

Weekly Macroeconomic Review

August 11, 2009

	Expectations derived from the capital market	Our forecast
Inflation in the coming months		1.0% in July 0.6% in August
Future cumulative inflation – next 12 CPIs (through June 2010 CPI)		3.3%
Inflation through July 2011 CPI (average annual rate)	3.5%	2.8%
Bank of Israel interest rate, 6 months ahead	1.60% (up 1.10)	1.00%
Fed interest rate, 6 months ahead	0.65% (up 0.40)	0.50%
Yield on Israeli Government 10-Year bond, 6 months ahead	5.71% (up 0.31)	5.71%
Yield on US Treasury 10-Year bond, 6 months ahead	4.04% (up 0.25)	4.25%
Dollar exchange rate, 6 months ahead	NIS 3.84 (unchanged)	NIS 3.84 (unchanged)

Israel

The Bank of Israel announced that it would stop its daily foreign-currency purchases. The BOI also reiterated last week's statement that it would "*act in the foreign-currency market in the event of exceptional fluctuations in exchange rates incongruent with basic economic conditions, or when the foreign-currency market is not functioning properly.*"

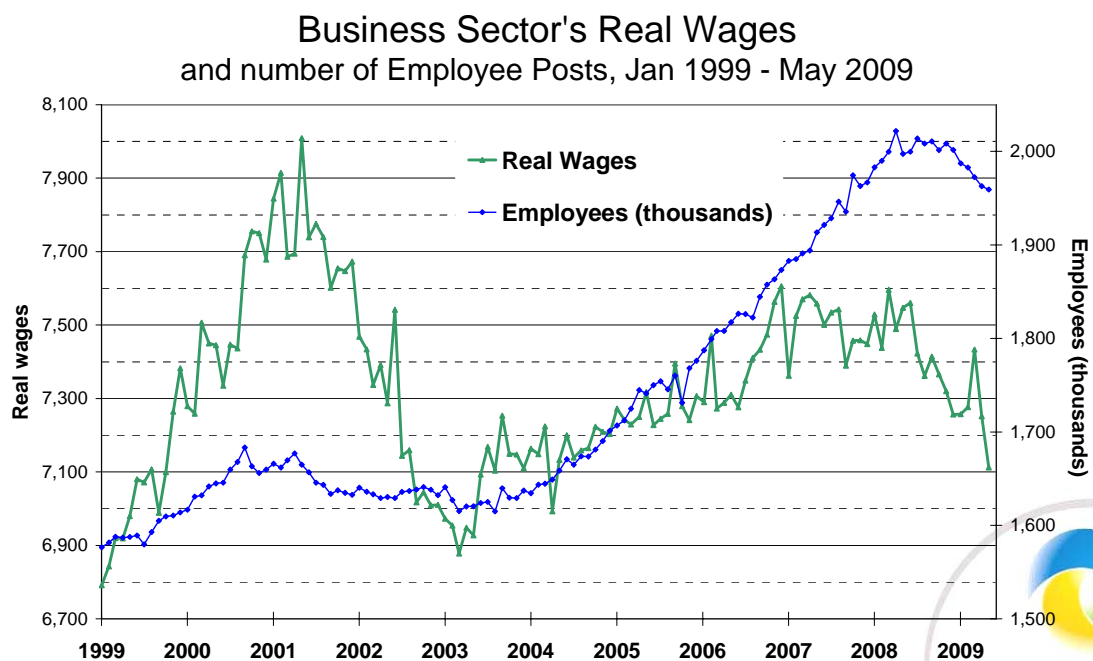
At this stage, it appears that the exceptional intervention initiated by the BOI a week ago is aimed at increasing its flexibility and preparing for the cessation of its regular intervention in the foreign-currency market. We estimate that if there is no rapid appreciation of the shekel, the BOI will gradually cease its exceptional intervention in this market. However, if the shekel continues to gain strength, the BOI will continue to intervene; the BOI hopes that the "threat" of continued intervention in its own right will stabilize the exchange rate and prevent further appreciation of the shekel.



In our opinion, the shekel exchange rate against the currency basket is not far from equilibrium; we do not expect substantial depreciation or appreciation at this stage.

State tax revenues totaled ILS 18.1 billion in July, the second-largest amount in history (after ILS 18.2 billion in July 2007). A considerable part of the sharp increase in revenue resulted from the increase in VAT and from advance imports of cars before the increase in purchase tax took effect, within the "green taxation" plan, at the beginning of August. However, it appears that revenues would have grown considerably even excluding these effects.

Employment and wage data for May indicate continued stagnation in the labor market and a decrease in average wages. **The number of employee positions of Israeli workers** grew at a minuscule rate of 0.1 percent in May, but decreased by 0.8 percent in the twelve months ended in May. **Average nominal wages for an employee position of Israeli workers** decreased by 1.6 percent in May and by 2.8 percent in the twelve months ended in May (a real decrease of 5.5 percent). The number of employee wages in the **business sector**, including non-Israelis, decreased by 0.2 percent in April, while real wages dropped sharply by 1.9 percent.



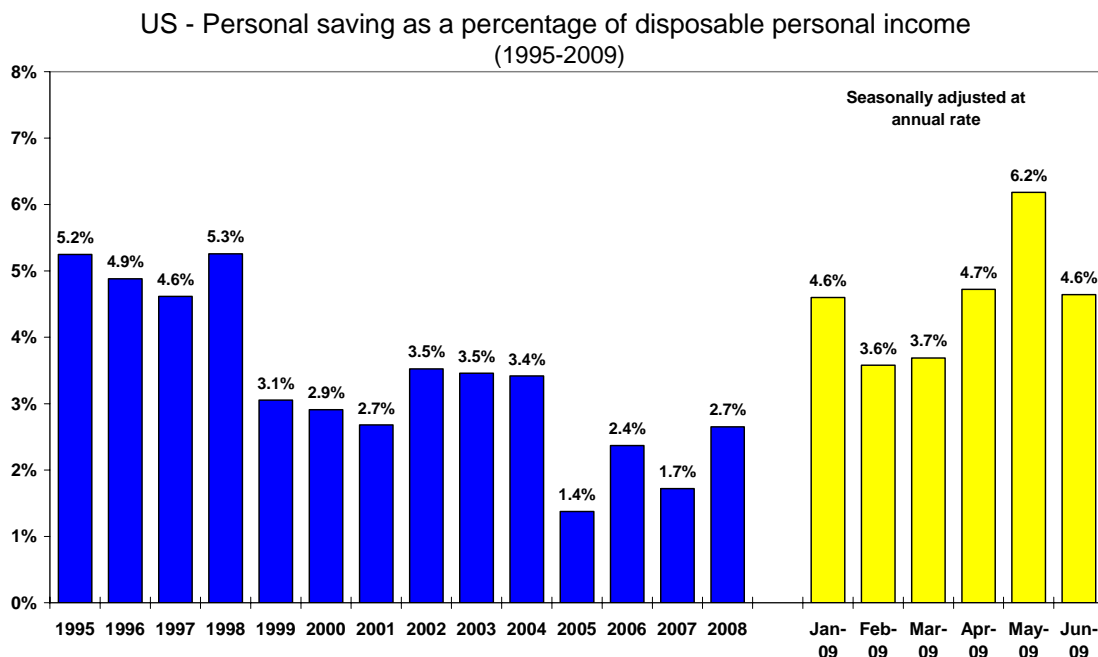
Growth forecasts for advanced economies

The *Economist* has published its **monthly Consensus Forecast** of growth rates in the advanced countries. Forecasts for Japan and the UK in 2009 decreased, but there were no significant changes in the forecasts for 2010.

United States

Data published over the last week were mixed. Data on income, consumption, and the ISM index contributed to the negative sentiment, which reversed at the publication of the employment report.

Real private consumption decreased by 0.1 percent in June, following 0.0 percent in May and a decrease of 0.2 percent in April. The **rate of households' savings** decreased to 4.6 percent in June, after an exceptional 6.2 percent in May, influenced by government fiscal incentives.

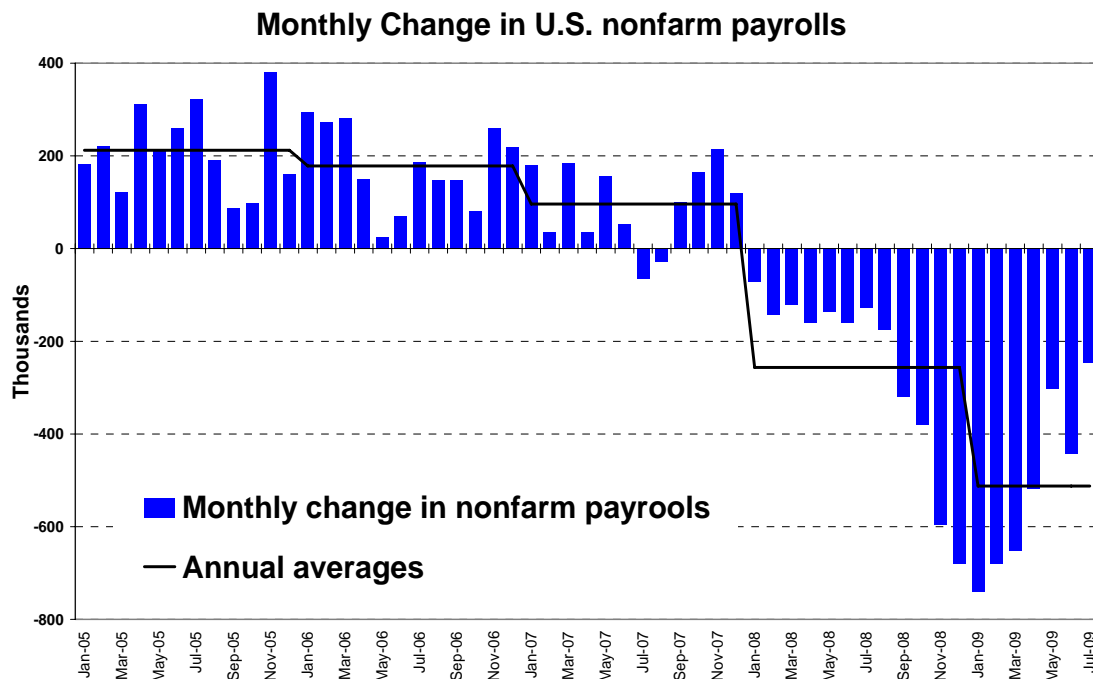


Core inflation of private consumption prices (core PCE) stood at 0.2 percent in June, following rates of 0.1 percent in May and 0.3 percent in April.

The **ISM service sector index** reached 46.4 points in July, below expectations.



The employment report for July was surprisingly positive. The number of employed persons decreased by 247,000, versus expectations of a steeper decline of 320,000.



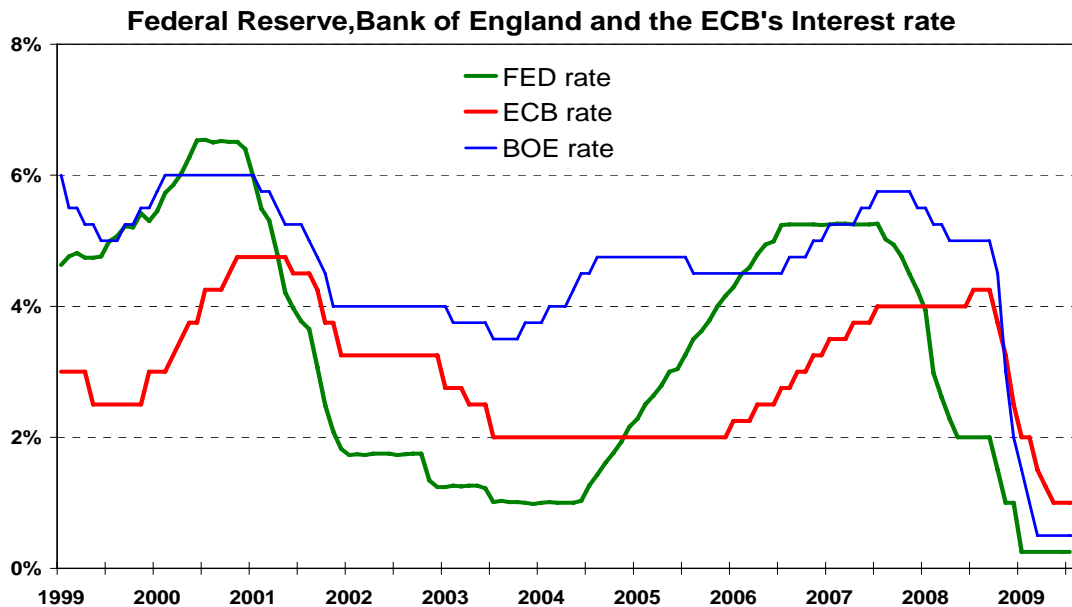
The unemployment rate decreased by 0.1 percentage points, in contrast to expectations, to 9.4 percent. A contributing factor was the decrease of 0.2 percentage point in the workforce participation rate, to 65.5 percent.

Following the employment figures, equity markets posted gains, yields of long-term government bonds rose sharply, expected inflation in the coming years increased, the expected Fed interest rate rose, and the dollar gained strength against other major currencies.

Europe

The European Central Bank left the interest rate unchanged for the third consecutive time, at 1.0 percent, as expected. The Bank of England also left the interest rate unchanged at 0.5 percent, in line with expectations.





Although the BOE's interest-rate decision was not surprising, it increased its quantitative expansion plan by GBP 50 billion to GBP 175 billion, beyond expectations. The BOE estimates that bond purchases will be carried out over a period of three months.

Important Announcements in the Coming Week

- The Central Bureau of Statistics (CBS) will publish Israel's foreign trade data, and the Fed's interest-rate decision will be announced in the US, on Wednesday, August 12.
- Data on retail sales will be published in the US, and the initial estimate of growth in the second quarter of 2009 will be published in the euro zone, on Thursday, August 13.
- The consumer price index for July will be published in Israel, the US, and the euro zone on Friday, August 14.
- The CBS will publish initial estimates on national accounts and growth in the second quarter of 2009 on Sunday, August 16.



This review is posted online at www.harel-finance.co.il/macro in Hebrew

and at www.harel-finance.co.il/macro/ENG in English.

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