

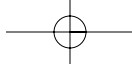
Major Provisions of the Budget, Fiscal year 2001

**STATE BUDGET
PROPOSAL FOR FISCAL YEAR
2001**

MAJOR PROVISIONS OF THE BUDGET

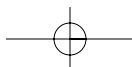
Jerusalem

October 2000



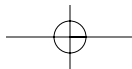
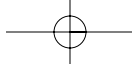
To the Reader,

This publication summarizes the major provisions of the 2001 budget proposal. Additional material related to the government activities can be found in detailed books of this budget proposal.



Major Provisions of the Budget, Fiscal year 2001**CONTENTS**

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Major Provisions of the Budget, Fiscal year 2001

PART A

**BUDGET LAW
FOR FISCAL YEAR 2001**

Budget Bill for Fiscal Year 2001

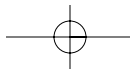
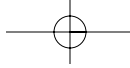
Budget Proposal for Fiscal Year 2001 and First Appendix (Condensed)

Forecast of State Revenues and Borrowing in Fiscal Year 2001

Forecast of State Revenues not Collected on account of Tax Benefits, 2001

Budget Proposal for Fiscal Year 2001: Government Enterprises

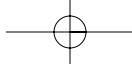
(Second Appendix, Condensed)



Major Provisions of the Budget, Fiscal year 2001

BUDGET BILL FOR FISCAL YEAR 2000–2001

- Definitions**
1. In this bill:
 - “**Budget item**”: a sum of money or a number of salaried positions appearing on a title line underlined with a double broken line;
 - “**Area of activity**”: a sum of money or number of salaried positions appearing on a title line underlined with a single broken line;
 - “**Program**”: a sum of money or number of salaried positions appearing on a line with no special marking;
 - “**Fiscal Year 2001**”: the year beginning on January 1, 2001, and ending on December 31, 2001;
 - Any other term**: as defined in the Foundations of the Budget Law, 1985 (hereinafter: Foundations of the Budget Law).
- The Expenditure Budget and Its Apportionment**
2. The Government is authorized to spend NIS 245,813,318,000 in Fiscal Year 2001. The apportionment of this sum or any part thereof into budget items, areas of activity, and programs is as spelled out in the first column of the First Appendix, that headed “Expenditure.”
- Revenue-Dependent Expenditure Budget**
3. In addition to the sum the Government is entitled to spend under Paragraph 2, it is entitled to spend NIS 12,116,726,000 in Fiscal Year 2001 as revenue-dependent expenditure. The apportionment of this sum or any part thereof into budget items, areas of activity, and programs is as spelled out in the second column of the First Appendix, that headed “Revenue-Dependent Expenditure.”
- Personnel Ceilings**
4. The Government is entitled to fill 55,080 salaried positions in Fiscal Year 2001. The apportionment of this number or any part thereof into budget items, areas of activity, and programs, is as spelled out in the fourth column of the First Appendix, that headed “Personnel Ceilings.”
- Government Enterprise Budget**
5. a. In addition to the sums shown in Paragraphs 2 and 3 above, the Government is entitled to spend in Fiscal Year 2001 the sums listed in the first column of the second section of the Second Appendix (hereinafter: “Government Enterprise Budget”). The apportionment of these sums into budget items, areas of activity, and programs is as shown in that section.



The Budget Documents

- b. In addition to the number of salaried positions that the Government is entitled to fill in Fiscal Year 2001 under Paragraph 4 of the foregoing, the Government may fill 17,183 salaried positions in Government enterprises. The apportionment of these positions into budget items, areas of activity, and programs is as shown in the third column of the second section of the Government Enterprise Budget.
- c. The forecast of revenues to be used to cover the Government Enterprise Budget in Fiscal Year 2001 is as shown in the first section of the Second Appendix.

Provisions Concerning Specific Budget Items

6. In Fiscal Year 2001:

- a. Pursuant to the Government proposal, the budget in Item 17 will be apportioned into areas of activity and programs by a joint subcommittee of the Knesset Finance Committee and the Foreign Affairs and Defense Committee.
- b. At the request of the Minister of Finance concerning use of the General Reserve under Paragraph 12 of the Foundations of the Budget Law for a purpose falling within the purview of the Office of the Prime Minister, the aforementioned subcommittee will be replaced by a special subcommittee appointed by and composed of members of the Knesset Foreign Affairs and Defense Committee.

Loan from the Bank of Israel

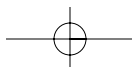
- 7. The sum borrowed from the Bank of Israel in Fiscal Year 2001 for the purpose of repaying government debts to the Bank of Israel will not exceed NIS 1,050,000,000, as stipulated in Paragraph 48(b) of the Foundations of the Budget Law.

Effective Date

- 8. This law goes into effect on Tevet 6, 5761 (January 1, 2001).

Gazetting

- 9. This law shall be gazetted in Reshumot within three months of the date of its enactment.



Major Provisions of the Budget, Fiscal year 2001

Budget Proposal for Fiscal Year 2001 (NIS Thousands)

First Appendix (Condensed)	Expenditure	Revenue- Dependent Expenditure	Spending Authorization	Personnel Ceiling
Grand total	245,813,318	12,116,726	68,468,440	55,080.0
Part A: Regular Budget	174,902,700	10,270,713	53,674,202	55,080.0
Part B: Development Budget and Capital Account	69,860,618	1,846,013	14,794,238	
Part C: Repayment of debts to Bank of Israel	1,050,000			
Part A: Regular Budget	174,902,700	10,270,713	53,674,202	55,080.0
Governance and Administration	17,140,428	1,248,491	2,791,749	33,355.0
01 President of the State	24,081	191		43.5
02 The Knesset	263,896	135		374.0
03 Members of the Government	17,355			
04 Office of the Prime Minister	540,173	12,130	43,414	914.5
05 Ministry of Finance	1,334,617	148,025	9,347	5,444.0
06 Ministry of the Interior	344,857	16,834	56,200	745.5
07 Ministry of Internal Security	5,590,937	356,054	1,728,722	20,842.0
08 Ministry of Justice and Religious Affairs	1,624,351	485,989	771,832	3,172.0
09 Ministry of Foreign Affairs	1,088,348	94,909		1,024.0
11 Office of the State Comptroller (*)	143,385			516.0
12 Pensions and Compensation	4,749,493			
13 Miscellaneous expenses	317,815	94,877	70,449	
14 Funding of political parties	157,676			
19 Ministry of Science, Culture, and Sports	722,050	23,178	96,625	86.0
26 Ministry of the Environment	221,394	16,169	15,160	193.5
Defense	37,504,331	4,528,417	39,766,321	2,130.0
15 Ministry of Defense	37,117,015	4,375,000	39,500,000	1,904.5
16 Civilian emergency expenditure	258,783		238,680	
17 Coordination of operations in the territories	128,533	153,417	27,641	225.5
18 Local authorities	4,317,775			

* By law, the State Comptroller's budget is determined by the Knesset Finance committee and is published separately. The figures presented here are shown for information purposes only.

The Budget Documents

Budget Proposal for Fiscal Year 2001 (Continued)

(NIS Thousands)

	First Appendix (Condensed)	Expenditure	Revenue-Dependent Expenditure	Spending Authorization	Personnel Ceiling
	Social Services	73,517,359	3,471,592	2,357,676	14,938.0
20	Ministry of Education	23,351,320	1,008,923	1,326,604	1,871.0
21	Higher Education	5,319,359			
23	Ministry of Labor and Social Affairs	4,026,617	959,163	117,983	3,527.0
27	Transfers to National Insurance	21,115,730			
24	Ministry of Health	12,720,863	1,429,256	11,811	8,429.5
25	Benefits for the disabled	1,547,384	1,803		49.5
29	Ministry of Housing and Construction	268,723	10,758		677.0
30	Ministry of Immigrant Absorption	2,039,603	60,289	632,174	363.0
32	Basic commodity and farm produce subsidies	2,416,528	1,400	269,104	
46	Demobilized Soldiers Law	708,816			21.0
56	Equality of Rights for Persons with Disabilities Commission	2,416			
	Economy and Administration	9,179,445	1,022,213	4,342,749	3,657.0
33	Ministry of Agriculture	1,150,485	185,942	214,171	1,370.0
34	Ministry of National Infrastructures	213,466	4,969		294.5
31	Fuel system expenditure	109,048			
35	Atomic Energy Commission	147,985			
36	Ministry of Industry and Trade	154,792	23,253		469.5
37	Ministry of Tourism	528,619	8,252	381,852	168.5
38	Support for nondwelling industries	2,299,784	631,829	3,293,832	
39	Ministry of Communications	61,467	239	8,000	98.0
40	Ministry of Transport	366,243	88,747		992.5
42	Construction and housing grants	3,583,410	53,260		
43	Survey of Israel	73,706	25,622	7,588	259.0
28	Maintenance of interurban roads	427,960		437,306	
54	Regulatory authorities	62,480	100		5.0
44	Credit subsidies	38,621			
45	Interest and commission payment	28,569,674			
	Reserves	4,635,067		4,415,707	1,000.0
47	General reserve	4,635,067		4,415,707	1,000.0

Major Provisions of the Budget, Fiscal year 2001

Budget Proposal for Fiscal Year 2001 (Continued)

(NIS Thousands)

First Appendix (Condensed)	Expenditure	Revenue-Dependent Expenditure	Spending Authorization	Personnel Ceiling
Part B: Development Budget and Capital Acct.	69,860,618	1,846,013	14,794,238	
=====	=====	=====	=====	
Development Budget	13,163,784	1,846,013	14,794,238	
Governance and Administration Investment	552,425	362,533	815,759	
=====	=====	=====	=====	
51 Government buildings	45,037	225,424	154,892	
52 Police and prisons	204,394	123,051	462,295	
53 Courts	209,695	703	100,339	
55 Treasury	93,299	13,355	98,233	
57 Local Authorities	542,234		567,734	
=====	=====		=====	
Social Service Investment	6,219,926	1,160,983	7,391,571	
=====	=====	=====	=====	
60 Education	699,126		978,401	
67 Health	379,965	86,658	269,940	
70 Housing	5,140,835	1,074,325	6,143,230	
Nondwelling Industry Investments	5,849,199	322,497	6,019,174	
=====	=====	=====	=====	
72 Agriculture	11,701	9,608	18,298	
73 Water system	808,912		762,393	
76 Development of industry	107,718	169,789	234,477	
78 Tourism	146,994	1,276	173,239	
79 Transport	3,405,664	69,014	3,502,173	
83 Miscellaneous development expenses	1,368,210	72,810	1,328,594	
84 Payback of debts	56,696,834			
=====	=====			
Part C: Payback of debts to Bank of Israel	1,050,000			
=====	=====			
99 Interest to Bank of Israel	500,000			
Principal to Bank of Israel	550,000			

The Budget Documents

Forecast of State Revenues and Borrowing in Fiscal Year 2001 (NIS Thousands)

2001 Budget Proposal		
1.	Grand Total	245,813,318
	=====	=====
Part A:	Current revenues	174,902,700
Part B:	Revenues from borrowing and capital account	69,860,618
Part C:	Revenues from Bank of Israel	1,050,000
Part A:	Current Revenues	174,902,700
	-----	-----
	Taxes and compulsory payments	153,920,000
	-----	-----
	Income and property taxes	86,300,000
	-----	-----
001	Income tax	73,300,000
002	Value Added Tax on NPOs and financial institutions	7,450,000
003	Land betterment tax	1,300,000
004	Real-estate purchase tax	2,500,000
005	Property and sales tax	50,000
007	Payroll tax	1,700,000
	Taxes on expenditure	67,620,000
	-----	-----
011	Customs and import levies	1,600,000
012	Value Added Tax, including defense imports	43,720,000
013	Purchase tax	9,800,000
015	Excise	950,000
018	Fuel tax	6,100,000
020	Stamp tax	1,150,000
024	Motor vehicle fees	2,365,000
025	Other fees and licenses	1,935,000

Major Provisions of the Budget, Fiscal year 2001

Forecast of State Revenues and Borrowing in Fiscal Year 2001 (Continued) (NIS Thousands)

2001 Budget Proposal		
	Interest and earnings	2,711,496
	=====	=====
034	Foreign-exchange interest	145,844
035	Domestic-currency interest	2,565,652
	Royalties	1,131,000
	-----	=====
042	Royalties from business enterprises	1,000
043	Royalties on natural resources	100,000
044	Royalties from government companies	530,000
045	Dividends from government companies	500,000
	Miscellaneous revenues	3,272,087
	-----	=====
046	Reimbursements on account of previous years' budgets	100,000
047	Revenues from miscellaneous services	2,634,347
050	Use fees for government properties	157,740
048	Earmarked revenue in excess of estimate	380,000
	Transfer from Part B	13,868,117
	-----	=====
Part B:	Revenues from Loans and Capital Account	69,860,618
	-----	-----
	Payback on account of Government investments and loans	7,789,526
	-----	-----
051	Collection of principal	6,614,000
053	Collection of principal in foreign exchange	70,266
076	Revenue from sale of state land	1,105,260
	Pension and severance-pay provisions	45,104
	-----	-----
071	Provisions by economic units	11,275
072	Provisions by government enterprises	11,275
073	Pension provisions-companies	22,554

The Budget Documents

Forecast of State Revenues and Borrowing in Fiscal Year 2001 (Continued) (NIS Thousands)

2001 Budget Proposal		
	Capital gains	3,000,000
	-----	-----
075	Sale of companies and banks	3,000,000
	Domestic borrowing	51,168,843
	-----	-----
081	Loans from National Insurance Institute	6,833,644
082	Income from issues and deposits	44,335,199
	Loans and grants from overseas	21,725,262
	-----	-----
900	Israel Bonds	4,205,000
901	Less distribution expenses	-210,000
	Loans and grants from the U.S.:	
902	– Defense assistance	8,475,000
904	– Civilian assistance	2,991,000
907	– Other loans	4,150,000
908	Bank loans	2,114,262
	Transfer to Part A	-13,868,117
	-----	-----
Part C:	Revenues from the Bank of Israel	1,050,000
	=====	=====
	Advance for financing of debt to Bank of Israel	1,050,000

Major Provisions of the Budget, Fiscal year 2001

Estimate of Tax Benefits* in 2001

(NIS Millions, 2001 Budget Prices)

Total	28,210		
1. Income Tax Division	25,010		
a. Factor benefits	1,400		
1. Encouragement of Capital Investments Law		1,180	
– General			150
– Nonresident investors			230
– Alternative track			800
2. R&D, oil exploration, and films		50	
3. Credit for shift labor		170	
b. Capital market benefits	17,310		
1. Provident funds, net		6,500	
– Benefits at point of deposit			7,600
– Taxation at point of withdrawal			-1,100
2. Advanced-training funds		2,300	
3. Interest income on indexed assets		5,100	
4. Interest income on unindexed assets		2,000	
5. Capital gains on the stock exchange		1,400	
6. Exemption on redemption of share in cooperative association		10	
7. Tax deferral on distribution of warrants to workers		–	
c. Social welfare and population dispersion	3,830		
1. Income-tax exemption for nonprofit organizations			
2. Exemption for Ministry of Defense allowances		250	
3. Exemption for National Insurance allowances		2,040	
– Child allowances			1,500
– Old-age and survivors' benefits			420
– Other Benefits			120

* State revenues not collected as a result of tax benefits extended.

The Budget Documents

Estimate of Tax Benefits* in 2001

(NIS Millions, 2001 Budget Prices)

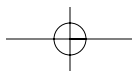
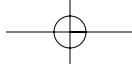
4. New-immigrant credit		80
5. Medical-expense credit		20
6. Special welfare credit		50
7. Charitable donations credit		120
8. Benefits for blind and disabled		330
9. Credit for development-area residents		880
10. Credit for employers in Eilat		60
d. Family benefits		
(excl. child-allowance exemption)	1,740	
1. Credit for single-parent families		40
2. Half credit-point for women		400
3. Credit for children (including single-parent families)		700
4. Credit for non-working spouse		600
e. Miscellaneous income-tax benefits	350	
1. Gambling income exemption		100
2. Exemption for letting of dwelling		200
3. Demobilized soldiers		50
f. Real-estate tax benefits	380	
1. Real-estate purchase tax reductions		60
2. Land-betterment tax exemption for dwelling		0
3. Limited land-betterment tax for historical properties		320
2. Customs and VAT Division	3,080	
a. Customs and purchase tax	880	
1. New immigrants		200
2. Returning Israelis		50
3. Israeli tourists		130
4. Motor-vehicle accessories (air bags and ABS)		200
5. Conditional exemptions		300
b. Value Added Tax	2,200	
1. Fruit and vegetables		1,350
2. Tourism services		700
3. Eilat Law		150
3. Fees	120	

* State revenues not collected as a result of tax benefits extended.

Major Provisions of the Budget, Fiscal year 2001

Government Enterprises – Budget Proposal for Fiscal Year 2001 (NIS Thousands)

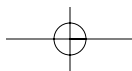
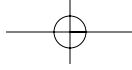
Second Appendix (condensed)	Income Expenditure	Spending Authorization	Personnel Ceiling
Total income	10,429,822		
=====	=====		
89 Finance Ministry and Prime Minister's Office enterprises	275,279		
94 Government hospitals	4,680,652		
95 Jaffa and Hadera Ports	30,619		
96 Postal Bank	196,574		
98 Israel Lands Administration	5,246,698		
Total expenditure	10,429,822	431,220	17,183.0
=====	=====	=====	=====
89 Finance Ministry and Prime Minister's Office enterprises	275,279		113.0
94 Government hospitals	4,680,652		16,570.5
95 Jaffa and Hadera Ports	30,619		3.0
96 Postal Bank	196,574		4.0
98 Israel Lands Administration	5,246,698	431,220	492.5



Major Provisions of the Budget, Fiscal year 2001

PART B

GENERAL REVIEW



2001 BUDGET POLICY

Size of the Budget

- The State Budget for 2001 is **NIS 245.8 billion**.
- The budget, including revenue-dependent expenditure, is **NIS 257.9 billion**.
- Expenditure not including servicing of debt (principal) is **NIS 205.6 billion**.
- Budget expenditure will be equal to **43.8 percent** of the projected Gross Domestic Product.

Budget Goals

The main goal of the 2001 Budget Proposal is to support the rapid growth that the Israeli economy has displayed in the past six quarters, in order to transform it into sustainable growth that will fulfill the economy's growth potential for many years.

Economic growth is the only way to ensure a continued decline in unemployment and a steady upturn in employment. The acceleration of growth is being powered by the business sector and, especially, by exports. However, long-term sustainability will occur only if the correct economic conditions are preserved; otherwise, the growth rate may subside rather quickly. An essential condition for sustainable growth, driven by the business sector, is a responsible and consistent budget policy that corresponds to the trends that are typical of developed Western countries.

The government has an additional important goal: to reduce inequality in income distribution, which has worsened in recent years. The aim in this regard is to raise the economic income of households that currently rank in the lower deciles and to reduce these households need for direct state financial assistance.

Below are the main budget measures that the government intends to invoke in order to attain these goals.

The Budget Policy

Budget Framework

As in past years, the budgetary policy for 2001 aims to achieve four main targets:

1. **Continued reduction of the government deficit as a percentage of Gross Domestic Product:** A low government deficit sends the business sector a message of stability and helps the business sector to finance its investments. Governments in most developed countries have slashed their deficits considerably in recent years. Many countries have budget surpluses or expect to have them in 2001. In 2000, Israel's total government deficit (not including allocation of credit) is projected at 1.75 percent of GDP, 0.75 percent under the government's target. The main reason for the unexpectedly small deficit is an increase in tax revenues, occasioned mainly by the acceleration of economic growth.

Consequently, the government has decided to correct the downward trajectory of the deficit so that the total government deficit (not including allocation of credit) will not exceed 1.75 percent of GDP in 2001. In 2002 and 2003, the deficit will be lowered by at least 0.25 percent of GDP each year relative to the preceding year, and in 2003 the deficit will not exceed 1.25 percent of GDP. Thus, the government of Israel continues to indicate clearly that its deficit will continue to contract, like the prevailing trend in developed countries.

Continued downscaling of government expenditure relative to GDP helps the business sector to expand. An oversized general-government sector impedes the business sector, and general government is still larger in Israel than in most Western countries.

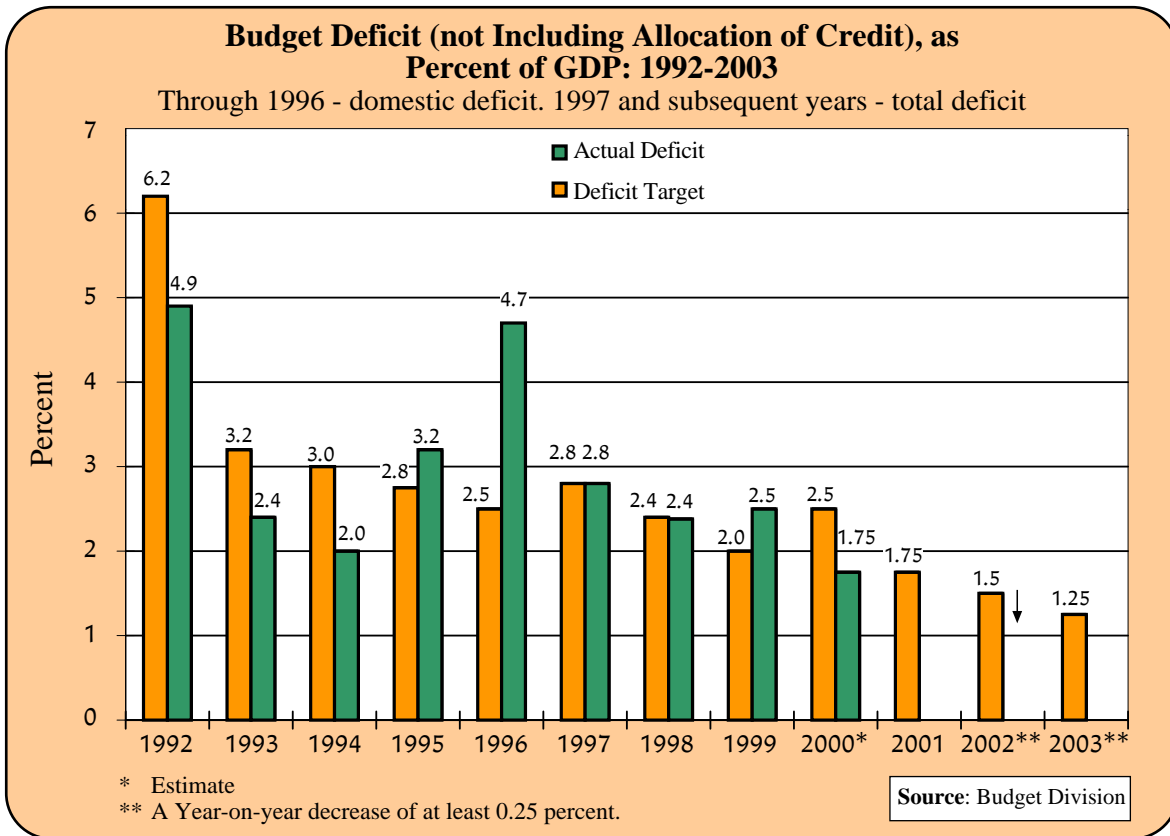
The 2001 Budget Proposal allows this important trend to continue by reducing government expenditure from 44.7 percent of GDP in 2000 to 43.8 percent in 2001.

2. **Lowering the tax burden** is crucial for the preservation of economic growth. The tax burden rose in 2000 as a result of an increase in tax collections occasioned by the acceleration of growth. Consequently, in August 2000 purchase taxes were slashed by NIS 1 billion in annual terms. The government intends to continue reducing the tax burden in 2001 by cutting personal tax rates and widening tax brackets, especially for the middle classes, and by expanding the tax base and eliminating certain exemptions.
3. **Continued drawdown of government debt in terms of GDP**, from 94 percent in 2000 to 91 percent in 2001. In 1998 the debt: GDP ratio climbed to 107 percent as against 104

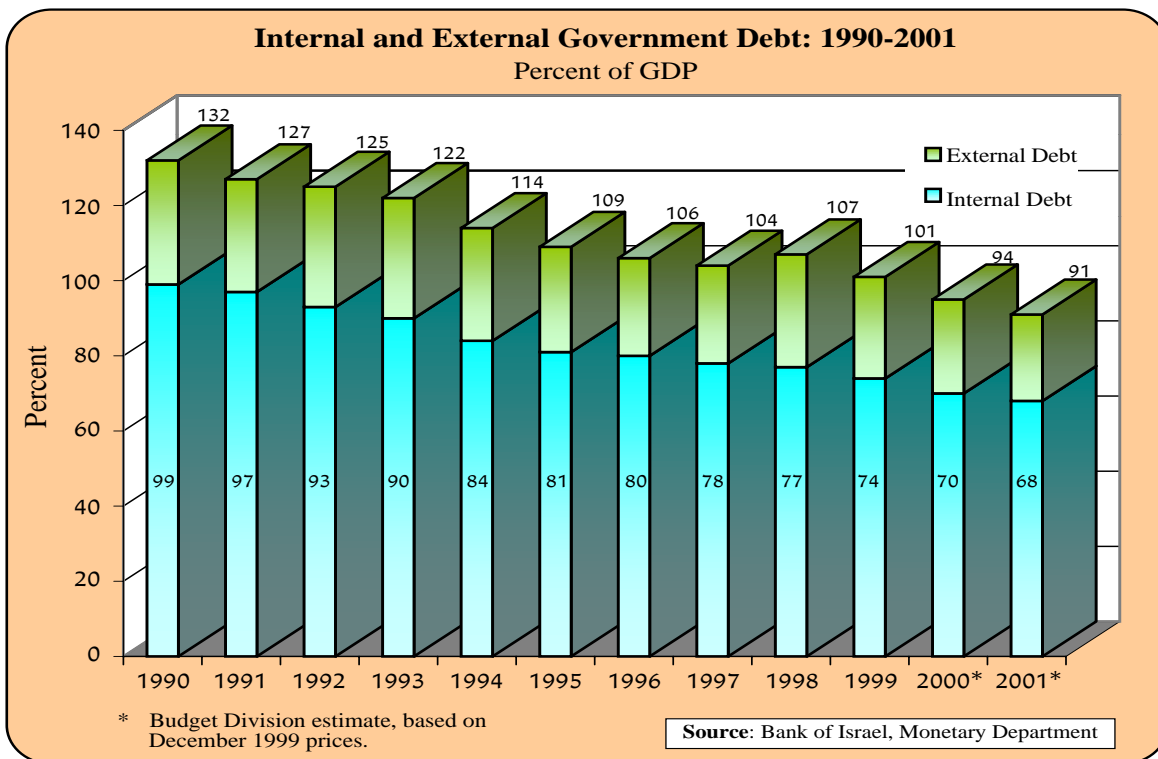
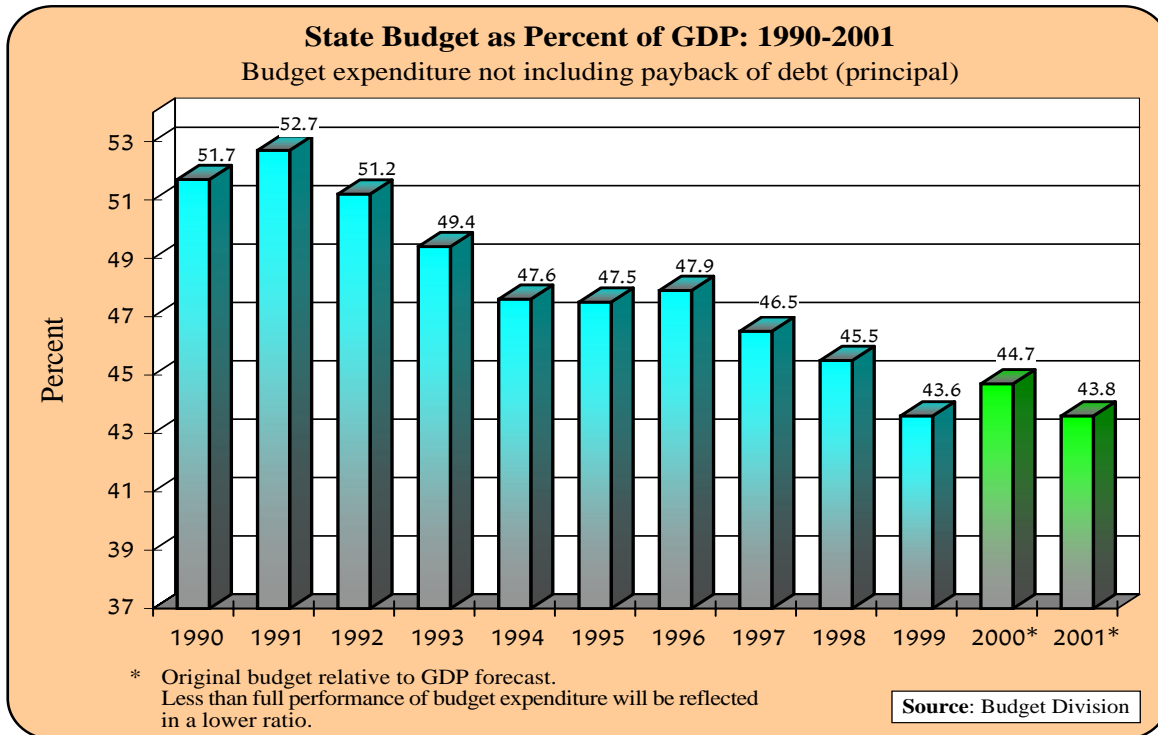
Major Provisions of the Budget, Fiscal year 2001

percent in 1997, mainly because of the steep currency depreciation in late 1998. Government debt has been declining steadily since then, due to a decrease in government deficit and partial funding of the deficit by privatizing state-owned companies and selling state-held equity in banks.

The size of the government debt in Israel, relative to GDP, is significantly higher than that in Western countries (under the Maastricht Treaty, a ceiling of 60% was set). Movement toward this goal is essential to make it easier for the business sector to expand its activity and also to lower the burden of interest payments in the state budget relative to GDP.



The Budget Policy

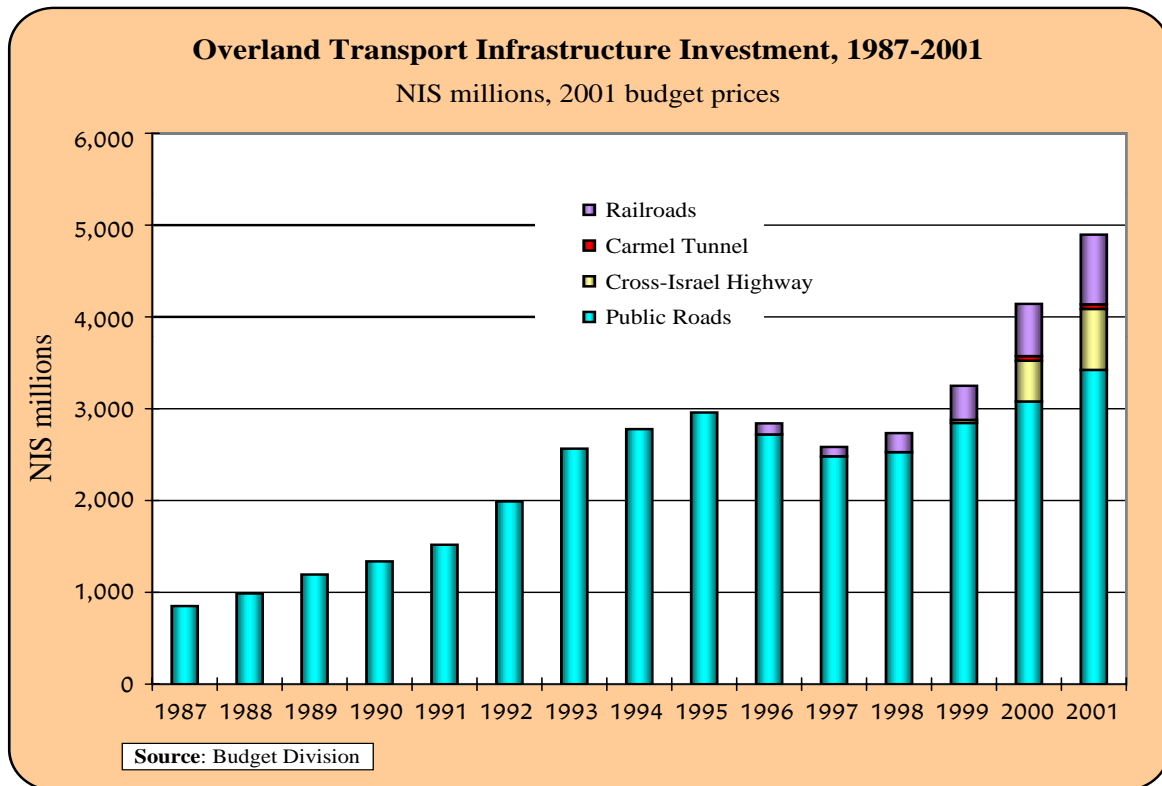


Major Provisions of the Budget, Fiscal year 2001

Composition of the Budget

The state budget proposal for 2001 includes a decrease in current expenditure by civilian government ministries, a decrease in some transfer payments, and additional spending cuts to be achieved by efficiency measures and structural changes in various domains. As a counterweight to the cutting of expenditure and the efficiency measures, the budget will invest NIS 700 million more in overland transport infrastructure than in 2000 (including NIS 600 million in cash) and NIS 100 million more in the water system.

The extra funding for investments in overland transport infrastructure will bring the total investment on this account to NIS 3.8 billion. This increase, 18.6 percent relative to 2000, is meant for investments in roads, railroads, and public transport. In addition to direct investments from the state budget, the government will take action to attract private investment by issuing B.O.T. tenders for mass-transit systems in Jerusalem and greater Tel Aviv.



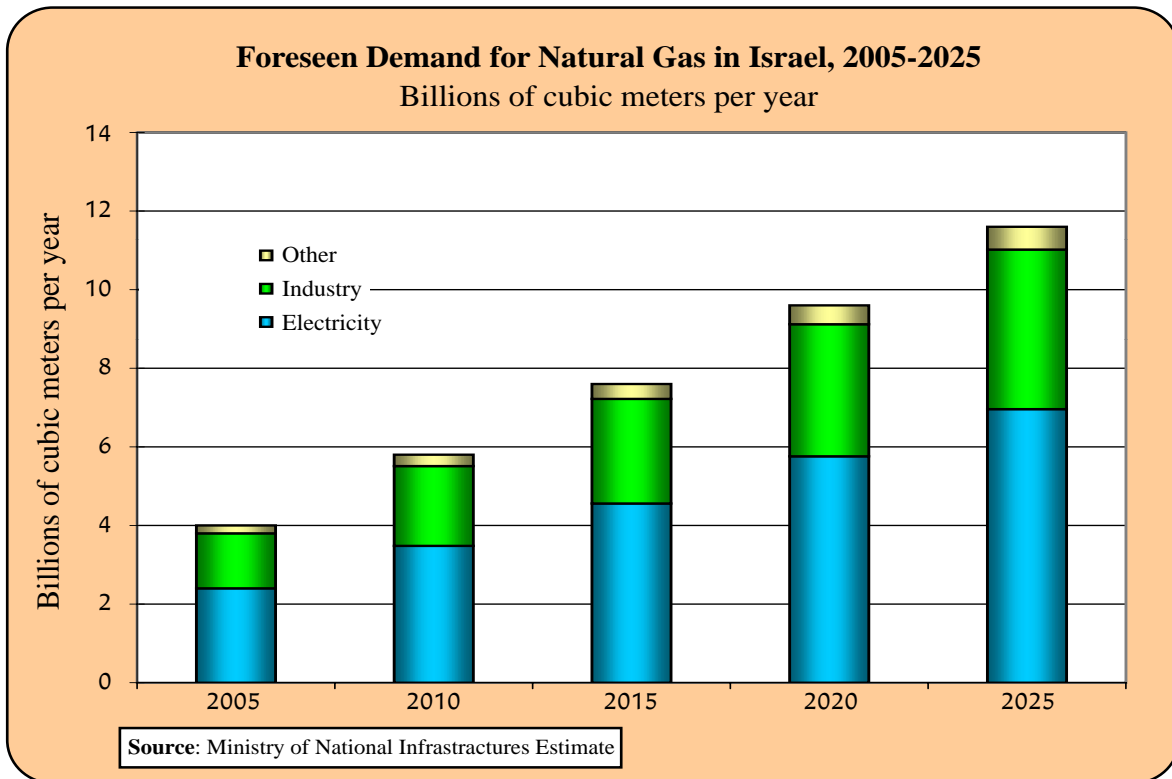
The Budget Policy

Investments in the water system will increase by NIS 100 million in 2001, mainly to improve the quality of treated effluent for agriculture; to make this water suitable for a wider variety of uses; to desalinate seawater, and to improve wells.

However, the government will not content itself with this increase in infrastructure investments; it intends to promote structural changes in various infrastructure fields that will induce a significant increase in private and public investments in physical infrastructure.

In energy, the government will continue to attract private electricity producers by selecting locations for the construction of private production facilities and inviting bids for private production. As for natural gas, the structure of the natural gas system will be adjusted, allowing Israel to make the most efficient use of the gas reserves that were discovered offshore in early 2000.

In **communications**, action to competitivize domestic communications will continue, by allocating frequencies for new operators in competitive bidding and by additional measures.



Major Provisions of the Budget, Fiscal year 2001

Furthermore, bids will be invited to allocate frequencies for personal mobile communication providers, making it possible to increase the number of subscribers and to expand the services offered.

In **water**, legislative changes affecting the water system will be pushed ahead to require owners of water delivery and catchment infrastructures to make these services available to other producers as well, thus facilitating the integration of additional players in the water system and encouraging them to invest in developing water sources, either by drilling wells or by desalinating brackish water.

The 2001 budget proposal provides supplements of NIS 360 million for improvements in education, NIS 40 million for basic vocational training for unemployed persons who are entitled to income-maintenance benefits, NIS 50 million for culture, and NIS 50 million for support of industrial R&D.

In **education**, the enrollment rate in prekindergartens (the 3–4 age cohort) will be increased, special education and education in the Arab and Bedouin sector will be reinforced, enrollment in residential schools will be expanded, the state's participation in Project Matriculation 2000 (which aims to turn out a larger number of matriculates) will be increased in conjunction with the Andrea and Charles Bronfmann Philanthropy program, and more new classrooms will be built. The enlarged allocation for these matters is in addition to the NIS 600 million increase in the base of the regular budget of the Ministry of Education, relative to 2000, so that total expenditure for education and culture will be about NIS 1 billion greater in 2001 than in 2000.

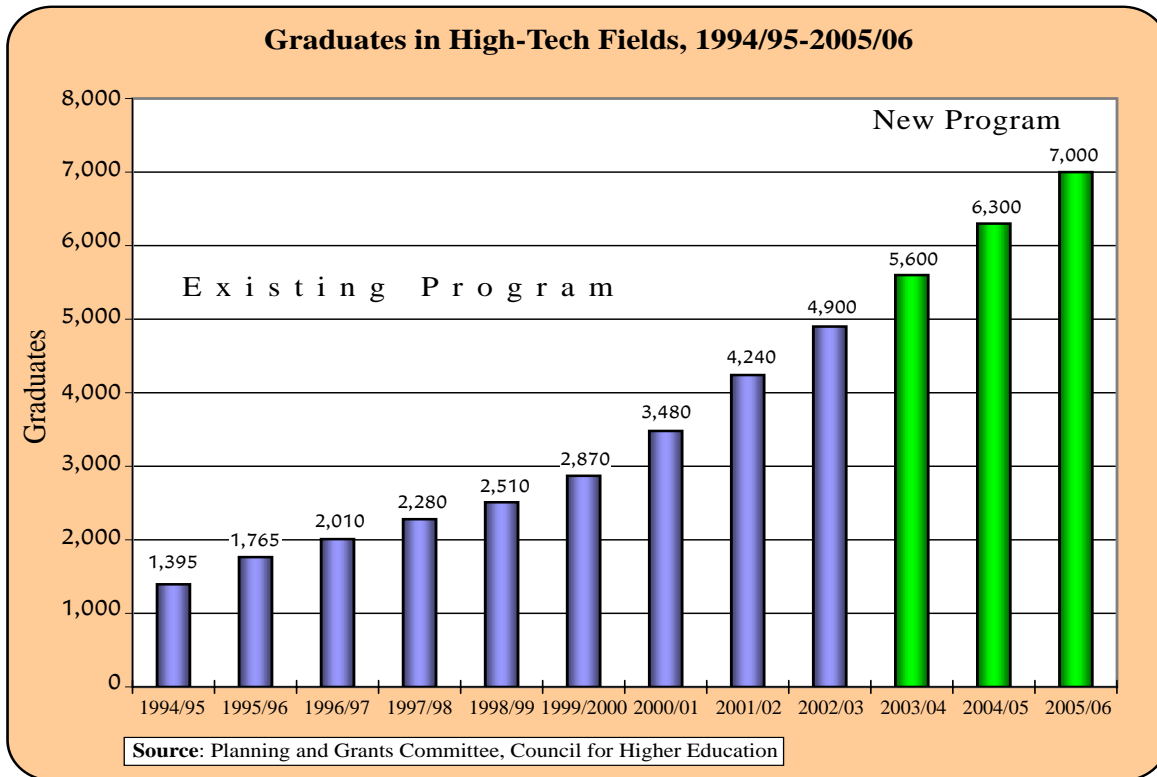
Additional Structural Changes

To achieve sustainable growth and reduce inequality in income distribution, the government has decided to make structural changes in a variety of fields, beyond those enumerated above.

Improvements in schooling and vocational training: Economic growth in Israel is typified by rapid expansion of high-tech industry and is driven by technological and scientific progress. The structural change that the economy has been experiencing over the past decade has given Israelis a much higher return on their schooling.

The rising return on schooling has exacerbated inequality in income distribution between

The Budget Policy



the well schooled and the poorly schooled. Although it is necessary to expand higher schooling in occupations that high-tech industry requires, action is also needed to enhance schooling and vocational training among the jobless. This will expand the economy's growth potential and reduce inequality in income distribution.

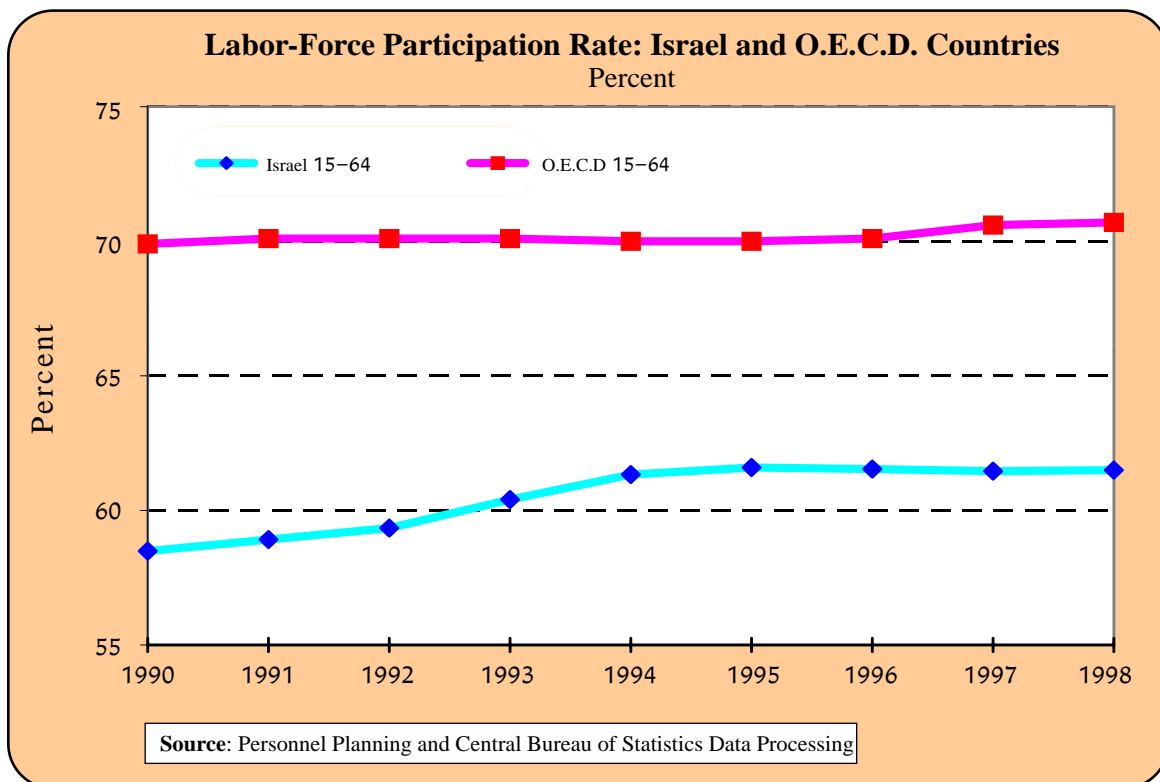
Accordingly, the government has decided to create programs that will allow higher-education institutions to turn out more graduates in high-tech disciplines and exact sciences, and to emphasize vocational training and training for occupations that high-tech industry needs. The government has also decided to implement a program in which jobless persons who receive income-maintenance benefits will be given basic skills to re-enter the labor cycle.

Increasing the labor-force participation rate: Israel's average rate of participation in the civilian labor force (in the 15–64 age cohort) was 61.5 percent in 1998. Although the participation rate has been growing slowly since the 1970s, it is still much lower than that in the OECD countries, which report 70.5 percent participation in the same age cohort.

Major Provisions of the Budget, Fiscal year 2001

This low rate of labor-force participation is severely harmful to the economy's growth potential and competitiveness. It is also one of the reasons for the increase in inequality in income distribution.

To return recipients of income-maintenance benefits to the labor force, the government has decided to create a combined program of vocational training and support in the process of returning to work, among other things.



Elimination of barriers in land and housing: The construction industry does not need government involvement. Housing prices are set in the marketplace, at the point where housing supply and demand converge. The homebuilding industry has been contracting in recent years, after a rapid expansion prompted by immigration from the former Soviet Union in the first half of the 1990s.

The construction industry contracted due to an especially high level of activity in the preceding period and a decline in demand, occasioned among other things by a decrease in the pace of immigration. The change of trend in the business cycle has prompted the

The Budget Policy

industry to make a readjustment, and in 2001 homebuilding is expected reverse direction and grow somewhat. In view of the expected recovery of the industry and the strong effect of housing prices on the Consumer Price Index, it is the government's duty to assure the absence of barriers in land and housing that would prevent full adjustment of housing supply to demand within a reasonable period of time and without price increases.

Thus, the government has resolved to take a series of actions to eliminate barriers in respect to housing in order to facilitate enough homebuilding to meet the rising demand. In this context, it was decided to make more land available for building and to make land use more efficient by creating new modalities of urban renewal, such as "clear-and-build" projects.

Enhancing competitiveness: The Israeli economy is characterized by a high degree of centralization and lack of competition in infrastructure, imports, production, and marketing. In many fields, the structure of the Israeli economy has resulted in higher price levels here than in other developed economies.

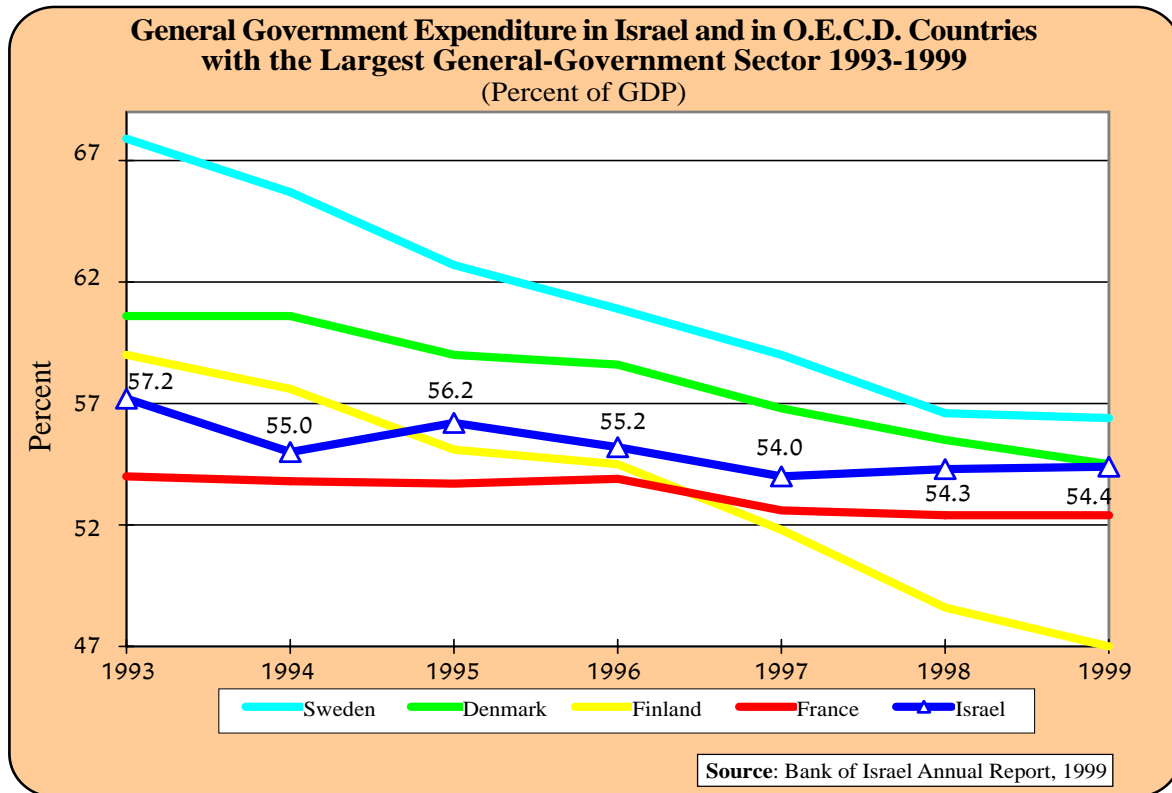
An across-the-board enhancement of competitiveness will reduce the prices of goods and services that both households and businesses consume. Lowering prices will lower production costs, make the economy more competitive, and help sustain the growth process. In the context of its budget decisions for 2001, the government approved a plan that contains a series of proposals in transport, manufacturing, energy, and agriculture. The proposals pertain to expanding the cycle of competition in various goods and services.

Downsizing and streamlining the central-government and general-government sectors: An oversized general-government sector is a hindrance to the business sector because general government competes with the business sector for production factors. Furthermore, general government has to impose taxes to finance its activity, thereby inflicting further damage on the business sector.

Israel has a much larger general-government sector than the standard in developed Western countries (54 percent of GDP as against 45 percent, respectively). Furthermore, general-government expenditure, in terms of its share in GDP, has long been declining in most Western countries but has been relatively stable in Israel (even though the share of central-government expenditure in GDP has been falling).

It is very important to streamline general government in Israel, and this sector can indeed be downsized without detriment to the level of services that it provides. The government resolutions for 2001 include structural changes in higher education, religious services, labor

Major Provisions of the Budget, Fiscal year 2001



and social affairs, transport, and many additional fields, all of which to make general government leaner and more efficient.

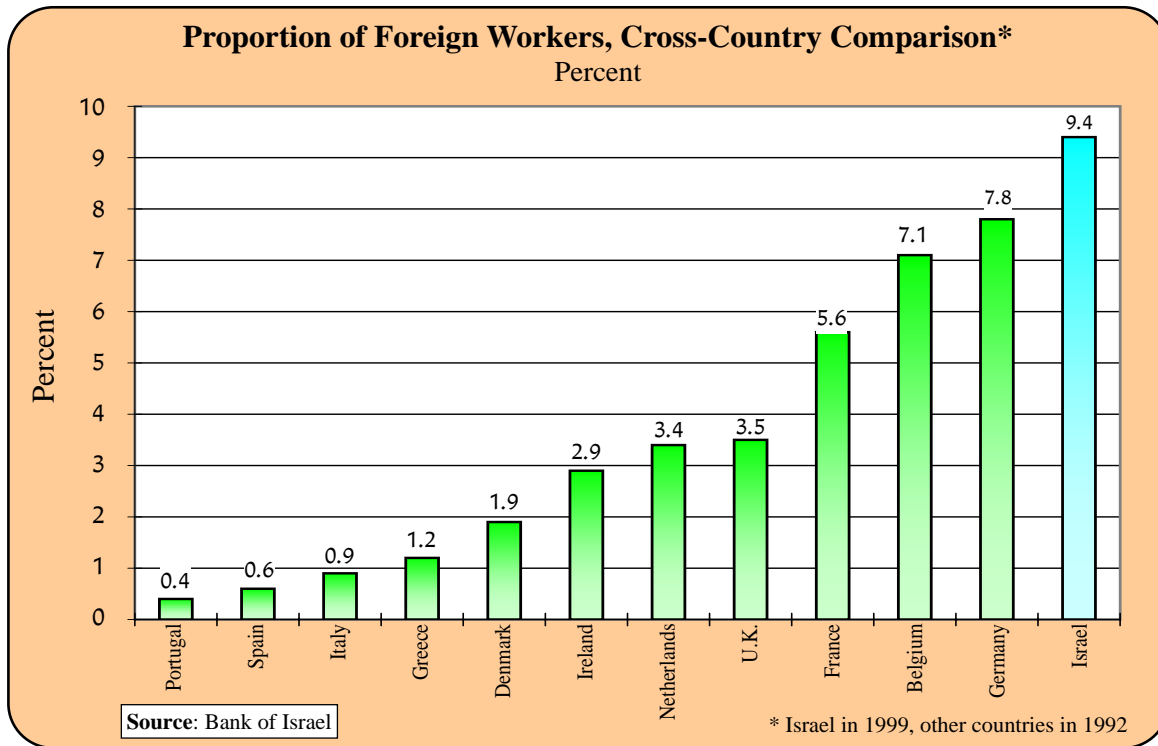
Additional Emphases in the Budget Proposal

Reducing the employment of foreign workers: The use of foreign workers in Israel has expanded significantly over the past decade. According to the Central Bureau of Statistics, there were some 220,000 foreign workers (legal and illegal) in Israel in 1999. Relative to the size of the domestic labor force, Israel has one of the largest populations of nonresident workers in the world.

This phenomenon has several negative aspects. Among other things, its employment is detrimental to the employment of Israelis and helps keep wage levels low, especially in occupations that do not require special skill, and the high proportion of foreign workers in Israel aggravates inequality in income distribution. Hence the importance of reducing the use of foreign labor.

The Budget Policy

Thus, the government has decided to resume the enforcement of laws against the employment of illegal foreign workers with determination and on a large-scale and, concurrently, to approve the regulations pertaining to fees for the employment of legal foreign workers.



Integration into the global economy: In recent years, Israel has been undergoing an advanced process of global economic integration. To assure the continuation of economic growth, a domestic business environment as competitive as that in the developed countries must be assured.

A modern and open economy finds it difficult to grow over time when the legal framework that determines the way business is conducted, and the tax rules, are substantially different from those in the most advanced economies. In such a situation, one fears that businesses and companies will move to other countries and transfer their main centers of activity away from Israel.

To attain the aforementioned goals, the government is promoting various legislative amendments that pertain, among other things, to taxation, corporations, and electronic-commerce infrastructure.

Major Provisions of the Budget, Fiscal year 2001

ANALYSIS OF THE STATE BUDGET PROPOSAL

Budget expenditure in 2001, not including payback of principal on debts and transfers to the Bank of Israel, in constant prices, is 2.75 percent higher than the original 2000 budget. The total state budget in 2001, in constant prices (including payback of principal), is 6.7 percent higher than the original 2000 budget. Tax revenues are expected to exceed expected revenues in 2000 by 0.9 percent in real terms.

Expenditure

Below are the main real expenditure-side changes in the 2001 budget proposal relative to the original 2000 budget:

Total expenditure, including payback of principal on account of debts, will increase by 6.7 percent in 2001.

Civilian consumption will increase by 2.2 percent, mainly because domestic wage expenditure will rise.

Defense consumption will climb by 3.5 percent, due to government resolutions concerning the 2001 defense budget.

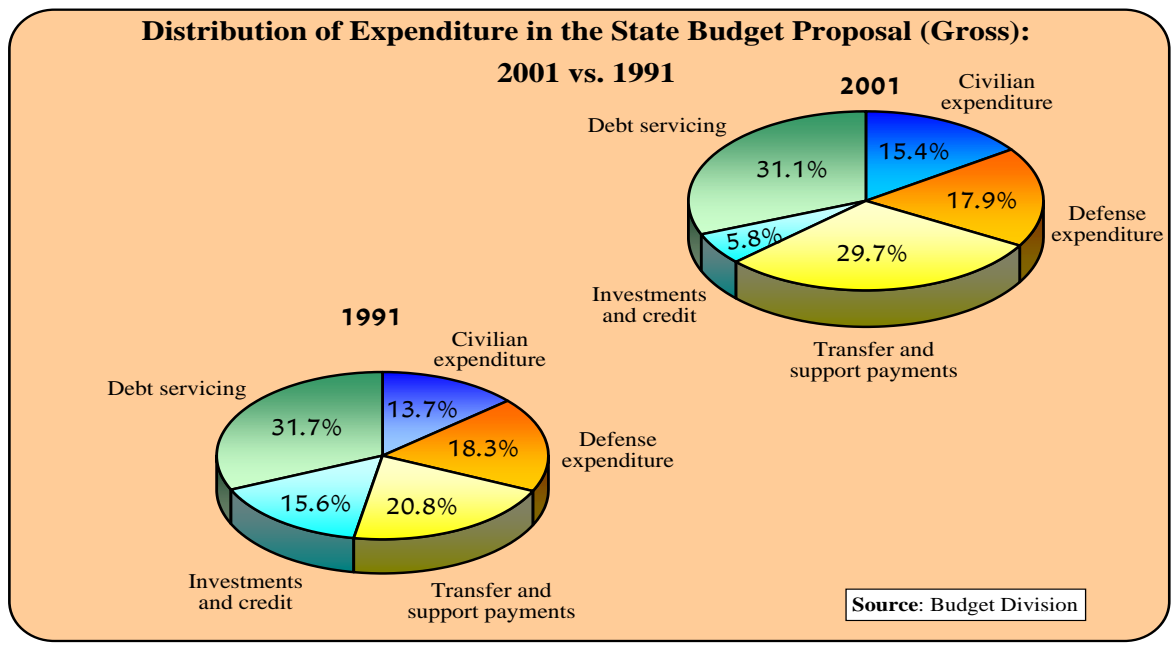
Transfer payments and support will increase by 2.2 percent because transfers to municipal authorities, individuals, and public institutions will rise.

Interest payments will increase by 7.5 percent, due to the increase in the government debt and higher costs of raising capital.

Payback of principal will climb by 24.4 percent, as a result of the structure of the debt payback tables.

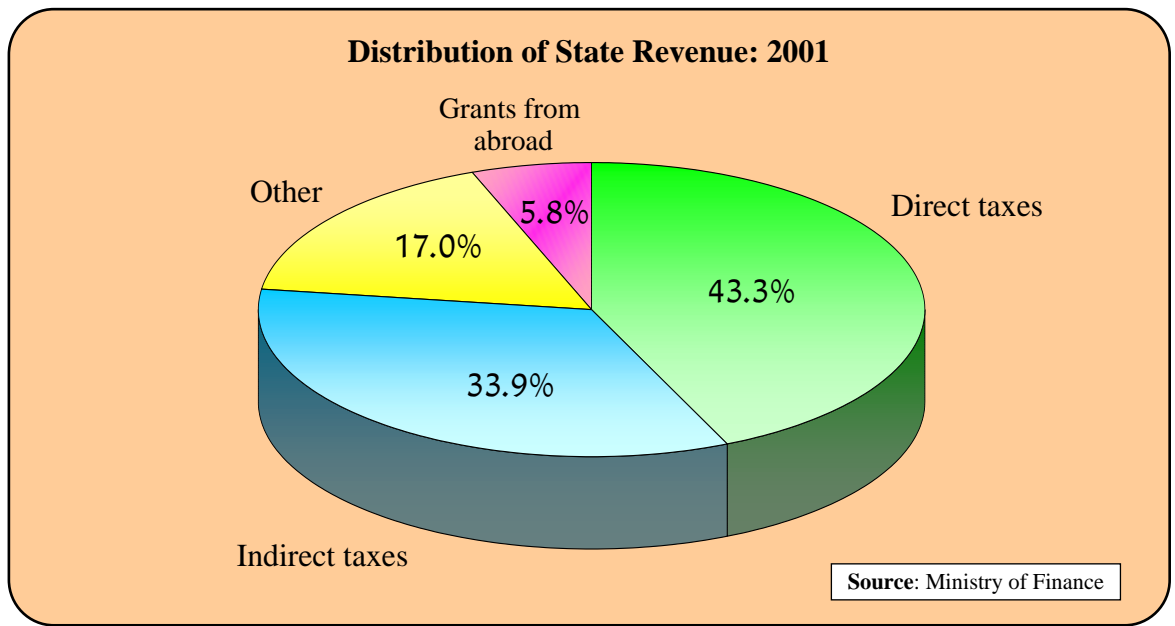
Allocation of credit will decrease by 12.7 percent.

Analysis of the State Budget



Revenues

Estimate state tax revenues in 2001 are expected to exceed expected revenues in 2000 by 0.9 percent in real terms, due to the growth of Gross Domestic Product and legislative changes (see Part 4 below for details).



Major Provisions of the Budget, Fiscal year 2001

State Budget Deficit

The total deficit in the 2001 budget, not including allocation of credit, will be NIS 8.4 billion—1.75 percent of GDP.

The domestic deficit in the 2001 budget, not including allocation of credit, will be NIS 2.5 billion—0.52 percent of GDP.

The foreign deficit in the 2001 budget, not including allocation of credit, will be NIS 5.9 billion—1.23 percent of GDP.

The total deficit in 2001 will be NIS 6.3 billion.

Funding of the total deficit in 2001

(NIS billions)

Financing of the Total Deficit: 2001 (1)	NIS Billions
Estimated revenue from sale of SOEs and banks (2)	3.0
Borrowing from abroad (net)	0
Borrowing from the public (net)	3.3

-
1. The components used to finance the deficit may be substitutable.
 2. In 2001, the State's holdings in Bank Leumi le-Israel and Bezeq are to be sold. The consideration for these sales exceeds the programmed deficit. Furthermore, since there is uncertainty about the likelihood of receiving the entire consideration in 2001, the estimate for revenue from the sale of SOEs and bank equity in the 2001 budget proposal is NIS 3 billion.

Analysis of the State Budget

Budget Proposal for Fiscal Year 2001 (NIS Thousands)

	1999 Actual Results	2000 Original budget	2001 Budget Bill
1. Total expenditure and credit allocated	178,727,438	194,176,321	205,587,593
===== Thereof: domestic	164,061,334	176,804,369	186,962,902
- Consumption and investment	80,259,977	86,582,981	92,154,581
Thereof: domestic	71,400,403	75,666,953	80,618,771
- Transfers and subsidies	64,539,028	66,488,955	70,199,364
- Interest payments	24,972,911	26,380,410	28,608,032
Thereof: domestic	19,167,849	19,924,486	21,519,151
- Issue of credit	3,715,087	5,249,220	4,586,276
- Other expenditure	5,240,435	9,474,755	10,039,340
2. Total revenues and grants	169,715,013	183,737,101	199,285,583
===== Thereof: domestic	153,456,110	164,497,101	186,483,473
- Tax revenues	127,887,966	136,550,000	153,920,000
- Other revenues	30,778,545	34,927,101	33,899,583
Thereof: payback of credit	5,170,142	5,720,000	6,684,266
- Grants from abroad	11,048,502	12,260,000	11,466,000
3. Surplus (+) [deficit (-)]	-9,012,425	-10,439,220	-6,302,010
===== Surplus (+) [deficit (-)], excl. net credit	-10,467,480	-10,910,000	-8,400,000
Thereof:			
Domestic	-11,983,666	-12,688,048	-2,507,153
Foreign	1,516,186	1,778,048	-5,892,847
4. Financing*			
===== 4.1 Borrowing abroad (net)	-280,769	1,695,054	
----- Acceptance of loans	6,727,569	10,076,000	10,259,262
Payback of debt	7,008,338	8,380,946	10,259,262
4.2 Domestic borrowing (net)	7,462,553	5,244,166	3,302,010
----- Acceptance of loans	38,441,823	38,442,080	44,335,199
Payback (principal)	30,979,270	33,197,914	41,033,189
4.3 Capital gains	2,121,565	3,500,000	3,000,000

*Funding abroad and domestic funding may be substitutable.

Major Provisions of the Budget, Fiscal year 2001

Gross Expenditure by Economic Classification (not including Bank of Israel) (NIS thousands)

	1999 Actual Results	2000 Original budget	2001 Budget Bill
Net expenditure	208,819,235	226,101,080	244,763,318
=====	=====	=====	=====
Revenue-dependent expenditure	7,895,811	9,654,101	12,116,726
Total gross budget (1+2)	216,715,046	235,755,181	256,880,044
=====	=====	=====	=====
1. Total expenditure and credit	178,727,438	194,176,321	205,587,593
-----	-----	-----	-----
1.1 Civilian consumption	33,912,454	37,844,014	39,188,172
-----	-----	-----	-----
– Domestic payroll	21,791,527	23,712,098	24,500,450
– Domestic procurements	10,951,504	12,306,654	12,995,863
– Overseas wages and procurements	1,169,423	1,825,262	1,691,859
1.2 Defense consumption	39,209,798	39,001,911	42,587,495
-----	-----	-----	-----
– Payroll	3,368,953	14,745,807	14,894,302
– Transfer payments		1,473,619	1,520,978
– Procurements	27,767,249	12,677,052	15,255,625
– Construction		766,742	796,116
– Procurements abroad	7,669,000	8,814,398	9,579,741
– Emergency expenses and coordination of operations in the territories	404,596	524,293	540,733
1.3 Transfers and subsidies	64,535,174	66,488,955	70,199,364
-----	-----	-----	-----
– To local authorities	9,541,011	8,734,592	9,608,611
– To religious councils	167,166	156,206	198,616
– To individuals and institutions	48,963,651	37,663,450	37,853,113
– For basic-commodity prices	1,592,874	1,801,050	1,842,972
– Other supports	4,270,472		
– Transfers to National Insurance Institute		18,133,657	20,696,052
1.4 Investments and credit	10,860,371	14,992,284	14,968,935
-----	-----	-----	-----
– Direct investment	7,145,284	9,743,064	10,382,659
– Thereof: housing	1,776,607	2,367,413	2,480,872

Analysis of the State Budget

Gross Expenditure by Economic Classification (Continued) (not including Bank of Israel) (NIS thousands)

	1999 Actual Results	2000 Original budget	2001 Budget Bill
– Credit	3,715,087	5,249,220	4,586,276
– Thereof: housing	3,153,015	4,346,344	3,707,741
1.5 Interest payments	24,972,911	26,380,410	28,608,032
-----	-----	-----	-----
– Domestic interest	19,125,158	19,883,373	21,480,793
– Credit subsidies	42,691	41,113	38,358
– Interest abroad	5,805,062	6,455,924	7,088,881
1.6 Miscellaneous expenditure	4,749,556	5,094,959	5,404,383
-----	-----	-----	-----
– Payback of principal to National Insurance	4,749,183	5,094,959	5,404,383
– Miscellaneous	373		
1.7 Reserves	487,174	4,373,788	4,631,212
-----	-----	-----	-----
2. Payback of debt (principal)	37,987,608	41,578,860	51,292,451
-----	-----	-----	-----
– Domestic debt to the public	30,979,270	33,197,914	41,033,189
– Debt abroad	7,008,338	8,380,946	10,259,262

Major Provisions of the Budget, Fiscal year 2001

Revenues and Borrowing (Condensed) (Not including Bank of Israel) (NIS Thousands)

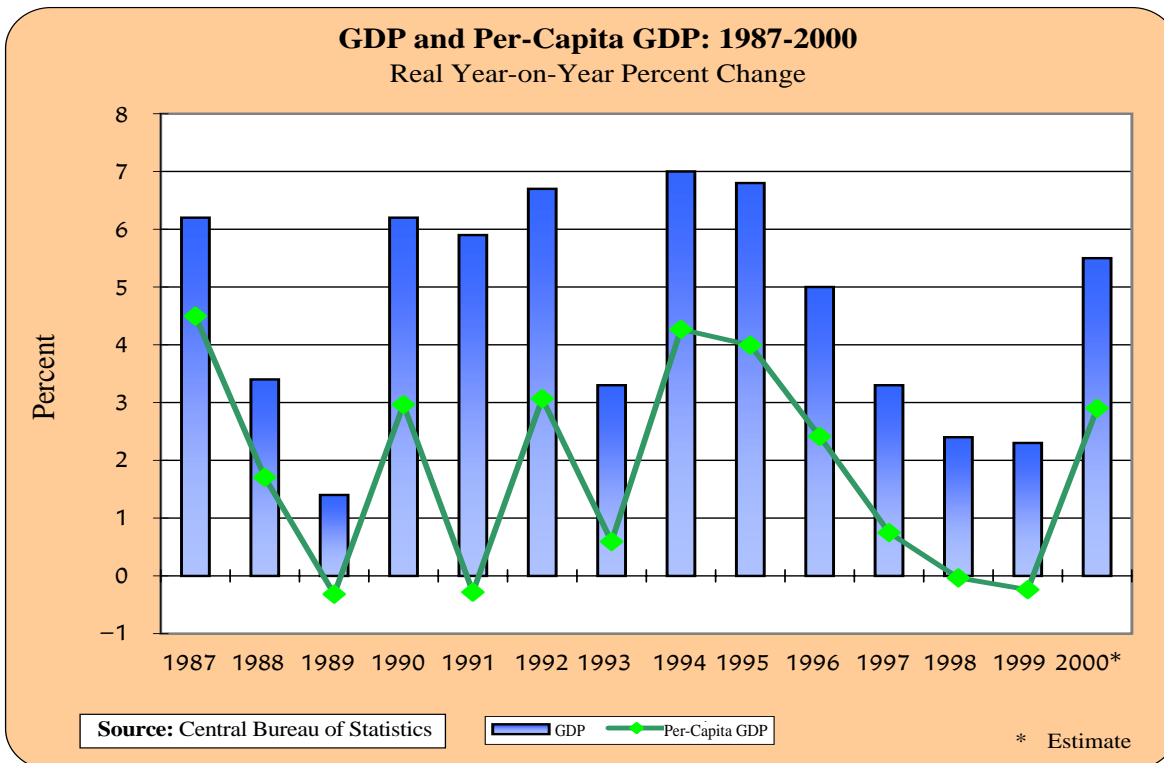
	1999 Actual Results	2000 Original budget	2001 Budget Bill
Grand Total	208,731,124	226,101,080	244,763,318
Part A: Current revenues	156,359,539	165,987,491	174,902,700
Part B: Loan and capital-account revenues	52,371,585	60,113,589	69,860,618
Part A: Current revenues	156,359,539	165,987,491	174,902,700
Taxes and compulsory payments	127,887,966	136,550,000	153,920,000
Income and property taxes	69,689,157	73,730,000	86,300,000
Taxes on expenditure	58,198,809	62,820,000	67,620,000
Interest, royalties, and misc.	11,739,585	12,970,000	7,114,583
Transfer from Part B	16,731,988	16,467,491	13,868,117
Part B: Loan and capital-account revenues	52,371,585	60,113,589	69,860,618
Collection of principal	5,170,142	5,720,000	6,684,266
Miscellaneous	34,896	1,093,000	1,150,364
Capital gains	2,121,565	3,500,000	3,000,000
Domestic borrowing	44,000,899	43,932,080	51,168,843
Borrowing from National Insurance Institute	5,850,000	5,490,000	6,833,644
Revenue from issues and deposits	38,150,899	38,442,080	44,335,199
Loans and grants from abroad	17,776,071	22,336,000	21,725,262
U.S. defense assistance	6,975,905	8,610,000	8,475,000
Civilian assistance	4,072,597	3,650,000	2,991,000
Israel Bonds (net)	3,423,235	3,694,000	3,995,000
Other borrowing	3,304,334	6,382,000	6,264,262
Transfer to Part A	-16,731,988	-16,467,491	-13,868,117

Main Economic Developments

MAIN ECONOMIC DEVELOPMENTS

Growth

The National Accounts data for the first half of 2000 show that the recovery of economic activity that began in the second quarter of 1999, as reflected in rapid growth of Gross Domestic Product and GDP of the business sector, has become solid. According to the latest estimates from the Central Bureau of Statistics, GDP expanded by 5.4 percent in the first half of the year (seasonally adjusted). This pace, substantially higher than the GDP growth rate in 1998-1999 (2.4 percent and 2.3 percent, respectively), is expected to continue at the annual level as well and will allow per-capita GDP to expand by 2.9 percent in 2000 as against - 0.2 percent in 1999. The acceleration of growth in the past year was powered mainly by an impressive increase in exports and not by an upturn in domestic demand. This kind of growth is highly desirable, since it occurs without inflation pressures and may be long-lasting.



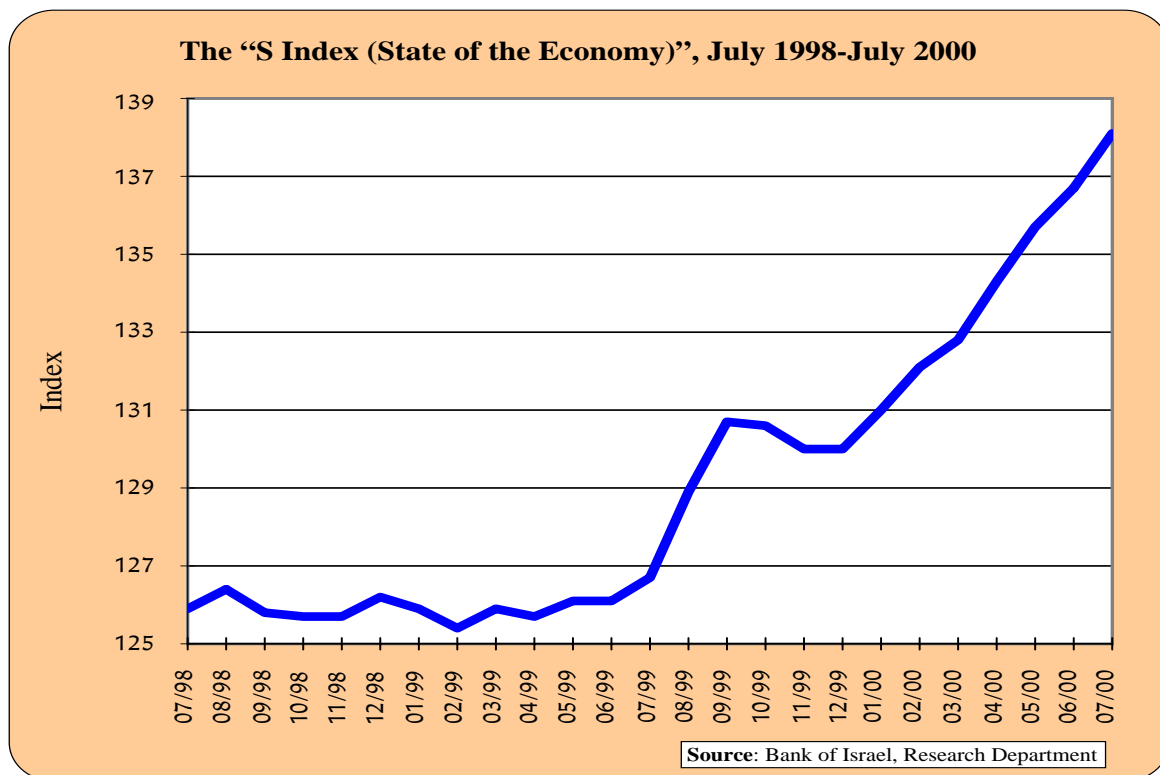
Major Provisions of the Budget, Fiscal year 2001

Gross Domestic Product of the business sector increased in the first half of 2000 by 7.9 percent in annual terms, proving that the business sector is the locomotive of growth. In comparison, GDP of the business sector expanded by only 2 percent in 1999.

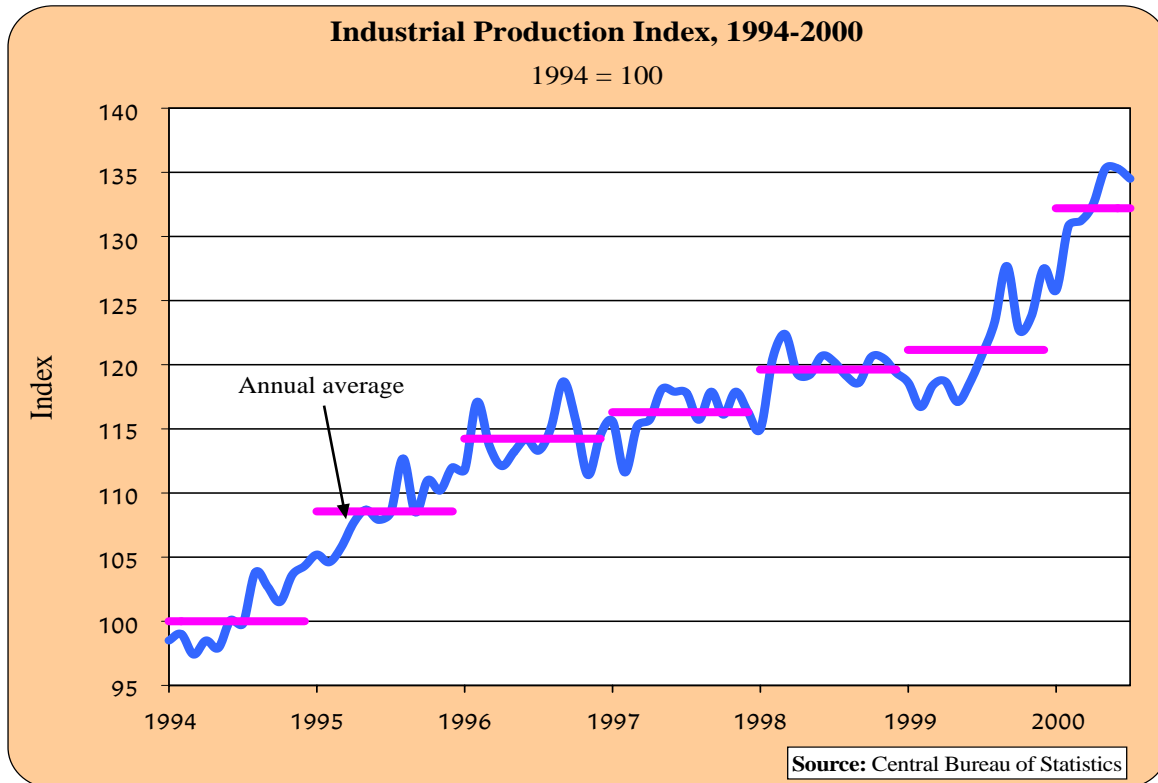
An examination of the composition of demand shows that investments have continued to rise even as private consumption has expanded and public consumption has slowed. Furthermore, according to estimates from the Central Bureau of Statistics, exports of goods and services are poised to increase by 21.3 percent as against only 10.7 percent growth of imports.

Nonresidential Industries

The most recent economic indicators that are used to gauge domestic activity point to continued expansion of activity in most industries. According to the Monetary Department of the Bank of Israel, the “S-Index”, a composite index that monitors the state of the economy, climbed at a 7.5 percent annual pace in the first half of 2000 as against 4.1 percent and 1.7 percent in 1998 and 1999, respectively.



Main Economic Developments



The Industrial Product Index points to continued expansion in industry, which accounts for about 30% of the business sector. During the first half of 2000 this index rose by 12.5% in annual terms (seasonally adjusted), after a rise of only about 1.4% in 1999. The process of structural change in the composition of Israeli industry continued in 2000. The rapid growth, which is led by high-tech industry, rests in part on other sectors as well.

The companies' survey conducted by the Bank of Israel for the second quarter of 2000 also reinforces the expansive trend in economic activity. According to the survey, industrial, transportation, and telecommunications companies, hotel, business services, and commerce reported continued growth in the second quarter of the year.

The increase in industrial activity is reflected in an impressive rise in industrial exports. Data for the first eight months of the year point to an increase of about 24% in industrial exports (excluding polished diamonds) and software exports, over the corresponding period in 1999. IMF data indicate that this increase in exports should be seen against the backdrop of a rise in the rate of increase in world trade from 4.6% in 1999 to 7.9% in 2000.

Major Provisions of the Budget, Fiscal year 2001

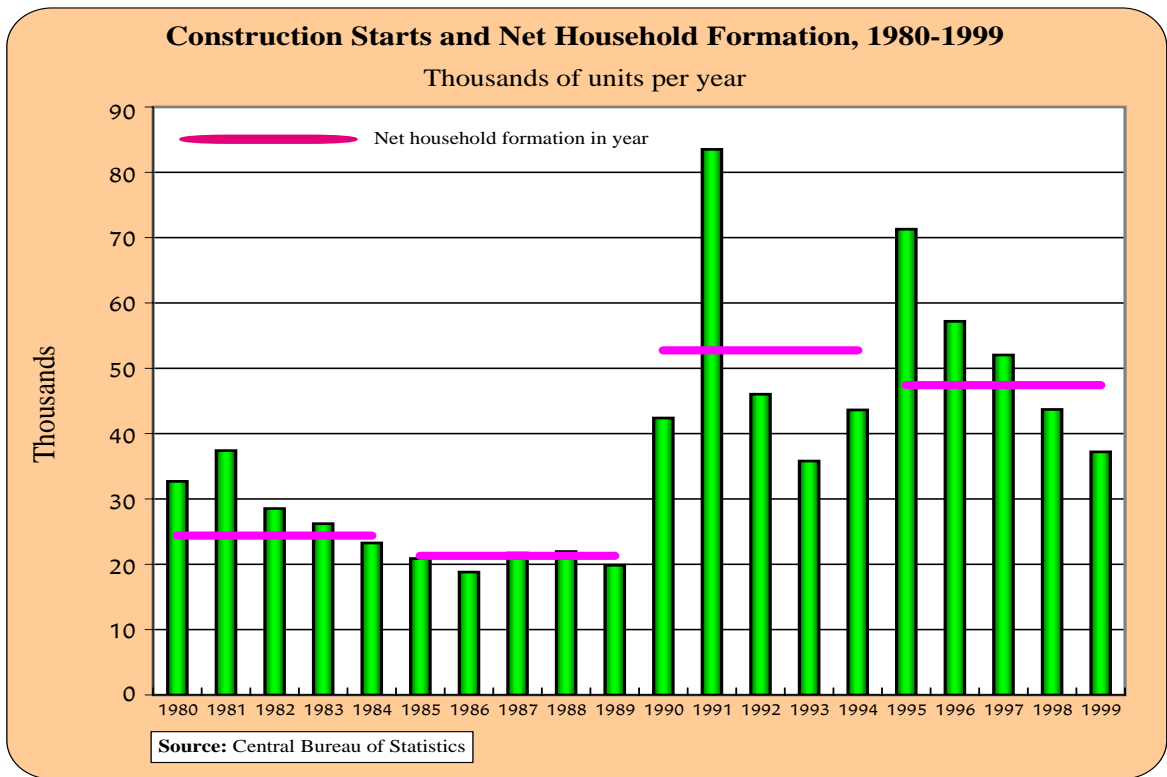
Construction

Most indicators of construction activity do not point to a clear turnaround in the downtrend that has beset this industry since 1995. In the first half of 2000, residential investment contracted by 0.8 percent in seasonally adjusted annual terms, continuing the downtrend that has been observed in the past few years.

Housing Supply

Release of land: The Israel lands Administration released enough land for 10,800 dwellings in the first half of 2000, down 21.3 percent from the corresponding period a year ago, when enough land for the construction of 13,700 dwellings was released.

Housing starts: there were 18,100 housing starts (in private and public building) in January – May 2000, 17 percent up on monthly average from the monthly average in the corresponding period in 1999.



Main Economic Developments

Housing completions: 18,300 dwellings were completed (in private and public construction) in January—May 2000, 7 percent more than in the corresponding period in 1999 and 2 percent more than the monthly average in 1999 (3,655 dwellings in 2000, 3,596 in 1999).

Housing Demand

Number of transactions (existing and new dwellings): according to land-betterment tax and real-estate purchase tax data, 8,049 transactions took place on monthly average in January—July 2000, 3 percent more than in the corresponding period in 1999. In the first five months of the year, 2,020 new dwellings were sold on monthly average, down 2 percent from the corresponding months in 1999.

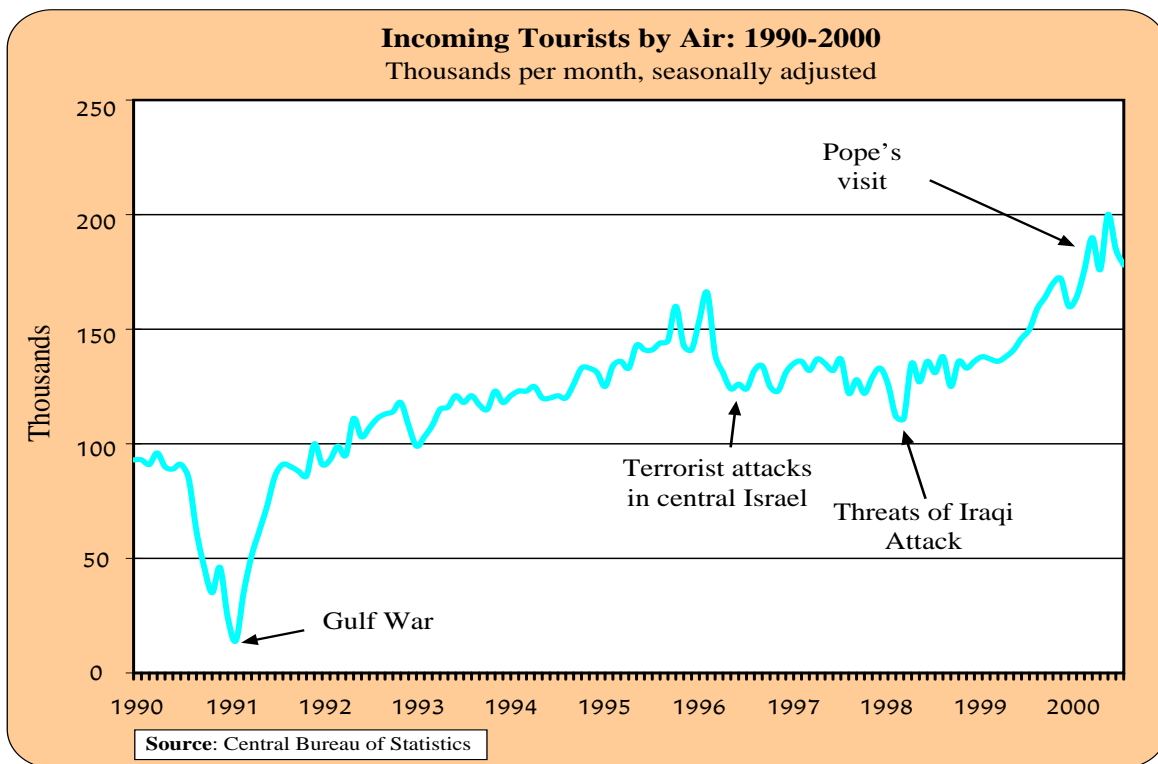
Longevity of unsold inventory of new dwellings (average in months) is a good indicator of the state of the housing market; an increase in this figure over time points to an oversupply and a decrease indicates excess demand. The average longevity was 13.9 months in the second quarter of 2000, slightly down from the first quarter.

Major Provisions of the Budget, Fiscal year 2001

Tourism

Data for the first half of 2000 pointed to continued recovery of tourism after this industry tumbled into a severe slump in the middle of 1996. In the first six months of the year, inbound tourism outpaced its level in the corresponding period in 1999 by 30 percent.

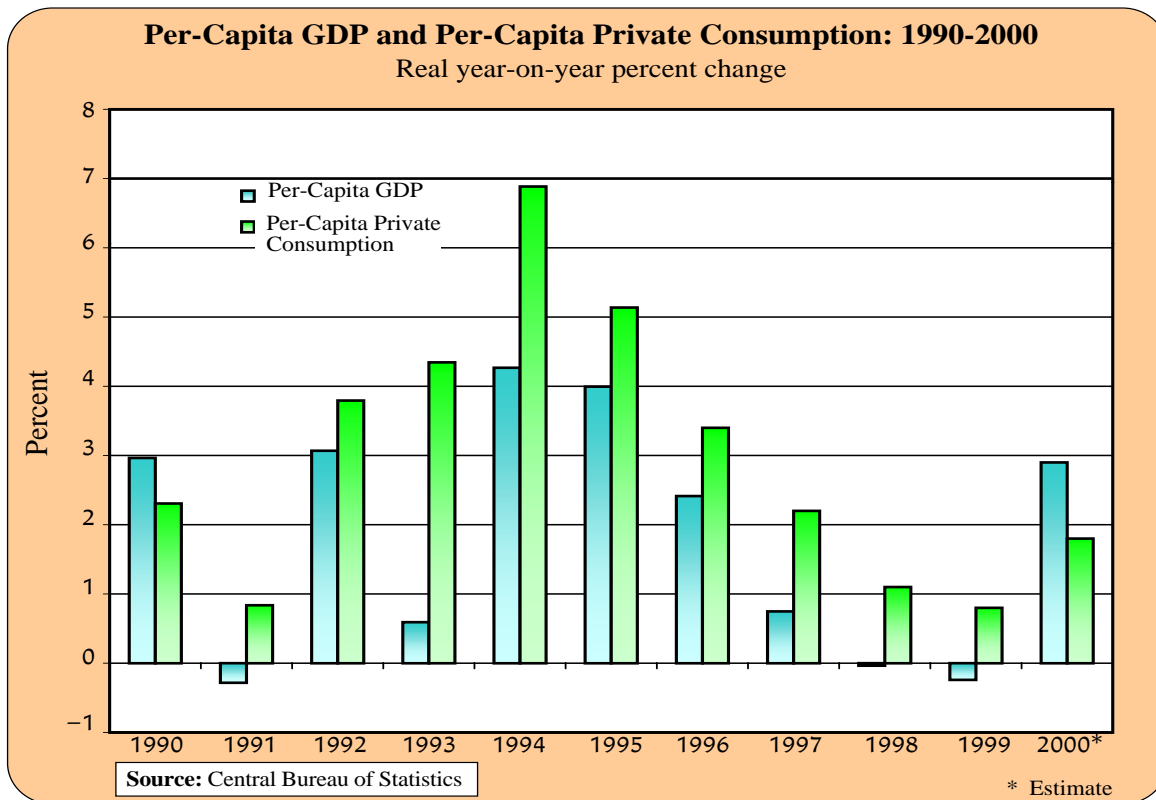
Not only inbound tourism but also person-nights in domestic hotels have been trending up by 16 percent in the first eight months of the year relative to the corresponding period in 1999, reflecting increases of 31 percent in person-nights by inbound tourists and only 4 percent in person-nights of Israelis.



Private Consumption

Private consumption has been rising gradually after a lengthy slowdown that began in 1995. In the first half of 2000, private consumption climbed by 4.4 percent, representing a 1.9 percent increase in per-capita private consumption (both figures in annual terms). The upturn in private consumption in 2000 is composed of brisk growth in consumption of

Main Economic Developments



durable goods (10.2 percent) and slower growth in current consumption (3.8 percent). Importantly, private consumption expanded by 3.4 percent in 1999.

The upturn in private consumption in the past year provides further evidence of the end of the economic slump and reflects the rapid acceleration of economic activity. Demand is also being fueled by falling unemployment rates and the gradual descent of real interest rates.

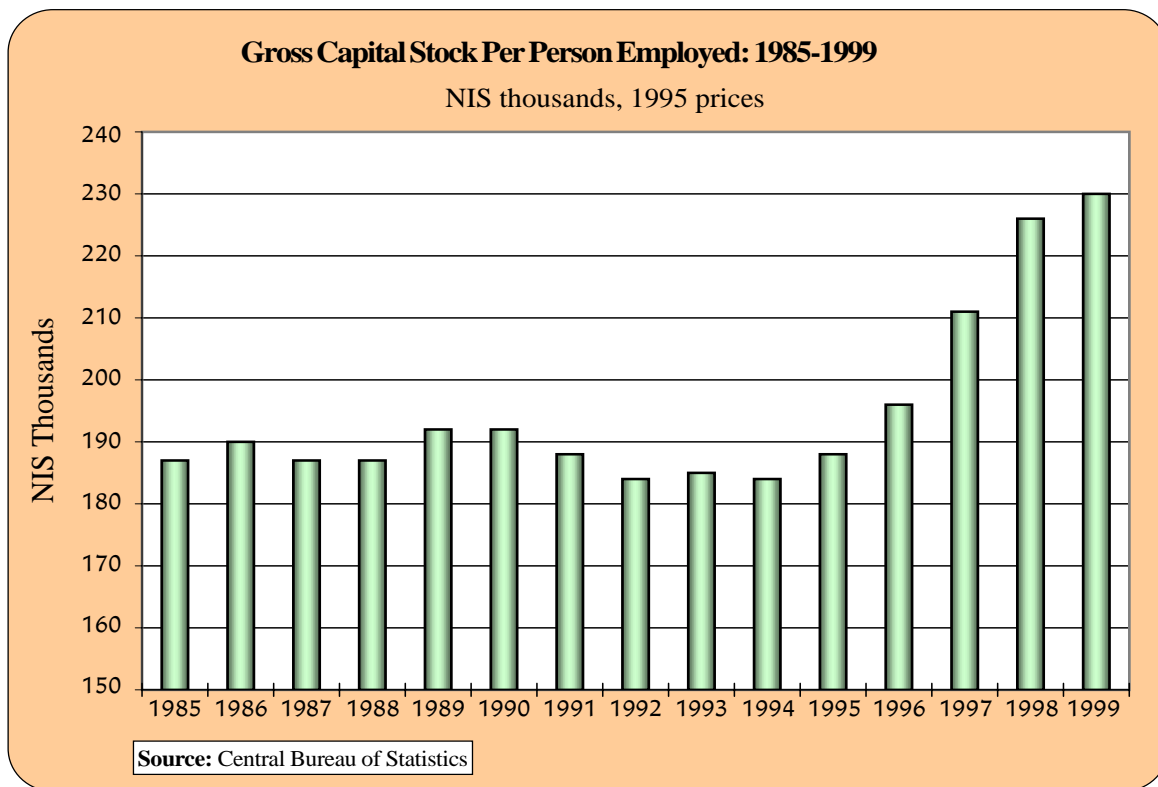
Investment

The general recovery of economic activity that began in the second quarter of 1999 is reflected in an increase in investments. After negative growth rates in 1997 and 1998, fixed investments turned around in 1999, increasing by 0.6 percent, and showed further recovery in 2000 by rising by 1.8 percent in annual terms in the first half the year. During the latter period, as in 1999, the increase was composed of an upturn in nonresidential investments (3.7 percent) and a decline in residential investments (-0.8 percent).

Major Provisions of the Budget, Fiscal year 2001

In 2000, as in 1999, the vigorous growth of nonresidential investment originates, among other things, in an upturn in imports of capital goods, which increased by 14.8 percent in the first seven months of 2000 relative to the corresponding period in 1999.

Imports of raw materials are another indicator of the business sector's expectations of future economic trends. After flat performance in 1999 – an increase of only 1 percent raw-materials imports accelerated by 14 percent in the first seven months of 2000 relative to the corresponding period in 1999.



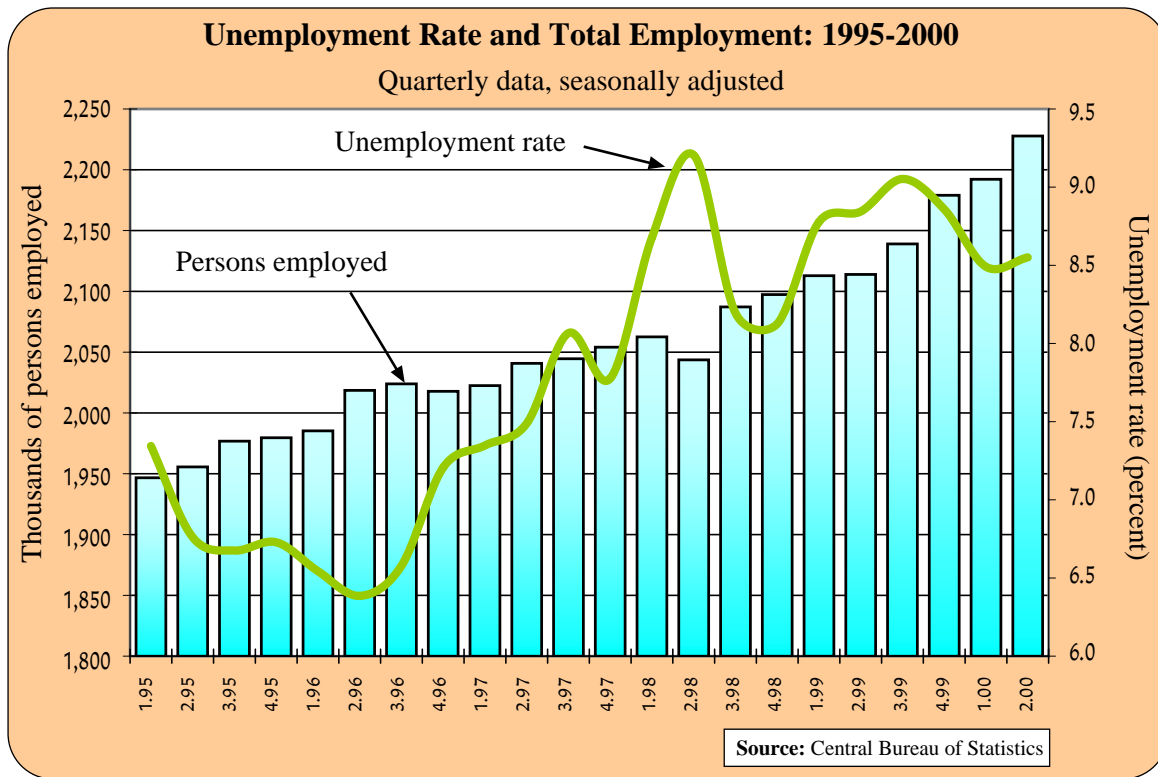
Employment

The high growth rates over the past year have been accompanied by an impressive increase in employment – 114,000 newly employed persons, most of whom found their jobs in the business sector. This figure is compatible with the typical scenario of emergence from economic slump: expansion of employment in the business sector coupled with stability in the public sector, which is less strongly affected by the state of the economy.

Main Economic Developments

Despite the encouraging job-creation figures, the unemployment rate (seasonally adjusted) has been declining less vigorously and came to 8.6 percent in the second quarter of 2000 as against 8.9 percent on average in 1999. The decrease has been gentle because the civilian labor-force participation rate has been rising steadily over the past year.

The labor-force participation rates in 1998 and 1999 were 53.4 percent and 53.8 percent, respectively. Data from the Central Bureau of Statistics show that the rate climbed to 54.5 percent in the second quarter of 2000 (seasonally adjusted). Since Israel typically has a very low labor-force participation rates relative to the standard in developed countries, an increase in this rate is a positive sign. Because a low labor-force participation rate has negative implications for potential product, the government resolved, in its economic-policy debates for 2001, to take a series of measures that will boost the rate.



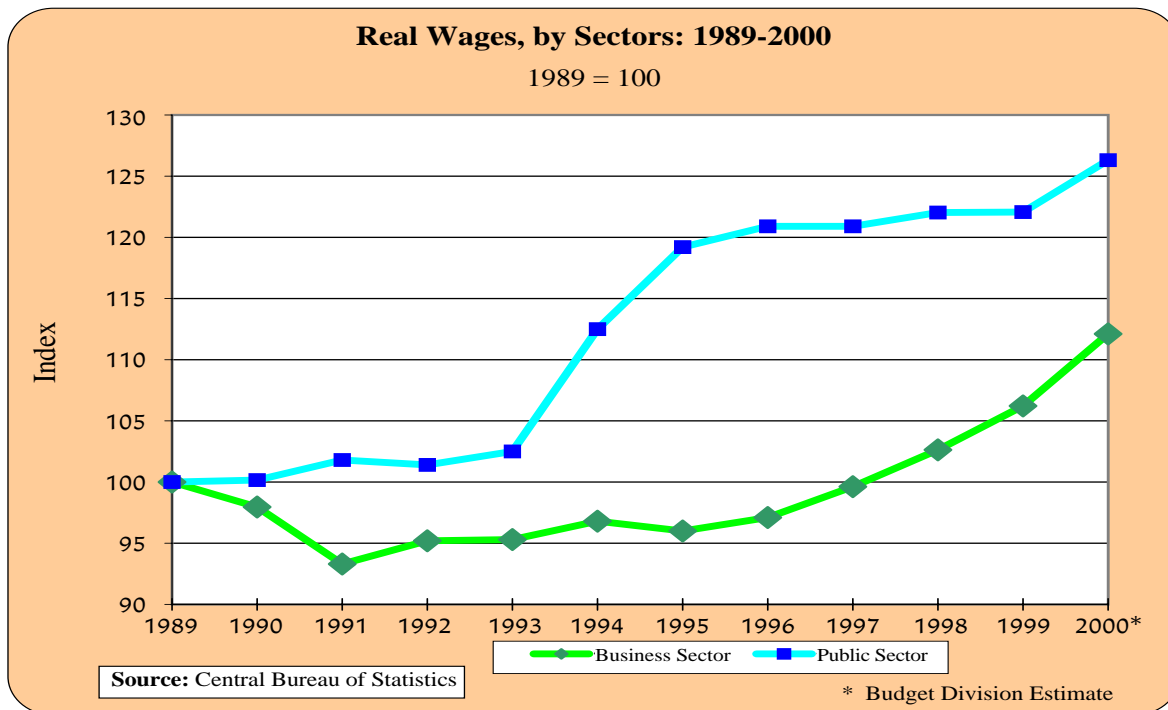
Major Provisions of the Budget, Fiscal year 2001

Wages

Real wage increases in the business sector accelerated by 7.4 percent in the first half of the year relative to the corresponding period in 1999, following real increases of 3 and 3.5 percent in 1998 and 1999, respectively. The steep upturn in 2000 was prompted mainly by difficulties that the business sector has encountered in internalizing the economy’s move to an environment of low inflation, price stability, and accelerated growth over the past year.

Real wages in manufacturing continued to climb in the first half of 2000, rising by 6 percent relative to the corresponding period in 1999. It should be borne in mind that real wages in manufacturing climbed by 5.3 percent in 1999. Israel’s economic restructuring over the past decade—the transition from traditional to high-tech industries—also helps to explain the steady increase in business-sector wages. The number of high-tech firms and their wage levels have been rising with each passing year.

In general government, real wages climbed by 4.5 percent in the first half of 2000 after having shown no increase in 1999. Accordingly, the disparity that developed in the past decade between the rates of wage increase in general government and the business sector has begun to narrow gradually.



Main Economic Developments

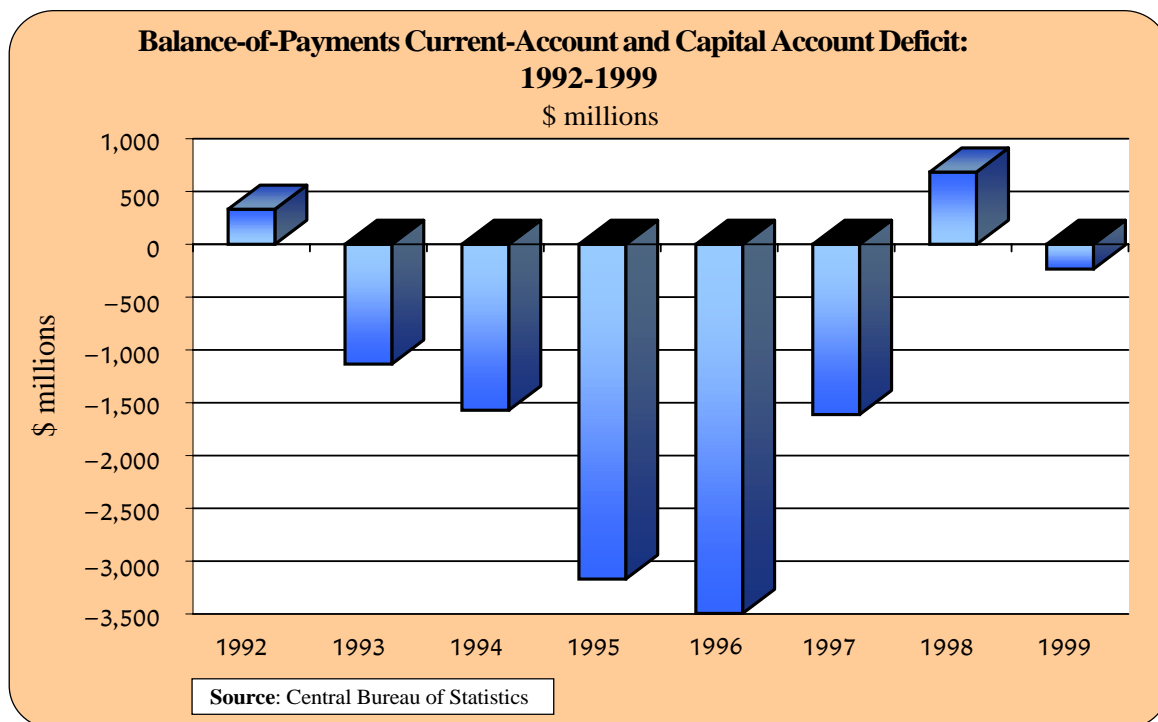
Balance of Payments and Foreign Trade

The deficit on balance-of-payments current account was \$1.1 billion in the first half of 2000, as against \$1.5 billion in the corresponding period in 1999.

The current account of the balance of payments improved significantly in 1996–1998 due to the upturn in high-tech exports, an improvement in Israel's terms of trade, and the import-restraining effect of the economic slump. The trend reversed direction in 1999, mainly due to a massive increase in imports of goods and services, occasioned by a rapid upturn in imports of capital goods.

According to figures released by the Central Bureau of Statistics in the second quarter of 2000, Israel's terms of trade worsened because export prices declined more steeply than import prices – by 2.4 percent and 0.6 percent, respectively.

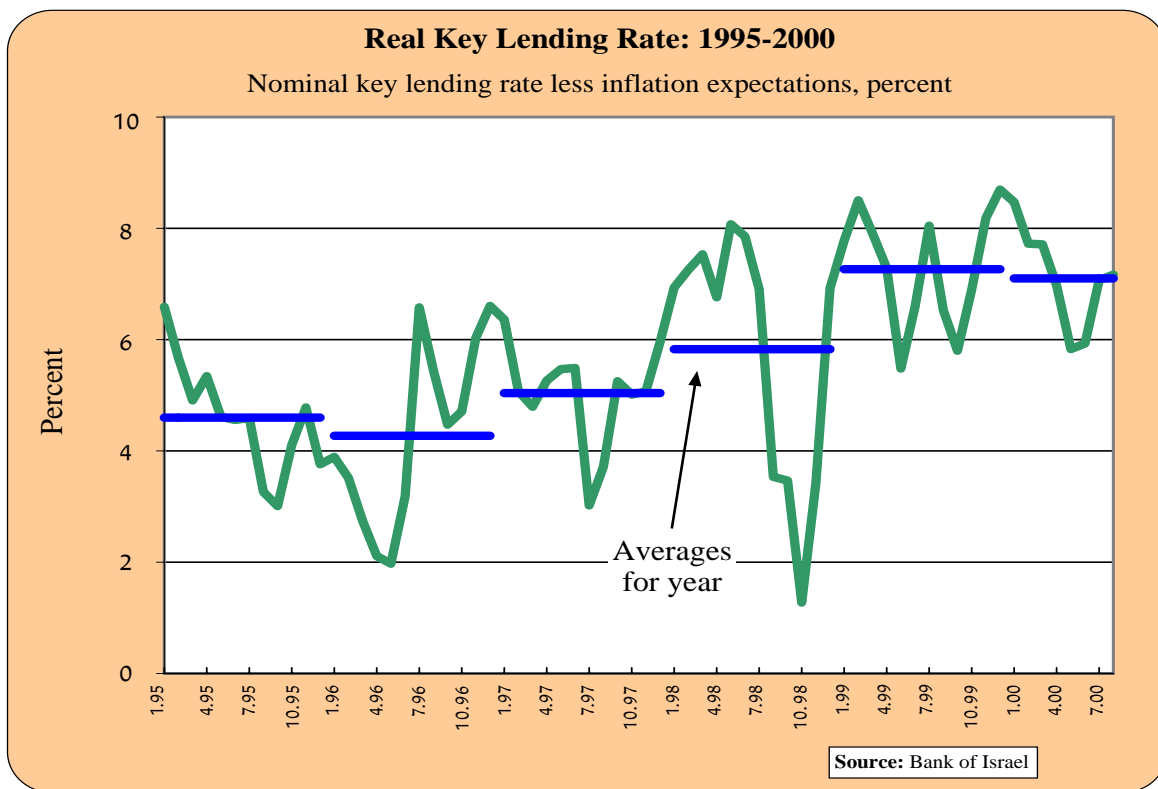
In the estimation of the International Monetary Fund, global trade will expand briskly in 2000. This development explains, among other things, the sharp upturn in exports of goods and services this year. In the first half of 2000, nondiamond exports expanded by 19.4 percent as against an increase of only 10.7 percent in imports of goods and services.



Major Provisions of the Budget, Fiscal year 2001

Monetary Policy

The Bank of Israel continued to apply monetary restraint in 2000. Nominal interest rates have not been declining as quickly as inflation in the past year or so, resulting in continued high real interest on Bank of Israel sources – 7.1 percent on average in the first eight months of the year as against 5.8 percent on average in 1998.

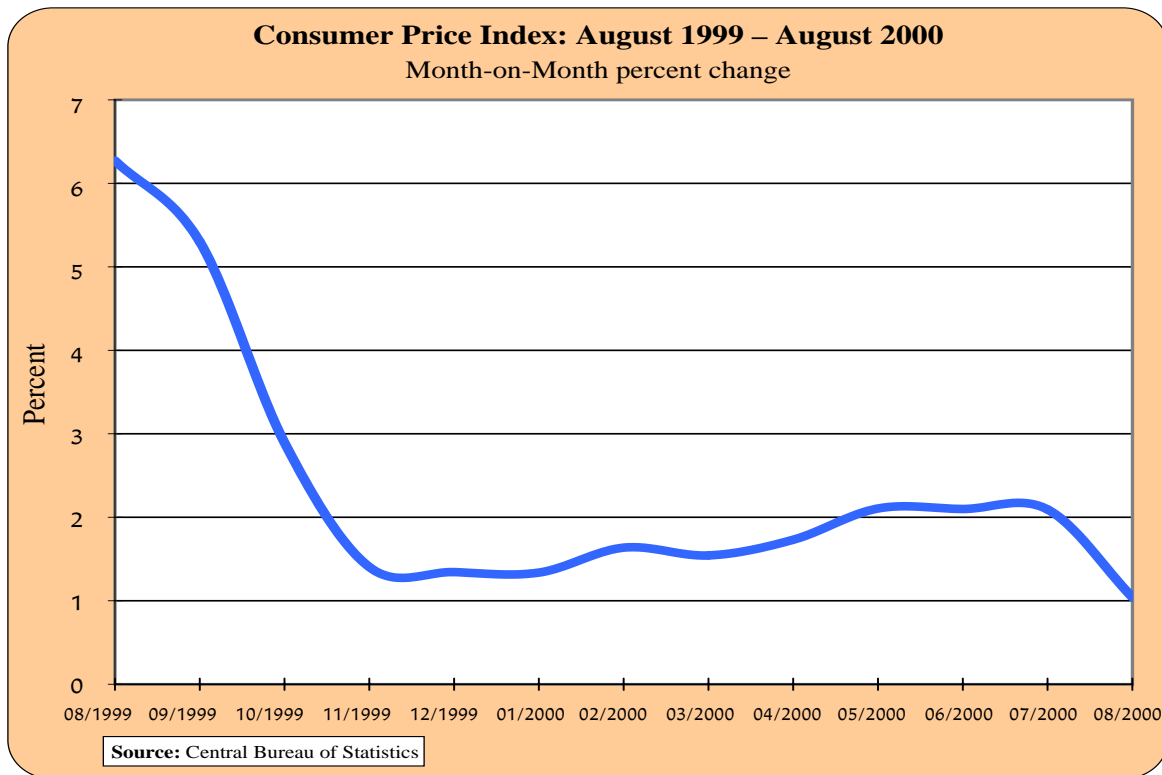


“Narrow money” (the M1 aggregate) increased in 1999 by 14.3 percent, outpacing the GDP growth rate by far. The reasons for this exceptional increase in M1 included concerns about the Y2K bug and the central bank’s preparations for it. In the first eight months of 2000, the growth rate of “narrow money” fell to only 10.1 percent.

Budget Deficit

In 1999, the total government deficit (not including allocation of credit) came to 2.5 percent, missing the target by 0.5 percent. The deficit was composed of a 2.9 percent deficit in domestic activity and a 0.4 percent surplus in activity abroad. The entire overrun in 1999

Main Economic Developments



came from the revenues side, including tax revenues, which increased with unexpected sluggishness due to the economic slowdown.

Thus, the Reduction of the Deficit Law was amended in 2000 and the government set a new target: a deficit no higher than 2.5 percent in 2000. In practice, according to early estimates, the total government deficit in 2000 (not including allocation of credit) will come to 1.75 percent of GDP. The deficit will fall short of the programmed level in the 2000 budget because of a sharp upturn in tax collection in 2000, reflecting rapid growth of economic activity and, in part, the slump in tax collection in the first half of 1999.

Accordingly, in its economic policy debates for 2001, the government set the deficit target at 1.75 percent of GDP and resolved that the total government deficit shall not exceed 1.25 percent in 2003. In each of the years 2002 and 2003, the deficit will contract by at least 0.25 percent of GDP relative to the previous year's deficit.

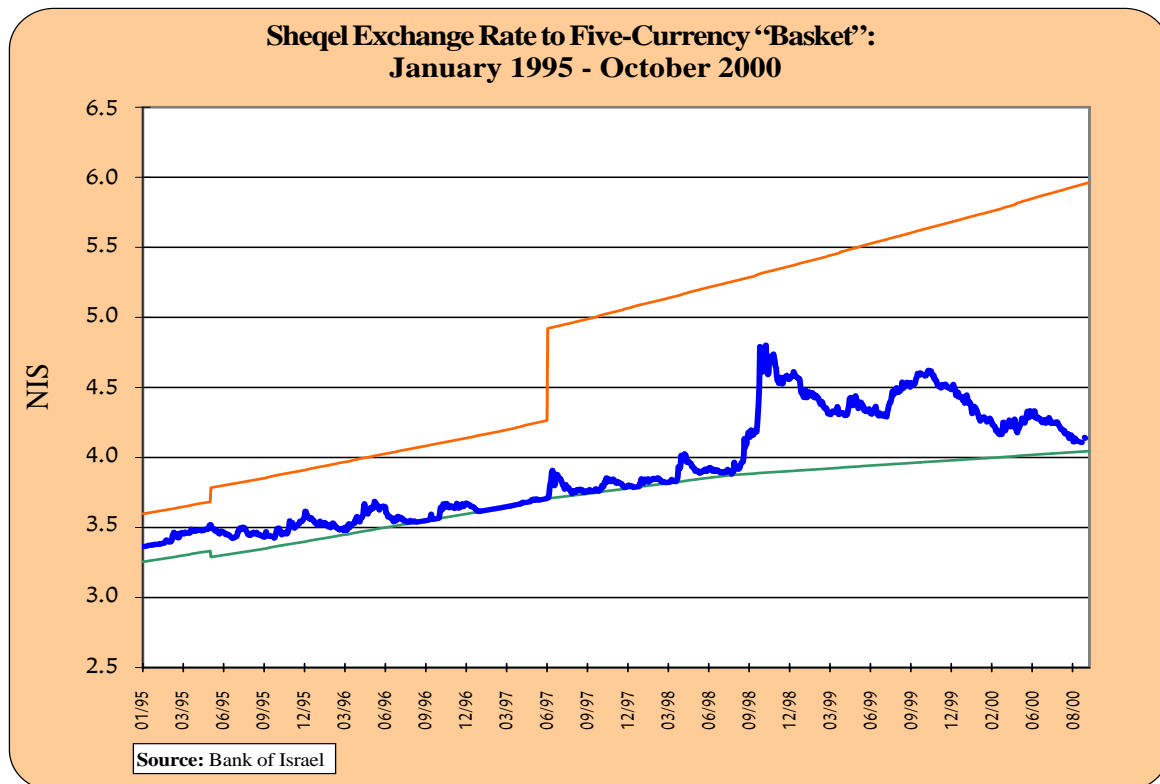
Major Provisions of the Budget, Fiscal year 2001

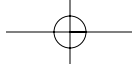
Inflation

The Consumer Price Index rose by 0.1 percent in the first eight months of 2000 as against 0.4 percent in the corresponding period in 1999. The steep disinflation is the result of tough monetary restraint, currency appreciation, and the NIS 1 billion reduction in purchase taxes that was carried out in August 2000.

Exchange Rate

In the course of 1999, the sheqel gained 2.5 percent against the five-currency “basket” and a negligible 0.4 percent against the dollar. The pace of currency appreciation intensified in 2000, as the exchange rate declined in the first eight months of the year by 3.4 percent against the dollar (because the EURO lost ground to the dollar) and by 6.5 percent against the “basket.”





Main Economic Developments

The protracted appreciation is the result of continued monetary restraint by the Bank of Israel and the awakening of domestic and global economic activity, which prompted an impressive increase in foreign investment. The sheqel continued to appreciate in the first half of 2000, as in 1999. The exchange rate continued to approach the bottom of the diagonal band and was 1.9 percent from the bottom in early September.

