

CHAPTER XVI

THE SECURITY MARKET

THE NOMINAL value of new securities issued in 1957 was IL. 60.9 million.

The total amount issued in 1957 represented but 7 per cent of the economy's gross investment. The stock market did not play an important part in raising investment capital. New securities placed with the public in 1957 included only Government and Keren Hayessod bonds, the latter carrying a Government guarantee. Industry and business did not resort to the stock market for finance. Most of the new issues were linked to the dollar exchange rate or to the consumers' price index, and part thereof allowed holders tax relief. Government stock included for the first time short-dated savings bonds, which may well point to the beginning of a short-term investment market. The public also acquired other short-dated investments in 1957, apart from those offered on the stock exchange, such as bills, and speculative assets, such as postage stamps.

1. THE SCOPE OF THE STOCK MARKET

The aggregate nominal value of securities listed on the Tel Aviv Stock Exchange (so far, the only one in this country) was IL. 218.7 million¹ at the end of 1957 (see Table XVI-1), against IL. 158.4 million at the end of 1956. The share of Government and Government-guaranteed bonds rose from 81 per cent at the end of 1956 to 84 per cent in 1957. It may, therefore, be said that the Israel stock market remained largely confined to the loans of public and semi-public bodies. The share of non-Government debentures not carrying a Government guarantee fell during the period under review from 8 per cent to 7 per cent, whereas the share of equities and preference shares which, at the end of 1956, made up 11 per cent of the securities quoted on the stock exchange, was reduced to 8.5 per cent by the end of 1957.

2. BUYERS OF SECURITIES

The better part of the new securities was subscribed by institutional investors, in particular provident funds and banks. To enjoy tax relief, provident funds were required, according to the regulations promulgated in August 1957, to place a

¹ Excluding bonds of the Immigrant Housing Loan—1957 which have not yet been registered at the stock exchange.

TABLE XVI-1

*Nominal Value of Securities listed on the Tel-Aviv Stock Exchange Ltd.,
1956-1957*

<i>Type of security</i>	<i>1956</i>		<i>1957</i>	
	<i>Million IL.</i>	<i>Percentages</i>	<i>Million IL.</i>	<i>Percentages</i>
<i>Government loans</i>				
Linked bonds	48.5	30.6	87.8	40.1
Unlinked bonds	63.4	40.0	66.8	30.5
<i>Total</i>	111.9	70.7	154.6	70.7
<i>Government guaranteed loans</i>	16.3	10.3	29.6	13.5
<i>Other securities</i>				
Equities	14.6	9.2	16.0	7.3
Preference shares	2.7	1.7	2.7	1.2
Linked bonds	5.8	3.7	7.4	3.4
Unlinked bonds	7.1	4.5	8.4	3.8
<i>Total</i>	30.2	19.1	34.5	15.8
<i>Grand total</i>	158.4	100.0	218.7	100.0

SOURCE: The Tel-Aviv Stock Exchange Ltd.
Note: Discrepancies due to rounding.

certain portion of their assets in "approved investments" (meaning, primarily, securities of the type on offer in 1957). Provident funds are estimated to have subscribed about 40 per cent of the new loans, either on their own account or through their investment company. Even though balance sheets have not yet been published for 1957, the share of securities among total assets of provident funds may be expected to have increased.

Banks took up about 15 per cent of the loans issued in 1957. In a series of agreements concluded with the Ministry of Finance, they engaged to acquire approved securities¹ against a given percentage of the deposits accumulating under approved saving schemes.²

In 1957, these deposits rose by IL. 15.1 million, and securities held against them increased by IL. 6.2 million. Yet the investment portfolios of banks and credit cooperative societies increased by only IL. 3.2 million. The share of securities among the assets of banking institutions declined from 6.5 per cent to 5.8 per cent. This may be partly explained by the considerable purchases of Defence bonds by the banks in 1956—the year of the Sinai Campaign—which increased the importance of investment portfolios in their balance sheets to an ex-

¹ Government and government-guaranteed bonds, or securities enjoying tax relief according to the Encouragement of Saving Law.

² See Chapter XV, Personal Saving.

ceptional degree at the end of 1956. It is, furthermore, likely that some of the new securities taken in by banking institutions in 1957, replaced others which were sold or redeemed in the course of the year. At any rate, there are no indications that the arrangements relating to the placing of savings deposits in securities induced the banks particularly to increase their investment portfolios.

Other institutional investors, including insurance and investment companies, subscribed 5–10 per cent of the new issues.

About 15 per cent of the new loans were allocated to individuals as a premium, over and above the official rate of exchange, against foreign currency sold to the Ministry of Finance.

The part taken up by other investors (private investors not entitled to this premium) did not exceed 25 per cent of the new issues.

It may well be said that the Government is the main borrower in the domestic stock market, while institutional investors, who in practice have to place most of their assets in public bond issues, are the principal lenders.

3. SHORT-DATED SECURITIES

The new securities issued in 1957 included three series of savings bearer bonds (Immigrant Housing Savings Loan, 1957), which represented an innovation among Government securities offered till now. These are unlinked bonds, redeemable five years after their date of issue. They may, however, be returned to the Administration of State Loans before maturity, or surrendered to the Treasury in settlement of taxes or for other compulsory payments at their par value plus compound interest accumulated from the date of issue. The average interest rate varies between 3 per cent per annum after six months and about 6 per cent per annum at the end of the fifth year. The income from these savings bonds is tax-free and need not be included in income tax returns. An unusually liquid type of asset, these bonds were soon regarded as short-dated instruments, even if this was not the legislators' intention. Offers came mainly from recipients of personal restitution payments from Germany who had received them as a premium on foreign exchange sold to the Treasury (see below). Towards the end of the year, trade in these securities became rather brisk, and the premises for a short-term security market were thus set.

4. NEW BOND ISSUES

The aggregate nominal value of securities issued in 1957 was IL. 60.9 million, against IL. 45.9 million¹ in 1956. The net increase in the nominal value of securities outstanding, i.e. after the deduction of redemptions effected in 1957,

¹ Including IL.8.3 million (nominal value) Defence Loan; 1956. This amount differs from the figure published in the Bank's Annual Report for 1956.

was, therefore, IL. 54 million, against IL. 39.1 million in 1956. The following new securities were purchased by the public in 1957:

TABLE XVI-2
New Issues, 1957
(thousands of IL.)

<i>Security</i>	<i>Nominal value</i>	
<i>Defence Loan—1956</i>		
6½% registered bonds	18,250	
4¾% bearer bonds	11,750	
Premium bonds, bearer	10,000	
	40,000	
<i>Less: Bonds subscribed and fully paid in 1956</i>	8,313	31,687
<i>6% Keren Hayessod—U.J.A. 1959/68</i>		
Registered bonds	4,569	
Bearer bonds	7,931	12,500
<i>Immigrant Housing Loan—1957</i>		
6% registered bonds	142	
4½% bearer bonds	1,494	
Premium bonds, bearer	5,093	
Savings bonds, bearer	6,500	13,229
Popular Loans, premium bonds		1,498
Other securities		1,960
<i>Total</i>		60,874

(a) *Defence Loan, 1956*

The issue of the Defence Loan, 1956¹ began in the autumn of 1956, when bonds to the nominal value of IL. 27 million were underwritten by a group of financial institutions. The underwriters engaged to pay to the Ministry of Finance 20 per cent of the par value by the end of the year, the balance to be paid in monthly instalments, until August 1957. The public, too, was offered to buy these bonds on an instalment basis, against cash payment of 20 per cent of the bond value at the time of subscription. By the end of 1956, financial institutions had transferred to the Ministry of Finance the equivalent of IL.8.3 million (nominal value). Total subscriptions exceeded this amount, which represented only the equivalent of purchases fully paid. The issue of this loan was widely canvassed, the patriotic

¹ Details concerning this loan will be found in the Bank's Annual Report for 1956, pp. 395-396.

aspect of the subscription being fully emphasized. In June 1957, when the loan was first quoted on the Tel Aviv Stock Exchange, it proved to have been considered by the public as a long-term investment. Expectations that substantial quantities would be offered in particular by companies and businessmen not usually investing in securities, did not materialize.

(b) *6% Keren Hayessod—U.J.A. 1959/68*

Subscription of this loan, issued to the value of IL. 12.5 million, was opened in August 1957. This was the second loan in the series offered by the Keren Hayessod within 13 months. The first and second loans carried similar provisions, but differed in duration and interest rates. The duration of the second loan exceeds that of the first loan by two years: interest carried is $\frac{1}{2}$ per cent less than that allowed for the first issue. Both issues were underwritten by a syndicate of financial institutions. The fixing of lower interest for the second issue was prompted by the expectation that the difference between that rate and the interest on previous linked bond issues would cause the prices of the latter to move up. However, these hopes did not materialize. On the contrary, whereas the first loan was taken up by the public within a short time, several months passed until subscription of the new issue was completed. The reason for this delay was that the subscription to the new loan opened shortly after the Defence Loan had been placed, i.e. at a moment when the market was saturated and when some linked bonds were at a discount. As a result, investors preferred the older bonds to the new ones. Furthermore, the opening of this subscription coincided with that of the Immigrant Housing Loan, 1957. Also, in accordance with the instructions of the Ministry of Finance, a 20 per cent premium was granted from July 1957 on the sale of foreign currency by recipients of capital transfers¹ from abroad, received after the beginning of June 1957: this premium was accorded in the form of Government bonds. During the latter half of 1957, recipients of such transfers (mostly personal restitution payments from Germany) were assigned securities to the nominal value of IL. 8.6 million, and many of them were in a hurry to realize these securities. Bonds offered by these quarters brought prices down and attracted demand, which in turn interfered with the placing of the second issue of the Keren Hayessod loan. In this connection it may be noted that institutional investors, the most important buyers in the market, were not able to absorb the offer of the older issues, being bound by regulations to buy stock only from the underwriters and not from second hand.

(c) *Immigrant Housing Loan, 1957*

For similar reasons and because the absorptive capacity of the market is generally limited, only IL. 13.2 million (nominal value) of the Immigrant Housing

¹ Transfers deriving from inheritances, legacies, personal restitution payments etc. received in specified foreign currencies, according to the instructions of the Controller of Foreign Exchange.

Loan,¹ 1957 were placed in 1957, an amount representing about 25 per cent of the sum authorized. Most of these bonds including savings bonds to the nominal value of IL. 6.5 million were allocated to beneficiaries of personal restitution payments from Germany in accordance with the regulations outlined above. As has already been stated, a considerable portion of the savings bonds was sold by recipients of personal restitution payments in need of cash. At first, these bonds were offered at such low prices that their return, free of income tax, amounted to 15 per cent per annum. Towards the end of the year, prices moved up and the net return was about 10 per cent per annum.

5. LINKING TRENDS

The major part of the new issues were either linked Government bonds or Government-guaranteed bonds. It may be noted that in 1957, there was a reversal in the investor's attitude in those cases where he had the option to choose the link.² Whereas in the years 1955-1956, two-thirds of the new issues were linked to the consumers' price index, there was an evident trend in favour of the link to the dollar exchange rate in 1957 (see Table XV-3). Sixty per cent of all interest-bearing bonds of the Defence and the Immigrant Housing Loans, and 74 per cent of the bearer bonds (mainly purchased by investors in the higher income brackets), were linked to the dollar. It would seem that this trend reflected not only investors' expectations as to the exchange rate of the Israel pound. It equally expressed doubts whether the rise of the general price level was fully reflected in the consumers' price index.

Only the 6% Keren Hayessod-U.J.A. bonds were largely linked to the consumers' price index, because this loan was based on the index number for July 1957 (258), which was lower than the index number for any previous month in 1957, thus making the index link more attractive. The considerable weight carried by provident funds in the subscription of this issue was yet another reason. In view of the fact that wages are linked to the index, provident funds are inclined to favour this type of link also for their own assets. It is obvious that current returns on bonds linked to the index rise *pari passu* with the index. This provides an income above that secured from dollar-linked bonds as long as the official exchange rate remains unchanged.

One-eighth of the principal of the 6½% Palestine Electric Corporation 1957/64 issue, or about IL. 1.25 million (nominal value), was redeemed late in 1957. Holders of index-linked bonds enjoyed a premium of 13.3 per cent due to the link. This was the first redemption instalment of linked loan capital, and it demonstrated the advantages offered by the link.

¹ This loan is described in greater detail in Chapter XIX, The Activities of the Bank of Israel.

² The premium bonds of the Defence Loan and of the Immigrant Housing Loan are linked to the dollar exchange rate by law.

TABLE XVI-3
New Issues of Securities by Type of Link, 1957

Type of security	Linked to			
	\$ exchange rate		Consumer price index	
	Thousand IL.	Percentages	Thousand IL.	Percentages
Defence Loan—1956*				
6½% registered bonds	8,500	46.6	9,750	53.4
4¾% bearer bonds	8,750	74.5	3,000	25.5
Premium bonds, bearer	10,000	100.0	—	—
	27,250	68.1	12,750	31.9
6% Keren Hayessod—U.J.A. 1959/68				
Registered bonds	520	11.4	4,049	88.6
Bearer bonds	2,862	36.1	5,069	63.9
	3,382	27.1	9,118	72.9
Immigrant Housing Loan—1957				
6% registered bonds	105	73.9	37	26.1
4½% bearer bonds	1,055	70.6	439	29.4
Premium bonds, bearer ^b	5,093	100.0	—	—
	6,253	93.0	476	7.0
Total	36,885	62.4	22,344	37.7
Total, excluding premium bonds	21,792	49.4	22,344	50.6

* Including bonds subscribed to in 1956.

^b Linked to the dollar exchange rate by law.

6. THE AGREEMENT BETWEEN THE INSURANCE COMPANIES AND THE PALESTINE ELECTRIC CORPORATION LTD.

In 1957, a loan agreement was concluded between ten insurance companies, the Palestine Electric Corporation Ltd. and the Ministry of Finance, for the purchase by the insurance companies of P.E.C. stock to the nominal value of IL. 50 million, guaranteed by the Ministry of Finance. According to this agreement, the loan is to consist of 6% bonds, linked partly to the dollar and partly to the consumers' price index. The insurance companies are to make their subscriptions semi-annually, according to their requirements. These bonds will not be on offer to the public. Maturity dates (10, 15, 20 and 25 years from the date of issue) are staggered in accordance with the needs of the insurance companies which, in 1957, began to issue linked life-insurance policies.¹ In the past, no outlets for long-term value-linked investments had been open to these companies. The maturity dates of the bonds issued in accordance with this agreement exceed those of previous issues and thus answer the particular investment requirements

¹ See Chapter XV, Personal Saving.

of the insurance companies. The companies, for their part, undertook to place in this loan 60 per cent of their accumulating linked life insurance reserves, and not less than IL. 1 million per annum during the first five years of the agreement. This is the first important case of a direct placement in Israel, the investor buying directly from the issuing body, and not through the market. In 1957, stocks so bought by insurance companies amounted to IL. 449,550.

7. STOCK PRICE TRENDS

(a) *Linked bonds*

Linked bonds remained fairly constant during most of the year and did not depart very much from nominal prices, weakening somewhat, however, in the latter half of 1957. 3½% Tavei dollar 1959/68, which may be considered as linked bonds, strengthened almost continuously, from 72¾ at the beginning to 83¾ at the end of the year, while 4% Registered Sterling "A" Stock 1954/61 moved between 84½ (lowest price in the year) and 94½ (highest). They declined in the autumn, following rumours of an impending sterling devaluation, and stood at 89⅝ at the end of the year.

(b) *Other Government bonds*

Trade in unlinked Government bonds was fairly brisk in the second half of the year, when investors were mainly attracted by the relatively high redemption yields and the drawing prospects of some of the loans. Investors in this type of securities were thus compensated for the absence of the linking clause. Popular (premium) loans, compulsory loans, and Mandatory bearer bonds rallied and showed considerable fluctuations during the year.

(c) *Preference Shares*

No notable changes occurred in the prices of preference shares.

(d) *Equities*

As a result of the linking provisions, the rates of interest and the income tax relief attached to Government and Government-guaranteed securities, they became a competition for equity stock, the prices of which continued to drop in 1957. While the price index of linked Government bonds rose from 275 to 313 in 1957, that of equities declined from 162 to 152 (see Table XVI-4).

It was because of this competition and in view of the possibility of financing real investment with Government aid, that joint-stock companies did not appeal to the public for new capital. Apart from some bonus shares and a few minor changes in equity capital, no equity stock was issued in 1957. Generally speaking, the role of the stock market was thus limited to channelling private savings to the Government. It did not play its part as direct intermediary between entrepreneurs and capitalists.

TABLE XVI-4

*Index of Security Prices based on Quotations of Tel-Aviv Stock Exchange Ltd.,
1949-1957*

(Average 1950=100)

End of period

	Government stock and bonds linked to foreign exchange or to consumers' price index	Other debentures		Preference shares	Equities
		Government	Non- Government		
Average 1949	80.9	—	99.5	95.7	95.9
Average 1950	100.0	100.0	100.0	100.0	100.0
Average 1951	110.8	98.1	100.0	107.9	130.8
Average 1952	133.2	98.0	96.0	109.3	136.8
Average 1953	204.4	97.6	90.3	128.3	155.6
Average 1954	290.5	98.7	86.9	171.5	228.8
Average 1955	266.4	99.6	82.0	167.0	218.9
Average 1956	276.9	99.5	78.0	156.4	188.1
Average 1957	303.5	103.6	75.8	157.4	161.6
1956 December	277.2	100.2	75.2	155.5	166.9
1957 January	275.5	101.2	75.1	157.1	161.9
February	301.3	102.6	75.8	158.3	170.5
March	290.7	103.3	75.4	157.8	167.9
April	297.5	105.3	75.8	157.2	166.6
May	298.4	103.8	75.9	157.2	164.0
June	304.9	104.0	76.4	158.0	161.5
July	313.6	104.3	77.5	158.6	163.4
August	316.8	104.7	77.2	158.6	163.3
September	320.7	103.6	75.7	157.7	158.7
October	313.7	103.6	74.6	157.3	148.3
November	314.4	104.2	75.1	155.6	153.8
December	312.6	103.8	74.9	156.1	151.5

SOURCE: Central Bureau of Statistics.

It should be noted that, concurrently with these factors impeding the development of the stock market, others were at work. Owners of existing enterprises, as well as the promoters of new ventures (especially the smaller ones) were hesitant in associating themselves with capitalists who were not connected with them by family ties or who were outsiders to existing capital groups. The difficulties facing the comparatively small entrepreneur willing to raise capital through the stock market and the expenses connected therewith, as well as the fact that foreign capital flows mostly through official channels, made for even greater reliance on loan capital by entrepreneurs. Hence the reduced ratio between own funds and loan capital, and the increasing demand for bank and Government

credit. That was the reason why the Government became a partner in enterprises which, under different conditions, could have done without the help extended to them in this form.

In 1957, the Government decided in principle to adopt certain measures to increase company profits. The defence tax on company profits was eventually abolished and the maximum rates of income tax for companies were reduced. Moreover, companies will in future be allowed higher depreciation charges for tax purposes on machinery and equipment than in the past. Although these measures were evidently designed to improve company profits and consequently the shareholders' position, it may be worth noting that the market did not rally to the news and no changes occurred in the price trend of equities.