

## Weekly Macroeconomic Review

March 11, 2009

	Expectations derived from the capital market	Our forecast
<b>Inflation in the coming months</b>		0.2% in February 0.4% in March
<b>Future cumulative inflation – next 12 CPIs (through January 2010)</b>		2.0%
<b>Inflation through May 2010 CPI (average annual rate)</b>	0.7%	2.5%
<b>Bank of Israel interest rate, 6 months ahead</b>	0.85% (up 0.10)	0.75%
<b>Fed interest rate, 6 months ahead</b>	0.40% (up 0.15)	0.25%
<b>Dollar exchange rate, 6 months ahead</b>	NIS 4.22 (unchanged)	NIS 4.26 (up 1.2%)

## Israel

**State tax revenues** amounted to only ILS 13.5 billion in February. This figure is consistent with our estimate of an expected shortfall of ILS 35-40 billion, or about 5 percent of GDP, in tax revenues this year, relative to the original planning in the state budget.

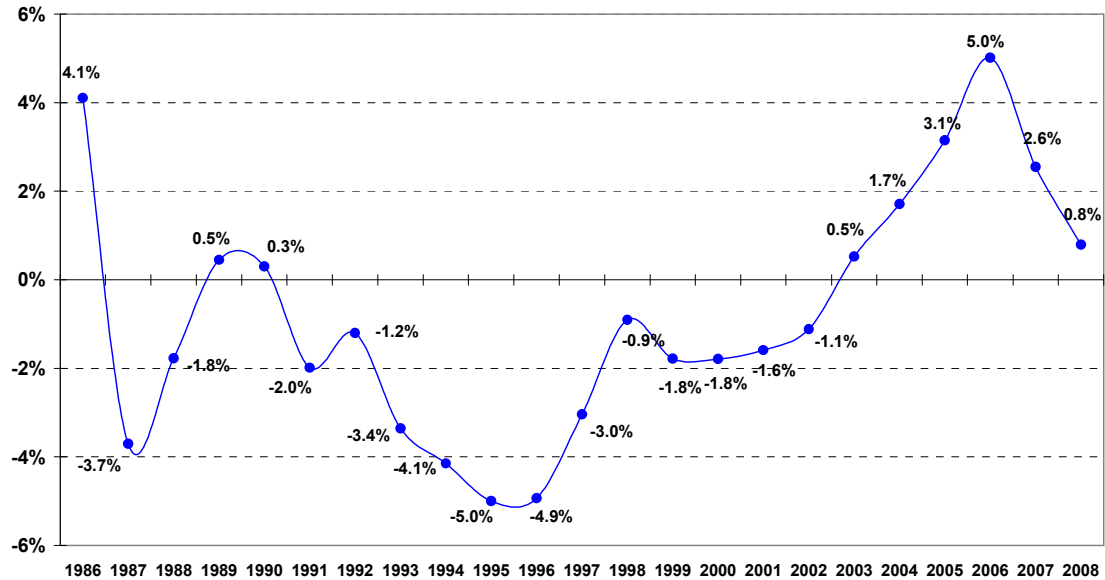
According to statements by the Governor of the Bank of Israel, the **BOI's growth forecast** for 2009 has been lowered to a negative 1.5 percent, from the estimate of a negative 0.2 percent in January. The Governor also noted that if the state budget deficit grows, the BOI recommends postponing the tax cuts planned for 2010 and cancelling tax exemptions. We agree with this position.

Based on the amended estimate of the Central Bureau of Statistics, **growth in 2008** stood at 4.0 percent, versus the 3.9 percent estimate published at the end of February; growth in the second half was 1.3 percent, versus 1.1 percent in the previous estimate. Private consumption, exports, and imports were adjusted upward.



The surplus in the current account of the balance of payments totaled 0.8 percent of GDP (USD 1.6 billion) in 2008, following 2.6 percent in 2007 and a record 5.0 percent of GDP in 2006.

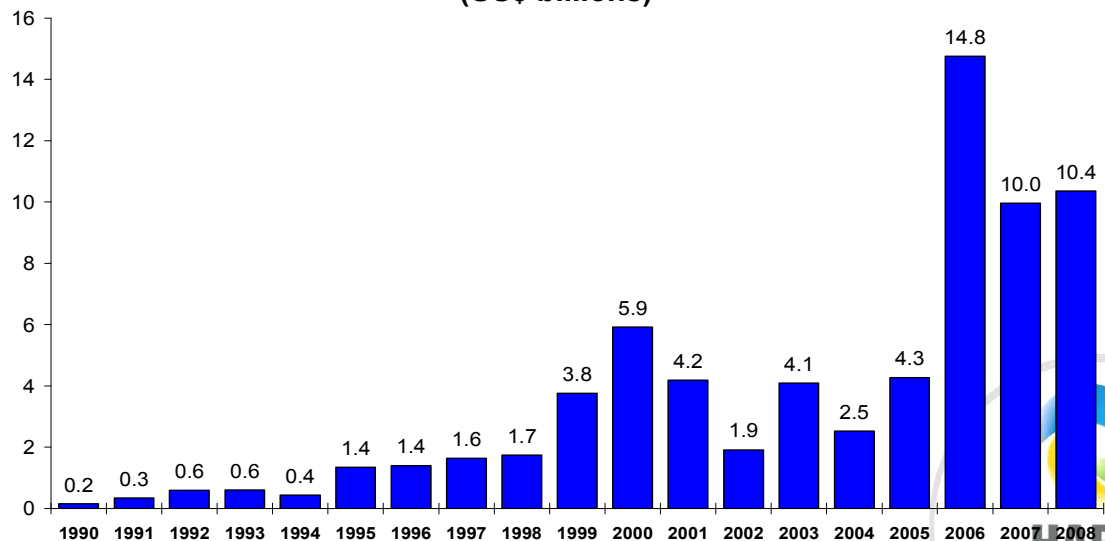
### The Current Account (as percent of GDP)



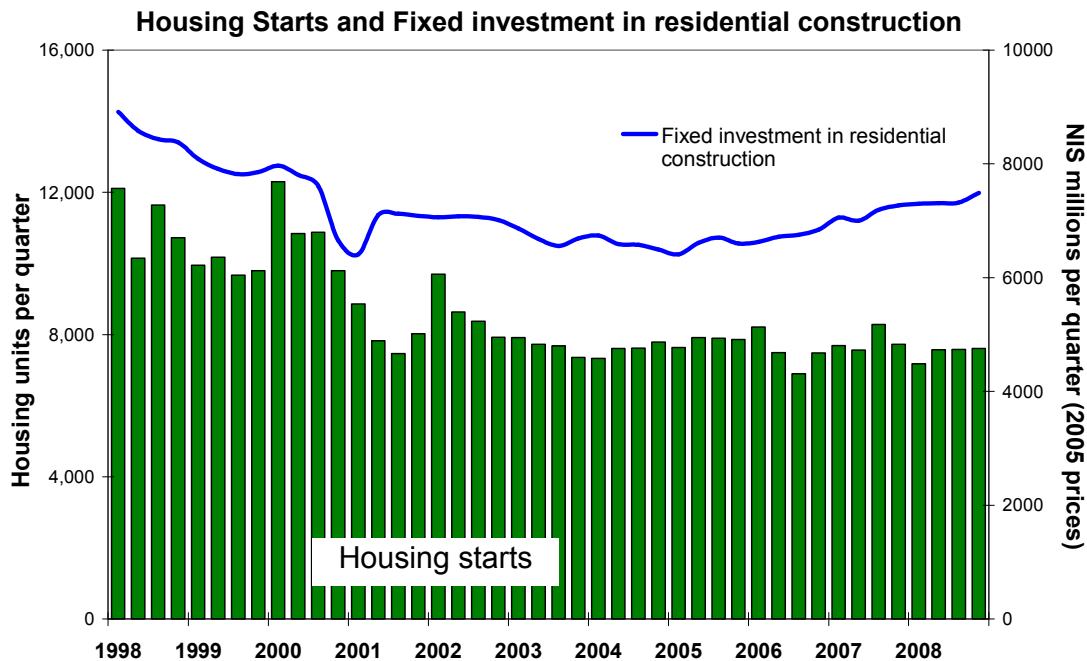
The surplus in the current account totaled USD 0.5 billion in the fourth quarter of 2008, versus USD 0.7 billion in the preceding quarter. **Exports and imports of goods and services** decreased by 13 percent in the fourth quarter, in dollar terms, based on data net of seasonal effects.

**Foreign direct investments in Israel** totaled USD 10.4 billion in 2008, similar to 2007. Direct investments in the fourth quarter reached USD 1.9 billion, versus an average of USD 2.9 billion in the preceding three quarters.

### Net Inflows of Foreign Direct Investment in Israel (US\$ billions)



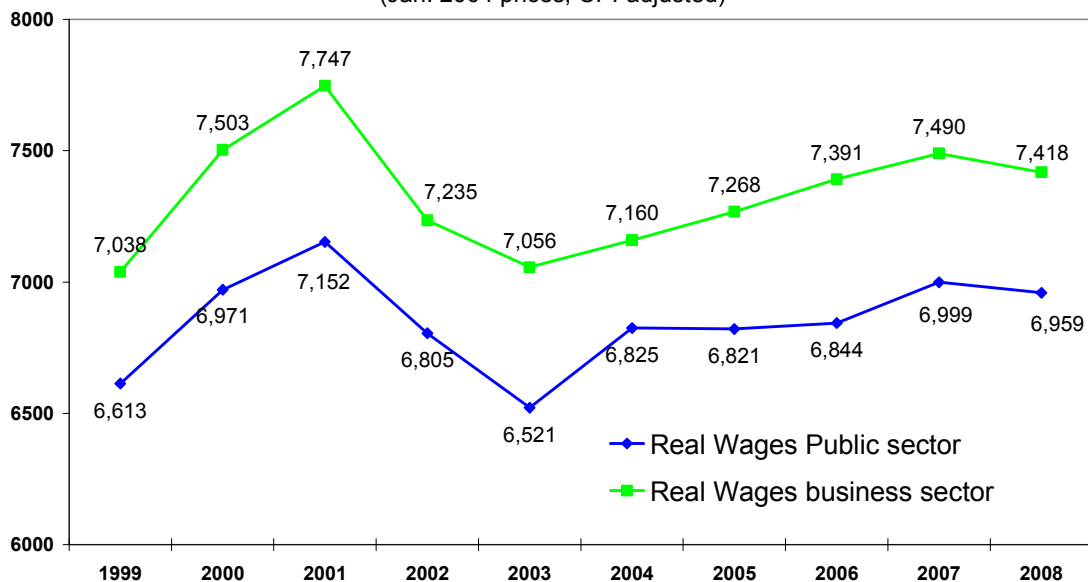
The number of construction starts remained stable in the fourth quarter of 2008.



The number of employee positions in the Israeli economy increased by 3.6 percent in 2008, following a 5.0 percent gain in 2007. Real wages decreased by 0.8 percent in 2008, following consecutive increases in 2003-2007.

### Real Wages, 1999-2008

(Jan. 2004 prices, CPI-adjusted)



The number of employee positions in the **business sector**, including non-Israelis, decreased by 0.4 percent in December, while real wages fell by 1.4 percent.

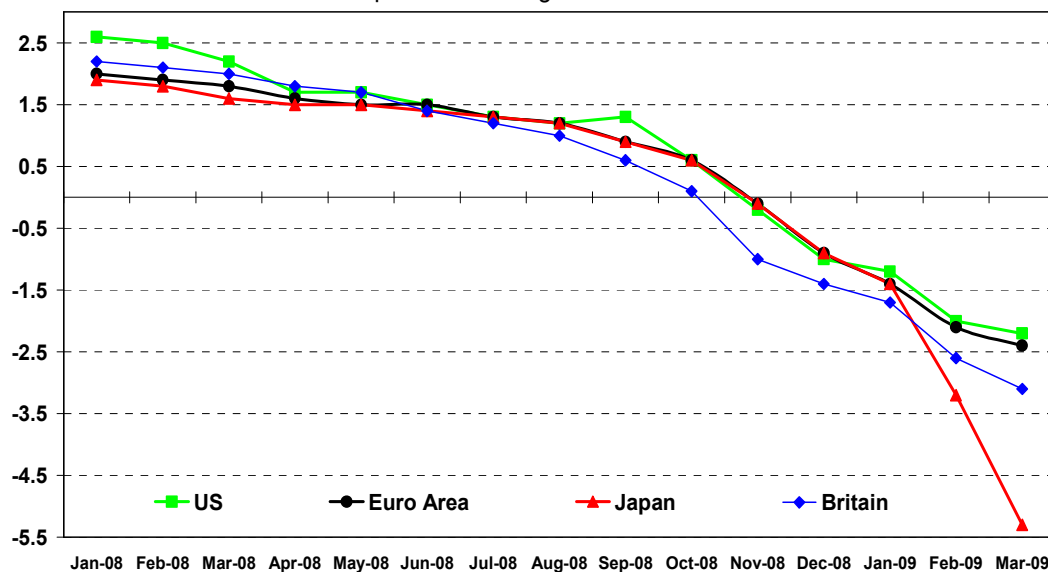
In line with our estimates, **expected inflation** derived from the capital market (the difference between the unlinked and linked government curves) through the May 2010 CPI grew to an annualized rate of 0.7 percent, from zero at the end of January. Despite the increase in inflation expectations in the last two months, we estimate that inflation during this period will be higher.

## Growth forecasts for advanced economies

The *Economist* has published its **monthly Consensus Forecast** of growth rates in the advanced countries: **Growth forecasts for 2009 continued to fall**, especially for **Japan** (negative 5.2 percent). Estimates for growth in 2010 are positive but moderate, at 1.9 percent in the US and 0.7 percent in the euro zone.

### Growth Forecasts for 2009

as published during the last months



Source: The Economist, Consensus Forecast

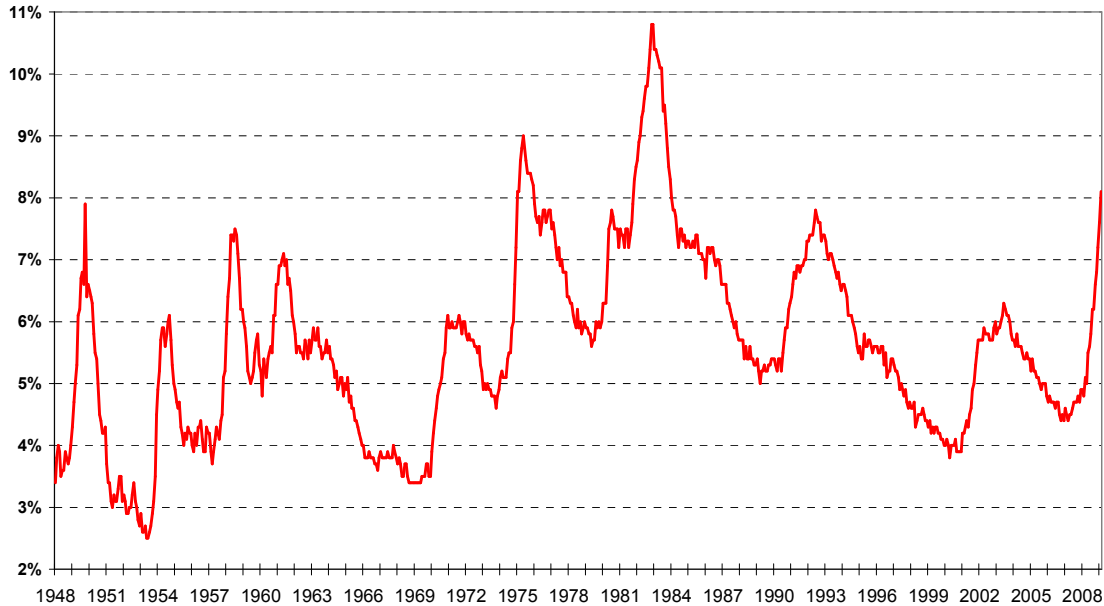
## United States

The Fed Chairman gave a speech this week emphasizing that the duration and scope of the crisis depend on the ability of the administration and the central bank to stabilize financial institutions, and declared that they would not allow large, important financial entities to collapse. These words contributed to sharp gains in the stock markets.



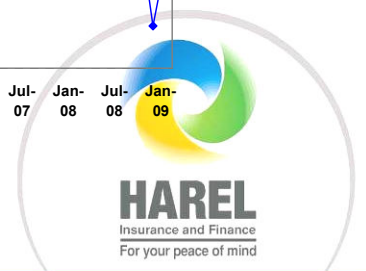
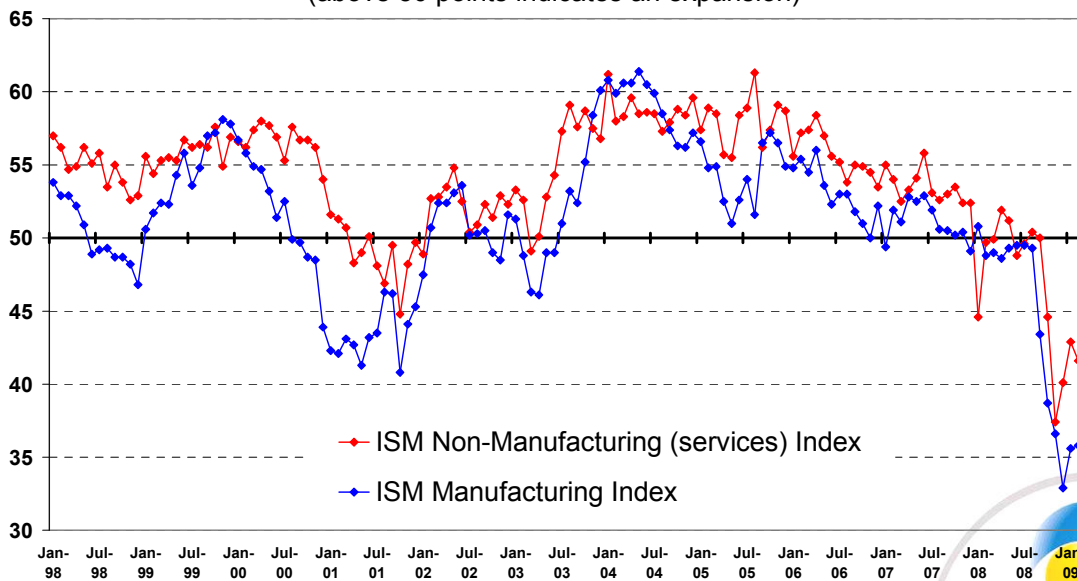
The employment report for February was weak. The labor market lost 650,000 jobs, as expected, but data for the previous months were adjusted downward. The unemployment rate rose to 8.1 percent, from 7.6 percent in January, the highest rate in sixteen years.

### U.S. Unemployment rate



The ISM service sector index in the US stood at 41.6 points in January, above expectations, but still below 50 points, indicating contraction.

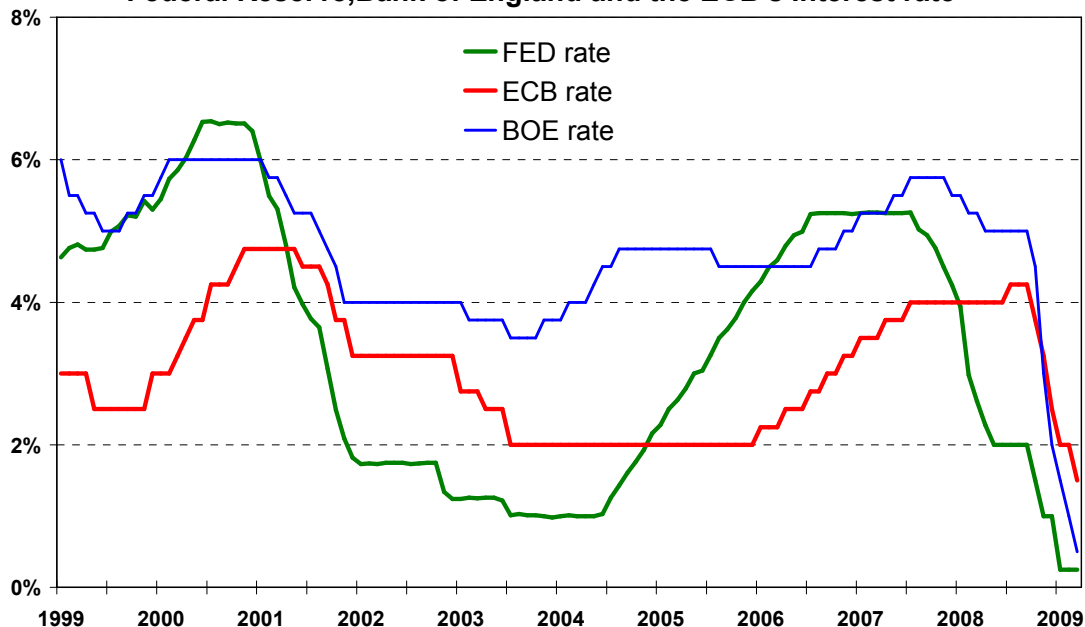
### The Institute for Supply Management Index (above 50 points indicates an expansion)



## Europe

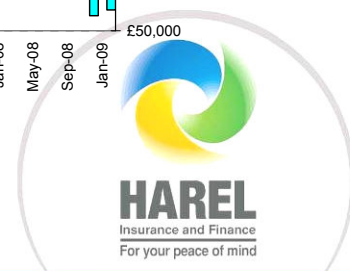
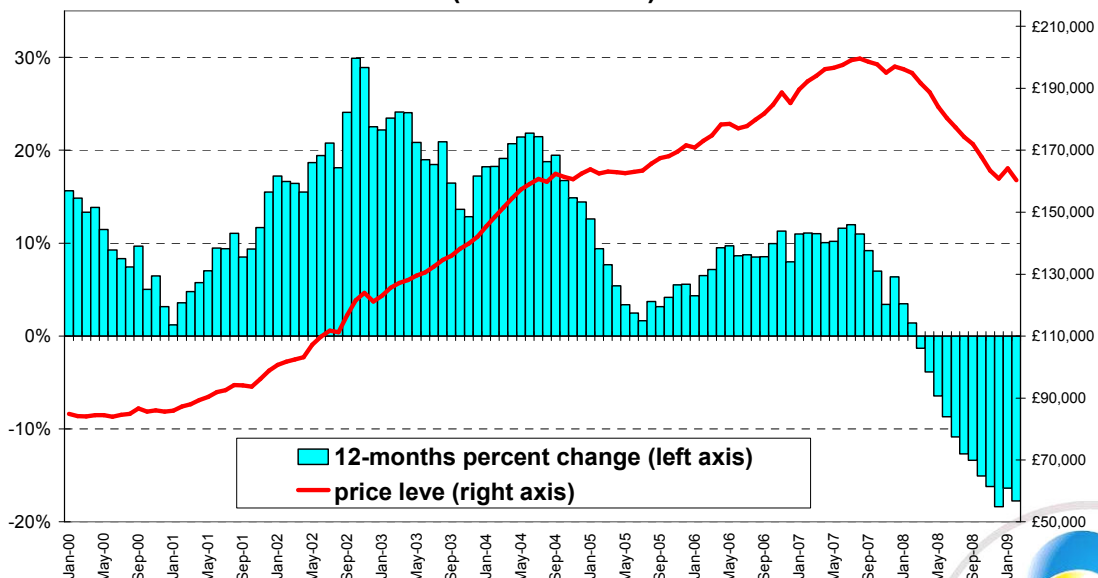
The European Central Bank (ECB) lowered the interest rate by 0.5 percentage points to 1.5 percent, in line with expectations. The UK central bank lowered the interest rate by 0.5 percentage points to 0.5 percent, the lowest level in the bank's history.

Federal Reserve, Bank of England and the ECB's Interest rate



The UK's Halifax house price index lost 2.3 percent in February, with prices 20 percent below the peak of August 2007.

UK house prices (Halifax index)



## Important Announcements in the Coming Week

- The CBS will publish Israel's foreign trade data on Thursday, March 12<sup>th</sup>.
- The CBS will publish price indices for February on Sunday, March 15<sup>th</sup>.
- The CBS will publish data on incoming tourism to Israel, and the CPI will be published in the euro zone, on Monday, March 16<sup>th</sup>.

This review is posted online at [www.harel-finance.co.il/macro](http://www.harel-finance.co.il/macro) in Hebrew

and at [www.harel-finance.co.il/macro/ENG](http://www.harel-finance.co.il/macro/ENG) in English.

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