4	4.9	3.4	3.7
Real estate and investment in subsidiaries	41.2	53.7	59.8	67.7	7.3	7.6	7.0	6.6
Outstanding premiums	84.0	97.2	111.7	127.4	14.9	13.7	13.0	12.5
Sundry debtors	55.7	84.1	102.9	102.8	9.9	11.8	12.0	10.1
Cash and demand deposits	51.1	61.0	72.1	76.7	9.0	8.6	8.4	7.5
Total assets	565.3	710.8	859.0	1,018.0	100.0	100.0	100.0	100.0
Liabilities								
Paid-up share capital	50.2	58.0	64.1	67.4	8.9	8.2	7.5	6.6
General and other reserves	37.8	47.2	51.6	56.6	6.7	6.6	5.6	5.6
Life insurance reserve (less reinsurance)	234.7	288.7	355.1	459.8	41.5	40.6	41.3	45.2
General insurance reserve (less reinsurance)	36.5	51.0	67.4	90.1	6.5	7.2	7.9	8.8
Extraordinary risks reserve	20.9	29.3	37.8	46.6	3.7	4.1	4.4	4.6
Deposits of reinsurers	52.4	72.6	90.3	58.8	9.3	10.2	10.5	5.8
Pending and approved claims (general and life insurance), less reinsurance	59.1	73.1	98.1	131.8	10.5	10.3	11.4	12.9
Current liabilities	73.7	90.9	94.6	106.9	12.9	12.8	11.4	10.5
Total liabilities	565.3	710.8	859.0	1,018.0	100.0	100.0	100.0	100.0

[a] Revised data.
[b] Estimate.
SOURCE: Central Bureau of Statistics.