

## Weekly Macroeconomic Review

April 20, 2009

|   | Expectations derived from the capital market | Our forecast                 |
|---|--|------------------------------|
| Inflation in the coming months                                  |  | 1.1% in April<br>0.4% in May |
| Future cumulative inflation – next 12 CPIs (through March 2010) |  | 1.8%                         |
| Inflation through May 2010 CPI (average annual rate)            | 1.7%   | 2.7%                         |
| Bank of Israel interest rate, 6 months ahead                    | 0.80%<br>(up 0.30)                           | 0.75%                        |
| Fed interest rate, 6 months ahead                               | 0.40%<br>(up 0.15)                           | 0.25%                        |
| Yield on Israeli Government 10-Year bond, 6 months ahead        | 5.20%<br>(up 0.30)                           | 5.35%                        |
| Yield on US Treasury 10-Year bond, 6 months ahead               | 3.10%<br>(up 0.20)                           | 3.25%                        |
| Dollar exchange rate, 6 months ahead                            | NIS 4.20<br>(unchanged)                      | NIS 4.25<br>(up 1.2%)        |

**Our next weekly review will be issued on Monday, April 27<sup>th</sup>.**

## Israel

The consumer price index rose by 0.5 percent in March, more than expected. The average forecast was 0.2 percent; our forecast was 0.3 percent. The index of wholesale prices, excluding fuels, rose at a high rate of 0.9 percent, while the housing index rose by 1.6 percent.

The March CPI and composition data reinforce our estimate, emphasized over recent months, that inflation in 2009 will be within the target range of 1 to 3 percent, rather than zero or negative, as many forecasters have predicted, including the Bank of Israel.



**The amount of means of payment** continued to grow very rapidly, by 8 percent in March and 41 percent in the twelve months ended in March, versus a 13 percent increase in the twelve months ended in March 2008.

**Inflation expectations** between mid-March and mid-April, according to calculations by the BOI, remained stable at 0.7 percent for the first year and 2.4 percent for the second year. After the publication of the March CPI, inflation expectations derived from the capital market rose to an annualized rate of 1.7 percent for the coming fourteen months (through the May 2010 CPI). This is a substantial increase in these expectations, relative to the zero or negative inflation expected several months ago; however, in our opinion this level is still slightly too low.

Due to the high CPI, the rapid increase in means of payment, and the increase in inflation expectations, no further expansion of **monetary policy** is expected in the next month. We estimate that the BOI will now prefer to wait, and observe inflation and expected inflation figures for a month or two, rather than risk further expansion beyond its earlier decisions.

**The BOI** has published its annual report and reduced its **growth forecast for 2010** from 2.3 percent to just 1.0 percent. In other words, the BOI expects the recession to continue in 2010, though at a lesser intensity than in 2009.

In addition, **the BOI clearly objects to the initiative for continued tax cuts** in the Israeli economy; Prime Minister Binyamin Netanyahu promised to continue and actually accelerate the pace of the tax cuts, prior to his election.

Not only does the BOI not support further tax cuts, it actually proposes considering a **postponement of the cuts planned for 2010** – the last reduction within the reform approved several years ago.

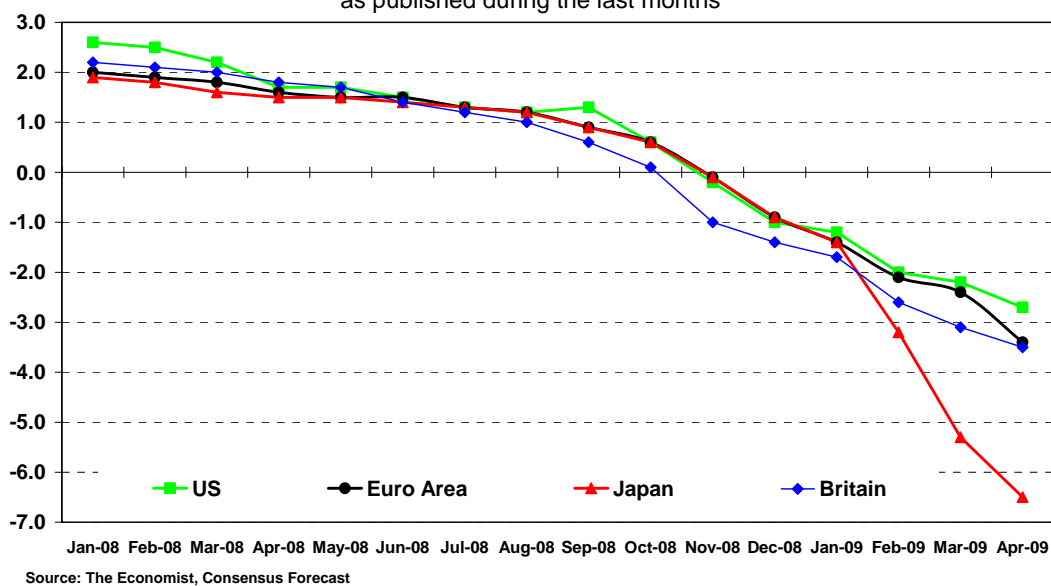
In the opinion of the BOI, "The continuation or further escalation of the recession could enlarge the deficit more than expected and threaten fiscal credibility. In such a case, deficit growth may be restrained by postponing the tax cut planned for 2010 or by halting some of the proposed measures."

## Growth forecasts for advanced economies

The *Economist* has published its **monthly Consensus Forecast** of growth rates in the advanced countries. Forecasts for all countries dropped sharply again. Strongly negative growth is now expected in 2009, with positive but near-zero growth predicted for 2010. In both years, growth in the US is expected to be better than in the other advanced countries.

### Growth Forecasts for 2009

as published during the last months



## United States

**Retail sales** decreased by 1.1 percent and **industrial production** decreased by 1.5 percent in March, both more than expected. Following an encouraging increase in February, **construction starts and permits** decreased by a sharper-than-expected 11 percent and 9 percent, respectively, in March.

The **consumer price index** fell by 0.1 percent in March, but core prices rose by 0.2 percent for the third consecutive month.

The University of Michigan's **consumer confidence index** rose to 61.9 points in April, according to an initial estimate, from 57.3 points in March, higher than expected.

## Europe

**Inflation in the euro zone** was 0.6 percent in March, in line with estimates.

The UK's central bank left the interest rate unchanged at a record low of 0.5 percent, as expected.

The announcement by the President of the ECB hinting at further interest-rate cuts contributed to the weakening of the euro.

## Important Announcements in the Coming Week

- Data on incoming tourism to Israel will be published on Monday, April 20<sup>th</sup>.
- Data on Israel's foreign trade will be published on Wednesday, April 22<sup>nd</sup>.
- Data on sales of existing homes will be published in the US on Thursday, April 23<sup>rd</sup>.
- Data on sales of new homes will be published in the US, and the initial growth estimate for the first quarter of 2009 and retail sales figures will be published in the UK, on Friday, April 24<sup>th</sup>.
- The Central Bureau of Statistics will publish the industrial production index and the trade and service sectors revenue index on Sunday, April 26<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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