



BANK OF ISRAEL

April 21, 2025

Report on the Bank of Israel's discussions prior to deciding on the interest rate

The discussions took place on April 6, 2025 and April 7, 2025.

General

The Monetary Committee sets the interest rate in a process that includes two discussions—the first in a broad forum, and the second in a narrower one.

In the broad-forum discussion, the relevant background economic conditions are presented, including the real and financial-monetary developments in Israel's economy and developments in the global economy. Participants in this discussion include the members of the Monetary Committee, senior representatives from the various departments of the Bank, and economists from the economic departments (Research and Markets), who prepare and present the material for discussion.

In the narrow forum—which consists of the Monetary Committee and a representative of the Markets Department—the Research and the Markets Departments present their views of the main considerations that should guide the setting of the monetary policy. An open discussion on monetary policy follows, which ends with a vote on the level of the interest rate. According to Section 18(c) of the Bank of Israel Law, 5770–2010, the decision on the interest rate is reached by majority vote of the members of the Monetary Committee who participate in the voting.

A summary view of the economic situation available at the time of the Committee's discussion is presented in the notice regarding the interest rate decision, which was published on April 7, 2025, and in the data file that accompanied the notice.

THE NARROW-FORUM DISCUSSION

The members of the Monetary Committee participating in the discussion decide on the appropriate rate of interest.

After the discussion, it was decided to keep the interest rate at 4.5 percent. All members of the Monetary Committee supported the decision.

The discussion focused on the geopolitical environment's impacts on the economy and on economic developments: global economic developments, developments in the financial markets and in the foreign exchange market, inflation and inflation expectations, the level of economic activity, the labor market, the housing market, fiscal developments, and the Research Department's forecast.

Main points of discussion

The Committee discussed the economic activity, which continued to recover moderately, against the background of geopolitical developments and in view of the announcement of the US administration's tariff program several days before the interest rate decision. This led to sharp market declines, a downward revision of forecasts for global growth and world trade, and an increase in inflation expectations in the US.

The Committee discussed the inflation environment. The inflation rate over the preceding 12 months declined to 3.4 percent, above the upper bound of the target range. Based on forecasters' assessments, the inflation rate is expected to continue to moderate toward the target in the upcoming months. Inflation expectations for one year ahead from the various sources are within the target range. Expectations for the second year forward moderated slightly and are within the target range. In the Committee's assessment, there are several risks for a possible acceleration of inflation or for its not entering the target range—the geopolitical developments and their impacts on economic activity, prolonged supply constraints, a deterioration in global terms of trade, and shekel volatility.

The Committee discussed developments in the foreign exchange market and in the financial markets. In the reviewed period, the shekel depreciated and the risk premium—as measured by the CDS and by government bond spreads—increased markedly, and its level is high compared to before the war. Similar to other countries, Israel's capital market also showed declines in equity indices, though they were more moderate.

Current indicators of economic activity show continued moderate improvement in activity. Credit card expenditure data in current prices show an increase in March, after some moderation in January and February. The Business Tendency Survey of the Central Bureau of Statistics shows a continued trend of recovery in recent months, and the aggregate balance for February increased and is similar to its prewar level. In

the services and trade industries there was stability in activity and in expectations, while in the construction industry there was a recovery in activity and in expectations, as the shortage in professional workers moderated. Fund raising by the high tech sector in the first quarter of 2025 is similar to its level in the preceding quarter.

The labor market continued to be tight. In February, the broad unemployment rate and the job vacancy rate remained stable. The employment and participation rates for those aged 25–64 are at a high level.

Activity is improving in the construction industry with an increase in the number of workers in the industry, but it is still impacted by labor force constraints. There has been an increase in building starts and permits relative to the previous quarter. Building completions also increased, but their level is still lower than before the war. Mortgage volume in February was approximately NIS 7.4 billion. In parallel, the upward trend in home prices continued, increasing by 7.7 percent in the past year.

The cumulative government-budget deficit in the past 12 months declined in February to 5.3 percent of GDP. From the beginning of the year, ministries' expenditures declined relative to the corresponding period in the previous year, mainly due to a continued decrease in expenditures on the war. Also contributing to the decrease in the deficit was an increase government tax revenues, which have been on an upward trend in recent months, among other things due to the taxation changes that went into effect in the beginning of the year.

The Research Department updated its macroeconomic forecast. The forecast also incorporates the developments due to the US administration's new tariff policy. The forecast's baseline scenario was compiled under the assumption that the direct economic impact of the moderate increase in the intensity of the fighting will continue for a limited time during the second quarter of the year. The Department's assessment is that during the forecast period supply is expected to continue to recover, to an extent that will contribute to moderation of the excess demand over time. In addition, according to the forecast, the new tariff policy announced by the US administration is expected to moderate the scope of world trade and to reduce Israeli exports. The Department assesses that GDP will grow by 3.5 percent in 2025 and by 4 percent in 2026, lower than the previous forecast. The inflation rate is expected to be 2.6 percent in 2025 and 2.2 percent in 2026. In the Department's assessment, the government's budget deficit will contract compared to the previous forecast, so that the debt to GDP ratio is expected to be approximately 69 percent at the end of 2025 and to decline to 68 percent of GDP in 2026.

This forecast is characterized by a high level of uncertainty, and the balance of risks to growth tends to the downside, and for inflation it tends to the upside. Beyond the high uncertainty deriving from the developments in terms of tariffs, incorporated in the baseline scenario, there is also uncertainty related to the development of the war—therefore, and similar to previous forecasts, the forecast process included an examination of an additional scenario, of the widening of the war. According to this scenario, an adverse impact of 0.5 percent in GDP is expected in 2025, mainly as a

result of a negative impact to labor supply, and an increase in the deficit of about 2 percent of GDP, so that the debt to GDP ratio will be 71 percent at the end of the year.

The Committee members discussed global conditions. The tariff policy announced by the US administration led to a sharp response in financial markets, a steep downward revision in the growth forecast and an increase in US inflation expectations. Since the declaration of the policy on Wednesday, the expected Fed interest rate path priced in by the markets declined sharply. Major US equity indices declined, as the S&P 500 Index fell by approximately 16 percent in the reviewed period (through Friday, April 4, 2025), of which 10.5 percent was since the announcement on Wednesday. US bond yields declined by 40 basis points in the period reviewed.

All 5 Monetary Committee members supported the decision to keep the interest rate unchanged at a level of 4.5 percent.

In view of the continuing war, the Monetary Committee's policy is focusing on stabilizing the markets and reducing uncertainty, alongside price stability and supporting economic activity. The interest rate path will be determined in accordance with the convergence of inflation to its target, continued stability in the financial markets, economic activity, and fiscal policy.

The next monetary policy decision will be published on Monday, May 26, 2025.

The dates of interest rate decisions for 2025:

<https://www.boi.org.il/en/economic-roles/monetary-policy/interest-rate-announcement-dates-2024/>

Participants in the narrow-forum discussion:

Members of the Monetary Committee:

Prof. Amir Yaron, Governor of the Bank and Monetary Committee Chairperson

Mr. Andrew Abir, Deputy Governor

Dr. Adi Brender, Research Department Director

Prof. Naomi Feldman

Prof. Zvi Hercowitz

Other participants in the narrow-forum discussion:

Dr. Golan Benita, Markets Department Director

Dr. Oded Cohen, Chief of Staff to the Governor

Mr. Nadav Eshel, Assistant to the Governor

Ms. Nurit Felter-Eitan, Director of the Communications, Public Affairs & Community Relations Department

Ms. Liat Indig, Deputy Spokesperson

Dr. Ziv Naor, Bank of Israel Spokesperson

Ms. Dana Orfaig, Research Department

Ms. Nava Ostrov, Monetary Committee Secretariat