

## Weekly Macroeconomic Review

February 2, 2010

	Expectations derived from the capital market	Our forecast
Inflation in the coming months		Minus 0.2% in January Minus 0.2% in February
Future cumulative inflation – next 12 CPIs (through November 2010 CPI)		2.0%
Inflation through July 2011 CPI (average annual rate)	2.3%	2.4%
Bank of Israel interest rate, 6 months ahead	1.60% (up 0.35)	2.00%
Fed interest rate, 6 months ahead	0.30% (up 0.05)	0.30%
Yield on Israeli Government 10-Year bond, 6 months ahead	5.28% (up 0.26)	5.25%
Yield on US Treasury 10-Year bond, 6 months ahead	3.91% (up 0.25)	4.25%
Dollar exchange rate, 6 months ahead	NIS 3.71 (unchanged)	NIS 3.71 (unchanged)

### Israel

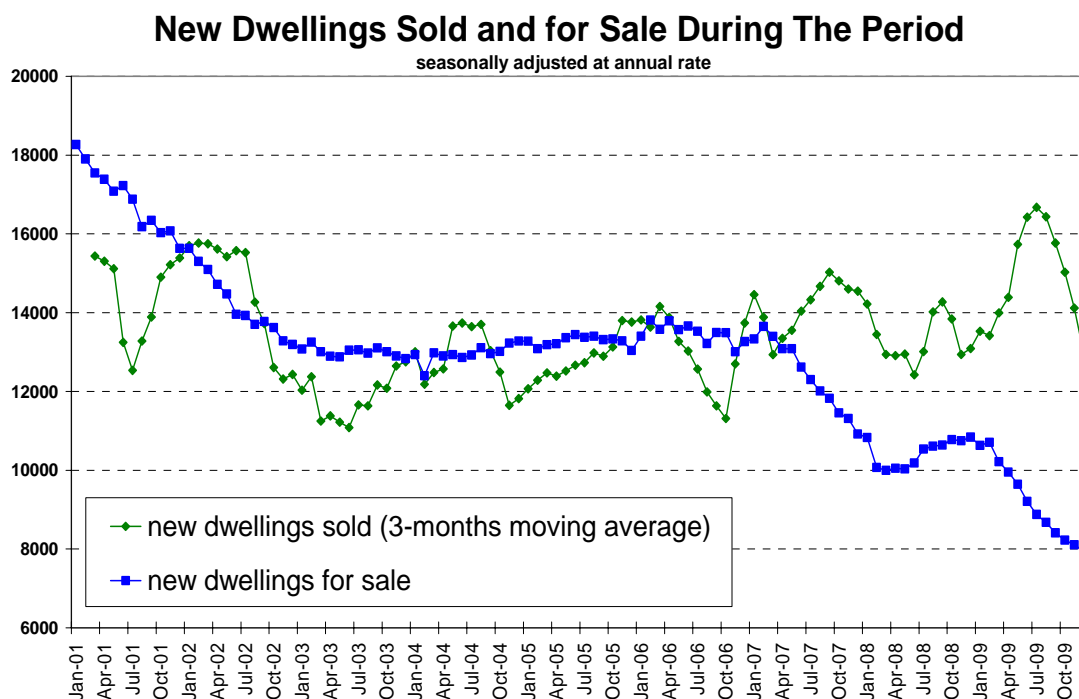
The Bank of Israel has published its quarterly **Inflation Report**. This report contains an essential change from previous publications: It presents a forecast by the BOI's research division concerning inflation and interest rates in the coming two years. Previously, the BOI only published the results of two econometric models, which often generated very different results, without specifying which forecast the BOI believed to be accurate. **We have recommended** this change many times over the last few years, and of course, we welcome the decision. In our opinion, the new format substantially strengthens the transparency and credibility of monetary policy, improves the ability of the public and of capital-market players to understand BOI policy, and increases the accountability of BOI decisions.



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As for the **research division's actual forecast**: Twelve-month inflation, which stood at 3.6 percent in the last quarter of 2009, is expected to fall to approximately 2.50 percent in the last quarter of 2010 and 2.00 percent in the last quarter of 2011. Meanwhile, the **BOI interest rate** is expected to rise to about 3.25 percent in the last quarter of 2010 and 5.00 percent in the last quarter of 2011. **We believe** that inflation will be slightly lower in 2010, and the interest rate will rise a bit less quickly. The difference between our estimate and the research division's forecast may stem from the fact that our growth forecast is somewhat less optimistic than the BOI's estimate.

The number of new homes sold decreased by 11 percent in December and by 12 percent in the twelve months through December. The supply of homes for sale decreased by 2 percent, reaching a new low.



## Developments in the Global Economy

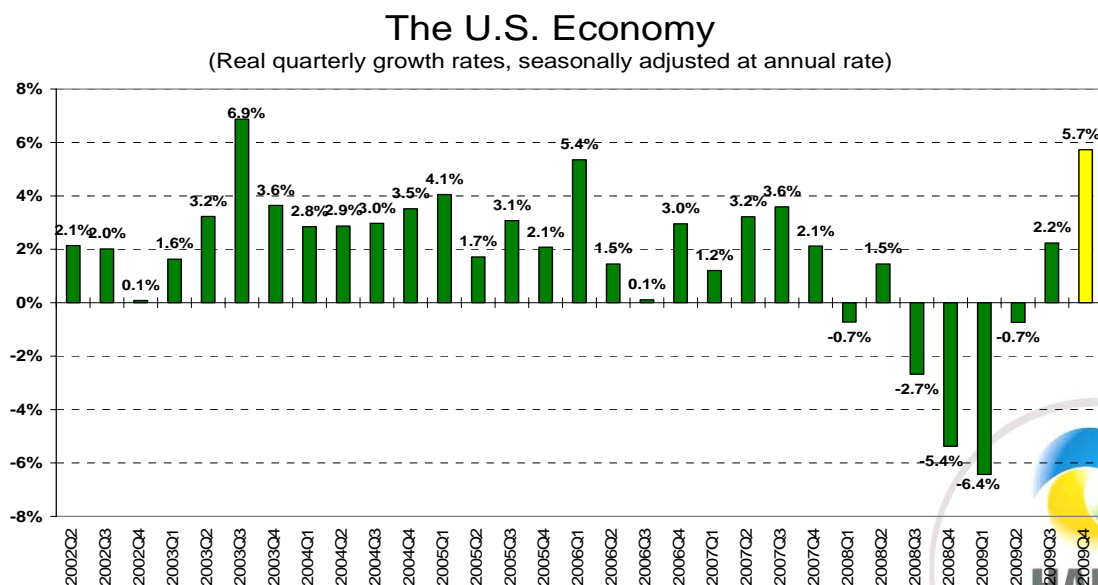
The International Monetary Fund (IMF) has adjusted its global growth forecast upward. The revised forecast predicts **global growth** of 3.9 percent in 2010, following negative growth of 0.8 percent in 2009, with 2.1 percent growth in the advanced countries, including **2.7 percent in the US** and **1.0 percent in the euro zone**. These estimates are slightly lower than the average forecast in the *Economist* survey for 2010 (2.8 percent in the US and 1.4 percent in the euro zone).

The IMF expects global growth in 2011 to reach 4.3 percent, with the growth rate in the US slowing to 2.4 percent and euro-zone growth reaching 1.6 percent. The inflation forecast for the advanced countries stands at an annual average of 1.3 percent in 2010 and 1.5 percent in 2011.

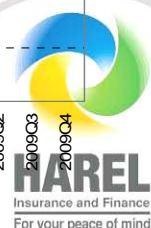
## United States

The Fed left the interest rate unchanged at 0-0.25 percent, as expected.

According to an initial estimate, the **US economy grew** at an annualized rate of 5.7 percent in the last quarter of 2009, far above earlier estimates. However, the increase in inventories, which is not expected to recur in the coming quarters, had a decisive contribution to the high growth rate. Excluding this element, the growth rate was only 2.2 percent.



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The ISM manufacturing sector index stood at 58.4 points in December, above expectations.

Real private consumption increased by just 0.1 percent in December. The core price index (the PCE deflator) also rose by only 0.1 percent in December. Households' rate of savings increased to 4.8 percent in December, from 4.5 percent in November.

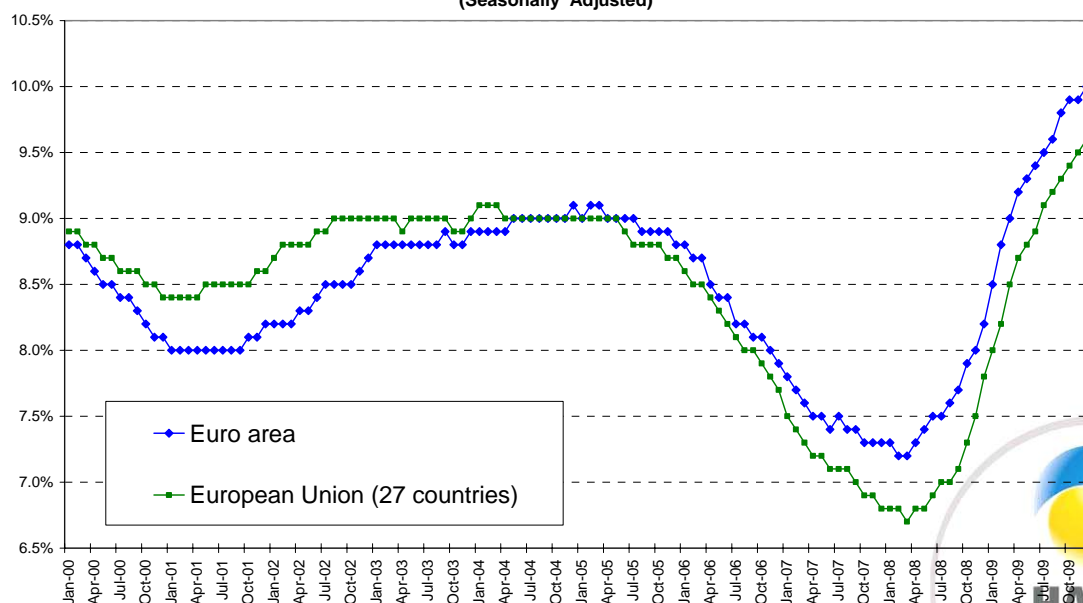
The average annual savings rate reached 4.6 percent in 2009, versus 2.7 percent in 2008 and 1.7 percent in 2007. The increase in the savings rate over the last two years was a natural reaction to the economic crisis and the decline in home prices. In our opinion, the increase in the savings rate will continue in the coming years, tempering the growth of private consumption and slowing the growth rate of the American economy.

## Euro zone

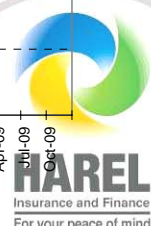
Twelve-month inflation reached 1.0 percent in December (according to the initial estimate), slightly lower than expected.

Unemployment in the euro zone was 10.0 percent in December, up from 8.2 percent in December 2008.

**Euro area and Eu27 Unemployment rates**  
(Seasonally Adjusted)



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## Our forecast of cumulative changes in price indices due to be published during the coming three months

Forecast change, December 2009 to March 2010

Consumer Prices Index (CPI)	Housing component in the CPI (mainly rent prices)	Prices of Owner-Occupied Dwellings	Price Index of Inputs in Residential Building	Wholesale Price Index of Manufacturing (excl. Fuel)
-0.4%	-0.4%	2.9%	0.0%	-0.8%

## Important Announcements in the Coming Week

- Data on retail sales in the euro zone and the ISM services sector index in the US will be published on Wednesday, February 3.
- Interest-rate decisions will be announced in the UK and the euro zone on Thursday, February 4.
- The employment report will be published in the US on Friday, February 5.
- Israel's Central Bureau of Statistics will publish data on jobs and average wages on Sunday, February 7.

This review is posted online at [www.harel-finance.co.il/macro](http://www.harel-finance.co.il/macro) in Hebrew and at <http://www.harel-group.com/finance.html> in English.

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