

## CHAPTER XVII

### THE SECURITY MARKET

#### 1. THE NEW ISSUE MARKET

THE NOMINAL value of securities publicly issued in 1958 was IL.78.7 million. This was IL.17.7 million more than in 1957, but the larger volume of redemptions caused the net amount of new issues to be smaller in 1958 than in the previous year—about IL.44 million, as against IL.49 million.

To gauge the quantitative importance of new issues, it is well to compare their volume with the size of capital formation in a given period of time. In 1958, net issues—after the deduction of redemption—equalled 4.8 per cent of gross investment, as against 5.6 per cent in 1957. These low proportions may partly be explained by some characteristics of the Israel economy. Here, the main sources of investment capital are not so much private savings as capital imports through Government and other public channels. Investment decisions, too, are largely made by public authorities. The Government itself invests in postal services, transportation, road construction, the erection of public buildings, etc., and the National Institutions invest in land reclamation, afforestation and new settlement. Moreover, the Government supplies considerable amounts of investment capital to the rest of the economy in the form of long-term loans and participations in the capital of public and mixed corporations. Thus, the public sector largely controls the distribution of investment funds within the economy.

Many firms prefer Government credit to other sources of capital, including the security market, chiefly for the following reasons:

(a) Private credit, including bank accommodation, consists almost exclusively of short-term advances.

(b) Since 1956, the tone of the security market has been set mainly by *debentures* "linked" to the cost-of-living index or to the official price of the dollar. At first, such bonds were issued by public bodies, and subsequently by financial institutions too. Long-term borrowing against "linked" bond issues is open to the Government and to concerns under its control, the Government always being in a position to finance the extra liability caused by the dollar or cost-of-living index "link" through taxation and other financial sources not at the disposal of private business firms. Financial institutions safeguard the stability of their bonds holders' claims by "linking" some of their own lending. But most other firms are less than keen to "link" their liabilities to the cost-

of-living index or to the dollar. However, the demand for ordinary—as distinct from “linked”—debentures declined when “linked” securities were introduced, and some potential borrowers were thus practically excluded from the market.

(c) The prospects of raising capital through new *share* issues have likewise dimmed. For several years now equity prices have been on the decline, while the prices of goods and services have gone up. This has discouraged potential investors from buying ordinary shares and, thence, no attempt was made to float new shares in the years 1957 and 1958.

(d) The attractiveness of ordinary shares as an investment has also been reduced by the tax discrimination against equity, as compared to loan, capital. The interest service on loan capital may be included among the business expenses of the borrowers, and in the case of share companies interest payments accordingly reduce the profits liable to income tax and company profit tax. But dividend payments are liable to both these taxes (which in the fiscal year 1958/59 absorbed 46 per cent of distributed net profits). Moreover, dividends are added to shareholders' other income liable to income tax at the full rate, whereas the maximum tax on interest from most “linked” debentures is at the rate of 25 per cent.

(e) The fact that most of the company shares listed on the Tel-Aviv Stock Exchange confer upon their owners only limited voting powers has also weakened the potential investors' interest in ordinary shares.

These factors have reduced both the relative importance of new issues as a means of raising investment capital, and the weight of the stock exchange in the capital market. It may also be pointed out that by reason of the higher rates of interest prevailing outside the organized market, considerable amounts have been invested in short-term credit transactions outside that market rather than in securities traded on the stock exchange or in bank deposits. In view of the interest differential, some owners of capital have preferred to lend money to borrowers whose credit requirements have not been fully satisfied by the Government and the banks, and to the Government's creditors (contractors and suppliers).

The frequent recourse to Government credit by commercial firms explains not only the negligible share of corporate stocks and bonds in the new issue market, but also the capital structure of many firms, which has been marked by an excessive proportion of loan capital to total resources.

Both in 1957 and in 1958, only loan capital was raised against new security issues, while no new equity stock was offered to the public. The largest borrowers were the Government and other public bodies, the securities of which were guaranteed by the Government. New bonds issued by the public sector in 1958 totalled IL.64.1 million, or 80 per cent of all issues. The rest—totalling IL.14.6 million—were debentures of financial institutions, led by those of the Israel Industrial Institute (which commenced operations in 1958).

Between 1956 and 1958, new issues by the Government, the National Institutions and the local authorities totalled about IL.150 million, or 80 per cent of all issues made during these years.

Purchases tended to concentrate in the hands of institutional rather than individual investors. This was mainly due to two reasons:

(a) The large portion of personal savings accumulated with provident funds and banking institutions.

(b) The regulations whereby these institutions are to invest in securities a certain part of their assets.

Financial institutions (banking institutions, provident funds, investment companies and insurance companies) are estimated to have held securities to the value of IL.155 million at the end of 1958—equivalent to about 60 per cent of all the securities listed on the stock exchange at the time.

Over two-thirds of the net issues were "linked" bonds (IL.55.3 million, as against IL.50.9 million in 1957). Other new issues consisted entirely of Government bonds, of which IL.22.4 million were savings certificates issued under the Immigrant Housing Loan, 1957.

## 2. THE STOCK EXCHANGE LIST

The nominal value of securities listed on the Tel-Aviv Stock Exchange at the end of 1958 totalled IL.255 million, as against IL.219 million at the end of 1957.<sup>1</sup> The proportion of Government and Government-guaranteed bonds rose from 84.5 per cent to 86 per cent. No change occurred in the total nominal value of ordinary and preferred shares. These made up 7.5 per cent of the list at the end of 1958, as compared with 8.7 per cent at the beginning of the year. The nominal value of "linked" debentures without Government guarantee increased from IL.7 million to IL.10 million. The nominal value of all "linked" bonds increased from IL.125 million to IL.156 million, and their weight from 57 to 61 per cent of the aggregate nominal value of the list (see Table XVII-1).

## 3. THE PRINCIPAL INVESTORS

More than half the amount of the new issues in 1958 was taken up by institutional investors.

In order to qualify for income tax exemption, provident funds have been required to invest 65 per cent of their liquid assets in so-called "authorized" securities or in "special deposits" with banking institutions. The latter have,

<sup>1</sup> This increase does not tally with the nominal value of new issues because of the time lag between the issue and the registration of new securities. Moreover, savings certificates issued under the Immigrant Housing Loan, and some other stocks and bonds, are not registered on the Stock Exchange at all.

TABLE XVII-1

*Securities Registered on the Tel-Aviv Stock Exchange, 1957-1958*  
*Nominal Values*

(millions of IL.)

(End of period)

	1957		1958	
	millions of IL.	per cent	millions of IL.	per cent
<i>Government loans</i>				
Dollar-linked	75	34.3	85	33.4
Index-linked	13	5.9	25	9.8
Other	67	30.6	73	28.6
<i>Total</i>	155	70.8	183	71.8
<i>Government-guaranteed loans</i>				
Dollar-linked	13	5.9	14	5.5
Index-linked	17	7.8	22	8.6
<i>Total</i>	30	13.7	36	14.1
<i>Other securities</i>				
Ordinary shares	16	7.3	16	6.3
Preferred shares	3	1.4	3	1.2
"Linked" bonds	7	3.2	10	3.9
Other bonds	8	3.6	7	2.7
<i>Total</i>	34	15.5	36	14.1
<i>Grand total</i>	219	100.0	255	100.0

SOURCE: The Tel-Aviv Stock Exchange Ltd.

in their turn, agreed to invest 60 per cent of their "special deposits" in "authorized" securities. Consequently, a sizable portion of the amounts annually accumulated by provident funds has been invested in such securities. The above regulations and the agreements concluded by the banks with the Treasury specify that "authorized" securities must be purchased directly from the issuing body or from the underwriters, and not in the secondary market. This tends to accelerate the absorption of new issues. The new arrangements came into force in 1958, and subsequently provident funds began to step up their security purchases so as to adjust their assets structure. Provident funds, together with their joint investment company, bought an estimated IL.23 million worth of new securities in 1958—i.e., about 30 per cent of all new issues. Banking institutions, in addition, acquired securities to the tune of IL.2.3 million, against the "special deposits" held on account of provident funds.

In 1958, banks and credit co-operative societies expanded their securities portfolios by IL.19.3 million,<sup>1</sup> bringing their total value up to IL.63.9 million. The increase, which was six times as large in 1958 as in 1957 (IL.3.2 million) may be attributed chiefly to the considerable expansion of the approved saving schemes operated by these institutions<sup>2</sup> and to the introduction of "special deposits". As already stated, banks have been required to invest in new securities 60 per cent of the provident funds' "special deposits," and a similar percentage of the amounts accumulated under their own saving schemes. On the latter account, banking institutions invested IL.14.5 million in new securities, besides the additional IL.2.3 million carried against "special deposits". The proportion of securities within the total assets of banking institutions rose, therefore, from 5.1 per cent<sup>3</sup> at the end of 1957 to 5.8 per cent at the end of 1958.

New securities purchased by banking institutions represented about 25 per cent of the total value of new issues in 1958. Private persons acquired some 45 per cent. Some 27 per cent thereof (IL.21.5 million) represented premiums granted, in the shape of savings bonds, to sellers of foreign currency to the Treasury, as against 14 per cent (IL.8.6 per million) in 1957.<sup>4</sup> That is to say, about half of the new Government securities issued in 1958 went as a premium to recipients of foreign currency remittances. A line must obviously be drawn between these securities and the others here discussed, not only in view of their particular mode of issue, but also because the bonds in question are redeemable half a year after their issue and may, therefore, be regarded in fact as short-term securities. Most of these certificates were indeed presented for redemption within six months of their issue.

The nominal value of securities purchased by individuals, apart from the premium mentioned above, may be estimated at IL.15 million, or less than 20 per cent of the total value of new issues in 1958. A similar amount was subscribed by individuals in 1957, when, however, these purchases accounted for 25 per cent of the total value of new issues.

#### 4. SHORT-DATED SECURITIES

In the absence of other short-term securities on the stock market, savings certificates of the Immigrant Housing Loan served as a substitute for them. These certificates are definitely redeemable five years after their date of issue, but six months after their issue they may be surrendered to the Administration of State Loans or presented to the Treasury, in settlement of taxes or

<sup>1</sup> Excluding securities of subsidiary companies.

<sup>2</sup> See Chapter XVI—"Personal Saving."

<sup>3</sup> Revised figure.

<sup>4</sup> The granting of such premiums began in the middle of 1957.

other compulsory payments. In both cases, they are accepted at par plus accrued interest.

In 1957 and 1958, about IL.29 million worth of such savings certificates were issued. Most of them were allotted as premiums to individual persons, against foreign currency.<sup>1</sup> In accordance with the terms already referred to, IL.18.6 million worth of these certificates could have been presented to the Administration of State Loans. In fact, IL.17.6 million were so redeemed. Some of these certificates passed hands several times before redemption, their owners, in need of cash, having sold them on the market at a discount. Second-hand holders, as a result, derived from them a yield of about 7 to 10 per cent per annum, according to the conditions of supply and demand prevailing at the time of the transaction. These certificates are traded over the counter and on the Stock Exchange, although they are not officially listed. In 1958, trade in them was brisk, their monthly turnover on the Stock Exchange exceeding at times IL.700,000.

In 1958, considerable amounts were also invested by individuals in promissory notes and bills which are not traded on the Stock Exchange at all, such as claims originating from clearing accounts with the Accountant General, and Jewish Agency bills. In one of the leading banks, the annual turnover in these documents reached IL.7.7 million. In the absence of statistics, this figure may serve to indicate the scope of transactions in this sphere. It clearly reflects the existence of a demand for short-dated securities.

## 5. DESCRIPTION OF THE NEW ISSUES

The bonds issued in 1958 were similar in respect of interest, "linkage" and redemption terms to those issued in 1957, but differed in one respect: Whereas the 1957 issues were Government loans and Government-guaranteed loans of other public bodies (Keren Hayessod-U.J.A.), the ones floated in 1958 included also debentures of financial institutions, some of which, for the first time in several years, offered new bonds without a Government guarantee.

Table XVII-2 gives a list of the debentures issued in 1958.

### (a) *Government loans*

The floating of the Immigrant Housing Loan, 1957, which had begun in the second half of 1957, continued in 1958. In the latter year, IL.20.8 million worth of "linked" bonds and IL.22.4 million worth of savings certificates were issued. The latter were, for the most part, allotted as premiums to the recipients of foreign currency remittances, against the sale of foreign

<sup>1</sup> The nominal value of savings certificates issued in 1958 amounted to IL.22.4 million, of which IL.20.3 million were granted as premium to the recipients of foreign currency remittances.

TABLE XVII-2

*New Issues, 1958*  
(thousands of IL.)

<i>Security</i>	<i>Nominal value</i>	
<i>Government Loans</i>		
Immigrant Housing Loan, 1957		
6% Registered bonds	13,600.5	
4½% Bearer bonds	7,157.0	
Saving certificates (bearer)	22,423.0	
Popular Loan premium bonds	952.0	44,132.5
<i>Government-guaranteed Loans</i>		
6% Keren Hayessod-U.J.A., 1959/68 (series 3)		
(registered)	3,320.0	
(bearer)	9,180.0	
	12,500.0	
6% Local Authorities, 1960/69 (series 2)		
Registered bonds	3,013.6	
Bearer bonds	4,486.4	
	7,500.0	20,000.0
<i>Other loans</i>		
6½% General Mortgage Bank Ltd, 1961/68 (series 1)		
Debentures (bearer)	3,000.0	
6 %Bank Leumi Investment Co. Ltd., 1961/70		
(series 12)		
Debentures (registered)	1,800.0	
Debentures (bearer)	1,200.0	
	3,000.0	
6½% G.U.S.-Rassco Ltd., 1961/68		
Debentures (bearer)	200.0	
6% The Israel Industrial Institute, Ltd., 1960/69		
(registered) — subscribed	5,483	
(bearer)—subscribed	9,517	
	15,000	
Paid-up as at the end of 1958	8,372.5	14,572.5
<i>Total</i>		78,705.0

currency to the Treasury. Such persons were also allotted premium bonds to the nominal value of IL.724,000, issued within the framework of the same loan. At the same time, the Administration of State Loans took in premium bonds totalling IL.935,000 in exchange for other securities.

Other Government securities issued in 1958 were Popular Loan premium bonds. Their par value totalled approximately IL.1 million, a third of which were allotted as premiums to individual persons against the surrender of foreign currency.

(b) *Government-guaranteed loans*

The Government guaranteed two loans in 1958, one issued by the Palestine Foundation Fund (Keren Hayessod-U.J.A.) and the other jointly by the local authorities. These totalled IL.20 million and represented additional series of earlier issues. Both loans were "linked" to the dollar or to the cost-of-living index, at the buyers' option.

(c) *Loans of financial institutions*

Four financial institutions raised new loan capital through the issue of debentures in 1958. These issues resemble each other in most respects, but two of them carry (nominal) interest at the rate of 6 per cent per annum, and the other two at 6½ per cent. Maturities range from ten to twelve years, the redemption being effected in eight to ten annual instalments. In three cases, the principal and interest were "linked" to the dollar and in one case, the buyers were given the choice of "linkage" to the cost-of-living index or to the dollar. All four loans were approved under the Law for the Encouragement of Saving, and the interest on them is therefore subject to a maximum income tax at the rate of 25 per cent. The objects of the loans were various projects of public interest. Thus, the IL.3 million loan of the General Mortgage Bank was intended to finance housing schemes sponsored by the Ministry of Labour. The IL.3 million loan of the Bank Leumi Investment Company was intended partly to finance the construction of the underground railway now being built in Haifa and of a water reservoir in Jerusalem. The IL.15 million loan of the Israel Industrial Institute was earmarked for accommodation to industrial firms for purposes approved and on terms laid down by the Government.<sup>1</sup>

<sup>1</sup> The Government has undertaken to compensate the Institute for losses that may be incurred in case such credits are only partially linked, i.e., when the terms of "linkage" differ from the "linkage" of the debentures in question, which are fully linked.



## 6. DOLLAR *versus* INDEX "LINK"

The practice of "linking" long-term financial debts to the official price of the dollar or to the cost-of-living index has become widespread in the last few years. Its purpose is to guarantee, as far as possible, the real value of savings invested in financial assets.

In 1958, all securities newly issued, with the exception of savings certificates and Popular Loans, were "linked" to the dollar or to the cost-of-living index. Bonds to the amount of IL.29 million (nominal value) were "linked" to the dollar; and bonds to the amount of IL.26 million were "linked" to the index. Some of the loans were "linked" *a priori* to the dollar. The others were "linked" in accordance with the buyers' wishes. Trends were not uniform. On the average, 47 per cent of the latter type were linked to the dollar and 53 per cent to the cost-of-living index. However, as shown in Table XVII-3, there were con-

TABLE XVII-3  
*New Issues, by Types of "Linkage," 1958*  
(thousands of IL.)

Name of Loan (shortened)	Type	Dollar		Index	
		thousands of IL.	per cent	thousands of IL.	per cent
Keren Hayessod, series 3	Registered	283.5	8.5	3,036.5	91.5
Housing, series B	Bearer	36.0	11.0	290.2	89.0
Housing, series C	Registered	894.6	16.8	4,444.6	83.2
Housing, series A	Registered	604.9	27.8	1,569.1	72.2
Housing, series B	Registered	1,397.8	29.9	3,276.0	70.1
Keren Hayessod, series 3	Bearer	2,972.6	32.4	6,207.4	67.6
Local Authorities, series 2	Registered	988.6	32.8	2,025.0	67.2
Housing, series A	Bearer	791.5	58.6	559.1	41.4
Housing, series C	Bearer	1,573.2	59.1	1,087.6	40.9
Housing, series D	Registered	930.7	65.8	482.8	34.2
Industrial Institute <sup>a</sup>	Bearer	6,522.2	77.9	1,850.3	22.1
	Registered				
Local Authorities, series 2	Bearer	3,521.6	78.5	964.8	21.5
Housing, series D	Bearer	2,628.2	93.2	191.2	6.8
6½% Mortgage Bank, series 1	Bearer	3,000.0	100.0	—	—
6% Bank Leumi Invest. Co.	Bearer	1,200	100.0	—	—
	Registered	1,800	100.0	—	—
G.U.S.—Rassco, 1961/68	Bearer	200.0	100.0	—	—
<i>Total</i>		29,345.4	53.0	25,984.6	47.0
<i>Total (excluding bonds "linked" to the dollar only)</i>		23,145.4	47.1	25,984.6	52.9

*General note:* Loans are arranged in an ascending order of the percentage of dollar "linked" bonds.

<sup>a</sup> The loan was issued as dollar-linked, but subscribers were accorded the right to convert their debentures into index-linked bonds up to the 20th April, 1959.

siderable differences between the various loans as regards the breakdown by the two types of "linkage."

At the beginning of 1958, investors preferred to "link" their bonds to the cost-of-living index, but the tendency changed in the middle of the year, and towards the end of the year there was observed a marked preference for the dollar "link." This shift may partly be due to the exclusion of the "fruit and vegetables" item from among the components of the index published monthly by the Government. There ensued a certain lack of orientation concerning the payment of principal and interest on loans linked to the cost-of-living index, which may have caused the public to refrain from index-linked investments. However, the main reasons for the overwhelming demand for dollar-linked securities at the end of 1958 were the monetary developments in Western Europe (the devaluation of the French franc and the steps towards convertibility in most West European countries) as well as the expectations with regard to economic developments in Israel.

The "link" to the cost-of-living index was mainly preferred by institutional investors, and especially by provident and pension funds, the reason being that wages are also "linked" to the index, and that some of the liabilities of these funds are dependent on the wage level, too.

Between 1955 and 1958, there were considerable fluctuations in the preference for one type of "link" over the other. In 1955 and 1956, some two-thirds of the "linked" loans issued were "linked" to the cost-of-living index. In 1957, there was a preference for the dollar "link." In the first half of 1958, the index "link" was again the more popular—in contrast with the last six months of the year.

## 7. SECURITY PRICES

There were no uniform trends in security prices in 1958. This is illustrated by the indices (Tables XVII-4 and XVII-5). The dull note which prevailed in the latter half of 1957, continued during the first three months of 1958. In May, security prices recovered a little, following the introduction of measures designed to achieve this end. At the end of the summer, this trend came to a halt, at least as regards index-linked debentures, which—after having temporarily risen above their "adjusted" par level<sup>1</sup>—again fell a few points beneath it. As already stated, this decline might be due—at least partly—to the exclusion of the "fruit and vegetables" item from the monthly calculation of the cost-of-living index. Dollar-linked bonds remained firm, and improved considerably in December 1958.

<sup>1</sup> The face value *plus* accumulated interest and the increment due to the "linkage" conditions.

Ordinary shares fluctuated little throughout the year and their level was much the same at the year's end as at its beginning.

TABLE XVII-4  
*Index of Security Prices, 1956-1958*  
 (Base: 1958 average=100)

	<i>"Linked" bonds</i>		<i>Other Government bonds</i>	<i>Other bonds</i>	<i>Ordinary shares</i>	<i>Preferred shares</i>
	<i>dollar</i>	<i>index</i>				
1956, Average	91.95	87.30	96.2	101.0	127.1	101.0
1957, Average	96.22	93.43	100.1	99.6	109.3	101.6
1958, Average	100.00	100.00	100.0	100.0	100.0	100.0
1958 January	96.11	95.71	101.0	98.8	99.7	100.2
February	97.28	96.55	100.2	98.7	100.1	99.7
March	97.21	97.09	100.5	98.3	96.8	99.0
April	97.30	96.37	99.8	98.6	96.9	98.8
May	100.34	97.55	99.6	98.4	98.6	99.7
June	102.62	99.99	100.8	101.0	104.7	99.9
July	102.37	100.52	100.2	101.3	101.4	99.9
August	103.12	102.45	100.0	101.6	101.2	100.5
September	102.52	102.46	99.3	101.3	100.5	100.5
October	101.18	103.08	99.7	101.4	99.7	100.0
November	100.26	101.71	98.8	100.5	98.8	101.0
December	99.62	106.55	98.8	100.4	100.3	100.7

SOURCE: Central Bureau of Statistics (provisional figures).

The prices of Government (other than "linked") bonds declined somewhat. No serious changes were registered in the quotations of other securities.

At the beginning of the year, the Minister of Finance appointed a committee comprising officials of the Treasury, the Bank of Israel and commercial bankers, to investigate and make recommendations with a view to expanding the security market. The committee made itself felt on the stock exchange through technical recommendations aimed at improving the price level of securities. The time table for new issues, as well as their volume, were carefully planned. In accordance with the committee's recommendation, two of the new loans issued in the first half of the year were offered to financial institutions only, thus preventing pressure on the prices of existing securities. Furthermore, financial institutions required by law to invest part of their assets in "authorized" securities were allowed to purchase such securities on the stock exchange, whereas previously they had been obliged to acquire them in the new issue market. In return, these institutions undertook not to sell securities on the market, as long as this facility was extended to them. The new arrange-

ment increased the demand for existing "linked" bonds, and the resultant higher quotations apparently encouraged other investors, too, to put their money into securities.

TABLE XVII-5  
*Prices of "Linked" Bonds, 1956-1958*  
*(Adjusted par value<sup>a</sup>=100)*

	<i>Index linked<sup>b</sup></i>	<i>Dollar linked<sup>c</sup></i>
1956, Average	99.38	102.63
1957, Average	97.55	100.28
1958, Average	97.97	100.40
1958 January	96.69	97.62
February	96.00	97.70
March	95.35	97.22
April	95.32	96.91
May	97.13	98.97
June	98.13	100.54
July	101.53	101.44
August	101.21	101.67
September	100.55	101.74
October	98.76	103.30
November	97.46	101.06
December	97.52	106.66

<sup>a</sup> *Adjusted par value*: The face value plus accumulated interest and the increment due to "linkage" terms.

<sup>b</sup> As from July 1958, the item "fruit and vegetables" was excluded from the cost-of-living index published monthly by the Central Bureau of Statistics. For the computation of this index, the cost-of-living index was temporarily adjusted.

<sup>c</sup> Including only securities the purchasers of which had the option to link their holdings either to the cost-of-living index or to the dollar.

SOURCE: Central Bureau of Statistics (provisional figures).