

CHAPTER XV

THE SECURITIES MARKET

1. MAIN DEVELOPMENTS

THE ECONOMIC CHANGES that took place in 1973 left their impress on the securities market. The sharpening of inflation during the first nine months of the year and its further exacerbation in the aftermath of the Yom Kippur War, together with the postwar developments in the domestic and foreign markets, strongly affected the magnitude and pattern of demand for securities. Purchases of bonds pegged to the consumer price index soared at the expense of nonlinked financial assets, short-term liquid assets, and to some extent also shares (although the share market slump this year did not stem solely from the changed pattern of demand for financial assets).

The stronger demand for linked bonds was met by a greatly increased volume of net new issues, which were sold directly to households, businesses, and nonbank financial institutions. Net issues added up to IL 1,058 million, compared with IL 126 million in 1972. Sales were briskest in the last two months of the year, reflecting the exceptionally buoyant demand after the war and the plummeting of Short-Term Loan holdings, but they displayed a rising tendency in the rest of the year as well. Moreover, the public's bond holdings swelled by IL 530 million during the year and IL 240 million worth of negotiable compulsory loan certificates were distributed. The bond portfolio of the general public thus soared by IL 1,828 million in 1973, as contrasted with only IL 659 million the year before; in addition, there was a sharp upswing in approved saving scheme balances, which indirectly boosted demand for option-type bonds (not included in these data). One of the factors fueling the demand for index-linked bonds during the first nine months of the year was the absence of expectations of an imminent devaluation of the IL as against the dollar, as reflected in the turnover in securities traded in foreign currency and in the small agio on the Natad and free-market dollar.

Sales of long-term bonds—to social insurance funds and insurance companies—did not expand to the same extent as those for medium terms. This is attributable to the fact that demand for the former derives from the accumulation of contractual savings through the insurance sector, which is determined by long-term considerations and hence is not very sensitive to short-term changes in economic conditions. In 1973 net issues of this type of paper amounted to IL 1,132 million, compared with IL 898 million the year before.

The increase in net bond issues of all types other than compulsory loans outran GNP prices; it therefore represented a real growth in the amount of capital raised through securities of this sort, as well as in its share in national income. In real terms, the 1973 gain came to a staggering 90 percent, bringing up the weight of this source in national income from 5.2 to 9.5 percent, despite a drop in the national saving rate this year.

The more buoyant demand for bonds slightly depressed their yield to maturity in the secondary market while expanding the volume of trade therein. However, the growth of such transactions slumped sharply compared with 1972—38 as against 129 percent. Apparently the year reviewed witnessed a much greater degree of homogeneity in the investing public's expectations and in the reshuffling of its securities portfolio.

In the share market, on the other hand, prices retreated 24 percent. At the same time new issues of stocks, capital notes, and convertible bonds reached an unprecedented IL 627 million, or about one-quarter of the beginning-of-the-year share portfolio. Demand for such securities apparently began to let up at the beginning of the year, and the negative impact of this development on share prices became more pronounced in the course of the year due to the flooding of the sagging market with a huge volume of new issues.

As a result of these developments, the net overall rate of return on share holdings tumbled to an average of -16.2 percent; adjusting for the rise in the consumer price index depresses the real rate to -34 percent.

The growing bearish tone of this market can be ascribed to several factors: the overvaluation of share prices in the previous year; the increasing monetary tightness, which dampened demand on the part of those financing their investments by borrowed funds as well as of financial institutions, and the exacerbation of inflation, which made bonds much more glamorous than equities since they generally respond more quickly to changes in the general price level than do the latter.

As already noted, in 1973 the volume of new equity issues reached IL 627 million (of which IL 327 million was in shares and IL 300 million in capital notes and bonds convertible into shares), as compared with IL 200 million in 1972 and no issues at all in the two preceding years. Nevertheless, those forces which resulted in most of the fresh equity capital being raised by financial institutions continued to operate in the year reviewed, although among the companies making placements on the Tel Aviv Stock Exchange were three new faces (in industry and in property development), which between them raised IL 32 million.

In contrast to the situation in the bond market, the gloom in the equity market deepened after the October war, although it is not clear exactly to what extent this was directly influenced by the fighting and its aftermath.

Demand for the Short-Term Loan cooled in 1973. This is understandable

given the above developments in the financial assets market and the fact that this paper is not linked and yields a relatively small return. To ensure the continued sale of the loan, which is essential for the conduct of monetary policy, the Bank of Israel reached an agreement with the commercial banks whereby they committed themselves to bring up the balance of the loan at a predetermined rate; the banks undertook to encourage the general public to purchase this instrument and to make up any shortfall from their own means. As a result, the amount of Short-Term Loan certificates in circulation rose IL 105 million from the end of January to the end of September 1973 to reach IL 819 million. Upon the outbreak of hostilities this agreement was in effect terminated, with the consequence that the balance plunged by IL 400 million in the last three months of the year and continued to fall precipitately in the early part of 1974, until this paper actually ceased to be a significant component in the economy's financial assets portfolio.

Activity in securities traded in foreign currency was rather dull in the pre-war period due to the absence of expectations of an imminent devaluation of the IL in relation to the dollar. Pazak and Tamam balances, on the other hand, swelled noticeably. While the external value of the IL is a leading determinant of demand in both markets, in the case of securities traded in foreign currency short-term expectations are more decisive, while as regards Pazak and Tamam, where there is no possibility of pulling out or reentering the market, long-term expectations are dominant—although when there are very strong short-term devaluation expectations, this too affects the demand for Pazak and Tamam. After the war devaluation expectations sharpened, as evidenced by the rise in the agio on the Natad and the free-market dollar, as well as by the livelier demand for bonds pegged to the exchange rate.

2. THE BOND MARKET

The year reviewed witnessed an ebullient demand for linked Israeli currency bonds, especially those for medium terms (purchased mainly by households, businesses, and financial institutions), while sales of long-term bonds, which are acquired by social insurance funds and insurance companies in accordance with Treasury regulations, expanded at a milder rate.¹ The heavier demand was met by an increased supply from three sources: net new issues, the appreciation of the existing stock of bonds, and the distribution of certificates of negotiable compulsory loans collected in the past. While demand took on hectic proportions in the postwar period, it rose in most months of the year.

New medium-term voluntary bond issues totalled IL 2,714 million in 1973,

¹ The data at our disposal relate to type of bond rather than type of investor. While as a rule there is a fairly high correlation between the two, we may still be erring slightly in attributing sales to one sector or another.

and less the value of series reaching maturity, the figure came to IL 1,908 million, compared with IL 963 million in 1972. From this should be deducted Absorption and Defense Loan redemptions. To be sure, these were originally compulsory loans, but since they became negotiable a fairly long time before reaching maturity and were held voluntarily by the public, the redemption of some of the series should be viewed as ordinary bond redemption. Net voluntary purchases of medium-term linked bonds therefore totalled IL 1,565 million, as contrasted with only IL 293 million in 1972—an increase of IL 1,273 million. It should be stressed that IL 733 million of the extra purchases were made in the last three months of the year, when Short-Term Loan holdings plunged by some IL 400 million, and only IL 540 million worth were made in the first nine months (see Table XV-2).

These figures include both direct purchases by the general public in the primary market and those made through approved saving schemes administered by the commercial banks.² After adjusting for the big increase in the latter, direct sales to the general public during the entire year added up to IL 1,058 million, as opposed to only IL 126 million in 1972.³

The overall growth of the medium-term bond portfolio of households, non-financial business concerns, and financial institutions (excluding purchases for approved saving schemes), which includes the increase in the public's holdings (IL 530 million) and the distribution of negotiable compulsory loan certificates (IL 240 million at market prices), came to IL 1,828 million this year, as against IL 659 million in 1972—a gain of IL 1,169 million. There was an especially steep rise in the proportion of new issues in the total increment—53 percent as against 19 percent in 1972. This is understandable given the heavy demand for bonds this year and the fact that this is the most flexible of the three components of supply.

Issues of long-term bonds to social insurance funds and insurance companies, which are determined by the growth of this sector's accumulation, reached IL 1,772 million in 1973; less principal, interest, and linkage differential payments, the figure was IL 1,132 million, compared with IL 898 million in 1972. Sales of such securities therefore lagged well behind the rise in those for medium terms. This is explained by the fact that demand for long-term bonds is determined primarily by the expansion of the social insurance funds, and it is not very sensitive to developments in the money and capital markets, at least in the short run.

The livelier demand for medium-term linked bonds must be viewed against

² This is not to imply that all purchases for the saving schemes were made in the primary market; our intention is merely to show the net effect on the bond market.

³ This sum also includes some bonds purchased indirectly through mutual funds and other financial institutions, but since the reference here is to liquid financial assets and since we were unable, nor was there any cogent reason, to decompose the system of financial intermediaries, we shall skirt this point.

Table XV-1
DOMESTIC SECURITY ISSUES, 1972-73^a
 (IL million)

	1972					1973					Increase or de- crease (-) in net proceeds (10-5)
	Gross issues	Redemp- tion of prin- cipal	Net issues (1-2)	Interest & link- age dif- ferentials	Total pro- ceeds (3-4)	Gross issues	Redemp- tion of prin- cipal	Net issues (6-7)	Interest & link- age dif- ferentials	Total pro- ceeds (8-9)	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Regular bonds											
Long term ^b	1,281.4	99.3	1,182.1	315.3	866.8	1,649.2	116.3	1,532.9	459.3	1,073.6	206.8
Government loans	3.5	9.3	-5.8	18.3	-24.1	74.6	8.5	66.1	20.8	45.3	69.4
Nongovernmental loans ^c	1,277.9	90.0	1,187.9	297.0	890.9	1,574.6	107.8	1,466.8	438.5	1,028.3	137.4
Long-term issues to insurance companies ^d	109.3	9.8	99.5	32.8	66.7	122.3	13.0	109.3	50.7	58.6	-8.1
Government loans	54.1	4.9	49.2	13.3	35.9	74.4	3.1	71.3	15.4	55.9	20.0
Nongovernmental loans ^e	55.2	4.9	50.3	19.5	30.8	47.9	9.9	38.0	35.3	2.7	-28.1
Option-type ^f	869.0	219.2	649.8	160.0	489.8	2,230.7	409.0	1,821.7	370.6	1,451.1	961.3
Government loans	495.9	122.7	373.2	84.3	288.9	1,253.7	164.0	1,089.7	143.0	946.7	657.8
Nongovernmental loans	373.1	96.5	276.6	75.7	200.9	977.0	245.0	732.0	227.6	504.4	303.5
Linked 6.5 percent loans	443.6	0.0	443.6	5.6	438.0	483.2	0.0	483.2	26.3	456.9	18.9
Government	241.6	0.0	241.6	3.5	238.1	347.2	0.0	347.2	11.5	335.7	97.6
Nongovernmental	202.0	0.0	202.0	2.1	199.9	136.0	0.0	136.0	14.8	121.2	-78.7

Total regular bonds traded in Israeli currency	2,730.3	328.3	2,375.0	513.7	1,861.3	4,485.4	538.3	3,947.1	906.9	3,040.2	1,178.9
Bonds traded in foreign currency ^g	156.9	48.2	108.7	89.9	18.8	16.0	72.0	-56.0	102.5	-158.5	-177.3
Compulsory loans^h											
From the public											
Absorption Loan	0.0	70.6	—	58.0	—	0.0	84.8	—	91.9	—	—
Defense Loan	588.4	303.8	—	202.6	—	798.2	15.3	—	150.5	—	—
Compulsory Savings Loan	592.5	0.0	—	0.0	—	540.0	—	—	—	—	—
Compulsory War Loan	—	—	—	—	—	88.9	—	—	—	—	—
Voluntary War Loan ⁱ	—	—	—	—	—	140.0	—	140.0	—	140.0	—
Bank Defense Loan	129.0	0.0	129.0	0.0	129.0	160.3	0.0	160.3	0.0	160.3	31.3
Shares and convertible bonds											
Shares ^j	143.2	0.0	143.2	0.0	143.2	326.8	0.0	326.8	0.0	326.8	183.6
Convertible bonds	56.0	0.0	56.0	0.0	56.0	299.3	0.0	299.3	0.0	299.3	243.3

^a Excluding sales of foreign securities in Israel. The data in this table relate only to issues with a prospectus and securities of the Government, Jewish Agency and its subsidiary, which are issued without a prospectus. The data relate to actual sales and not authorized issues.

^b Issued mainly to social insurance funds.

^c Consists mainly of financial institution issues.

^d The reference is to the deposits made by the insurance companies with the Bank of Israel and not to the value of Insurance Companies Loan certificates into which the deposits are converted at fixed dates during the year. These estimates assume that none of the bonds issued by the Israel Electric Corporation and registered on the Stock Exchange were held by insurance companies.

^e By the Israel Electric Corporation.

^f Includes the redemption of prize-bearing bonds, unlinked bonds, bonds with mixed linkage, and bonds linked to the foreign exchange rate, in the amount of IL 35.5 million in 1972 and IL 40.9 million in 1973.

^g The data were calculated in Israeli pounds according to the official rate of exchange (\$ 1=IL 4.2).

^h The amount collected from the public and not the value of the certificates distributed.

ⁱ Cash sales, i.e. excluding sales against Bank of Israel credit.

^j Share issues of companies listed on the Stock Exchange which were offered to shareholders of record or to the general public.

SOURCE: State Loans Administration, Bank of Israel.

the sharpening of inflation since 1971 and its further aggravation in the early part of the current year, as well as the lag in adjusting the securities portfolio of households and business. It was reasonable to expect a rise over the year in the proportion of linked bonds in the optimal investment portfolio at the expense of nonlinked financial assets, and wide sections of the saving public have become increasingly aware of the importance of hedging themselves against the erosion of the real value of their financial investments. In the face of the high inflation prevailing in the past, and especially that expected in the future, this phenomenon found striking expression in the year reviewed. For the first time since the 1960s there was a decline in the balance of such nonlinked financial assets as time deposits and the Short-Term Loan to the tune of IL 380 million, despite the monetary expansion and the sizable overall growth of the public's financial assets portfolio.

Rampant inflation influences the demand for holding bonds in another way: the more the accumulated linkage differentials on bonds build up, the more liquid the security becomes, in the sense of diminished risk of loss of principal; the outcome is an increase in the proportion of bonds not only in the long-term financial investment portfolio, but also in the liquid balances of business firms and households (see Chapter XIII, "Money Supply, Credit, and the Banking Institutions"). This gradual shift from nonlinked liquid assets to linked bonds, which assumed enormous proportions in 1973, injected a new, weighty element into the bond market and helped to fuel demand for this type of financial asset, despite the decline in the rate of private saving. This development was greatly facilitated by the existence of a large stock of bonds with relatively short maturities.

Demand for bonds was also stimulated by the fact that equities were in the grip of a severe bear market from February onward, as well as the absence of a devaluation of the Israeli pound in relation to the dollar in the near future, which enhanced the attraction of bonds and lured to this market a good proportion of the long-term investors and short-term speculators alike. Still another factor was the widening of the differential between the nominal interest rate on subsidized credit from various sources (pension and provident funds, loans from employers, development budgets, and even ordinary commercial bank credit) and the return on linked bonds; this induced both households and businesses to finance consumption and investment as little as possible from own means and to become borrowers in the credit market and lenders in the bond market at one and the same time, from profit and not liquidity considerations.

It was against this backdrop that hostilities broke out and accentuated the processes already at work, mainly by stoking still more the heated inflation from both internal and foreign sources, but also as a result of the expanded supply of credit in the economy and the growing mood of uncertainty con-

cerning employment and the business outlook in general. The outcome was a feverish demand for bonds during this period, which was met mostly by way of new issues. In the final months of the year net issues topped IL 818.6 million, compared with only IL 196.6 million in the last quarter of 1972 (see Table XV-2).⁴ The flurry of bond sales, which carried over into the early part of 1974, was accompanied by an increased demand for foreign currency assets, and dampened demand for money and other unlinked liquid assets.

(a) *New issues*

As already indicated, the net amount of capital raised through medium-term bond issues in 1973 was IL 1,565 million, while that through long-term bonds totalled IL 1,132 million, as against IL 328 million and IL 898 million respectively in 1972. To these sums must be added sales of the Voluntary War Loan from October, which yielded the Treasury's coffers IL 140 million by year's end. Total absorption through the various types of bonds (excluding compulsory loans and the Bank Defense Loan issue) thus reached IL 2,837 million, as contrasted with IL 1,226 million in 1972. This increase in the total amount netted the economy through bond issues eclipsed the rise in GNP prices, and constituted a real growth in the volume of funds mobilized and in their weight in national income. In real terms⁵ the amount of capital procured in this manner shot up 90 percent, bringing up its share in national income from 5.2 to 9.5 percent.

The monthly movement of gross and net sales is presented in Table XV-2. It shows a fairly stable quarterly level between January and September in medium-term bond issues, especially the net volume (these issues are the most interesting and significant from the economic standpoint); thus the advancing trend of the previous year was more or less arrested, although it plateaued at a much higher level. In contrast, the last quarter of the year (actually the last two months) saw a strong upsurge (discussed at the end of the previous section). There was also a somewhat heavier purchase of long-term bonds by social insurance funds and insurance companies. To some extent this flurry can be attributed to seasonal influences, but the main cause was the attempt to advance purchases in the face of the high inflation.

In contrast to 1972 and especially the early part of 1974, the year reviewed did not see any change in the characteristics of the array of bonds offered to the general public or to institutional investors, nor were there any temporary constraints on the supply of such debt instruments.

As regards the composition of the various types of medium-term bonds,

⁴ In this period Short-Term Loan holdings plummeted IL 400 million, and this undoubtedly explains part of the enormous growth of issues.

⁵ Deflated by the annual average rise in the implicit GNP price index.

End of period	Medium-term bonds sold to the public ^b					
	Option-type		6.5% index-linked		Total	
	Govt.	Other	Govt.	Other	Gross	Net ^c
1972	495.9	373.1	241.6	202.0	1,312.6	963.1
1973	1,253.7	977.0	347.2	136.0	2,713.9	1,565.4
January	98.9	79.5	54.5	21.7	254.6	133.9
February	86.3	40.9	36.8	16.5	180.5	135.8
March	53.9	32.6	16.3	11.5	114.3	59.0
April	92.9	88.0	47.0	18.6	246.5	-22.7
May	79.1	74.1	36.1	8.7	198.0	127.0
June	73.0	92.2	23.1	4.0	192.3	115.1
July	70.0	83.9	13.4	5.3	172.7	61.9
August	64.8	49.9	15.0	5.5	135.2	94.0
September	74.4	60.4	17.0	2.9	154.7	68.4
October	65.5	38.6	7.5	5.0	116.6	45.0
November	211.8	117.3	30.0	17.1	376.2	283.6
December	283.0	219.6	50.5	19.2	572.3	464.4

^a The data here refer to actual sales and not to the volume of issues offered. However, not all the issues were listed on the Stock Exchange, especially in the case of long-term bonds.

^b Excluding compulsory loans.

^c Less redemption of principal and interest and linkage differentials paid; excluding the Absorption and Defense Loans.

^d Including Hollis.

there was a notable increase in the share of option-type paper.⁶ This may seem surprising, for the steep rise in the general price level in effect erased the significance of the option offered investors, and to all intents and purposes these became linked bonds. The explanation lies entirely in the rapid accumulation of the bank-administered saving schemes, which created a lively institutional demand on the part of banks for this type of bond.

The rise in the weight of Government bonds compared with those of financial institutions reasserted itself this year: in medium-term issues the proportion rose from 56 percent in 1972 to 59 percent, and in those sold to social insurance funds and insurance companies it went up from 4 to 8 percent. This primarily reflects the Government's desire to reduce its use

⁶ Option-type loans permit the investor to choose, upon maturity, between a high rate of interest without linkage of the principal and interest and a lower rate with the principal and interest linked to the consumer price index.

(million)

Long-term bonds								
Sold to insurance companies & social insurance funds		Bank Defense Loan	Total denominated in IL		Bonds denominated in foreign currency ^d		Convertible bonds	Shares ^e
Govt.	Other		Gross	Net	Gross	Net		
57.6	1,333.1	129.0	1,519.7	1,027.2	156.9	18.8	56.0	143.2
149.0	1,622.5	160.3	1,931.8	1,292.5	16.0	-158.5	299.3	326.8
10.4	82.7	10.4	103.5	66.9	6.6	-0.6	50.0	17.3
8.0	72.5	10.4	90.9	46.4	—	-5.3	2.3	1.7
9.8	78.7	11.2	99.7	60.3	0.6	-37.5	—	4.1
7.4	91.9	—	99.3	45.9	—	-10.5	31.0	88.0
9.2	200.8	—	210.0	159.6	4.8	-3.4	30.0	16.0
11.3	72.6	—	83.9	30.1	—	-25.0	29.0	9.5
6.9	92.2	10.1	109.2	46.9	—	-6.6	75.0	89.0
33.9 ^f	129.0	9.9	172.8	121.1	—	-9.0	35.0	2.1
9.8	147.3	9.9	167.0	126.1	—	-11.0	47.0	66.0
4.0	215.1	27.5	246.6	180.4	—	-6.6	—	—
13.7	184.8	33.8	232.3	167.3	—	-12.3	—	33.1
24.6	254.9	37.1	316.6	241.5	4.0	-30.7	—	—

^e Excluding shares not listed on the Stock Exchange. Sales of unlisted shares issued with a prospectus amounted to IL 43.7 million.

^f Of this sum, IL 26 million represents the funding of a social insurance scheme deposit previously held with the Accountant General.

SOURCE: State Loans Administration.

of financial institutions as intermediaries in the floating of bond issues in order to reduce issue costs and perhaps also to ensure greater control over the funds so raised, rather than any change in investors' preferences (these two types of bonds are identical, except perhaps that Government bonds are slightly more liquid).

(b) *The secondary market*

Turnover in bonds, both on the Tel Aviv Stock Exchange and brokers' matching of buy and sell orders, totalled IL 4,824 million in the year reviewed, as against IL 3,484 million in 1972—an increase of 38 percent, compared with 123 percent in 1972 (see Table XV-8). The more laggard growth this year, despite the accelerated climb of bond prices, can be attributed both to the difficulty of sustaining the inordinately vigorous rate of 1972 and to the narrowing of the yield differential between the primary and secondary

Table XV-3
GENERAL TRENDS IN STOCK EXCHANGE TRADING, 1971-73
 (IL million, at market values)

	Bonds						Total	Short-Term Loan	Shares ^a	Total securities	
	Linked to the exchange rate	Linked to the c-o-l index	Option-type	Traded in foreign currency	Convertible into shares	Non-linked and mixed linkage					
1971	15.4	56.8	210.4	82.2	2.4	0.9	368.1	150.1	105.7	623.9	
1972	15.5	112.4	441.9	107.8	12.8	0.6	691.0	212.5	762.9	1,666.4	
1973	11.7	250.5	676.0	120.6	79.3	0.1	1,138.2	61.5	633.0	1,832.7	
January	1.2	14.5	42.1	12.9	7.8	0.0	78.5	23.9	176.3	278.7	
February	1.1	16.2	35.0	9.8	3.3	0.0	65.4	9.9	107.3	182.6	
March	1.0	14.2	49.3	9.4	1.9	0.0	75.8	3.3	41.1	120.2	
April	1.0	20.8	38.2	9.9	2.3	0.0	72.2	2.1	39.5	113.8	
May	0.9	26.5	52.5	10.5	7.6	0.1	98.1	1.7	49.8	149.6	
June	0.9	19.9	50.9	10.1	9.9	0.0	91.7	0.9	38.3	130.9	
July	1.0	22.7	39.7	10.4	10.5	0.0	84.3	1.0	63.7	149.0	
August	1.1	20.8	54.7	9.8	7.3	0.0	93.7	0.7	33.3	127.7	
September	1.0	27.0	79.2	9.3	14.0	0.0	130.5	0.7	32.4	163.6	
October	0.4	19.7	57.2	6.7	6.1	0.0	90.1	0.3	18.7	109.1	
November	0.4	15.6	72.8	9.2	3.7	0.0	101.7	0.6	19.6	121.9	
December	1.7	32.6	104.4	12.6	4.9	0.0	156.2	16.4	13.0	185.6	
			Percent annual increase or decrease (-)								
1971	-21.4	14.1	105.6	68.1	b	b	66.0	29.7	102.1	60.1	
1972	0.7	97.9	110.0	31.1	b	b	87.7	41.6	621.8	167.1	
1973	-24.5	122.9	53.0	11.9	b	b	64.7	-71.1	-17.0	10.0	
			Percentage distribution								
1971	2.5	9.1	33.7	13.2	0.4	0.1	59.0	24.1	16.9	100.0	
1972	0.9	6.7	26.5	6.5	0.8	0.0	41.4	12.8	45.8	100.0	
1973	0.6	13.7	36.9	6.6	4.3	0.0	62.1	3.4	34.5	100.0	

^a Listed ordinary and preferred shares, unlisted shares traded off the floor, and shares denominated in foreign currency. Data on monthly share turnover by share group and on over-the-counter trade appear in Table XV-6.

^b Because of the small sums involved the percentage change lacks significance.

SOURCE: Tel Aviv Stock Exchange.

Table XV-4
**AVERAGE NET YIELDS TO MATURITY^a OF BONDS TRADED
 ON THE STOCK EXCHANGE, 1973**

(percentages)

Month	Dollar linked ^b		Total	Index-linked ^c			Option-type ^e	
	0-2	5+		Absorption	6.5%		Development	
				Loan	index-linked	Loan		
Years to maturity			1½	5	6	2	3	
January	1.0	5.2	5.7	4.7	5.2	5.1	5.0	5.5
February	0.3	4.9	5.3	5.9	5.6	5.4	6.5	6.1
March	6.8	5.7	6.1	5.2	5.6	5.4	6.0	5.9
April	7.5	6.8	7.4	4.8	5.5	7.4	5.3	4.8
May	12.3	7.8	8.5	6.9	6.4	6.0	5.4	5.5
June	13.3	7.4	8.2	5.1	6.3	6.0	3.4	4.6
July	8.0	7.6	8.0	4.8	5.7	5.8	3.2	5.6
August	6.2	7.3	7.0	^d	^d	5.9	^d	^d
September	5.3	6.8	6.8	4.3	6.0	5.7	3.2	5.5
October	5.1	5.7	5.9	5.5	5.7	5.9	2.4	5.2
November	5.7	5.5	5.5	4.2	5.5	5.2	2.5	5.1
December	1.6	4.1	4.2	^d	^d	5.7	2.4	5.3

^a For option-type bonds the gross yield to maturity is given here, as this is what the investor will actually receive net because of the practice of bond washing (calculated according to the price of the security one day before maturity).

^b Data from the Central Bureau of Statistics.

^c Yields to maturity of index-linked and option-type bonds were calculated from a sample of two to four of the most actively traded bonds in the group.

^d Data not available.

markets, which attracted a larger percentage of the demand to the former. But this does not fully explain the slowdown, and apparently this development strengthens the assumption that in 1973 there was a greater degree of homogeneity in the investing public's expectations and thus also in the reshuffling of its portfolio in favor of linked fixed-interest securities, which largely precluded the need to sell bonds from its portfolio.

A breakdown of bond trade by type of issue (Table XV-3) shows a decline in the weight of nonlinked bonds, which is understandable given the development of demand in the course of the year. Option-type bonds remained on the top rung (59 percent of the total, as against 22 percent for linked bonds). This can largely be ascribed to the rapid growth of the approved saving schemes administered by commercial banks and the introduction on the Tel Aviv Stock Exchange of a new framework for trading in bonds according to yield (discussed below).⁷

Real yields to maturity held fairly stable during the year, fluctuating slightly

⁷ The development of turnover in bonds traded in foreign currency, capital notes, and convertible bonds is discussed below.

in those months when credit was tight or when demand for bonds grew very heated (see Table XV-4). Only in the latter part of the year, when demand for linked bonds soared and temporary supply difficulties cropped up in the primary market (due to the unexpected size of the demand), did yields decline in most series. The bond yields are hardly likely to be very volatile, since, unlike nominal yields, they are not very responsive to changes in the rate of inflation. The variability of such yields is connected with more basic developments in the economy, which are inherently slower. What is more, since there is a very elastic supply of new bonds, this has set a lower boundary on yields even in periods of rising demand, such as in the current year.

At the beginning of August the management of the Tel Aviv Stock Exchange introduced a major change in operating procedures by quoting bond yields rather than prices. Units of trade are very large compared with their usual size on the Exchange, amounting to IL 50,000.⁸ This has made a signal contribution toward improving the trading mechanism and to enhancing the ability of the Exchange to efficiently handle large transactions of private investors and big institutions (who in the past were forced to resort to the over-the-counter market or to spread their sales over numerous bonds and trading days); it is also forcing investors to make more rational decisions regarding bond investments.

Trade under the new system was conducted in 1973 only in option-type bonds and proved very popular. Monthly volume averaged IL 23 million until the outbreak of hostilities, and even in the postwar period it came to IL 8 million. Nevertheless, at the beginning of 1974 such trade was discontinued, for after modification of the linkage terms of the new types of bonds issued there ceased to exist (perhaps temporarily) a uniform method whereby brokers could translate yields into prices (and vice versa), which is a precondition for conducting trade of this sort.

Table XV-5 shows the movement of the index of bond prices during the year. A rise in the index is the net result of the accumulated linkage differentials and the change in market yields. Since the yields did not undergo any significant change in 1973, the rise in the index over the year (27 percent) closely matched that in the rate of inflation (26.4 percent), with the difference stemming from a slight decline in yields at the end of the year.

It is noteworthy that in October, the war month, the secondary bond market did not witness any significant developments in turnover or bond prices, a fact which helped to bolster the public's confidence in an investment in this type of financial asset during an emergency period.

Table XV-10 shows the concentration of secondary market trading in

⁸ Auctioning is for a block of bonds, with the required yield, period to maturity (within a three-month range), and the issuer being stipulated. This greatly facilitates arbitrage in bonds of the same type.

Table XV-5
MONTHLY INDEX OF SECURITY PRICES ON THE TEL AVIV
STOCK EXCHANGE, 1973

(December 30, 1972=100)

End of month	Bonds					Shares		
	Index-linked			Linked to foreign exchange rate	Mixed linkage	Total	Pre-ferred	Ordinary
	Linked to index only	Option-type	Total					
1973 January	102.2	101.9	102.0	102.2	100.0	102.0	108.7	108.6
February	102.4	100.2	101.1	102.7	100.9	101.1	96.9	102.0
March	103.8	101.3	102.4	95.9	102.7	102.3	98.1	102.0
April	106.1	105.9	106.0	92.9	102.3	105.8	93.1	98.2
May	107.3	106.5	106.8	90.1	102.5	106.6	95.8	102.4
June	110.0	108.5	109.2	92.6	105.5	108.9	93.7	95.9
July	111.4	110.4	110.8	95.3	105.8	110.5	93.4	96.9
August	112.9	111.0	111.8	97.7	107.8	111.6	86.3	97.7
September	114.9	112.2	113.4	103.0	109.5	113.2	80.5	91.8
October	118.9	115.2	116.8	102.7	109.3	116.5	76.9	89.9
November	122.2	118.5	120.1	104.0	114.9	119.8	68.5	83.2
December	127.0	122.3	124.3	113.8	118.3	124.1	63.4	79.8

SOURCE: Central Bureau of Statistics.

bonds. A glance at the data reveals three distinct groupings: in the first, numbering some 456 bonds this year as compared with 500 in 1972, the average daily turnover was extremely light (less than IL 2,000), with a large percentage of the bonds being inactive during the entire year. In the second group, numbering 174 bonds as against 120 in 1972, there was an active but relatively limited trade ranging from IL 2,000 to IL 10,000 on a daily average. The third group, which is the most heavily traded, included 90 bonds in 1973, compared with 42 the year before, with the average daily turnover exceeding IL 10,000 and in the case of some series even topping the IL 60,000 mark. It should be stressed that the reference is to trade on the Exchange only, which on an average accounts for only about one-quarter of total bond trade (see Table XV-8); hence these data should be regarded as only an indication of the actual volume of trade conducted in such paper.

3. THE SHARE MARKET

The year reviewed witnessed a continuation of the burgeoning demand for shares which began two years earlier, and was reflected by a 7.4 percent rise in the daily index of share prices in January. But in the following month

the boom began to fizzle out: demand for equities started to subside, a trend that continued through the rest of the year and became more pronounced in the postwar months. For the year as a whole the price index retreated 23.6 percent; allowing for the rise in the consumer price index, the real decline came to a disturbing 40 percent. Nevertheless, firms listed on the Stock Exchange raised an unprecedented volume of equity capital through new issues of shares, capital notes, and bonds convertible into shares—IL 627 million as against IL 200 million in 1972 and no new issues whatsoever in the two preceding years.

The cooling of demand for shares, and especially their skidding prices, can be attributed to several factors working in the same direction. First of all, share prices on the Tel Aviv Stock Exchange doubled on an average in 1972; if prices were previously undervalued, after this strong spurt they were overvalued. This, of course, made it less worthwhile to hold stocks at their new prices, and a wave of profit-taking set in. Secondly, at the beginning of the year the economy experienced some monetary tightness; as a result, less credit was available for financing security purchases, and banking and financial institutions were forced to dispose of part of their equity portfolio in order to meet the mounting demand for credit.

Against this backdrop of slumping demand for shares, the market was flooded with an enormous volume of new issues. Preparation of these issues began, of course, when the tone of the market was vigorously bullish, but because this is a protracted process, the placements were made only at the onset of the slump and when it was well underway. Under such conditions it was to be expected that the new issues, which accounted for fully one-quarter of the economy's total equity portfolio at the beginning of the year, would have a strong impact on market prices.⁹ What is more, unfortunately these were mainly issues of veteran companies on the Exchange, and not newly listed concerns. This more or less precluded the reshuffling of financial asset portfolios which would have taken place had stocks with new characteristics been offered. Thus the economy witnessed a reappearance of the situation that existed in the early 1960s: a secondary stock market boom followed by an upswing in new issues, most of which were floated when investors were already pulling in their horns and prices were sinking, thereby speeding the downturn.

If to this is added the mounting inflationary pressure (which affects yields in the bond market more quickly than those in equities), the lack of a stable nucleus of large institutional investors in shares, as well as of small long-term investors who do not enter the market only when the boom is close to its peak and pull out for several years as soon as it begins to peter out, we can understand the underlying forces which affected the stock market during the

⁹ To be sure, part of the capital note and convertible bond issues attracted fresh social insurance fund monies, but the size of the new issues of these three types of instruments was still large enough to decisively affect the movement of prices.

(December 30, 1972=100)

DAILY INDEXES OF SHARE PRICES, 1973

Table XV-6

End of month	General Stock Exchange index	Finance and insurance					Investment companies	Industry	Commerce and services	Land, construction, development
		General index of finance and insurance shares	Commercial banks	Mortgage banks	Specialized financial institutions					
January	107.4	108.7	120.5	107.7	101.4	105.7	105.3	108.4	108.1	
February	99.0	99.4	112.3	95.0	95.5	95.0	98.1	100.8	99.9	
March	98.2	100.2	112.3	94.5	97.7	94.3	97.2	95.7	98.7	
April	95.0	96.3	107.8	91.9	93.5	89.8	95.4	99.2	92.9	
May	95.5	98.0	111.6	93.6	91.6	88.9	97.1	96.5	92.3	
June	89.1	93.5	107.2	89.9	85.5	82.1	90.3	87.6	84.3	
July	92.3	95.5	107.1	94.3	86.1	84.6	95.3	89.8	87.2	
August	92.4	95.4	107.8	93.2	84.7	84.2	95.7	89.9	87.0	
September	87.1	90.0	102.1	87.6	80.1	80.9	90.3	82.6	81.4	
October	85.4	86.3	97.1	84.2	77.3	79.5	90.4	79.3	80.0	
November	79.1	80.8	89.2	81.6	73.5	73.1	82.7	72.5	74.1	
December	76.4	78.8	86.3	79.1	72.3	70.5	80.1	69.1	70.3	

NOTE: Wherever data according to this group breakdown were not available for December 30, 1972, the figures for January 2, the first day of trading in 1973, served as the base.

SOURCE: Central Bureau of Statistics.

year reviewed. Admittedly, in order to comprehend these factors we must also study developments in the listed companies themselves and their prospects for the next few years, but since the picture is not very clear we can not determine what impact this had on the stock market.

(a) *Primary market (new issues)*

Proceeds from new equity issues reached IL 326.8 million in 1973, while capital notes and convertible bonds yielded another IL 299.3 million; this compares with IL 143.2 million and IL 56 million respectively in 1972. The tendency for such issues to be concentrated in the financial group increased further this year: it accounted for fully 91.8 percent of the total, while the proportion of nonfinancial concerns came to a mere 8.2 percent; in 1972 the figures were 82.1 and 17.9 percent respectively. This pattern can be attributed to several factors. First, the financial institutions have been experiencing a vigorous expansion of business, and since there is need and sometimes institutional pressure to maintain a certain minimum ratio between equity and total assets, they must from time to time take advantage of a buoyant share market to procure equity capital. Secondly, the institutions have easy access to the primary securities markets and also serve as underwriters; as a result, their own flotation expenses are relatively low and they can therefore better ensure the success of their issues. In addition, it seems that the fact that they are relatively large precludes the possibility of raising capital through private placements. Furthermore, the paucity of family-owned financial institutions makes it natural for this group to turn to the Exchange to raise capital.¹⁰ By contrast, other companies, notably industrial concerns, have a better source of capital to tap, namely soft Government development budget loans. In addition, these companies display a reluctance to go public, with all that this implies concerning the obligation to reveal information on the firms' operations and the intervention of new shareholders in management, etc.

This year a fairly large number of companies turned to the primary new issues market to raise capital: 22 by way of shares and 17 through bonds, compared with 12 and six respectively in 1972. It is important to note that there is considerable overlapping in these two groupings. It seems that some companies were not confident that they could raise all the desired sum through shares, and so they resorted to convertible bonds. But there is no denying that this form of procuring capital has certain advantages to both the issuer (with respect to income tax and the transfer of profits to owners) and the investor (the diminution of risk without impairing the long-run prospects of his investment); as a result, this type of instrument can be used also in boom periods (see Bank of Israel, *Annual Report 1972*, p. 446).

¹⁰ Especially as under the conditions prevailing in the Israeli share market this does not involve any loss of control by the controlling group in the company.

Among the companies turning to the equity market this year were three in industry and the land and development group for which this was the first time they floated a share issue on the Stock Exchange. Compared with previous years, this is a fairly large number, but it should not be regarded as indicative of a change in trend.

Rights issues constituted 75 percent of total new issues this year, while only 21 percent was raised by placements with the general public (compared with 68 and 29 percent respectively in 1972).¹¹ There are three principal reasons for raising equity capital by way of a rights issue. First, some companies are legally bound by their articles of association to float new equity issues only in the form of stock rights. The second reason is to enable stockholders of record to retain their share in total capital and thus control of the firm, even if this is not explicitly stipulated in the articles of association. The third reason is to ensure the success of an issue, for the rights enable the existing stockholders to acquire new shares for less than the market price, thereby providing an incentive for them to exercise their rights. Given the conditions of the Israeli market, it seems that the dominant motivation has been a combination of the legal obligation and the desire to guarantee the success of the flotation. The convertible bond issues, on the other hand, were offered to the general public, rather than in the form of rights issues, but in some cases there was a preallotment to preferred investors (generally institutional). This was due to the desire to enable affiliated institutional investors to share in the profits of the flotation and to ensure a nucleus of institutional investors—a desirable situation in times of stock market slump and crisis.

As already mentioned, this chapter deals with equity issues for cash by listed companies, with the flotations being offered to all stockholders of record (by way of rights issues) or to the general public. At the same time, there was also an increase this year in the amount of shares listed for trade on the Exchange as a result of the conversion of IL 2 million (par value) worth of bonds into shares, the issue of IL 53 million (par value) worth of shares on a noncash basis, and the listing of IL 31 million (par value) worth of existing stocks; this compares with an increase of only IL 7 million last year in listings of all three types. The relatively large increment from these sources augmented the pressure of the new share offerings on the level of market prices, although to a lesser extent than those sold for cash.

In contrast to developments in the bond market, the war had a negative effect on the share market in general and on the primary market in particular. All the primary market developments described actually took place in the first three quarters of the year, and in the last quarter there was only a single

¹¹ The remaining sum in each of these two years represents sales to employees of the issuing companies (see Bank of Israel, *Annual Report 1972*, p. 447).

Table XV-7

MONTHLY SHARE TURNOVER ON THE TEL AVIV STOCK EXCHANGE, BY SHARE GROUP, 1973*

(IL thousand)

Month	Total Stock Exchange share volume	Commercial banks	Mortgage banks ^b	Specialized financial institutions ^b	Insurance	Commerce and services	Land and development	Industry	Investment companies	Shares sold off the floor
January	176,309	68,266	15,045	3,308	3,170	6,832	21,447	16,340	40,858	1,043
	69,697	28,200	5,731	1,061	759	2,010	6,185	8,111	17,640	
February	107,273	46,081	8,173	2,884	1,332	4,633	12,285	11,467	20,010	408
	54,297	29,413	4,164	4,550	297	1,036	3,144	3,842	7,851	
March	41,144	14,096	3,328	1,061	483	2,280	5,504	4,848	9,359	185
	33,841	23,931	2,222	403	140	489	1,682	1,395	3,579	
April	39,463	13,189	2,676	1,197	597	2,086	4,757	5,158	9,590	213
	23,645	11,949	1,557	1,916	249	633	1,791	1,817	3,733	
May	49,782	16,673	4,911	1,169	751	2,440	5,068	7,285	11,144	341
	34,675	17,398	2,031	719	339	782	1,773	3,318	8,315	
June	38,335	14,431	2,401	1,552	971	1,330	3,329	5,622	8,324	276
	24,738	14,744	1,518	328	473	484	1,602	2,232	3,357	
July	63,665	21,570	7,050	1,577	2,780	1,908	7,818	9,026	11,579	357
	45,576	27,357	3,415	331	1,888	499	3,775	3,318	4,993	

August	33,323	8,625	3,373	667	1,318	1,243	3,754	7,085	6,713	545
	25,734	15,062	2,358	875	278	342	1,546	2,611	2,662	
September	32,366	7,690	2,200	529	783	1,676	3,758	6,029	9,067	634
	24,455	12,050	1,147	159	257	801	1,874	2,059	6,108	
October	18,687	4,410	1,022	201	357	1,130	2,499	4,818	4,021	229
	13,357	4,532	586	70	103	533	872	2,197	4,464	
November	19,640	4,396	1,473	439	306	847	2,081	4,097	5,806	195
	17,854	6,156	719	92	71	350	1,104	2,373	6,989	
December	12,983	2,904	1,096	312	149	635	1,371	3,377	2,927	212
	16,349	7,471	474	67	115	374	816	1,668	5,356	
Total, 1973	1,017,180	420,594	78,670	26,467	17,966	35,373	99,835	120,093	214,544	4,638
On the Ex- change	632,970	222,331	52,748	14,896	12,997	27,040	13,671	85,152	139,497	4,638
Over the counter	384,210	198,263	25,922	10,571	4,969	8,333	26,164	34,941	75,047	
Total, 1972	1,112,871									

^a Upper and lower figures indicate the volume of trade on and outside the Stock Exchange (the over-the-counter market) respectively.

^b Shares traded in both Israeli and foreign currency.

SOURCE: Tel Aviv Stock Exchange.

issue. However, it may be argued that this development was foreseeable because of the slump in the secondary share market and the consequent shelving of planned new issues.

(b) *Secondary share market*

The secondary market for listed shares was plunged into a deepening gloom in the year reviewed. After the daily index of share prices climbed 7.4 percent in January and trading volume on the Exchange and in the over-the-counter market reached IL 246 million, most prices and turnover began to lose ground: between the end of January and the end of December the daily index of share prices tumbled 29 percent, while turnover fell to a IL 70 million monthly average.

The factors behind the stock market slump were discussed at the beginning of the chapter; here we shall elaborate on its various manifestations. Tables XV-5 and XV-6 show the movement of share prices during the year. After peaking in January, the daily index of share prices began to slip, and it continued downward almost uninterruptedly, with the trend gathering momentum after the war. At the end of 1973 the index stood at 76.4 percent of its level at the end of the previous year, with the drop being steeper in the commerce and services, investment companies, and land and development groups, and milder in financial shares.

Table XV-8
QUARTERLY TURNOVER ON TEL AVIV STOCK EXCHANGE
AND OVER-THE-COUNTER MARKET, 1972-73

	Shares				Bonds ^a			
	Over-the-counter market	On the Exchange	Total	Ratio (1) ÷ (3)	Over-the-counter market	On the Exchange	Total	Ratio (5) ÷ (7)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1972	349.9	762.9	1,112.8	0.31	2,791.1	691.0	3,484.1	0.80
1973	384.2	633.0	1,017.2	0.38	3,685.3	1,138.2	4,823.5	0.76
Percent increase or decrease (-)	9.8	-17.0	-8.6		31.9	64.7	38.4	
1973 I	157.8	324.7	482.5	0.33	687.5	219.7	907.2	0.76
II	83.0	127.6	210.0	0.39	637.1	262.0	899.1	0.71
III	95.8	129.4	225.2	0.43	929.0	308.5	1,237.5	0.75
IV	47.6	51.3	98.9	0.48	1,431.7	348.0	1,779.7	0.80

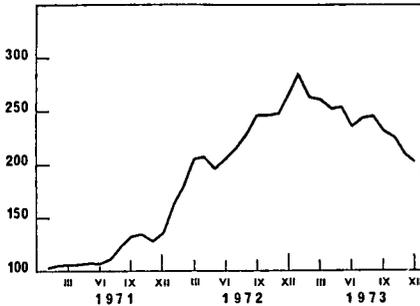
^a Excluding the Short-Term Loan; including bonds traded in Israeli and foreign currency, capital notes, and convertible bonds.

SOURCE: Tel Aviv Stock Exchange.

Figure XV-1

DAILY INDEX OF SHARE PRICES,
1971-73

(December 1970=100)



The setback in equity trading volume can be seen in Table XV-7. Overall volume fell from IL 246 million in January to a IL 29 million trickle in December, with the proportion of trade conducted outside the Exchange rising from 28 percent in the fourth quarter of 1972 to 48 percent in the final quarter of the current year (see Table XV-8). This suggests an undesirable decline in the proportion of transactions conducted in the "variables" and an increase in that conducted in the opening round. This changing pattern of trade indicates a drop in the share of small investors

in total trade in comparison with the institutional investors and large transactions in the over-the-counter market—developments impairing the significance of, and credibility in, the prices set on the Exchange.

The impact of the share market slump on the net overall rates of return¹² in this market can be seen in Table XV-9. The overall arithmetic average net yield on an investment in all listed ordinary shares in 1973 fell to -16.2 percent, with the lower decile being -35.5 percent and the upper decile only 7.1 percent. All share groups lost ground; the highest average nominal loss was sustained by investment companies (-25.9 percent), and the lowest by financial stocks (-9.8 percent). The fact that the price and yield decline permeated all groups strengthens the assumption that the variability in share prices over time stems primarily from general market factors and is influenced to only a minor degree by group affiliation.

In contrast to previous years, when the stocks that were most heavily traded and had the largest volume of listed capital were the ones with the highest average yield, this year they were the ones that suffered the heaviest losses. It would therefore seem that they are more vulnerable to market trends than those of small companies and inactive stocks.

Unlike the secondary market for shares, the secondary market for capital notes and convertible bonds experienced a larger turnover in the year reviewed. This was connected with the dramatic increase in the stock of such securities listed on the Exchange and the reshuffling of portfolios in the wake of the numerous new issues this year. Nevertheless, along with the retreating of share prices, prices in this market too skidded, although for lack of a separate

¹² On the method of calculating the net overall rates of return, the significance of each of the three measurements, and the results of the calculations for 1969-72, see R. Zentler, "The Profitability of Investment in Common Stocks on the Tel Aviv Stock Exchange, January 1969-June 1972", Bank of Israel, *Economic Survey*, No. 41.

Table XV-9
NET OVERALL RATES OF RETURN ON AN INVESTMENT IN LISTED ORDINARY STOCKS, SELECTED PERIODS, 1970-73
 (percentages)

Period	Lowest overall rate of return	Overall rates of return by deciles					Highest overall rate of return	Arith-metic average rate of return	Average overall rate of return		Number of stocks	Number of companies
		10	25	50	75	90			Weighted by total listed capital ^a	Weighted by annual volume of trade ^b		
1. Banking, financing, insurance												
31.12.72-30.6.73	-29.8	-15.6	-10.6	-3.7	5.0	9.8	63.1	-1.8	4.0	-0.7	39	24
30.6.73-31.12.73	-37.9	-19.2	-14.9	-6.9	0.7	2.3	30.3	-7.6	-14.8	-12.4	39	24
31.12.72-31.12.73	-37.9	-29.0	-24.5	-8.4	2.3	10.4	30.4	-9.8	-11.5	-12.7	39	24
2. Land and development												
31.12.72-30.6.73	-20.8	-17.9	-15.9	-6.2	1.5	3.6	21.0	-5.8	-9.2	-9.7	14	11
30.6.73-31.12.73	-30.1	-23.8	-19.3	-17.0	-6.8	5.6	14.8	-13.0	-11.2	-16.2	14	11
31.12.72-31.12.73	-41.0	-32.7	-31.3	-24.3	-4.9	4.3	17.6	-17.7	-19.1	-24.1	14	11
3. Industry and commerce												
31.12.72-30.6.73	-40.9	-25.6	-16.9	-6.4	1.4	7.9	16.7	-8.5	-14.2	-12.3	34	22
30.6.73-31.12.73	-33.1	-28.2	-18.4	-9.1	-0.1	8.2	29.3	-9.1	-5.9	-8.0	34	22
31.12.72-31.12.73	-39.2	-35.1	-30.4	-22.2	-5.5	5.0	22.7	-17.4	-19.7	-19.6	34	22
4. Investment companies												
31.12.72-30.6.73	-28.6	-26.4	-18.4	-15.2	-10.8	-2.4	2.2	-14.2	-21.1	-16.7	17	14
30.6.73-31.12.73	-24.7	-23.4	-21.7	-15.9	-7.4	-3.5	0.5	-13.8	-8.0	-12.0	17	14
31.12.72-31.12.73	-43.8	-36.9	-34.7	-28.5	-23.1	-9.8	2.7	-25.9	-27.8	-27.0	17	14
5. Total companies listed on the Exchange^c												
31.12.72-30.6.73	-40.9	-23.2	-15.3	-7.1	2.2	8.2	63.1	-6.5	-4.8	-6.7	108	74
30.6.73-31.12.73	-37.9	-25.2	-18.2	-10.5	-0.2	2.9	30.3	-10.0	-12.1	-12.3	108	74
31.12.72-31.12.73	-43.8	-35.5	-29.5	-20.9	-5.3	7.1	30.4	-16.2	-16.8	-18.3	108	74
31.12.71-31.12.72	-10.5	-38.5	68.2	105.3	135.8	175.3	361.9	106.8	109.8	112.8	108	75
31.12.70-31.12.71	-22.0	5.3	17.4	33.3	44.2	71.2	160.0	38.7	34.8	44.9	111	77

^a According to the composition of listed capital, at market prices, at the end of the previous year.

^b According to the composition of trade in the year for which the calculation is made, except for the 1972 data, which were calculated on the basis of the 1971 composition.

^c Includes several stocks that are not classified under any of the four above-mentioned groups.

SOURCE: Bank of Israel calculations.

Table XV-10

**DISTRIBUTION OF ORDINARY SHARES AND BONDS^a BY DAILY^b
TRADING VOLUME, 1972-73**

Daily volume (IL '000)	Ordinary shares ^c				Bonds ^d			
	1972		1973		1972		1973	
	No. of shares	Percent of total volume	No. of shares	Percent of total volume	No. of bonds	Percent of total volume	No. of bonds	Percent of total volume
Not traded	—	0.0	—	0.0	185	0.0	210	0.0
0-0.2	—	0.0	—	0.0	168	0.6	87	0.0
0.2-0.4	—	0.0	—	0.0	48	0.9	28	0.0
0.4-1.0	—	0.0	1	0.0	56	2.2	67	1.6
1.0-2.0	1	0.1	3	0.1	42	3.6	64	3.2
2.0-4.0	5	0.4	5	0.4	33	6.3	63	6.5
4.0-10.0	9	1.8	14	2.6	90	35.0	111	28.3
10.0-20.0	14	6.2	11	4.0	31	25.0	71	34.7
20.0-40.0	18	14.6	15	11.6	8	13.5	13	12.9
40.0-60.0	8	10.4	9	11.5	1	3.6	4	6.6
60.0-80.0	8	14.7	5	9.5	1	3.3	1	2.5
80.0-160.0	8	27.8	7	21.6	1	5.0	1	3.7
160.0-240.0	3	16.6	2	11.6	—	0.0	—	0.0
240+	1	7.4	2	27.1	—	0.0	—	0.0
Total	75	100.0	74	100.0	664	100.0	720	100.0

^a The data for shares relate to trade in listed shares sold on the Stock-Exchange (both on and off the floor) and in the over-the-counter market, while the data on bonds relate only to trade on the Exchange. The distribution of shares is by issuer only and not by individual issues; that is, all types of shares issued by a particular company are treated here as a single unit. In the case of bonds, however, each series listed on the Exchange is treated as a single unit, and appears in this table if it was listed for trade during the entire year.

^b Assuming 250 trading days in the year.

^c For a group breakdown see Appendix Table A-XV-2 (in Hebrew only).

^d Excluding the Short-Term Loan.

SOURCE: Tel Aviv Stock Exchange.

price index for this market the exact extent of the decline cannot be ascertained.

Table XV-10 presents the distribution of daily share turnover on the Stock Exchange and in the over-the-counter market by size groups. It will be seen that there is considerable variance between the different groups, with the lowest decile being IL 4,000 and the upper decile over IL 80,000. The 1973 decline in total turnover is also reflected in this table, which reveals that on an average stocks moved down one group, although nine (12 in 1972) still had an average daily turnover in excess of IL 80,000.

4. SHORT-TERM LOAN

Demand for the Short-Term Loan, which began to wane in the last quarter of the previous year, weakened further at the beginning of 1973. This was mainly due to the relative disadvantages of this type of investment, which is not value-linked and offers a relatively low return. In view of the monetary policy of the Bank of Israel, this was a disturbing development, and following discussions with the commercial banks an underwriting agreement was concluded which helped to bring up the outstanding balance of the loan until the outbreak of war.

Table XV-11
SECURITIES LISTED ON THE TEL AVIV STOCK EXCHANGE,^a
AT PAR AND MARKET VALUES, 1972-73
(IL million)

End of period	1972		1973		Percent increase or decrease (-)	
	Par value	Market value	Par value	Market value	Par value	Market value
Bonds	5,337.4	7,156.0	7,687.8	10,938.0	44.0	52.9
Linked to the foreign exchange rate	74.9	117.9	65.7	110.1	-12.3	-6.6
Index-linked	1,699.8	2,437.2	2,482.1	3,955.4	46.0	62.3
Traded in foreign currency	1,207.1	1,209.8	1,173.6	1,195.5	-2.8	-1.1
Option-type	2,331.5	3,366.7	3,928.6	5,650.4	68.5	67.8
Mixed linkage	2.6	5.8	1.0	2.6	-61.5	-51.7
Nonlinked	21.5	19.5	26.8	23.8	24.7	22.0
Convertible bonds	83.0	104.9	382.5	361.4	460.8	344.5
Shares	1,161.2	2,833.2	1,491.7	2,783.9	28.5	-1.7
Ordinary and preferred	973.9	2,606.9	1,305.0	2,557.9	34.0	-1.9
Traded in foreign currency	187.3	226.3	186.7	226.0	-0.3	0.0

^a Quoted securities only.

The main provision of this agreement, which was to be in force from January 18 to November 14, 1973, was a commitment by the commercial banks to underwrite the growth of the balance in circulation at a predetermined rate, by making up the shortfall in the public's purchases. The balance was to rise by IL 3-4 million a week, with interruptions in certain predefined periods of seasonal monetary tightness.

The results of this agreement are set forth in Table XV-13. In January the balance plunged by IL 35 million due to developments during the fortnight before the agreement went into effect. Subsequently the level began to turn upward, rising from IL 714 million at the end of January to IL 819 million at the end of September.

Table XV-12

NEW SHARE AND CONVERTIBLE BOND ISSUES,^a BY GROUP, 1972-73

(IL million)

Group	1972				1973			
	Shares	Convertible bonds and capital notes	Total	Percent of total	Shares	Convertible bonds and capital notes	Total	Percent of total
Commercial banks and bank holding companies	84.6	30.0	114.6	57.5	184.7	60.0	244.7	39.1
Mortgage banks	15.0	6.0	21.0	10.5	27.3	56.0	83.3	13.3
Specialized financial institutions ^b	4.3	0.0	4.3	2.2	4.2	10.0	14.2	2.3
Insurance	0.0	0.0	0.0	0.0	5.4	0.0	5.4	0.9
Commerce and services	0.0	0.0	0.0	0.0	7.2	8.0	15.2	2.4
Land, construction, development, and citrus	18.7	7.0	25.7	12.9	1.7	2.3	4.0	0.6
Industry	4.0	6.0	10.0	5.0	23.6	9.0	32.6	5.2
Investment and holding companies	16.6	7.0	23.6	11.9	72.7	154.0	226.7	36.2
Total	143.2	56.0	199.2	100.0	326.8	299.3	626.1	100.0

^a Excluding bonus shares, bonds converted into shares, noncash sales, and the listing of existing issues.^b For servicing specific branches.

For large investors the Short-Term Loan underwent a slight change in its basic characteristic. The commercial banks offered this paper to big individual investors at a discount, i.e. a price yielding a higher rate of return than that obtainable on certificates purchased at source; this sometimes reached 15 per cent or more net, with the differential between it and the yield on original-issue certificates being covered by the banks. The banks did this in order to fulfill their commitments under the underwriting agreement during the period when the opportunity cost of money to banks and the general public alike was on the rise. This permitted the growth of the balance in circulation during the first three quarters of the year, with part of the certificates being held by the general public, part retained in the portfolio of the banks signatory to the agreement, and part sold to large investors at a discount.

The war and the ensuing change in monetary policy led to the termination of the underwriting agreement and the discontinuation of the banks' support in selling this paper. As a result, demand for the Short-Term Loan declined, which unquestionably would have happened at the beginning of the year were it not for this agreement. In the last three months of the year the balance plummeted by IL 400 million to stand at IL 420 million, and the downtrend grew sharper in the early months of 1974. This was in line with the trend in all nonlinked assets; however, its intensity was much greater, for this paper, as already noted, was at a disadvantage compared with the other assets as regards rate of return and also because of the policy adopted

Table XV-13
SHORT-TERM LOAN HELD BY THE PUBLIC, 1973
(IL million)

End of period ^a	Balance	Increase or decrease (-)
1972 December	748.3	
1973 January	713.7	-34.6
February	727.4	13.7
March	726.9	-0.5
April	733.4	6.5
May	755.6	22.2
June	771.1	15.5
July	788.3	17.2
August	808.3	20.2
September	818.5	10.2
October	704.1	-114.4
November	563.2	-140.9
December	420.0	-143.2

^a The end of the last week of trading in the month.
SOURCE: State Loans Administration.

by the commercial banks after the termination of the underwriting agreement of pushing time deposits at the expense of this instrument. Another contributory factor was the rising nominal yield and liquidity of linked bonds, which made them competitive with the Short-Term Loan even from the standpoint of a short-term investment.

As a result of these developments, the Short-Term Loan contributed IL 328 million to the growth of the money base during the year. Together with interest payments and the disagio, the external infusion generated thereby came to IL 401 million. This occurred entirely in the last quarter of the year, and was in line with the monetary policy aims.

5. COMPULSORY LOANS

Collection of compulsory loans from the public continued in the year reviewed, with a new loan being added after the war. Proceeds from previous loans—Defense and Savings—amounted to IL 798 million and IL 540 million respectively, while those on account of the War Loan reached IL 89 million by year's end, bringing up the total volume from IL 1,181 million in 1972 to IL 1,427 million. The increase stemmed not only from the imposition of the new loan, but also from the growth of employees' earnings and profits, the base for collections. Compulsory loans cannot be regarded as part of the primary securities market, but they do account for part of the total capital mobilized in the economy and to some extent have supplanted purchases of ordinary securities.¹³ It should be stressed that the compulsory loans collected in 1973 will not become negotiable for a number of years (the Defense and 1970 Savings Loan certificates distributed this year are also not negotiable as yet despite some attempts to make them so). Therefore they will not be able to affect the secondary securities market, as the distribution of negotiable Absorption and Defense Loan certificates did in earlier and even in the current year.

In addition to the compulsory loans, which were collected from all persons earning a taxable income and from employers, IL 160 million was collected on account of the special Defense Loan issue to banks. Together with the latter, the total volume rose from IL 1,587 million in 1972 to IL 1,310 million in 1973.

6. SECURITIES TRADED IN FOREIGN CURRENCY AND THE NATAD MARKET

The absence of expectations of an imminent devaluation of the IL, which marked the entire prewar period of 1973, had a moderating effect on activity in securities traded in foreign currency, and depressed the agio and the volume

¹³ For a more detailed discussion of how compulsory loans are treated in the analysis of the securities market see Bank of Israel, *Annual Report 1970*, p. 394.

Table XV-14
**NET PURCHASES^a OF FOREIGN SECURITIES
 OUT OF TAMAM AND NATAD FUNDS, 1971-73**
 (\$ million)

End of period	1971	1972	1973			
			Total ^b	Listed in Israel	Hollis	Listed abroad
Net purchases						
January	5.1	1.7	3.2	2.0	0.6	0.6
February	3.9	-0.1	7.7	5.8	1.2	0.7
March	0.8	-0.3	-2.3	-1.7	0.1	-0.7
April	4.6	-1.1	-2.0	-1.9	-0.2	0.1
May	3.4	7.1	2.8	1.3	0.8	0.7
June	5.2	4.4	5.4	3.2	0.7	1.5
July	5.1	4.1	3.3	1.4	0.7	1.2
August	1.9	2.6	-3.4	-1.9	-0.3	-1.2
September	2.5	0.0	1.8	0.8	1.2	-0.2
October	2.1	-0.5	0.2	0.2	0.3	-0.3
November	0.9	0.3	-1.0	-1.0	0.0	0.0
December	3.1	1.3	0.9	0.6	0.1	0.2
Total net purchases	38.6	19.5	16.6	8.8	5.2	2.6
Revaluation ^c	34.4	18.8	-27.8	-19.9	-8.1	0.2
Total increase in holdings	73.0	38.3	-11.2	-11.1	-2.9	2.8
Holdings at end of period	325.3	363.6	352.4	178.7	89.5	84.2

^a Total securities purchased, less total securities sold during the period.

^b Includes \$9.3 million differentials due to changes in foreign exchange rates.

^c The differential arising from the revaluation of the portfolio according to the prices at the end of March; does not include the increment arising from changes in foreign exchange rates.

SOURCE: Based on data on the Foreign Exchange Department, Ministry of Finance.

of such holdings, as well as the share of these assets in the economy's total financial assets portfolio.¹⁴ This continued the trend begun in 1972, but at a stronger rate. Whereas in 1972 net issues of such securities totalled IL 18.8 million, this year the figure came to -IL 158.5 million (see Table XV-1); moreover, while in 1972 the average monthly price of the Natad dollar stood above its minimum rate of IL 4.23/\$ in several months, this year (until the outbreak of war, which constituted a turning point in this respect) this did not happen in a single month, even though the rate of conversion of Tamam funds, the source of fresh money in the Natad market, was lower than in 1972.

The fact that the public did not anticipate a change in the value of the IL against the dollar in the near future was reflected in the price of both the Natad and the free-market dollar. Nevertheless, since the latter market attracts not only financial investors but other demand and supply factors as

¹⁴ By "imminent" we refer to a period which renders worthwhile, given the alternative yields on Israeli currency financial assets, an investment in securities traded in foreign currency.

Table XV-15

**NATAD AND FREE-MARKET DOLLAR RATES, NATAD BALANCES,
AND HOLDINGS OF SECURITIES TRADED IN FOREIGN CURRENCY, 1972-73**

(IL million)

End of period	1972							1973						
	Secur- ities traded in foreign cur- rency ^a	Natad bal- ances	Total	Natad dollar rate (monthly average, in IL) ^b	Agio on Natad dollar (%)	Free- market dollar rate (monthly average, in IL) ^b	Agio on free- market dollar (%)	Secur- ities traded in foreign cur- rency ^a	Natad bal- ances	Total	Natad dollar rate (monthly average, in IL) ^b	Agio on Natad dollar (%)	Free- market dollar rate (monthly average, in IL) ^b	Agio on free- market dollar (%)
January	327.0	20.8	347.8	4.23	0.7	4.42	5.2	366.9	14.3	381.2	4.23	0.7	4.56	8.6
February	326.9	18.0	344.9	4.23	0.7	4.40	4.8	374.6	15.4	390.0	4.23	0.7	4.54	8.1
March	326.6	20.0	346.6	4.23	0.7	4.37	4.0	372.2	16.6	388.8	4.23	0.7	4.44	5.7
April	325.5	19.6	345.1	4.23	0.7	4.37	4.0	342.4	15.1	357.5	4.23	0.7	4.42	5.2
May	351.4	10.1	369.5	4.23	0.7	4.39	4.5	345.2	14.9	360.1	4.23	0.7	4.39	4.5
June	355.8	17.2	373.0	4.28	1.9	4.49	6.9	350.6	14.8	365.4	4.23	0.7	4.40	4.8
July	359.9	15.8	375.7	4.33	3.1	4.45	6.0	353.9	15.9	369.8	4.23	0.7	4.42	5.2
August	362.5	15.8	370.3	4.27	1.7	4.40	4.8	350.5	16.7	367.2	4.23	0.7	4.42	5.2
September	362.5	15.3	377.8	4.23	0.7	4.40	4.8	352.3	16.2	368.5	4.23	0.7	4.50	7.1
October	362.0	15.4	377.4	4.23	0.7	4.40	4.8	352.5	19.7	372.2	4.25	1.2	4.63	10.2
November	362.3	14.9	377.2	4.23	0.7	4.42	5.2	351.5	21.7	373.2	4.33	3.1	4.75	13.1
December	363.6	16.0	379.6	4.23	0.7	4.46	6.2	352.4	24.7	377.1	4.56	8.6	4.93	17.4

^a Including revaluation increments arising from changes in foreign exchange rates and the adjustment of holdings according to prevailing market prices (in March or April).

^b Monday and Thursday averages.

SOURCE: Bank of Israel, Central Bureau of Statistics, and the Foreign Exchange Department, Ministry of Finance.

well, the agio here was higher than on the Natad dollar, averaging about 6 percent in the first nine months of the year.

The portfolio of foreign securities traded in foreign currency held by Israeli residents (including both issues of Israeli institutions and foreign securities) shrank by \$ 11.2 million. This was the net result of a \$ 27.8 million capital loss due to a decline in the prices of these securities, a \$ 9.3 million capital gain arising from foreign exchange rate changes, and a net investment of \$ 7.3 million. Natad balances rose a notch this year, further evidence of the uncertainty of their owners about the worthwhileness of investing in securities of this type.

The relative listlessness of this market, in which investors can legally deal in foreign currencies and securities, occurred in a year of drastic changes in the parities between the various foreign currencies. This reaffirms the assumption that demand for such securities in Israel stems primarily from the investor's desire to hedge himself against the erosion of the Israeli pound, and not from a desire to play the foreign exchange and foreign security markets. In this context it is important to note the differential development between this market and the demand for holding Pazak and Tamam balances (which swelled this year). It seems that even though the external value of the IL is a major determinant of demand in both markets, in the case of Natad and foreign securities short-term expectations are dominant, while as regards Tamam and Pazak, where the investor cannot pull out or reenter the market, long-run expectations are of paramount importance (though when there are very strong expectations of an imminent devaluation of the IL, demand for Pazak and Tamam is also affected). It may therefore be concluded that during the first nine months of the year investors did not anticipate an imminent devaluation of the IL, but were expecting a devaluation in the more distant future.

The October war, with all its implications in the medium and short run, changed the public's expectations, and the agio began to rise steeply, reaching 8.6 percent in December in the Natad market and 17.4 percent for the free-market dollar. This coincided with the advance in the price of bonds pegged to the exchange rate from 104 at the end of November to 113.8 at the end of December, a trend which carried over through the early part of 1974.

Figure XV-2
THE AGIO ON THE NATAD AND
FREE-MARKET DOLLAR, 1966-73
(percent)

