

## Weekly Macroeconomic Review

September 29, 2009

	Expectations derived from the capital market	Our forecast
Inflation in the coming months		0.0% in September 0.3% in October
Future cumulative inflation – next 12 CPIs (through August 2010 CPI)		2.6%
Inflation through July 2011 CPI (average annual rate)	2.2%	2.3%
Bank of Israel interest rate, 6 months ahead	1.50% (up 0.75)	1.50%
Fed interest rate, 6 months ahead	0.40% (up 0.15)	0.40%
Yield on Israeli Government 10-Year bond, 6 months ahead	5.26% (up 0.27)	5.26%
Yield on US Treasury 10-Year bond, 6 months ahead	3.52% (up 0.22)	4.00%
Dollar exchange rate, 6 months ahead	NIS 3.77 (unchanged)	NIS 3.77 (unchanged)

## Israel

The Bank of Israel interest rate remained unchanged, in line with our estimate; other estimates ranged from no change to a 0.25-point rate hike. The BOI's announcement gave no hint of future interest-rate policy.

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 are also within the target range.
- 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.

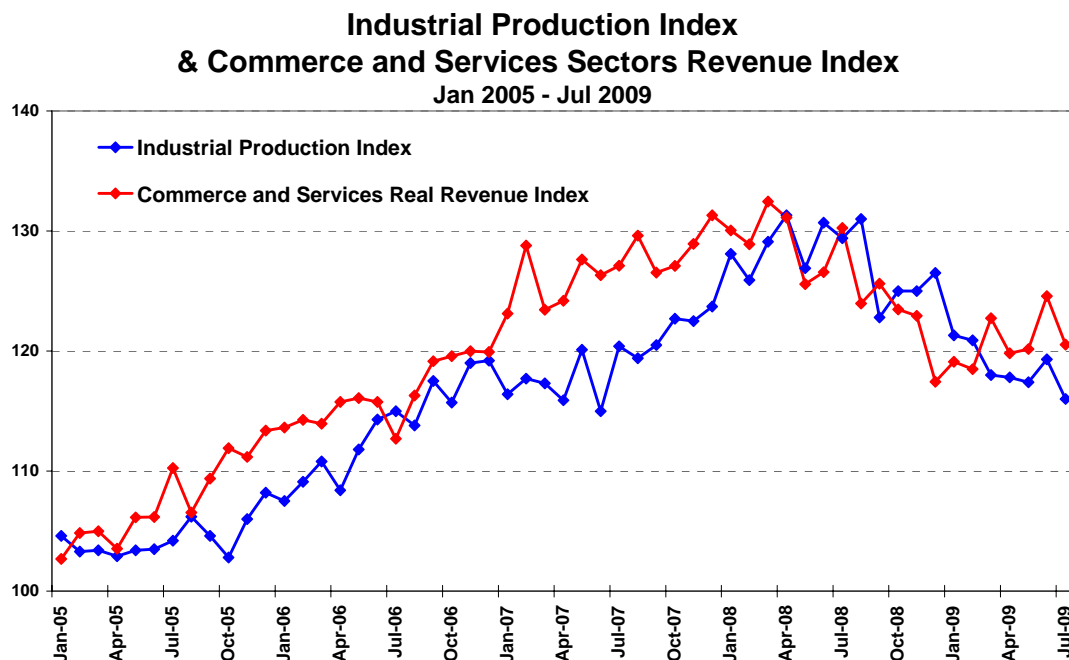
Tel: 1-800-310-330 | [www.harel-finance.co.il](http://www.harel-finance.co.il)



From our perspective, all three factors were already true last month (when the BOI raised the interest rate), remain true today (when the BOI made no change to the interest rate), and will still be true in the next few months (when the BOI may or may not raise the interest rate).

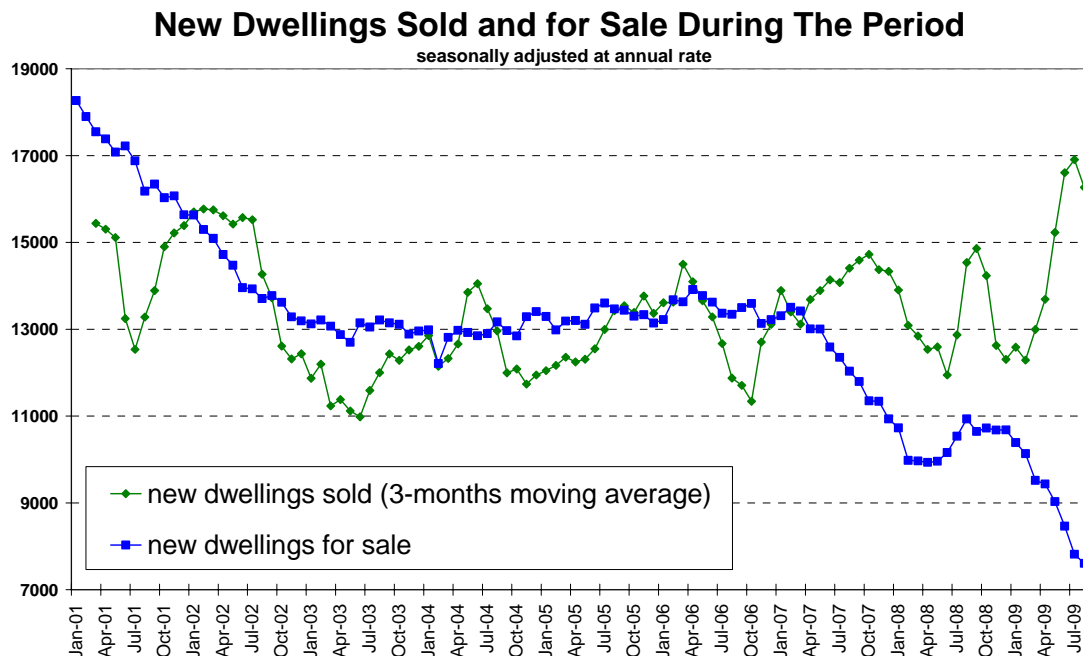
The point is that the BOI needs to continue to raise the interest rate in the near future, but at a moderate pace. Thus, an increase of 0.25 percentage point at an average frequency of once every two months, or possibly slower, seems reasonable given the economic conditions, the considerable increase in money supply, world monetary policy, and the goal of preventing pressures towards rapid appreciation of the shekel.

Indices of real activity in July were weak. The **industrial production index** decreased by 2.8 percent, and by 10 percent in the twelve months ended in July. The **trade and service sectors revenue index** was down by 3.2 percent, and by 7 percent in the twelve months ended in July.



The Bank of Israel's composite index rose by 1.3 percent in August, mainly due to strong foreign-trade data.

The number of new homes sold decreased by 16 percent in August and by 18 percent in the twelve months ended in August. The supply of homes for sale also fell, reaching a new low. This may signal further upward pressures on housing prices.



## United States

In line with advance estimates, the Fed left the interest rate unchanged at 0.00-0.25 percent. The Fed's press release showed confidence in the pace of the economy's recovery and emphasized that the very low interest rate would remain in place for a long period. The Fed also announced the continued purchase of mortgage-backed securities, though at a slower pace. As a result, expectations for the Fed's future interest rate decreased (the market now estimates the interest rate in one year's time at just 0.75 percent), and long-term government bond yields fell.

Sales of existing homes decreased, surprisingly, by 2.7 percent in August. The median price of homes sold also fell slightly, according to data from the Realtors' Association. Figures for New home Sales were also a disappointment as they hardly rose in August.



## Important Announcements in the Coming Week

- The initial estimate of inflation in the euro zone will be published on Wednesday, September 30.
- Data on private income and consumption and the ISM manufacturing sector index will be published in the US on Thursday, October 1.
- The employment report will be published in the US on Friday, October 2.
- The purchasing managers' index and data on retail sales will be published in the euro zone, and the ISM service sector index will be published in the US, on Monday, October 5.

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.

Please address comments or questions to Mr. Ofer Klein at  
[oferk@harel-finance.co.il](mailto:oferk@harel-finance.co.il)

*If you would like to be removed from the Harel Group mailing list,  
please let us know in a reply to this e-mail.*