

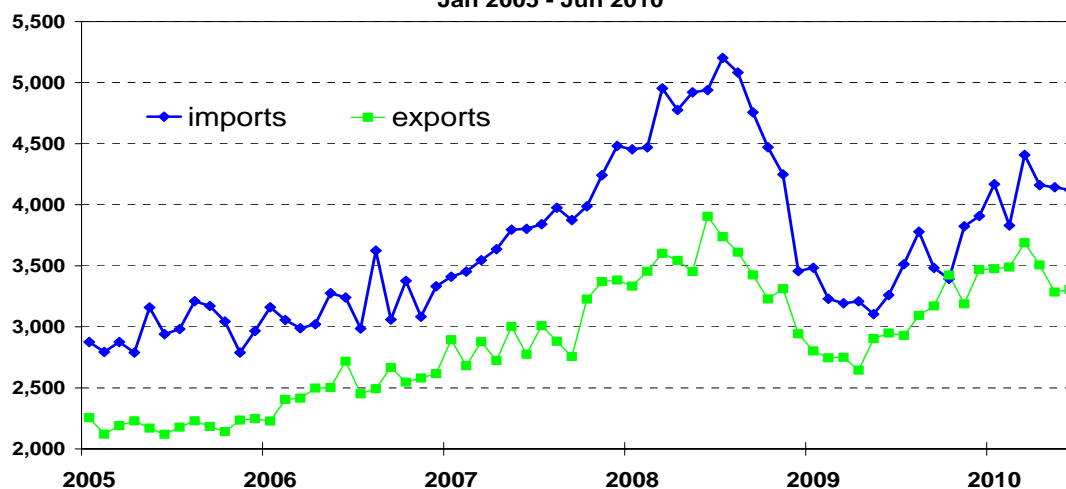
	Expectations derived from the capital market	Our forecast
Inflation in the coming months		0.2% in June 0.7% in July
Future cumulative inflation – next 12 CPIs (through May 2011 CPI)		3.0%
Inflation through July 2011 CPI (average annual rate)	3.3%	3.4%
Bank of Israel interest rate, 6 months ahead	2.00% (up 0.50)	2.25%
Fed interest rate, 6 months ahead	0.25% (unchanged)	0.25%
Yield on Israeli Government 10-Year bond, 6 months ahead	4.96% (up 0.21)	5.10%
Yield on US Treasury 10-Year bond, 6 months ahead	3.24% (up 0.20)	3.90%
Dollar exchange rate, 6 months ahead	NIS 3.87 (unchanged)	NIS 3.83 (down 0.8%)

## Israel

**State tax revenues** totaled ILS 14.0 billion in June, less than expected, reinforcing estimates that growth has cooled considerably in recent months. In our updated forecast, state revenues in 2010 will still be higher than planned in the budget, but the surplus will be relatively low, likely around 1 percent of GDP (ILS 8 billion) or even less. The tax revenue forecast in the Ministry of Finance's **budget proposal** for 2011 and 2012 may well prove to be overly optimistic, leading to a higher-than-planned budget deficit (3 percent of GDP in 2011 and 2 percent of GDP in 2012). If the deviation from the deficit targets is large, the government will later be obliged to apply additional budget cuts and/or raise taxes.

Foreign-trade data stabilized in June, following weakness in the preceding months. **Exports of goods** (excluding diamonds, ships, and aircraft; in dollar terms) grew by 1 percent in June, following a decrease of 6 percent in May and 5 percent in April. Exports increased by 12 percent in the twelve months ended in June. **Imports of goods** decreased by 1 percent in June and increased by 26 percent in the twelve months ended in June.

**Exports and Imports of Goods**  
(US\$ millions per month, excl. diamonds, ships & airplanes)  
Jan 2005 - Jun 2010



The meeting minutes of the Bank of Israel's latest interest-rate decision contain several interesting comments:

- “In the discussion of the decision on the interest rate for July, all of the board members recommended leaving the interest rate unchanged at 1.5 percent.” **Significance:** The BOI Governor’s decision to wait before raising the rate was widely supported within the bank, at least at the level of the department heads.
- “Based on all of the factors, given current data, the expected range of increases of the Bank of Israel interest rate is 1-1.5 percentage points over the next twelve months.” **Significance:** This somewhat convoluted but highly important sentence says that the BOI estimates that the interest rate will rise every 2-3 months, on average, over the next year.

- “It was noted in the discussion that inflation expectations one year ahead derived from the capital market increased in June (monthly average) to near the upper limit of the target range. Some of the participants attributed this increase to an increase in expected inflation, while others stressed the possibility that technical factors that did not express changes in inflation expectations one year ahead had affected the price of CPI-linked bonds.” **Significance:** The BOI is uncertain whether inflation expectations actually increased, or whether this was only the effect of the shortage of CPI-linked bonds.

**Labor-market data** in April indicated a moderate increase in the number of employed persons and a decrease in wages. The number of employee positions of Israeli workers rose by 0.6 percent in April and by 3 percent in the twelve months ended in April. Average wages of Israeli employees declined by 1.1 percent in April and increased by 3 percent in the twelve months ended in April (no change in real terms). **In the business sector**, the number of employee positions rose by 2 percent over the twelve-month period and average real wages per employee position decreased by 0.3 percent.

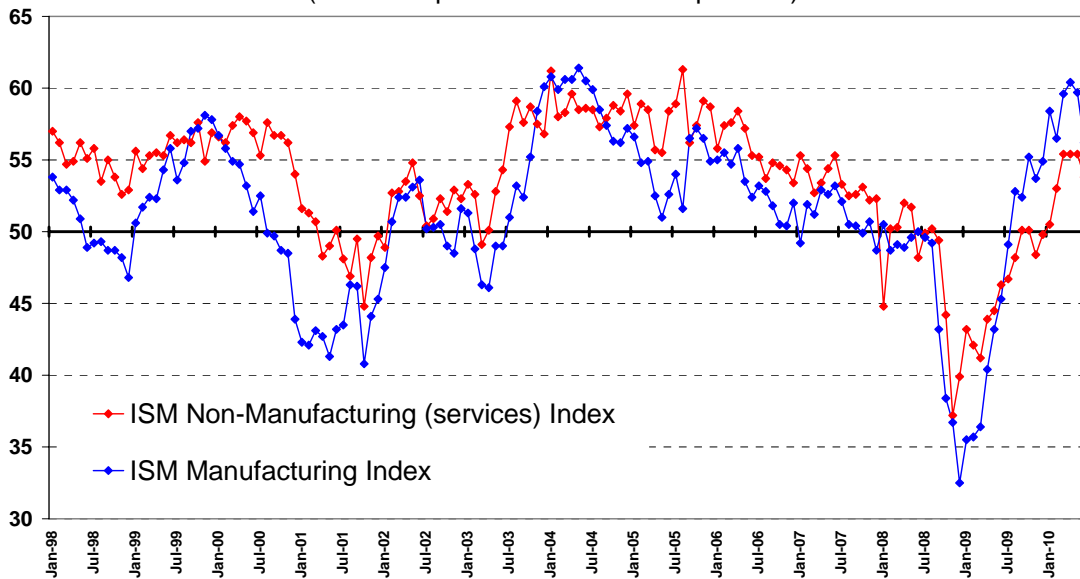
The number of **incoming tourists** to Israel by air increased by 1 percent in June and by 23 percent in the twelve months ended in June.

## United States

The **ISM service sector purchasing managers' index** fell to 53.8 points in June, lower than expected. Indices in recent months point to a slowdown in growth in the United States during these months, although the growth rate is still positive (values higher than 50 indicate expansion).

## The Institute for Supply Management Index

(above 50 points indicates an expansion)



### Our forecast of cumulative changes in price indices during the coming three months

Forecast change, May 2010 index to August 2010 index

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)
1.3%	4.2%	1.6%	1.4%	1.3%

## Important Announcements in the Coming Week

- The consumer price index will be published in the eurozone and data on retail sales will be published in the US on Wednesday, July 14.
- Israel's Central Bureau of Statistics (CBS) will publish price indices for June on Thursday, July 15.
- The consumer price index will be published in the US on Friday, July 16.
- The CBS will publish an update of growth data for the first quarter of 2010 on Sunday, July 18.
- The CBS will publish the industrial production index and the trade and service sectors revenue index on Monday, July 19.

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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