

## Weekly Macroeconomic Review

October 27, 2009

	Expectations derived from the capital market	Our forecast
Inflation in the coming months		0.3% in October 0.0% in November
Future cumulative inflation – next 12 CPIs (through September 2010 CPI)		2.4%
Inflation through July 2011 CPI (average annual rate)	2.4%	2.4%
Bank of Israel interest rate, 6 months ahead	1.35% (up 0.60)	1.35%
Fed interest rate, 6 months ahead	0.45% (up 0.20)	0.45%
Yield on Israeli Government 10-Year bond, 6 months ahead	5.26% (up 0.28)	5.30%
Yield on US Treasury 10-Year bond, 6 months ahead	3.80% (up 0.24)	4.00%
Dollar exchange rate, 6 months ahead	NIS 3.71 (unchanged)	NIS 3.71 (unchanged)

## Israel

The Bank of Israel interest rate remained unchanged at 0.75 percent, in line with our estimates. The BOI's announcement contained no clues regarding its future interest-rate policy. Similar to last month, the BOI noted three main reasons for its decision:

- Inflation, excluding seasonal effects and the effects of indirect taxes, has been in the middle of the target range in recent months; inflation expectations remained slightly above the midpoint of the target range again this month.
- The economic recovery continues in Israel and globally, but a negative GDP gap and a relatively high unemployment rate are still tempering inflationary pressures.
- The interest rates of the central banks in the leading economies are low, and are expected to remain so in the coming few months.

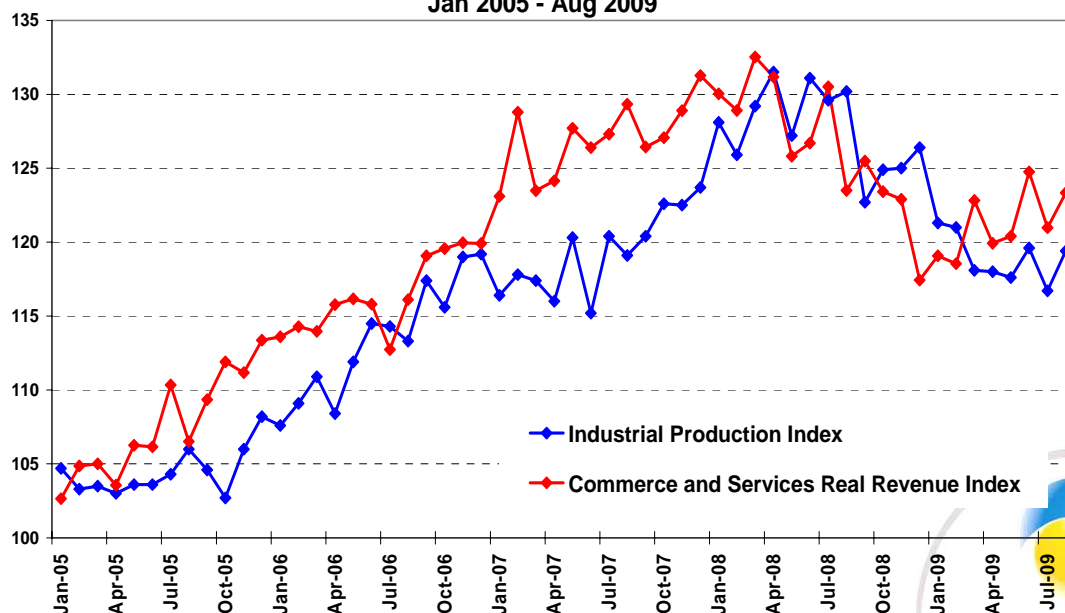


From our perspective, all three factors were already true in the last two months, and will still be true in the next few months. The BOI needs to continue to raise the interest rate in the near future, but at a moderate pace. An increase of 0.25 percentage points at two- or three-month intervals seems reasonable given the economic conditions, the considerable increase in the money supply, world monetary policy, and the goal of preventing pressures towards rapid appreciation of the shekel. If there are no surprises from the exchange rate or the forthcoming CPI, we expect a 0.25-point interest-rate hike **next month**.

Industrial production and trade and service revenues rose sharply in August, and tourists' hotel stays rose sharply in September. In our opinion, given the economic indicators published so far, relatively **high growth** is emerging for the third quarter. The initial growth estimate will be published on November 16.

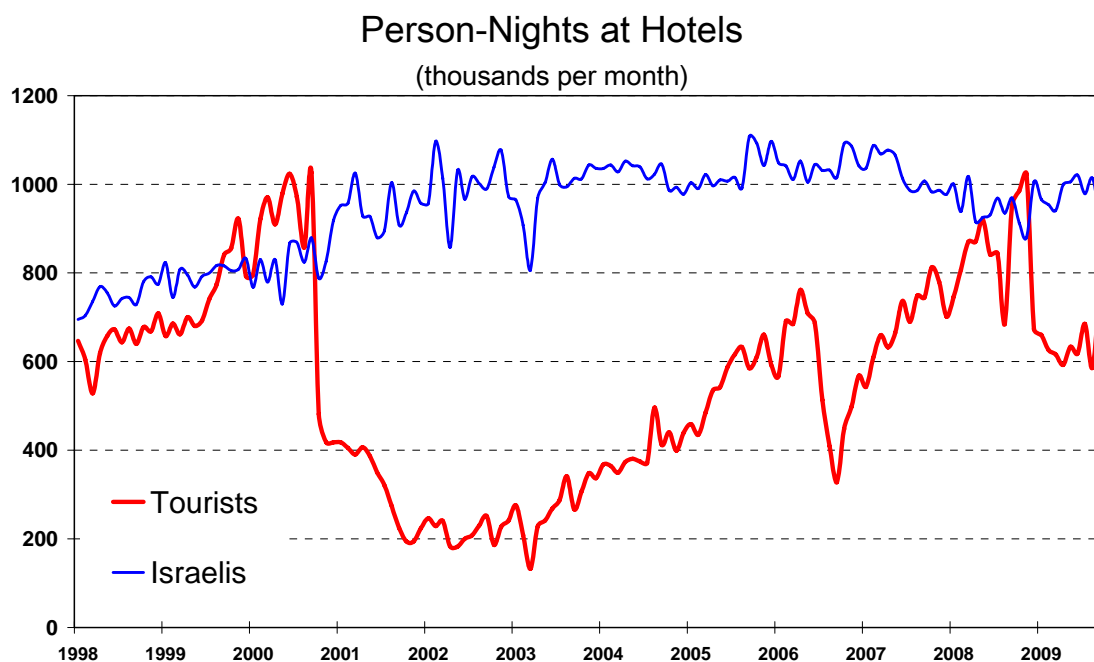
The trade and service sectors revenue index rose by 2 percent in August and remained unchanged in the twelve months ended in August. The industrial production index rose by 2 percent in August and fell by 8 percent in the twelve months ended in August.

**Industrial Production Index  
& Commerce and Services Sectors Revenue Index**  
Jan 2005 - Aug 2009



As a result, the **Bank of Israel's composite index** rose by 1.2 percent in September.

**Tourists' hotel stays** rose sharply in September, by 30 percent compared to August, but were still 20 percent lower year-on-year. Meanwhile, Israelis' hotel stays decreased by 9 percent in September and by 5 percent in the twelve months ended in September.



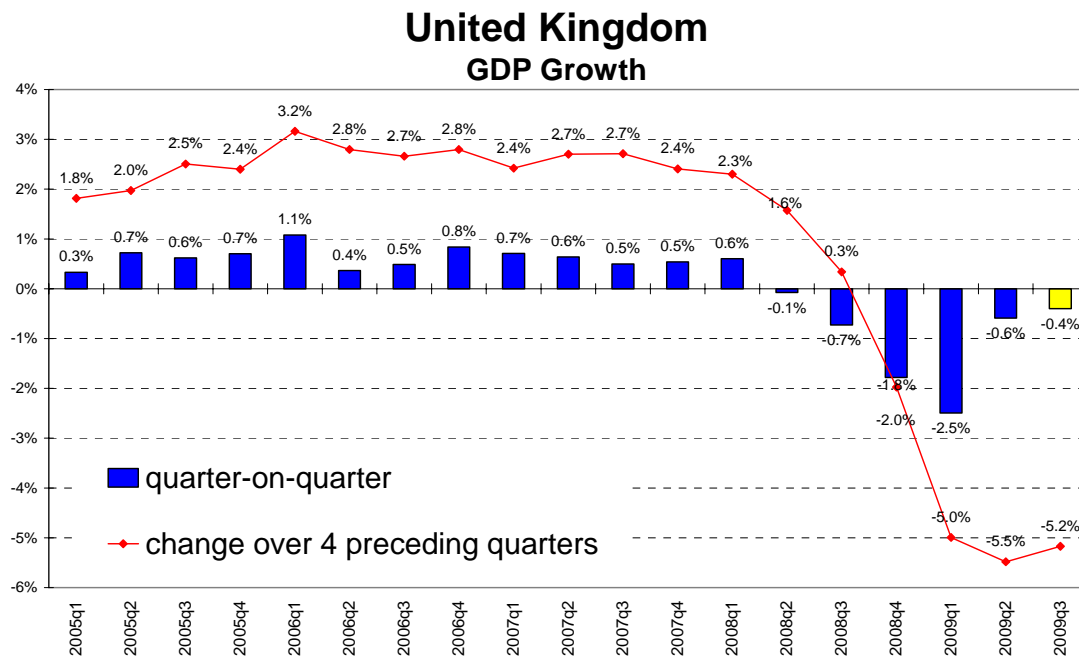
## United States

**Construction starts and permits** showed slight changes in September, in contrast to expectations of an increase. **Sales of existing homes** grew by 9 percent in September, more than expected. However, the median price of homes sold fell for the fourth consecutive month.

The **wholesale price index** surprisingly fell by 0.6 percent in September. The **core index** (excluding food products and energy) decreased by 0.1 percent, also below expectations.

## United Kingdom

In contrast to expectations, the British economy continued to contract, for the sixth consecutive quarter. According to initial estimates, **GDP** declined by 0.4 percent (1.6 percent annualized) in the third quarter of 2009.



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

Forecast change, September 2009 to December 2009

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)
0.6%	0.0%	0.2%	-1.3%	-1.7%



## Important Announcements in the Coming Week

- Data on sales of new homes will be published in the United States on Wednesday, October 28.
- Israel's Central Bureau of Statistics will publish data on sales of new homes on Thursday, October 29.
- The initial estimate of growth in the third quarter of 2009 will be published in the US on Thursday, October 29.
- Data on private income and consumption and the University of Michigan's consumer confidence index will be published in the US on Friday, October 30. The estimated CPI and the unemployment rate will be published in the euro zone.

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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