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Statement by the Hon. **YAAKOV NEEMAN**,
Governor of the Fund for **ISRAEL**,
at the Joint Annual Discussion

Message of Finance Minister of Israel

Yaakov Neeman

IMF / World Bank

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Thank you very much for the opportunity to address this distinguished group on behalf of the State of Israel. The joint meetings of the International Monetary Fund and the World Bank hold great significance for the world economy and for Israel as an active participant in the world economy .

It is a great privilege to hold the meetings here in Hong Kong since hand over to the Peoples Republic of China has been effected. The Jewish people owe a great debt to China for harboring Jewish refugees during the second World War. These refugees found haven in cities like Shanghai, Tianjin, and Harbin. I am reminded of the Talmudic expression that states, "he who saves a life, it is as if he has saved the entire world." With this spirit I would like to praise both Bretton Woods Institutions and their staff for their initiative with various programs to promote and assist poor countries. In particular I would like to commend their efforts to assist the incipient Palestinian economy, and thereby promote peace. We hope that these efforts will not be undermined by recurring acts of terrorism. Such acts endanger the peace process and bring devastation to the Palestinian and to their economy. We continue to seek peace and security with the Palestinian and with all other countries in the region.

Impressive achievements

Israel's economic achievements have been quite impressive. Today the State of Israel is a highly advanced, industrialized economy. This decade is especially remarkable. During the period 1990-1996, Israel achieved GDP growth of approximately 6% per year, based mainly on high value-added industries such as high-technology. This growth rate brought Israel to about 17,000 dollars GDP per capita in 1996.

Decline in **growth Rate**

However, in the middle of 1996 a decline in the **growth** rate occurred. It is important to emphasize that this slowdown is not a recession. Moreover the Israeli economy has the potential for an even higher growth rate than the indicators show. In order to realize this potential in the future, and to return to a growth rate of 5-6% a year, in June 1996, the Government of Israel acted quickly to find a solution to the problems of the previous two years.

The problems of the economy in 1996 and the policy

The central problem of the economy was the large deficit in the current account of the balance of payments, which, in principle, is the result of the government's budget deficit. The balance of payments deficit in 1996 was 5.6% of GDP. The budget deficit was 3.9% of GDP, compared to the 3.6% planned. The government, acted immediately upon entering office, and implemented drastic cuts in the budget for the following year, 1997. The planed budget deficit for 1997 is 2.8% of GDP, in accordance with Maastricht Convention.

The government also announced a gradual reduction in the budget deficit, with a ultimate target for the year 2001 - a deficit of 1.5%. In order to achieve this goal the Government of Israel is strictly following the course of the budget. As stressed in the IMF 1997 Annual Report we shall adhere to the deficit target for 1997 and the following years. I can state with confidence that this year we will not deviate from the deficit reduction goals that we set for ourselves and the 2.8% target will be met.

The change in the budget deficit track was immediately reflected in a significant improvement in the balance of payments. Today, our estimates suggest a deficit of 3.6% of GDP, compared to 5.6% in 1996, an improvement of 2 percentage points!

Policy for 1998- budget cut

Two weeks ago the Government approved the proposed budget of 1998. This budget sets a target of further reduction in the budget deficit to 2.4% of GDP. It includes an additional cut in government spending, without cutting expenditure on infrastructure. It also includes the setting of inflation targets designed to bring about a further reduction in the inflation rate. It is not easy to implement a restrictive policy during a time of slower economic growth. The fear of further slowdown, combined with rising unemployment, increases the pressure to abandon restrictive fiscal policy. However, we are aware that there are times

when we must exercise policy restraint in the short term in order to benefit in the long term.

Structural Reforms

Let me stress, our government, which has been in office for only 15 months, has taken strong and assertive actions to improve the economy. As I mentioned the first step was regarding the budget. However, we also believe that reforms are essential for growth. We have embarked on a series of structural reforms which are designed to remove government influence in the marketplace, promote the growth of the private sector, and enhance competition. In today's world of globalization the changes we have made are only the start. We have started deregulating many different industries and sectors of the economy. Among the structural changes, which the government approved, we can find examples in telecommunications, transportation, investments, construction, and medicine. The government, in cooperation with the Bank of Israel, have announced also on a plan that removes foreign exchange controls and that will make the Israeli Shekel fully convertible by the middle of next year.

Privatization

In this past year the Israeli Government has labored intensively to expedite the process of bank privatization. The fruits of this effort reached a climax two weeks ago with the sale of controlling share over the largest bank, Bank Hapoalim. The proceeds of this transaction may end up to be 2.1 billion dollars. It should be emphasized that the sale was carried out for a price that was 25%

above the book value and 16% above its valuation on the Tel-Aviv stock market. This unprecedented success reflects confidence in the Israeli economy and in its future course. The process of selling and privatizing must be handled carefully and responsibly. The importance of the process is not only in selling, but in enhancing competition and efficiency.

The proceeds generated by our successful overall privatization policy has far exceeded our projections. Our estimates for 1997 were about \$1.2 billion in revenue, today we expect a revenue of \$2.5 billion. Moreover we have raised more money this year than has ever been raised through privatization.

Hi-tech

The world market, with its' fierce competition and almost endless possibilities, is the target of most Israeli start-ups today. Israel has become one of the world's leaders in the high tech field. About one third of our export of goods is in Hi-Tech industries which in the last two years has grown at an annual rate of about 15%. It is remarkable to notice that over 3000 start-up high-tech projects are presently conducted in Israel.

Financial world markets

The world is aware of the economic possibilities that the Israeli economy has to offer. Many Israeli enterprises utilize the capital markets abroad to finance their products. After the United States and Canada, Israel has the largest number of

companies listed on NASDAQ. Most of these are in the high tech field. At the same time foreign Investment in Israel continues to increase.

To close

The economic forecast for the State of Israel is promising. We are making the necessary changes so the economy will prosper. I can assure you that we will keep to our plan for economic reforms. We will continue to pave the way towards a future of stability; sustainable economic growth; adhere to the target of reducing the budget deficit; reducing the rate of inflation; and prosperity.

Finally, On behalf of the State of Israel I would like to express my gratitude and appreciation to the Managing Director of the Fund Mr. Michael Camdessus and President of the World Bank Mr. James Wolfensohn. I would like to thank also the Executive Directors, the staff and the Joint Secretariat for successful and fruitful meetings.