

Weekly Macroeconomic Review

May 17, 2010

	Expectations derived from the capital market	Our forecast
Inflation in the coming months		0.4% in May 0.2% in June
Future cumulative inflation – next 12 CPIs (through March 2011 CPI)		2.8%
Inflation through July 2011 CPI (average annual rate)	3.0%	3.0%
Bank of Israel interest rate, 6 months ahead	2.00% (up 0.50)	2.00%
Fed interest rate, 6 months ahead	0.35% (up 0.10)	0.35%
Yield on Israeli Government 10-Year bond, 6 months ahead	5.11% (up 0.22)	5.15%
Yield on US Treasury 10-Year bond, 6 months ahead	3.66% (up 0.23)	4.15%
Dollar exchange rate, 6 months ahead	NIS 3.79 (up 0.3%)	NIS 3.78 (unchanged)

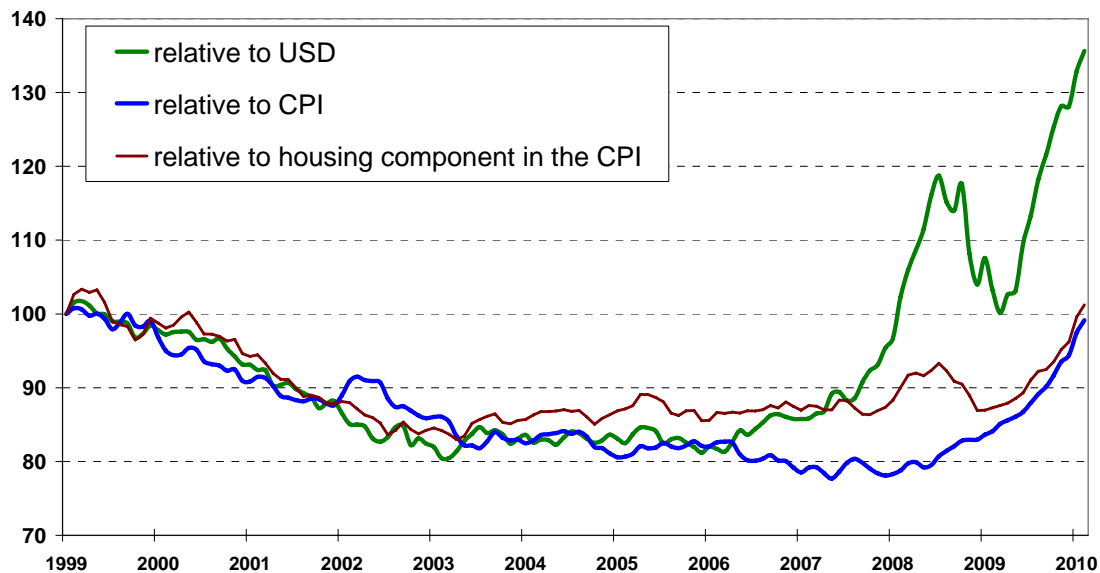
Israel

In our opinion, the escalation of the debt crisis in Europe, the negative effect of the crisis on expected global growth, and the substantial appreciation of the shekel against the euro (approximately 6 percent since the last interest-rate decision) are likely to somewhat dampen the **pace of interest-rate increases by the Bank of Israel**. We now estimate that the BOI will raise the interest rate only twice in the next six months, with the probability of an increase next week at less than 50 percent.

The consumer price index rose by 0.9 percent in April, in line with our forecast; the average forecast was 0.7 percent. Twelve-month inflation reached 3.0 percent.

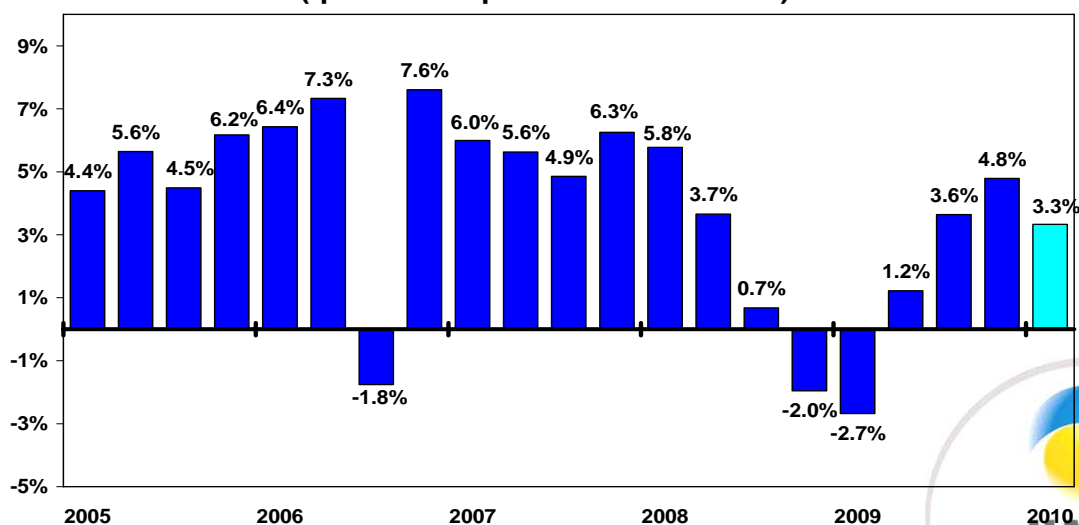
The housing item, which primarily reflects rent prices, rose by 1.0 percent. Prices of tenant-owned homes continued to rise, according to the last survey, by 1.1 percent, slightly less than in the preceding months. Prices of homes increased by 22 percent in the last twelve months.

Price of Houses, Jan 1999 - Feb 2010
Index (Jan 1999=100)



According to an initial estimate, the annualized growth rate in the first quarter of 2010 was 3.3 percent, lower than expected.

GDP Growth
(quarter-on-quarter at annual rate)

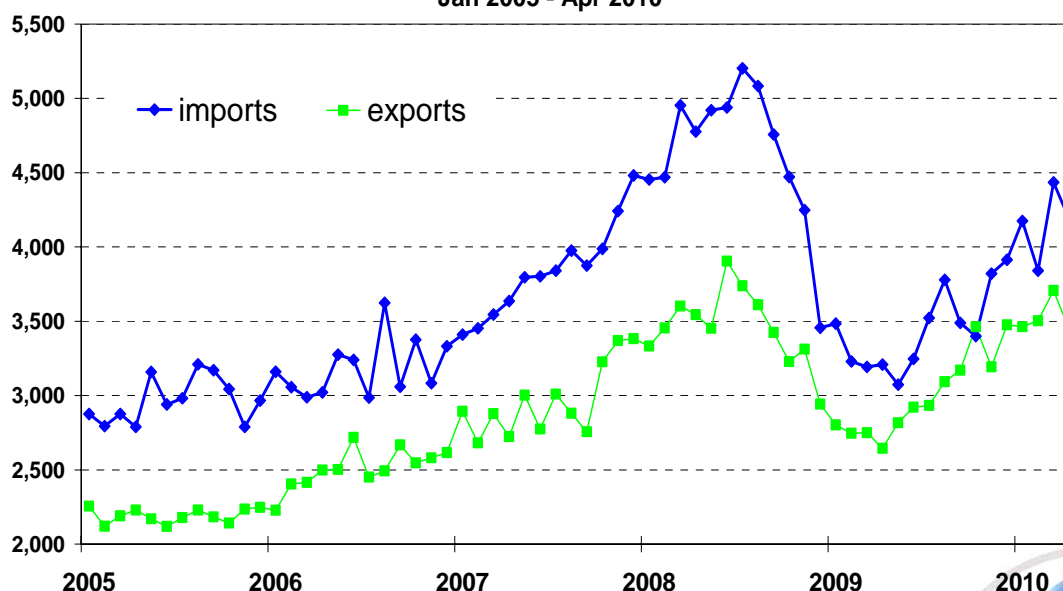


The business product grew at a strong rate of 4.8 percent, while private consumption grew at a moderate 1.6 percent. **Public consumption excluding defense imports** decreased by 4.4 percent, contributing to the weaker growth. **Real export data** were a negative surprise with a 9.9 percent decrease, excluding diamonds and start-up companies.

Our forecast for growth in 2010 was 3.1 percent at the end of March. The Bank of Israel provided a forecast of 3.7 percent growth a month ago; the data reinforce our estimate that the Bank of Israel's forecast is excessively optimistic.

Foreign-trade data for April were weak. **Exports of goods** (excluding diamonds, ships, and aircraft; in dollar terms) decreased by 7 percent in April, but were up by 30 percent for the twelve months ended in April. **Imports of goods** (using the same definition) fell by 6 percent in April, but rose by 30 percent in the twelve-month period. The **trade deficit** (using the same definition) continued to expand in April, to USD 0.74 billion.

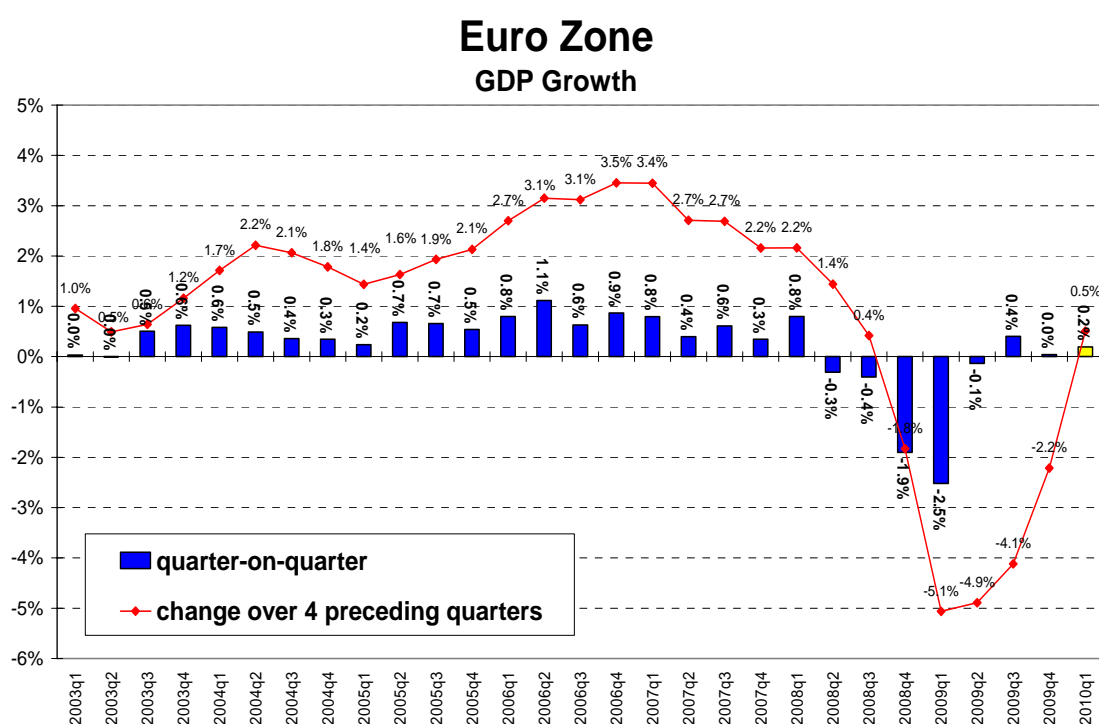
Exports and Imports of Goods
(US\$ millions per month, excl. diamonds, ships & airplanes)
Jan 2005 - Apr 2010



According to data of the Bank of Israel, average inflation expectations between mid-April and mid-May were at 2.7 percent for the first year, 2.5 percent for the second year, and 2.7 percent from the third year forward. The data reflect a slight decrease in the expectations for the first and second year, but a slight increase for the third year and beyond. The quantity of means of payment increased by 1.7 percent in April, but the rate of increase for the twelve months ended in April fell to 15 percent, from the peak of 65 percent last August.

Euro zone

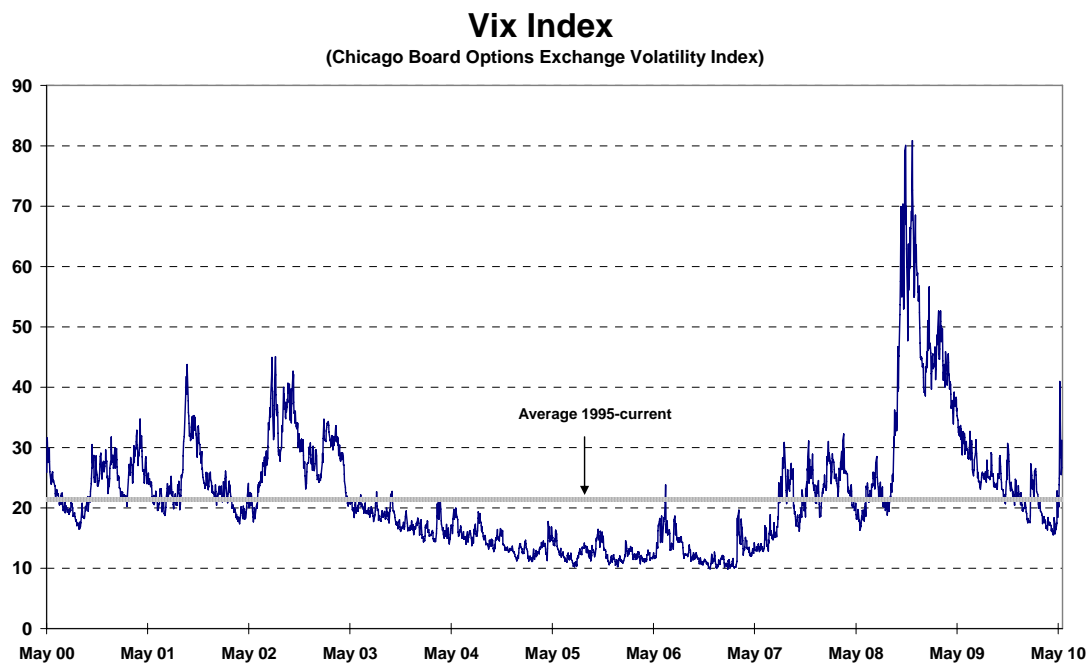
According to an initial estimate, the eurozone economy grew at an annualized rate of 0.8 percent in the first quarter of 2010.



United States

Retail sales grew by 0.4 percent in April, and by 9 percent in the twelve months ended in April, slightly above expectations.

The VIX index gained 42 percent in May, due to the uncertainty regarding the stability of the eurozone in the last two weeks.



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

Forecast change, April 2010 to July 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)
1.1%	3.1%	5.6%	1.6%	0.6%

Important Announcements in the Coming Week

- The consumer price index will be published in the eurozone on Tuesday, May 18. Data on construction starts and permits will be published in the United States.
- The consumer price index will be published in the United States on Wednesday, May 19.
- Israel's Central Bureau of Statistics will publish the industrial production index and the trade and service sectors revenue index on Thursday, May 20.
- The Bank of Israel will announce its interest-rate decision on Monday, May 24. Data on sales of existing homes will be published in the United States.

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

and at <http://www.harel-group.com/finance.html> in English.

Please address comments or questions to Mr. Ofer Klein at
oferk@harel-finance.co.il

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