Recent Economic Developments 126

September-December 2009

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Part 1: Review of Recent Economic Developments, September to December 2009[1]

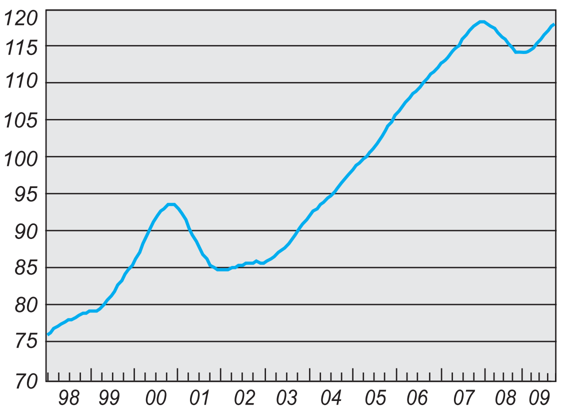
Main Developments

Israel's economic recovery from the crisis began in the second quarter of 2009 and gained strength in the period under review, September to December 2009. Exports expanded rapidly, domestic demand increased, and the labor market revived. That said, developments in Israel depend on the pace of the global exit from the recession. The growth in activity in Israel and expectations that it would continue resulted in stronger inflationary pressures and a rise in inflation expectations. Against this background, and in light of the need to persist with an expansionary policy supportive of economic activity, the Bank of Israel increased the interest rate slightly, to 1.0 percent, in the period reviewed, and the rate for January to 1.25 percent.

GDP increased in the third quarter of 2009 at an annual rate of 3 percent, and the Bank of Israel's composite state-of-the-economy index rose swiftly (Figure 1.1). The continued expansion of activity in the period reviewed encompassed most of the principal industries, and was led by manufactured exports; manufacturing production increased, as did trade and services revenue, and some renewal of activity in the construction industry was also recorded. These developments were reflected by increased imports of production inputs, consumer goods and investment. Activity, however, is still below its level in the pre-crisis period.

Figure 1.1

The level of economic activity,* 1998-2009**
(index: 2004 average=100)



* The Bank of Israel composite index, including the change in economic activity trend growth.
** To December 2009.

The surge in world trade, with the increase in world demand, led to a rapid rise in Israel's goods exports. The recovery in economies around the world, however, rests on extensive government aid programs, which greatly increased deficits and public debt. These, together with the problems still besetting the international financial system, form an obstacle to a rapid recovery from the slump and continued expansion of Israel's exports.

The increase in the public's wealth resulting from the recovery in the financial markets, together with the turnaround in the business cycle, the improvement in employment security and the halt to the erosion of the real wage boosted consumers' confidence, and with the help of the low interest rate resulted in further growth of private consumption in the third quarter, and in particular, of purchases of durables. Other indices relating to this period also point to the continuation of this trend. Fixed investment expanded, but if investment in commercial vehicles, which increased greatly due to changes in taxation, is excluded, fixed investment continued to contract, a feature consistent with over capacity.

Initial indications of an exit from the recession are evident in the labor market too: employment in the business sector has stopped contracting; the balance of employment (jobs filled *minus* terminations of employment) has improved, becoming positive for the first time in a year; the number of hours worked per employee has increased, as has the nominal wage; the number of work-seekers and of claims for unemployment pay have declined; the unemployment rate dropped slightly to 7.8 percent in the third quarter, and employers expressed positive expectations regarding their activity and manpower.

The improvement in economic activity was expressed also in increased tax revenues from the middle of the year. Direct tax revenues increased in the period reviewed with the revival of the capital market, improved company profitability, the rise in the nominal wage and the expansion of employment. Indirect tax revenues increased faster than did direct, mainly due to a rise in revenues from import taxes and from VAT in the domestic market as private consumption

[1] Based on data available by 20 January 2010.

improved. Government expenditure in the period reviewed were higher than the seasonal level consistent with full budget expenditure, among other things because some 2010 expenditure was brought forward to 2009. The total deficit excluding credit in 2009 reached 5.2 percent of GDP, compared with a ceiling of 6 percent set when the budget was passed.

The surplus in the current account of the balance of payment (seasonally adjusted) in 2009:Q3 was $1.3 billion, similar to its level in the previous quarter. The deficit in the goods account did not change, despite the deterioration in the terms of trade, and foreign trade data for the last few months show the continued momentum of exports and the increase in all categories of imports. The surplus in the services account shrank in the third quarter because of the fall in R&D exports, a correction for their exceptional rise in the second quarter. On the financial account, Israelis' investment abroad increased, with the steep rise in the foreign currency reserves held in the Bank of Israel; nonresidents' investments in Israel in all channels also increased markedly.

The capital market in Israel (and around the world) revived in the period reviewed: the value of assets (including residential properties) increased, and domestic issuance strengthened. The CPI rose by 0.6 percent, annual rate, but seasonally adjusted reflected an increase in the annual inflation rate to 4.1 percent. Inflation expectations and forecasters' assessments of future inflation rose slightly, and drew close to the upper limit of the inflation target range. The Bank of Israel's increased the interest rate for September by a quarter of a percentage point to 0.75 percent, the rate for December by another 0.25 percentage points, to 1 percent, and the January rate (after the period covered by this review) by another 0.25 percentage points, to 1.25 percent. The shekel appreciated against the dollar, against the background of the weakness of the dollar world wide, but expectations of shekel depreciation grew. Towards the end of the year the Bank of Israel reduced the extent of its intervention in the foreign currency market.

Aggregate real activity

According to preliminary National Accounts data for 2009, GDP increased by 0.5 percent (with a decline of 0.4 percent in business sector product), the outcome of a slight expansion of private and public consumption and a contraction of exports and investment. In the third quarter the upward trend of economic activity gained strength, following the positive turnaround in the previous quarter (Table 1.1). GDP increased at an annual rate of 3 percent (so that per capita GDP increased), and business sector product grew at a rate of 2.4 percent. As a result of the surge in imports, the sources available to the economy increased considerably, and there was a marked increase in exports and private consumption. The turnaround in economic activity started in the second quarter, and was headed by private consumption, due to the modest impact of the crisis on households and the improvement in their expectations.

Private consumption continued to grow rapidly in the third quarter, in particular consumption of durables,[1] and this is supported by various indices. This is consistent with the economic recovery and with expectations that it will continue, the increase in the value of the public's asset portfolio, the ending of the erosion of the real wage, the drop in unemployment, and hence the strengthening of employment security, the low real interest rate, and expectations of depreciation of the shekel. Consumers' confidence indices (of Globes Research and Bank Hapoalim) stabilized during the period under review, after rising steeply in the first half of the year, there was an improvement in the assessment of the consumers regarding the general economic situation and their personal situation in the near future, and they showed a greater tendency to purchase durables. Public consumption increased a little in the third quarter, as did civilian public expenditure.

Fixed investment surged in the third quarter of 2009, after a long period of contraction that was followed by stabilization in the second quarter, as did nonresidential investment in general and specifically investment in machinery and equipment. If investment in commercial vehicles, which jumped in the third quarter as a result of changes in taxes on vehicles, is excluded, however, nonresidential investment actually fell. Its decline was consistent with the large output gap and with companies' using their existing production capacity. This was the case despite the lower cost of financing and the easing of the credit shortage, as companies returned to the capital market for finance, and despite the appreciation of the shekel which made the import of capital goods more worthwhile. Residential investment expanded rapidly, while the slowdown in nonresidential construction persisted.

Goods and services exports (excluding diamonds) continued to increase in the third quarter as a result of increased global demand, especially in the US and Europe—which constitute Israel's main export markets—despite the strengthening of the shekel as reflected in the real effective exchange rate (the trade-weighted exchange rate of the shekel against the currencies of Israel's main trading partners) compared with the previous quarter. The high-tech industries headed the field

[2] In the third quarter there was an upsurge in car purchases due to the change in vehicle taxation (see the section on the budget for details), but even if that component is excluded, the consumption of durables still showed a very large increase.

of manufacturing exports in the period reviewed, whereas exports of the low-tech industries continued their downward trend. The diamond industry showed signs of recovery, but that has only a limited effect on the economy because it has a low added value. Services exports fell in the third quarter, the outcome of conflicting trends: exports of tourist services continued with their rapid expansion, whereas exports of other services, including high-tech services and even those of start-ups, contracted. An atmosphere of uncertainty surrounds the rate of expansion of Israel's exports, because the recovery of the global economy is at least in part dependent on large government support programs, which are expected to end, particularly in light of the heavy deficits and soaring public debt in many countries.

Civilian imports of goods and services (excluding ships, aircraft and diamonds) expanded very rapidly in the third quarter, after a long contraction that ended in the second quarter; the increase in imports was supported by the marked lowering of import prices relative to the GDP deflator. All categories of goods imports increased steeply—current consumer goods and durables, raw materials, and investment goods. These developments are consistent with the increase in production and consumption with the recovery in economic activity.

GDP prices (in quarterly terms) fell slightly in the third quarter. The recovery in economic activity was reflected in an increase in prices of private consumption; export prices fell considerably, while import prices fell more moderately, so that the terms of trade deteriorated.

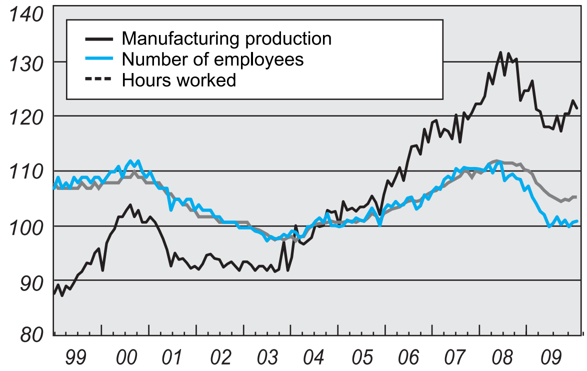
By-industry real activity

The continued expansion of economic activity was evident in most of the principal industries, with industrial exports at the forefront. Manufacturing production expanded by 7.9 percent in September–November compared with the previous three months (seasonally adjusted)—following a long downward trend (Table 1.2 and Figure 1.2)—due to the recovery in global and domestic demand. The expansion encompassed most two-digit industries (and in particular pharmaceuticals and electronic chips) and all levels of technological intensity, and was also reflected by other indices, such as raw material imports for manufacturing.

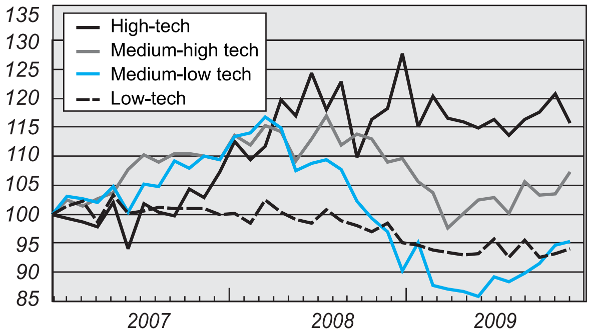
The notable and continued contraction of the number of employee posts in manufacturing and of labor input halted, and some industries actually recorded increases. This, together with the increased utilization of machinery and equipment in the fourth quarter reported in the Bank of Israel Companies Survey, indicates the start of the recovery

Figure 1.2

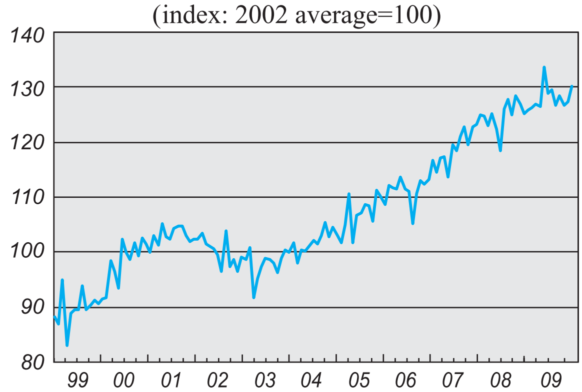
Manufacturing production, 1999-2009*
(index, 2004 average=100)



Manufacturing production by technological intensity of industry, 2007-09
(index: January 2007 = 100)



Large-scale retail trade, 1999-2009
(index: 2002 average=100)



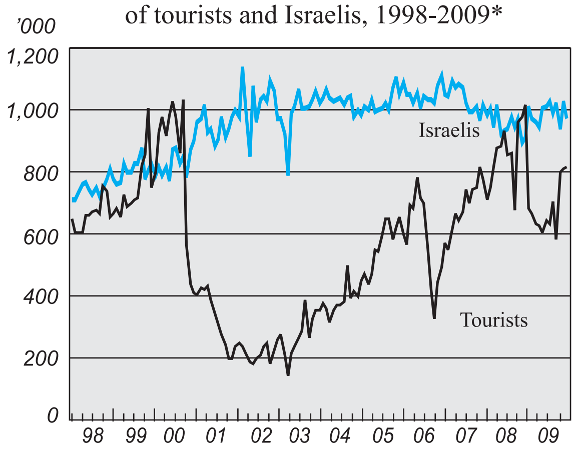
* To November 2009. Seasonally adjusted.

from the crisis and the expansion of activity, mainly based on existing production capacity.

Manufacturers' expectations regarding the last quarter of 2009 as reported in the Manufacturers' Association Survey, and for the beginning of 2010 as reported in the Bank of

Figure 1.3

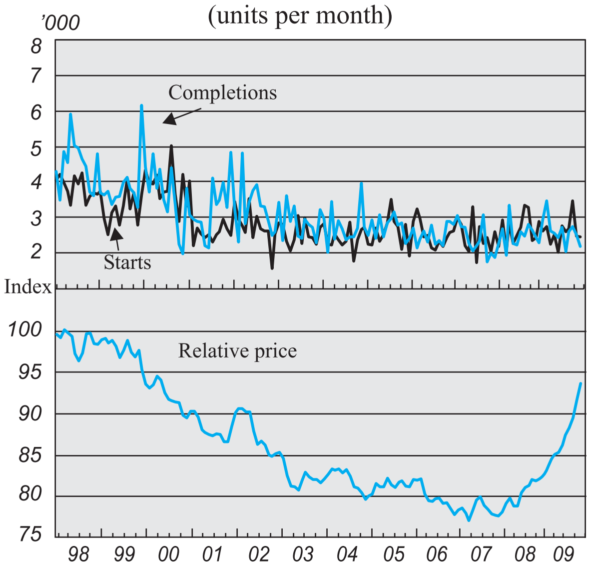
The hotel industry: monthly bed nights of tourists and Israelis, 1998-2009*



* To November 2009. Seasonally adjusted.

Figure 1.4

Housing starts and completions,* and relative price,** 1998-2009 (units per month)



* Original data, to October 2009.
** Prices of owner-occupied dwellings relative to CPI (index, January 1998=100). To October 2009.

Israel Companies Survey, promise well: export orders are expected to grow, the decline in employment will slow, investments will increase, and financing costs will drop.

Trade revenue in the last few months continued along the path of recovery (Figure 1.2). This can be seen from the figures of sales in retail chain stores and purchases via credit cards. Employment in the industry also continued to increase slowly. The Companies Survey reports that those engaged in trade expect that sales will expand in the first quarter of 2010, but without an increase in employment. Revenue of other services, such as financial and business services, accelerated in the period reviewed, and the number of employee posts in them increased. Business services companies expect activity and domestic and export orders to increase in early 2010.

In tourism, the rapid expansion of activity persisted in the period reviewed, as could be seen from the increase in the number of tourist arrivals and the number of their hotel bed nights (Figure 1.3), and in revenue and employment; bed nights of Israelis, however, fell slightly. Data from the World Tourism Organization (UNWTO) indicate that there are signs of recovery in tourism world wide.

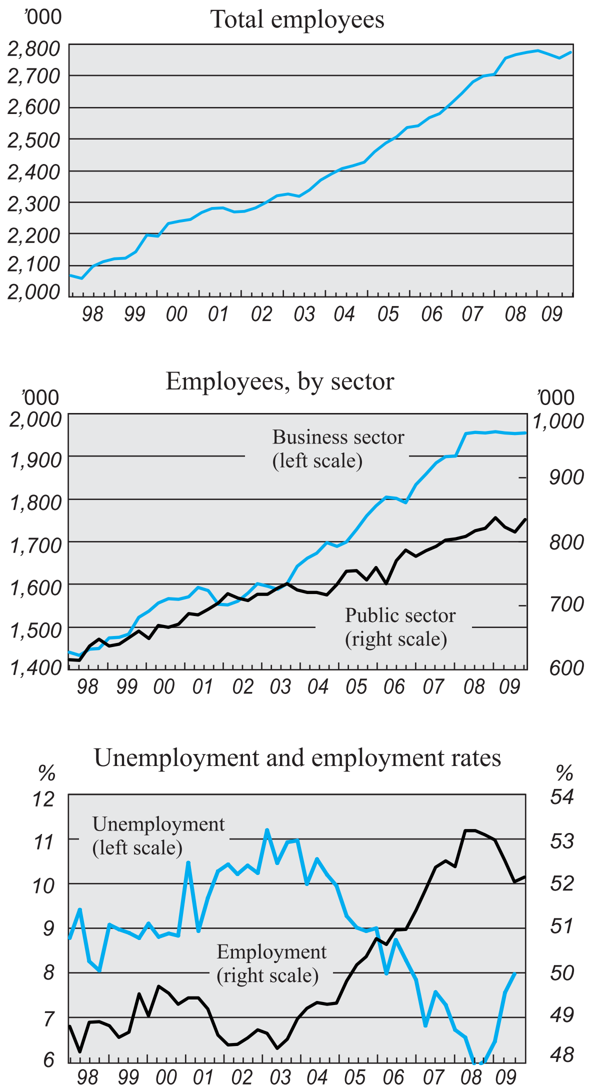
In construction**,** activity continued to revive. The number of building starts rose in the third quarter (Figure 1.4), and the number of building workers increase slightly. The number of home sales rose, reflected by the continued increase in mortgages. On the supply side, the stock of privately built new apartments for sale continued to fall, the index of construction input prices did not change, and in the Companies Survey contractors reported a more severe shortage of skilled manpower. Evidence of the reduced risk in construction is provided by the narrowing of the yield gaps between corporate bonds of construction companies and government bonds (Figure 1.16). The Companies Survey for 2009:Q4 reports expanded construction activity, with similar expectations for the beginning of 2010. The increased demand for residential housing, that derives in part from the low level of mortgage interest and the lack of attractive alternative investment channels, combined with the limited supply, led to the continued rise in prices.

The labor market

The labor market, which usually reacts with a lag to a turnaround in the business cycle, showed signs of recovery in the period reviewed, as could be seen from unemployment and labor input data in the Labor Force Survey for the third quarter (Table 1.3 and Figure 1.5). The unemployment rate started to drop (without a marked change in the rate of participation); it was 7.8 percent in the third quarter (seasonally adjusted), and reached 7.4 percent in November according to trend data—low by comparison with the levels in the advanced economies; the decline was all the more notable in light of the rising rates in many of those economies. The unemployment rate was also low relative to its record level in the previous crisis, during the second *intifada*. Labor input in the business sector rose, the result of the combination of ongoing stability in the number of

Figure 1.5

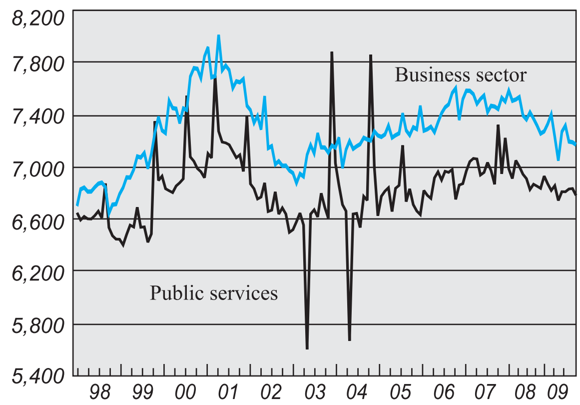
The labor market, 1998-2009*



* To September 2009. Quarterly data. Seasonally adjusted.

Figure 1.6

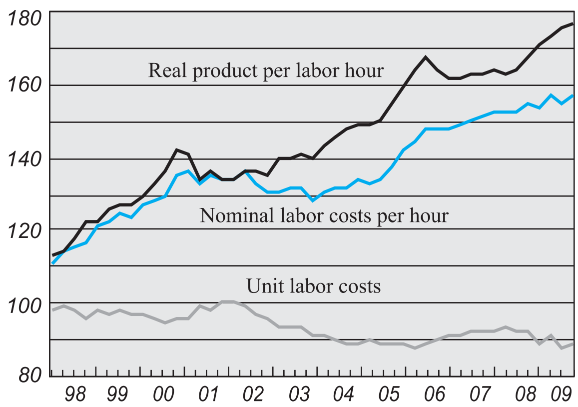
Real wage per employee post, 1998-2009*
(NIS, 2004 prices)



* To October 2009. Seasonally adjusted.

Figure 1.7

Index of nominal unit labor costs (gross) in the business sector, 1998-2009*
(1997 average=100)



* To September 2009. Quartely data. Seasonally adjusted.

Israeli employees (as employment in the public sector rose) with a significant increase in the number of hours worked per employee due in part to the rise in the share of those in full-time employment. The increase in the hours worked per business sector employee represents a correction of the decline during the recession. It is compatible with the process of recovery from a recession, which starts with an increase in hours worked per employee, followed by recruitment of additional workers only when the expansion of economic activity becomes more firmly established.

Other indices relating to the period reviewed also confirm that there was a positive turnaround in the labor market: the number of employee posts in the business sector stabilized after a long decline; the Employers Survey of the Ministry of Industry, Trade and Labor shows an increase in the number of vacancies in the business sector, for the first time in two years, and also a drop in the number of terminations of employment and an increase in jobs filled, giving a positive balance of employment for the first time in a year. These changes occurred in most of the principal industries. According to Manpower (Israel) Ltd, demand for staff rose moderately, reflected in the "vacancies" columns in the newspapers. It thus comes as no surprise that the number of work seekers (both old and new) decreased in the last few months, as did the number of claims for unemployment pay. According to the Employers Survey, employers expect that their payroll and level of activity will continue to improve, so that expectations became positive for the first time in a year.

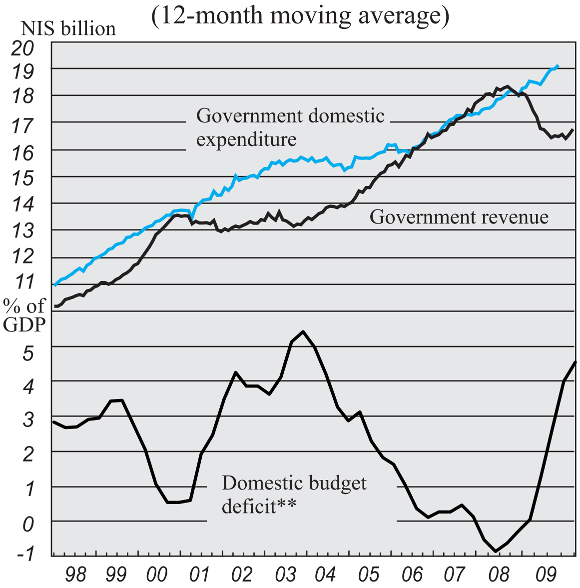
The expanded activity was also reflected in wages. The average wage per employee post in the business sector (seasonally adjusted) rose in the last few months, and the decline in the real wage, affected also by inflation surprise, ended (Figure 1.6) Unit labor costs in the business sector did not change in the third quarter, due to the fact that product per hour worked increased at the same rate as did hourly labor cost (Figure 1.7).

The government

The budget deficit in 2009 was about 5.2 percent of GDP (Table 1.4 and Figure 1.8), compared with the ceiling of 6.0 percent set when the budget was passed. The lower-than-planned deficit was the result of higher revenues than predicted in the budget—due to faster recovery of economic than expected—and expenditure close to the planned level. The overseas deficit slightly exceeded that set in the budget.

Figure 1.8

Government revenue and expenditure, 1998-2009*
(12-month moving average)



* To December 2009.
** Including the Jewish Agency.

Tax revenues in 2009 exceeded the figure in the budget by about NIS 4.7 billion, and in September to December the increase in revenues that started mid-year continued, owing to accelerated economic activity. Direct tax revenues increased in the period reviewed with the revival of the capital market, the improvement in companies' profitability, and the increase in the nominal wage and in employment, which were reflected by increased payments to the National Insurance Institute. Indirect tax revenues grew even faster than did direct, mainly because of increased receipts from import taxes and VAT in the domestic market as private consumption grew and also to some extent due to the increase in the VAT rate prior to the start of the period reviewed. Two reforms in the market for motor vehicles had opposing effects on revenues from import taxes on vehicles: (a) in August the "Green Tax" (with purchase tax rates rising with the degree of pollution caused) became operational, with the result that vehicle imports were brought forward to before the reviewed period to avoid the higher tax; (b) the value of the use of new leased vehicles was increased at the beginning of 2010, so that purchases were brought forward to the end of 2009. It should be noted that in the last few months the surcharge on water usage in excess of the allocated amount (the drought surcharge) was imposed partially, in the estimated amount of less that NIS 200 million. Land tax revenues shot up in the period reviewed with the renewed activity in the real estate market. Government expenditure were above the seasonal path consistent with full performance of the budget, partly as a result of 2010 expenditure being brought forward to 2009.

The balance of payments

The surplus in the current account of the balance of payments in the third quarter was $1.3 billion (seasonally adjusted), similar to that in the second quarter, but significantly higher than those in previous periods (Table 1.5). The surplus in the goods and services account shrank to about $1 billion, mainly because of the drop in exports of R&D services (following their exceptional increase in the second quarter), with high and similar rates of increase in goods exports and imports.

The deficit in the goods account in the third quarter of 2009 was $0.4 billion, the same as in the second quarter, despite the worsening of the terms of trade. Israel's foreign trade in the last few months reflected the expansion of economic activity in Israel and world wide: a surge in exports, particularly by the high-tech industries (Figure 1.10), as the situation of the high-tech sector in the US improved, as shown by the Tech-Pulse index, while the low-tech industries continued to contract (especially food and drinks exports), albeit slowly.

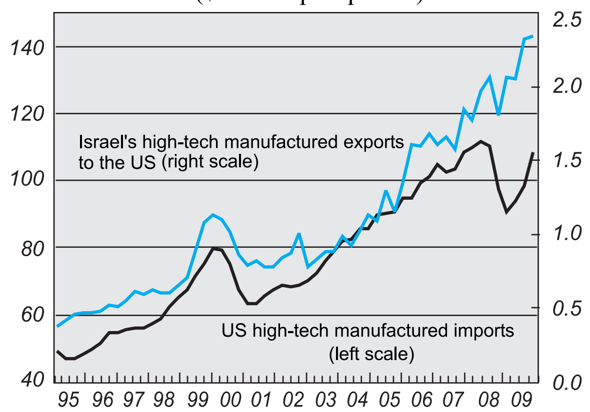
Figure 1.9

Foreign trade,* 1998-2009**
($ million per month)

* Excluding ships, aircraft, diamonds, and fuel.
** To December 2009. Seasonally adjusted.

Figure 1.10

Israel's high-tech manufactured exports to the US and US high-tech manufactured imports, 1995 to 2009*
($ billion per quarter)



* To November 2009. Seasonally adjusted

All categories of goods imports rose sharply—consumer goods, raw materials and capital goods.

The financial account in the third quarter shows the increase in Israelis' investment abroad, with the jump in the level of the foreign exchange reserves in the Bank of Israel, and nonresidents' investments in Israel via all channels also increased sharply. Israelis' direct investment abroad increased, while they sold some of their portfolio of foreign securities, mainly bonds, as well as realizing other investments, particularly commercial banks' deposits abroad. Nonresidents' greatly increased their investment in Israel, both direct and portfolio, mainly in bonds. Other investment also expanded, as commercial credit to Israeli importers grew, and with the IMF allocation to Israel of special drawing rights (SDR). There was a moderate drop in Israelis' income abroad, from direct investments and from foreign securities.

The terms of trade deteriorated by 6.9 percent in the third quarter (excluding ships, aircraft and diamonds), after a long period of improvement. This was due to the rise in the dollar prices of imports with the rise in prices of energy and primary commodities, and the fall in dollar prices of exports.

Global developments[2]

The advanced economies are gradually exiting the deep recession, with the revival of global demand and world trade and the recovery of the financial markets. Spearheading the expansion of activity is stronger production and the first signs of both a recovery in private consumption—with the halting increase in consumer confidence—and of some increase in investment. The continued expansion of economic activity is threatened by heavy government deficits that led to a sharp increase in public debt, instability in financial markets, fragility in banking systems, and very high rates of unemployment that are expected to rise even further in some countries. Central banks persisted with their expansionary monetary policies and continued to increase liquidity in the markets.

In the third quarter of 2009 global growth strengthened, and for the first time since the start of the crisis economic activity expanded in the advanced economies: GDP increased in the OECD by 2.5 percent (annual rate, compared with the previous quarter), in the US by 2.2 percent, and in the eurozone by 1.7 percent (in Spain and Greece, however, GDP still contracted). This recovery in the advanced economies was partial: whereas on the one hand manufacturing output increased, including that of the high-tech industries, exports grew, investments increased despite the difficulties of obtaining finance, and the purchasing managers and consumer confidence indices improved, on the other, private consumption was sluggish and unemployment rose. In the emerging market economies growth continued at a relatively rapid pace.

Growth forecasts for 2010 were revised upwards slightly, to 1.3 percent for the advanced economies (Table 1.6), and a higher rate for the emerging economies, mainly due

[2] For further details see the Bank of Israel Inflation Report No. 29, October–December 2009.

to buoyant activity in China and India. It appears that the recovery from the recession will be not be a quick process, as it rests in part on extensive fiscal intervention that will eventually come to an end—particularly in light of huge government deficits and soaring debts (mainly in southern European countries), which could result in downgrades of some countries' credit ratings (as has already occurred with Greece). Another factor that may also contribute to a slower exit from the recession is consumers' concern over possible future crises, severe credit restrictions, and a possible rise in unemployment, that would increase the saving rate and hold back the expansion of private consumption. Furthermore, the fragility of the financial and banking systems in several countries and their exposure to various market and asset risks constitute another element that could threaten future growth. (Examples of this are the difficulties that beset the Dubai government Investment Corporation, the investment of western banks in East European countries going through severe crises, and the continued bank loan write-offs in the US.) That said, world trade grew much faster in the period reviewed, and this trend is expected to persist in 2010, so that world demand for Israeli products is likely to increase.[3]

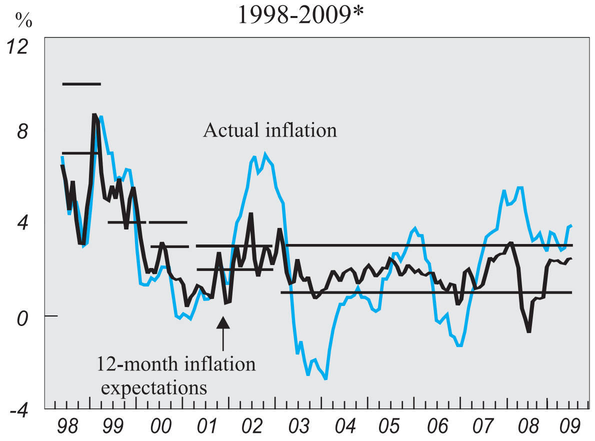
The recovery of the financial markets continued in September–December 2009. Share indices rose, The interbank interest rate spread and corporate credit margins shrank, and there was an upsurge in corporate bond issues. All these were the outcome of the expansionary monetary policy and public optimism about economic developments. Finally, despite the recovery in economic activity, which was accompanied by increases in energy and primary commodity prices, the rate of increase in consumer price indices in the advanced economies remained low, and it therefore seems that their central banks will persist with their expansionary monetary policies that will support real activity.

Prices, monetary policy, and the money and capital markets

The Consumer Price Index went up in 2009 by 3.9 percent, overshooting the upper 3 percent limit of the inflation target, due in large part to increases in the transport and communications and housing components. In September–December the index rose by 0.6 percent, annual rate, (Table 1.7 and Figure 1.11), and if seasonal factors are excluded the inflation rate was 4.1 percent. Inflation expectations also increased slightly, and reached the upper part of the target inflation range. The Bank of Israel rate of interest was increased for December by 25 basis points to 1 percent, still a very low level from a long-term perspective, reflecting

Figure 1.11

Inflation in previous 12 months, inflation expectations, and the inflation target, 1998-2009*



* 12-month inflation expectations as calculated by the Bank of Israel Research Department. To December 2009.

— Inflation target range.

monetary expansion, and the rate for January (outside the period covered by this review) was increased by another 25 basis points, to 1.25 percent.

Price increases in the last few months were due mainly to the following factors: the revival of economic activity and the rise in the value of the public's assets, together with increased consumer confidence and the low interest rate, led to an increase in private consumption; the expansionary monetary policy, combined with the turnaround in the business cycle, raised inflation expectations, which itself is likely to result in price increases at the present time; and world energy and commodity prices rose moderately. Operating in the opposite direction, i.e., to hold back price increases was the appreciation of the shekel and the wide output gap, reflected in high unemployment, among other things. The housing component of the CPI played a not insignificant role in the rise in the CPI in the period reviewed, and prices of owner-occupied housing, which are not part of the CPI, also continued to rise, partly due to the low mortgage interest rate and the lack of attractive alternative channels for investment.

One-year-forward inflation expectations derived from the capital market rose slightly (Figure 1.11)—at the end of the period reviewed they were about 2.5 percent , close to the upper limit of the target inflation range, and similar to the predictions of the private forecasters. The wide range of the forecasters' predictions is an indication of the uncertainty surrounding expected inflation. Inflation expectations for the

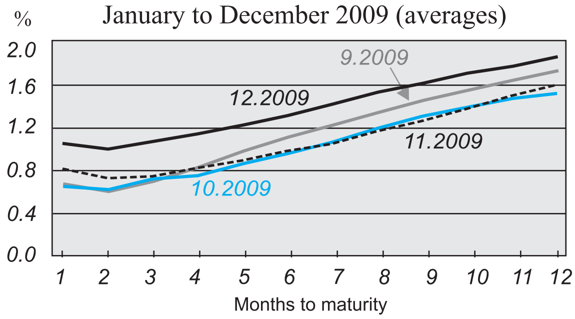
[3] The elasticity of Israel's exports to world trade is 1.4 (see Box 7.1, p. 302, in the Bank of Israel Annual Report, 2007).

long term also rose, and reached 2.8 percent for 2–4 years ahead, and slightly less for farther horizons.

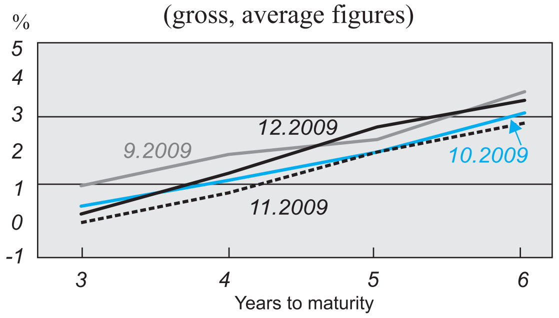
The real yield curve was moved upwards (Figure 1.12), in light of the economic recovery, the rise in inflation expectations to the upper part of the target inflation range, and the increase in yields in the advanced economies as a result of heavy borrowing by governments. Based on the *makam* yield curve, the market expects the Bank of Israel interest rate a year hence to be about 3 percent.

Figure 1.12

Makam yield-to-maturity curve, January to December 2009 (averages)



Yield-to-maturity of CPI-indexed government bonds,* January to November 2009 (gross, average figures)

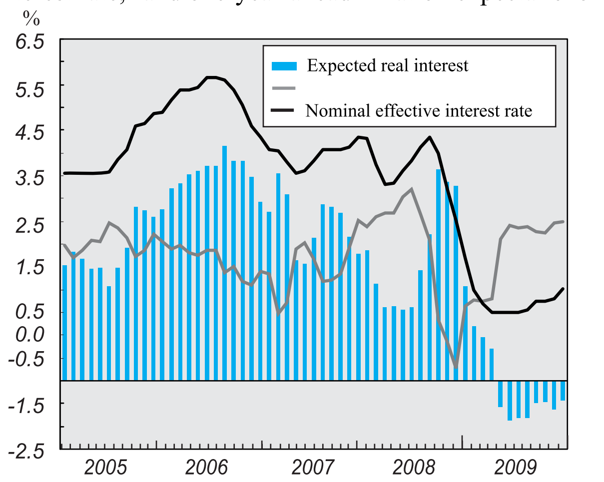


* Excluding the yield on CPI-indexed 10-year bonds.

The Bank of Israel increased the interest rate for September, before the start of the period reviewed, by 25 basis points, to 0.75 percent, as the first signs of a recovery in economic activity became evident, and inflation expectations rose to beyond the upper limit of the target inflation rage. With the moderate continued rise in inflation expectations and the strengthening of the assessment that economic activity would expand, the Bank of Israel increased the interest rate for December to 1 percent (and the rate for January, which falls outside the period covered by this review, was increased to 1.25 percent). The modest increase in the interest rate expressed the continued expansionary monetary policy, which supports real activity, in particular against the background of the prevailing uncertainty regarding future growth. The differential between the Bank of Israel's interest rate and the rates of other central banks (e.g., the FED and the ECB) widened, as the others kept their low rates unchanged. Nevertheless, the Bank of Israel's expansionary monetary is notable in an international comparison, and is expressed in the relatively low level of expected real interest, of a negative 1.3 percent (Figure 1.13).

Figure 1.13

Nominal effective interest rate,[a] the expected real interest rate,[b] and one-year-ahead inflation expectations[c]



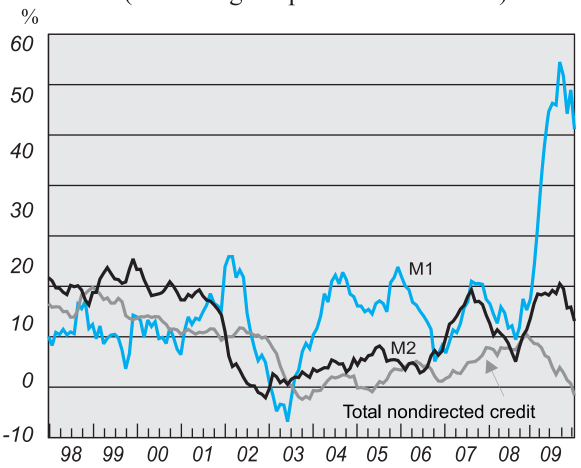
[a] The nominal daily interest rate, in annual terms (compound interest).
[b] The nominal effective interest rate *divided by* one-year inflation expectations.
[c] The yield on unindexed government bonds *divided by* the yield on indexed bonds.

The expansion of the money supply, including the liquid monetary aggregates, slowed and came to a halt in the period reviewed (Table 1.8 and Figure 1.14). This took place against the background of the turnaround in monetary policy—the increased interest rate, ending of the purchase of bonds, and reduction in foreign currency purchases. Bank credit to households contracted, despite the continued accelerated expansion of mortgage loans, and credit to the business sector remained almost unchanged.

During the period reviewed the Tel Aviv share price index rose by13 percent (Table 1.9), almost reaching the peak level it had reached toward the end of 2007, whereas share price indices in the advanced economies and in the emerging market economies stayed far below their pre-crisis levels of September 2008; this was due mainly to the greater severity of the recession world wide than in Israel. The increase in share prices in Israel encompassed nearly all industries, and in particular bank shares; real estate share prices, however,

Figure 1.14

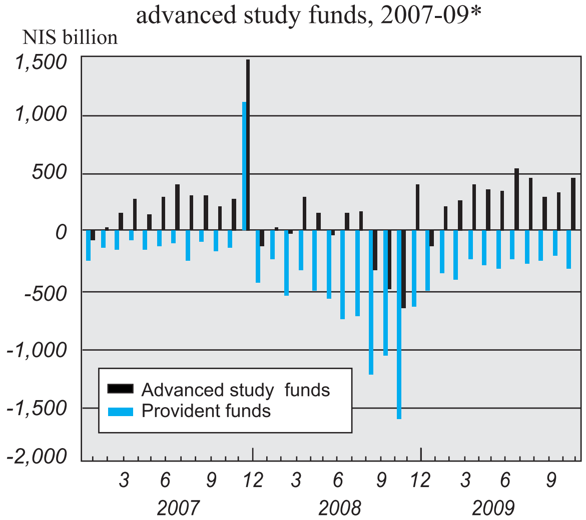
Monetary aggregates and credit, 1998-2009*
(real change in previous 12 months)



* To December 2009.

Figure 1.15

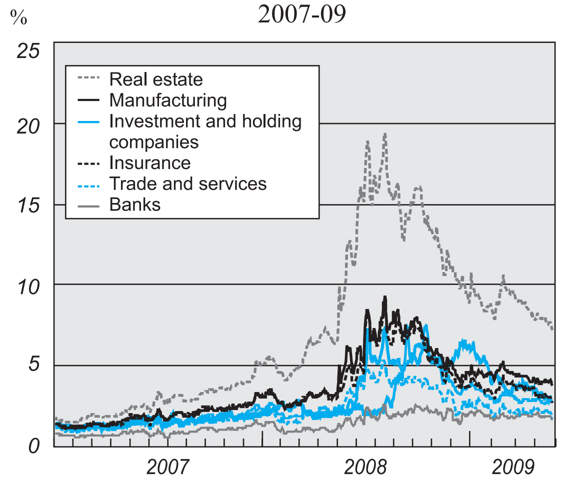
Accumulation of savings in provident funds and advanced study funds, 2007-09*



* To November 2009.

Figure 1.16

The gap between the weighted average yield of CPI-indexed corporate bonds and *Galil* government bonds, by industry, 2007-09



* To December 2009.

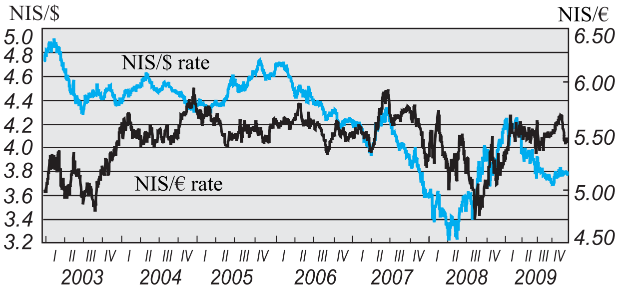
stayed where they were. The index of corporate bond prices continued increasing in the period reviewed, and the extent of bond issuance was similar to the level in the previous four-month period, with a moderate decline in yields relative to those on government bonds (Figure 1.16). The revival of the capital market, especially of the bond market, prompted the Bank of Israel to end its purchases of government bonds on the secondary market as early as the end of July. Capital market developments took place with the support of the expansionary monetary policy and expectations that the recovery in economic activity would be sustained.

As a result of the recovery in the financial markets, the value of the public's financial asset portfolio increased during the period reviewed, and recorded a rise of 16 percent from the beginning of 2009 to November. The increase was essentially a reflection of the rise in prices of securities, and in particular of share and bond prices of companies in Israel and abroad. The weight of securities in the asset portfolio continued to increase, at the expense of the share of cash and deposits, and the accumulation of savings in advanced study funds also persisted (Figure 1.15).

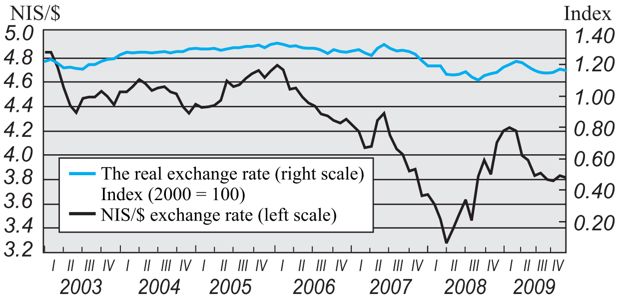
The shekel appreciated against the dollar in the period reviewed (Figure 1.17) against the background of the weakening of the dollar world wide and the intervention of the Bank of Israel in the foreign exchange market. Nevertheless, towards the end of the year, when the dollar strengthened around the world, the shekel also depreciated against it. Indices from the options market show an increase in the probability of shekel depreciation and a sharp drop in the probability of appreciation (the implied volatility of the exchange rate is low). This finding is supported by the Companies Survey, which also shows expectations of shekel depreciation in the coming year, despite the surplus in the current account of the balance of payments and some narrowing of the interest rate differential between Israel and other countries. The shekel depreciated against the euro in the period reviewed. The real effective exchange rate, calculated as a trade-weighted rate against a basket of currencies of Israel's trading partners, showed appreciation, but this reversed in the course of the period. In the period reviewed the Bank of Israel made discretionary purchases of foreign currency totaling $3.1 billion, in accordance with market developments—far below the extent of constant purchases in the past. This activity was cut back heavily in November and December. At the end of the year Israel's foreign exchange reserves stood at $60.6 billion.

Figure 1.17

The nominal NIS/$ and NIS/€ exchange rates, 2003-09*



The nominal NIS/$ exchange rate and the real effective exchange rate,[a] 2003-09



* To December 2009.

[a] The real effective exchange rate is the trade-weighted geometrical average exchange rate of the shekel against the 28 currencies of Israel's 38 main trading partners *minus* the difference between inflation in Israel and in those countries.

Table 1.1 National Accounts,[a] 2008-09

		Change from previous quarter					2009:QIII		
		2008		2009					
	2008[b]	III	IV	I	II	III	Change from previous quarter	Year on year change[b]	Last month for which data available
GDP	4.0	0.6	-1.6	-3.1	1.2	2.9	2.9	-0.2	Sep
Business-sector product	4.5	0.3	-2.9	-5.2	1.1	2.4	2.4	-1.2	Sep
Private consumption	3.6	0.9	-1.8	-3.5	10.2	5.6	5.6	2.5	Sep
Gross domestic investment	1.4	-7.8	15.2	-20.9	-28.5	-5.4	-5.4	-11.4	Sep
Fixed investment	4.4	-17.2	-4.3	-14.9	3.2	8.2	8.2	-2.3	Sep
Goods and services exports excl. diamonds	10.5	4.2	-23.5	-27.8	-2.3	3.4	3.4	-15.9	Sep
Goods exports[c]	2.9	-2.5	-43.1	-16.1	-19.7	29.2	29.2	-16.1	Sep
Services exports[c]	10.7	-0.1	-17.0	-41.1	64.8	-37.9	-37.9	-15.9	Sep
Goods and services imports excl. diamonds	7.2	-2.7	-5.9	-43.9	5.2	11.7	11.7	-11.3	Sep
Goods imports[d]	0.7	-5.9	-35.3	-41.5	16.5	25.3	25.3	-13.8	Sep
Services imports[d]	7.7	6.9	-12.8	-32.3	-0.9	-18.5	-18.5	-16.9	Sep
Public sector consumption	2.1	3.8	-0.3	-5.6	11.5	0.9	0.9	1.4	Sep
Public sector consumption excl. defense imports	2.2	7.1	-0.5	-7.2	18.4	3.8	3.8	3.2	Sep
Domestic use of resources	3.1	0.1	2.0	-6.9	1.7	4.8	4.8	0.3	Sep

[a] Percentage change in annual terms, at constant prices, seasonally adjusted.

[b] Unadjusted data.

[c] New calculation - excluding subsidies.

[d] New calculation - excluding taxes.

SOURCE: Central Bureau of Statistics.

Table 1.2. Indicators of Business Activity,[a] 2008-09

		Change from previous quarter						September - December 09		
		2008		2009				Change from previous period	Year on year change[b]	Last month for which data available*
	2008[b]	III	IV	I	II	III	II			
Composite state-of-the-economy index	-0.9	-3.8	-5.2	-3.8	1.5	5.0	5.8	5.8	1.6	Dec
Unit labor cost	0.1	0.9	-3.2	-3.4	-5.1	-4.2		-4.2	-4.2	Sep
Large-scale retail trade	4.4	16.2	-3.0	1.8	13.6	-10.1	5.1	-0.3	1.0	Nov
Manufacturing production										
(excl. diamonds)	7.0	-7.3	-7.5	-15.4	-5.0	3.3	9.5	7.9	-2.0	Nov
Index of trade revenue	0.3	-6.7	-16.5	-2.2	8.7	7.1	4.8	0.6	1.4	Nov
Index of trade and services revenue	-0.4	-4.3	-16.5	-3.3	6.2	3.9	5.6	2.5	0.4	Nov
Index of services exports	9.6	-27.9	12.6	-58.4	238.5	-64.8	68.6	-9.4	-6.0	Dec
Tourist arrivals	32.8	-19.1	0.4	-62.3	49.8	46.8	36.6	41.4	-0.2	Dec
Residential construction[b]	10.1									
Starts	10.1	20.5	16.6	-4.5	-1.5	-3.7			3.0	Oct
Completions	7.9	10.4	24.2	8.5	1.6	-1.0			-7.5	Oct
Nonresidential construction[b]	24.8									
Area of starts	24.8	26.2	-11.7	1.0	-53.2	-45.1		-45.1	-45.1	Sep
Survey of companies (net balance, percent)[c]										
Weighted balance of the business sector	1	1**	-29**	-38**	-12*	0*	19	19		Dec
Output of manufacturing firms	-7	-8**	-33**	-32**	-14*	3*	27	27		Dec
Sales by trading firms	-6	-4**	-46**	-55**	0*	2*	25	25		Dec

[*] When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[**] Not significant at 5% level.

[a] Percentage change, in annual terms, seasonally adjusted.

[b] Unadjusted data.

[c] The net balance is defined as the difference between the number of firms reporting a rise and those reporting a decline, as a proportion of all reporting firms.

SOURCE: Based on Central Bureau of Statistics and Ministry of Construction and Housing data.

Table 1.3. Indicators of Labor Market Developments,[a] 2008-09

		2008		2009				September - December 09		
	2009:QIII	III	IV	I	II	III	IV	Change from previous period	Year on year change[b]	Last month for which data available*
	('000)	percent change from previous quarter								
Civilian labor force	3,014.9	0.4	0.7	0.7	0.0	0.5		0.5	2.1	Sep
Israeli employees	2,779.2	0.3	0.2	-0.4	-0.5	0.7		0.7	0.5	Sep
of which: in general government	834.5	0.4	2.1	-1.8	-0.9	2.4		2.4	1.9	Sep
in business sector	1,956.0	-0.1	0.1	-0.1	0.0	0.0		0.0	0.0	Sep
Foreign workers and Palestinians (unadjusted)[c]	266.5	3.0	-0.3	-4.8	2.2	-0.3		-0.3	-3.3	Sep
Average hours worked weekly per Israeli employee	36.5	-1.6	-2.7	0.8	0.6	1.1		1.1	-2.5	Sep
Labor input in business sector (incl. foreign workers and Palestinians)	94,805	-1.0	-1.4	-0.7	0.2	0.7		0.7	-2.5	Sep
of which: Israelis	82,882	-1.5	-1.7	0.1	0.0	0.8		0.8	-2.3	Sep
Weekly labor input in general government (Israelis)	18,113	-0.5	-1.9	0.5	-0.8	4.1		4.1	0.2	Sep
Unemployed	235.7	2.6	7.8	17.3	5.3	-1.3		-1.3	25.3	Sep
Work seekers	204.7	7.0	5.6	9.4	4.4	-1.2	-2.3	-2.1	14.5	Nov
Claims for unemployment benefit	90.6	5.5	10.6	20.1	13.7	3.1	-3.0	-4.5	40.2	Dec
Balance of employment[d]		1.1	-0.5	-1.9	-0.6	-0.3				Sep
Real wage per employee post[e,f]	7,084.3	-33.0	-1.3	0.0	2.0	0.6	-0.1	-3.0	12.0	Oct
In general government	6,989.6	-46.0	-55.0	0.0	3.0	0.3	-0.6	-1.0	12.0	Oct
In business sector	7,128.0	-1.7	-1.1	0.3	-2.1	0.7	-0.9	-6.2	-3.0	Oct
Nominal wage per employee post[f]	8,069.9	-0.5	-0.6	0.4	-0.3	1.7	0.4	-0.9	0.5	Oct
In general government	7,962.1	-0.1	-0.1	0.6	0.1	1.5	-0.1	2.1	2.2	Oct
In business sector	8,119.7	-0.5	-0.3	0.5	-1.1	1.9	-0.3	-3.3	-0.2	Oct
		Percent, seasonally adjusted								
Participation rate	56.5	56.4	56.6	56.7	56.5	56.5				Sep
Employment rate	52.1	53.0	52.9	52.4	52.0	52.1				Sep
Unemployment rate	7.8	6.1	6.5	7.6	8.0	7.8				Sep
Depth of unemployment[g]	34.8	32.1	30.5	30.1	33.4	34.8				Sep

* When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[a] Percentage change, seasonally adjusted.

[b] Unadjusted data.

[c] Due to an error in the method of calculation, the data from January 2008 have been recalculated.

[d] Posts filled minus terminations of employment as a percentage of the total number of employees in businesses in the Ministry of Industry, Trade and Labor Employers Survey sample.

[e] At 2004 prices.

[f] Including foreign workers and Palestinians.

[g] Percent of unemployed seeking work for more than six months (unadjusted).

SOURCE: Central Bureau of Statistics, Labor Force Survey, except for data on Israelis, non-Israelis, and labor input in the business sector, and total Israelis employed, which are the Central Bureau of Statistics' National Accounts estimates.

Table 1.4. Government Budget Performance, 2008-09

		2008		2009				September - December 09		
	2008	III	IV	I	II	III	IV	Change from previous period	Year on year change	Last month for which data available*
Domestic deficit as percent of GDP	-0.5	0.6	-7.1	-1.1	-5.1	-1.2		-1.2	0.6	Sep
Deviation from domestic budget path, excl. credit extended[a]			(NIS billion)[b]							
Revenue	-4.4	-3.4	-3.3	-4.0	0.8	2.9	3.4	2.9	9.2	Dec
Expenditure	-1.0	-3.4	3.6	-4.7	2.1	-1.3	1.3	2.8	0.4	Dec
Deficit	-3.3	0.0	-6.8	0.6	-1.3	4.1	2.1	0.1	8.8	Dec
Total deficit excluding credit	-39.2	-0.9	-16.5	-4.0	-11.9	-2.9	-15.1	-7.1	-2.2	Dec
					Real percentage change, year on year					
Government tax revenue	-6.7	-9.0	-11.4	-15.1	-10.6	-1.6	8.5	-0.2	2.3	Nov
of which: income tax, net	-13.2	-15.6	-14.5	-20.9	-15.6	-12.4	-0.8	2.1	-2.9	Dec
VAT, gross	1.6	-0.1	-7.2	-14.0	-14.1	0.2	3.4	1.7	2.3	Dec
Government expenditure	1.0	-7.6	6.1	-5.8	8.6	7.6	0.3	11.3	4.4	Dec
National Insurance allowances	1.7	0.9	1.3	6.7	7.0	8.0	6.6	0.0	9.9	Nov
of which: Unemployment benefit	-0.0	0.7	17.2	47.9	71.2	69.4	45.2	-8.1	54.5	Nov
Income support[c]	-5.5	-4.7	-3.9	-3.0	0.9	0.7	3.5	-1.4	2.8	Nov
National insurance contributions received from the public	1.7	-1.5	-0.2	-2.2	-4.2	-1.5	-1.5	-0.9	1.7	Nov

* When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[a] Based on the deficit target.

[b] Year on year change. Does not refer to the seasonal path.

[c] Not including income supplement in old-age and survivors' pensions.

SOURCE: Based on Ministry of Finance and National Insurance Institute data.

Table 1.5. Foreign Trade, Balance of Payments, and the Reserves,[a] 2008-09

	2008[b]	2008 III	2008 IV	2009 I	2009 II	2009 III	2009 IV	September - December 09: Change from previous period	September - December 09: Year on year change[c]	Last month for which data available
	percent change from previous period[b]									
Trade in goods[d]										
Goods imports	15.6	0.3	-10.2	-17.7	-5.3	9.7	2.9	6.2	-14.8	Dec
of which: Consumer goods	20.2	4.7	-5.3	-9.7	-2.3	9.2	3.5	5.1	-3.1	Dec
Capital goods	16.7	-3.1	-8.8	-18.9	-9.9	12.0	-3.3	-3.1	-24.4	Dec
Intermediates	13.6	0.4	-12.5	-20.2	-4.4	8.9	5.3	10.6	-15.1	Dec
Goods exports	16.8	-1.2	-12.0	-12.4	1.2	10.1	7.5	11.2	1.9	Dec
of which: Manufacturing	17.9	-1.8	-11.7	-13.0	1.5	11.0	7.1	11.1	1.9	Dec
of which: High-tech	8.5	-3.2	-5.9	-3.1	11.1	7.5	3.2	8.4	20.4	Dec
Balance of payments	$ million									
Goods and services exports	81,249	21,159	17,817	15,717	16,289	16,360				Sep
Goods and services imports	84,313	22,863	18,267	13,996	14,855	16,827				Sep
Balance of trade in goods and services account	-3,064	-1,704	-450	1,721	1,434	-467				Sep
Current account	2,120	56	809	2,686	1,470	229				Sep
Financial account (excl. foreign exchange reserves)[c]	2,024	4,355	3,846	-681	2,222	5,795		5,795	4,355	Sep
of which: Nonresidents' direct investment[c]	2,410	2,788	1,723	1,310	707	1,452		1,452	2,788	Sep
Nonresidents' portfolio investment[c]	-39	-1,305	398	669	-262	1,312		1,312	-1,305	Sep
Residents' direct and portfolio investment abroad[c]	2,555	1,645	5,318	1,350	790	2,753		2,753	1,645	Sep
Bank of Israel reserves, end-period[c]	42,513	36,257	42,513	44,332	50,275	59,964	60,613			Dec
Net foreign debt (percent of GDP)[c]	-23.1	-21.4	-23.0	-25.6	-26.0	-26.6		-26.6	-21.4	Sep

[*] When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[a] Seasonally adjusted.

[b] The change relates to the dollar values of imports and exports.

[c] Unadjusted data.

[d] Not including ships, aircraft, diamonds, and fuel.

SOURCE: Based on Central Bureau of Statistics data.

Table 1.6. Indicators of Economic Development in Advanced and Developing Countries[a]

(annual rate of change, percent)[b]

	2006	2007	2008	Estimate 2009	Projection 2010
World GDP	5.1	5.2	3.0	-1.1	3.1
Advanced countries	3.0	2.7	0.6	-3.4	1.3
Developing countries	7.9	8.3	6.0	1.7	5.1
World trade	9.2	7.3	3.0	-11.9	2.5
Advanced countries					
Imports	7.4	4.7	0.5	-13.7	1.2
Exports	8.2	6.3	1.9	-13.6	2.0
Developing countries					
Imports	14.4	13.8	9.4	-9.5	4.6
Exports	10.9	9.8	4.6	-7.2	3.6
Commodity prices (US$)					
Oil[c]	20.5	10.7	36.4	-36.6	24.3
Nonfuel	23.2	14.1	7.5	-20.3	2.4
Inflation (CPI) in advanced countries	2.4	2.2	3.4	0.1	1.1
Short-term interest[d] (%)					
Dollar deposits	5.3	5.3	3.0	1.2	1.4
Euro deposits	3.1	4.3	4.6	1.2	1.6
Unemployment rate in advanced countries	5.7	5.4	5.8	8.2	9.3

[a] According to World Economic Outlook, Israel is classified as an advanced country. The advanced countries include the industrialized countries and some emerging markets.

[b] Except for unemployment and interest rates, which are actual rates.

[c] Average price of Brent crude in 2008 was $97 per barrel, excluding transport costs.

[d] Six-month Libor rate for US dollar deposits, and three-month Libor rate on euro deposits.

SOURCE: World Economic Outlook (IMF), October 2009 update.

Table 1.7. Selected Price Indices, 2008-09
(percent change)

		2008		2009						
	2008	III	IV	I	II	III	IV	Change from previous period[a]	Year on year change[b]	Last month for which data available*
				Change during the quarter[c]						
CPI	3.8	2.0	-0.6	-0.1	2.3	1.3	0.5	0.2	3.9	Dec
CPI excl. housing, fruit and vegetables	2.0	0.1	-1.4	-0.8	2.4	0.8	0.7	0.3	3.1	Dec
CPI excl. housing, fruit and vegetables, price-controlled goods, clothing and footwear	1.3	0.7	-2.9	-0.2	2.4	0.8	0.1	-0.3	3.2	Dec
Index of housing prices	12.1	8.2	4.9	1.3	1.5	2.3	0.3	1.1	5.6	Dec
Price index of owner-occupied homes[d]	10.6	2.2	0.2	2.7	3.8	4.1		8.8	18.0	Oct
Wholesale price index	-4.4	-0.1	-10.9	-0.9	1.6	2.5	0.2	1.1	3.4	Dec
Nominal unit labor cost	1.8	-0.5	-1.9	2.7	0.7	-0.4		-0.4	1.1	Sep
NIS/$ exchange rate	-0.9	5.5	9.1	7.5	-5.2	-4.5	0.6	-1.1	-2.1	Dec
NIS/ € exchange rate	-8.4	-2.4	2.2	4.5	1.5	-0.8	1.0	1.3	6.3	Dec
Real effective exchange rate[e]	-10.7	-13.3	-12.5	-2.1	4.8	1.5	3.2	-1.8	3.0	Dec
				Year on year change[f]						
CPI	4.6	5.1	4.6	3.4	3.2	3.2	3.6	1.1	3.4	Dec
CPI excluding housing, fruit and vegetables, price controlled goods, clothing and footwear	4.5	5.6	2.9	0.2	-0.2	0.0	1.9	0.5	1.5	Dec

* When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[a] December 2009 compared with August 2009.

[b] December 2009 compared with December 2008.

[c] Last month of each quarter compard with last month of previous quarter.

[d] Not part of the CPI.

[e] The real effective exchange rate is the trade-weighted geometric average shekel exchange rate against 28 currencies, representing Israel's 38 main trading partners, *minus* the difference between the inflation rate in Israel and in those countries.

[f] Period average.

SOURCE: Central Bureau of Statistics.

Table 1.8. Monetary Aggregates and Nondirected Bank Credit, 2008-09
(annual rate of change, percent)

		2008		2009				September - December 09		
	2008	III	IV	I	II	III	IV	Compared with previous period	Year on year change	Last month for which data available*
Rates of change	Change from previous quarter									
M1[a]	14.1	24.6	20.0	69.0	118.9	50.3	3.1	19.6	56.4	Dec
M2[b]	9.8	8.0	22.7	29.5	15.7	11.1	4.7	8.7	16.0	Dec
M3[c]	8.0	4.7	20.5	24.6	14.8	3.6	2.8	4.1	12.1	Dec
Nondirected bank credit	8.2	10.3	14.0	0.2	-2.3	1.2	1.5	2.6	0.8	Dec
Unindexed local-currency credit	18.2	15.8	19.1	6.5	2.8	9.3	7.0	8.6	7.0	Dec
CPI-indexed credit	4.9	6.9	1.8	-17.1	-8.5	5.0	-0.1	3.4	-5.4	Dec
Credit in and indexed to foreign currency	-12.8	-1.0	24.6	19.2	-7.9	-31.3	-16.3	-20.9	-8.9	Dec

* When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[a] Narrow money supply (demand deposits and cash in the hands of the public).

[b] M1 plus short-term local-currency unindexed deposits.

[c] M2 plus short-term CPI-indexed demand deposits.

SOURCE: Bank of Israel.

Table 1.9. Interest Rates, Yields, and the Share-Price Index, 2008-09
(quarterly average, percent)

		2008		2009				September - December 09		
	2008	III	IV	I	II	III	IV	Change from previous period	Year on year change	Last month for which data available*
Nominal interest										
SRO deposits	2.7	3.1	2.4	0.7	0.3	0.3	0.4	0.4	2.9	Nov
Nondirected local-currency credit	7.9	8.0	7.9	6.8	5.7	5.5	5.0	4.9	7.8	Dec
Effective interest on daily deposit auctions	3.6	3.8	3.3	1.2	0.5	0.6	0.8	0.8	3.3	Dec
LIBID 3-month dollar intrest	2.8	2.8	2.6	1.1	0.7	0.3	0.1	0.2	2.7	Dec
Yield to maturity on:										
Makam (12 months Bank of Israel bills)	3.9	4.4	2.9	1.2	1.1	1.5	1.7	1.7	3.2	Dec
Yield on 5-year bonds	2.9	2.7	3.6	1.8	1.6	1.5	1.1	1.2	3.4	Dec
Risk premium[a]		1.5	1.8	1.3	0.8	0.7	0.9	0.8	0.7	Dec
Inflation expectations, twelve months forward[b]	1.9	2.6	-0.2	0.7	1.8	2.3		2.3	2.1	Sep
General Tel-Aviv Share-Price Index (change from previous period)	-46.4	-17.9	-25.8	20.3	18.3	10.3	13.9	15.7	-34.5	Dec

* When the last month is December, the comparisons are of four-month periods; when the last month is September, the comparisons are quarterly; and when the last month is November, the three months September–November are compared with May–July.

[a] As measured by the 5-year credit-default-swap (CDS) market.

[b] Derived from the yield gap between indexed and unindexed bonds held by tax-exempt institutional investors, minus the X-day effect on the price of the bond.

SOURCE: Bank of Israel.

Part 2: Broader Review of Selected Issues

The Market Share of Israeli Export Goods

- Israel's market share in US imports is high, and its share in imports of other advanced economies and of the group of large emerging market economies (China, India, Russia and Brazil) is low on average.
- The export of Israeli goods to important economies, such as Germany, France and China, is smaller than expected, and to the US, India and Brazil is higher than expected, given the effect of the size of the GDP and GDP per capita of all Israel's trading partners, the composition of their imports, and their geographical distance from Israel.
- Israel has a high market share in countries whose imports include a high share of chemicals and in office and communication equipment, and in countries close geographically to Israel (e.g., Cyprus, Turkey and Jordan) and those with a large GDP (e.g., the US).
- Trade agreements with individual countries (Canada, Mexico, Egypt and Turkey) have helped to increase the market share of Israel's exports.

While Israel's market share in the export of goods to the US is relatively high, it is relatively low for other developed countries[1] (Figure 2.1 and table 2.1) and for the large emerging economies (Brazil, India, China and Russia). Over the past decade, the share of the large emerging economies in global output and imports has increased significantly, while the share of the US in global imports has fallen, a trend that is working against Israeli exports. In what follows, we will examine the export of Israeli goods to some ninety countries and will compare Israel's market share in a number of them. This is done on the basis of several variables that influence the share of Israel's exports in those countries' imports, including the composition of their imports, distance from Israel, the existence of a trade agreement, etc.

In order to analyze the factors that influence Israeli's market share in the various countries, we estimated a trade model[2] to explain the share of Israel's export of goods within each country's total imports of goods (excluding oil). The model included the following variables:[3] GDP[4] which represents the size of the target market, GDP per capita which represents the target market's level of development, distance from Israel, the existence/non-existence of a trade agreement[5] and the share of various categories of goods in total imports (excluding oil).[6] The sample period used is 1990–2008. A positive connection was found between the importing country's GDP and the share of Israeli exports in its total imports (excluding oil) and a negative relation was found for distance from Israel.[7] No effect was found for a trading partner's GDP per capita or for the existence of a trade agreement, on average. Israel's market share was relatively high in countries whose imports include a high share of chemicals and office and communication equipment, in which Israel enjoys a relative advantage. In contrast, Israel's market share was relatively low for countries whose imports have a high share of traditional manufactured goods.

In order to rank the countries, we compared Israel's actual market share in the imports of each target country (excluding oil) to the predicted share given its distance from Israel, GDP, composition of imports, etc.[8] It was found (Figure 2.2) that the shares of Israel's exports in the imports of the US, India and Brazil were higher than predicted ("surplus share") relative to the majority of countries in the sample. In contrast, the share of Israeli exports within the imports of China and most of the EU countries, especially Germany and France, was relatively low. The finding with regard to the European countries can be explained by the close trade relations within the EU. A calculation of the

[1] The following developed countries were included in the analysis: Sweden, Finland, Denmark, Iceland, Norway, Britain, The Netherlands, Belgium, Luxembourg, Germany, Switzerland, Austria, France, Spain, Portugal, Italy and Japan

[2] In the spirit of the gravity model. The basic gravity model, which is the one most commonly used to estimate international trade flows, was used to estimate Israel's trade with its trading partners using measures of economic size, such as GDP or total imports, and the distance of these countries from Israel.

[3] All the variables in the model, apart from the existence of a trade agreement, are expressed in natural logs.

[4] Throughout the analysis, GDP and GDP per capita are expressed in terms of their ratio to the corresponding global variables.

[5] The data for trade agreements was taken from the site of the Ministry of Industry, Trade and Labor.
A dummy variable was created for the existence of trade agreements with the aforementioned countries, with account taken of when the agreement went into effect. This is a complex task since the agreements do not apply to all traded goods and were put into effect in stages rather than all at once. In addition, Israel's trade agreement with the EU was signed subsequent to a number of previous trade agreements with some of the EU countries in the 1970s. see appendix A.

[6] Trade data was taken from the WTO site. The classification is according to the SITC (Standard International Trade Classification).

[7] See Appendix B.

[8] The difference between Israel's actual and predicted market shares are affected by factors not included in the model which may explain part of this difference, e.g., cultural differences between Israel and the target markets.

gap between actual Israeli exports and the levels predicted by the regression in nominal terms for the years 2007-08 shows that Israeli exports to important economies such as Germany, France and China are lower than their potential levels by more than $100 million for each of those countries (Figure 2.3).

We examined the change in the share of Israeli exports to the various countries between the years 2000 and 2008 (using the same model with the addition of a control for the year) and found a significant improvement in Israeli exports to Cyprus,[9] Turkey, Brazil and Finland (Figure 2.4). In contrast, there was a significant worsening in the share of Israeli exports to China, Russia and most of the European countries, including Austria, Switzerland and Germany (which is most likely the result of increased trade between the European countries during the current decade).

Israel has particularly close trade relations with the US. Israel's market share of goods imported to the US is 0.7 percent, which is at least twice its share in other countries. This is particularly significant taking into account the considerable distance between the two countries. Nonetheless, when the effect of US trade is neutralized in the model (by adding a dummy variable for the US), there was no major effect on these findings. Thus, Israel's market share remained relatively low for the imports of China, Germany and France and relatively high for India and Brazil (Figure 2.6). The change in the regression specification affected the size of the coefficients and their level of significance but not their signs.

We also examined Israel's market share in countries with which Israel has a trade agreement[10] (Figure 2.5). This was done by comparing the market share of Israeli exports during the year or two prior to the agreement taking effect and the average during the five or six years following. From this point of view, the findings appears to be mixed: all the trade agreements signed with individual countries (Canada, Mexico, Egypt and Turkey) increased the share of Israeli exports in their imports; however, the trade agreement signed with the EU[11] and EFTA did not increase Israel's market share in their imports (on average). This can be explained by the tightening of trade relations between the European countries.

Table 2.1
Israel's Share in Total Goods Imports (excluding oil) by Groups of Target Countries, and the Distribution of Global Goods Imports (excluding oil), 2001 and 2008 (percent)

	Share of Israeli exports in total imports		Market share of Israeli exports predicted according to the economic variables for 2008		Distribution of global imports of goods	
	2001	2008	with dummy variable for the US	without dummy variable for the US	2001	2008
US	0.58	0.69	-	0.24	21.10	14.62
Developed countries	0.28	0.24	0.26	0.30	48.52	44.90
China, India, Brazil and Russia	0.30	0.28	0.26	0.31	7.32	13.79
Other countries	0.28	0.30	0.24	0.26	23.07	26.70
Total	0.34	0.33	-	-	100.00	100.00

SOURCE: Based on Central Bureau of Statistics and IMF data.

9 The high surplus share of Israel's exports to Cyprus may reflect Cyprus's status as a transshipment point for goods destined for countries with which Israel does not have direct trading relations.

10 The analysis was carried out for six trade agreements that Israel has signed in the last 18 years.

11 The EU countries included in this category were those who signed a trade agreement that went into effect in 1995.

Figure 2.1

Market share of Israeli exports within total imports (excluding oil) of selected countries, 2001 and 2008

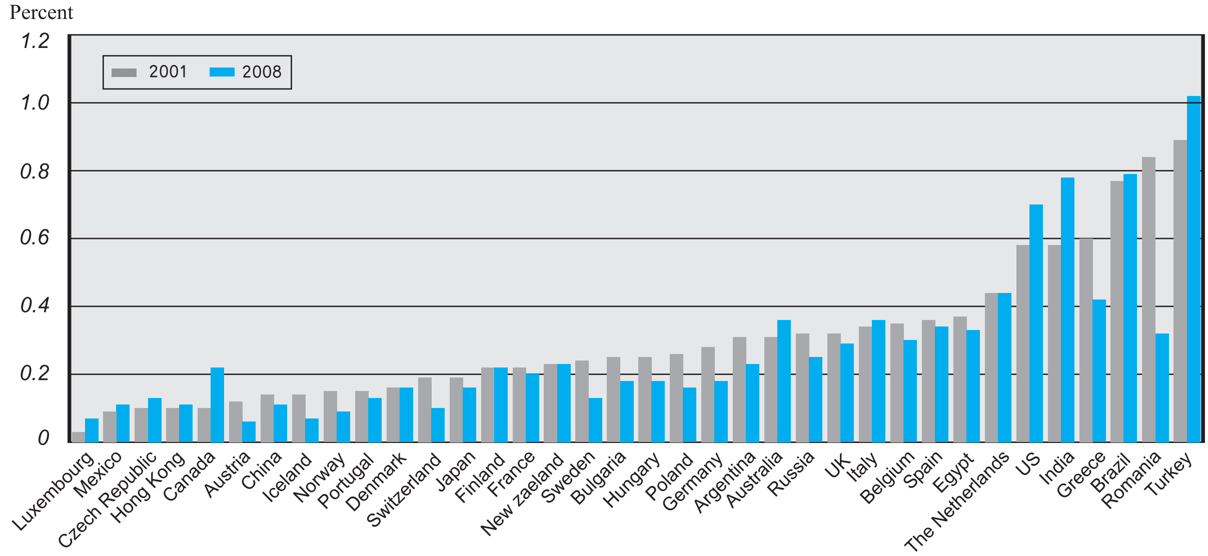
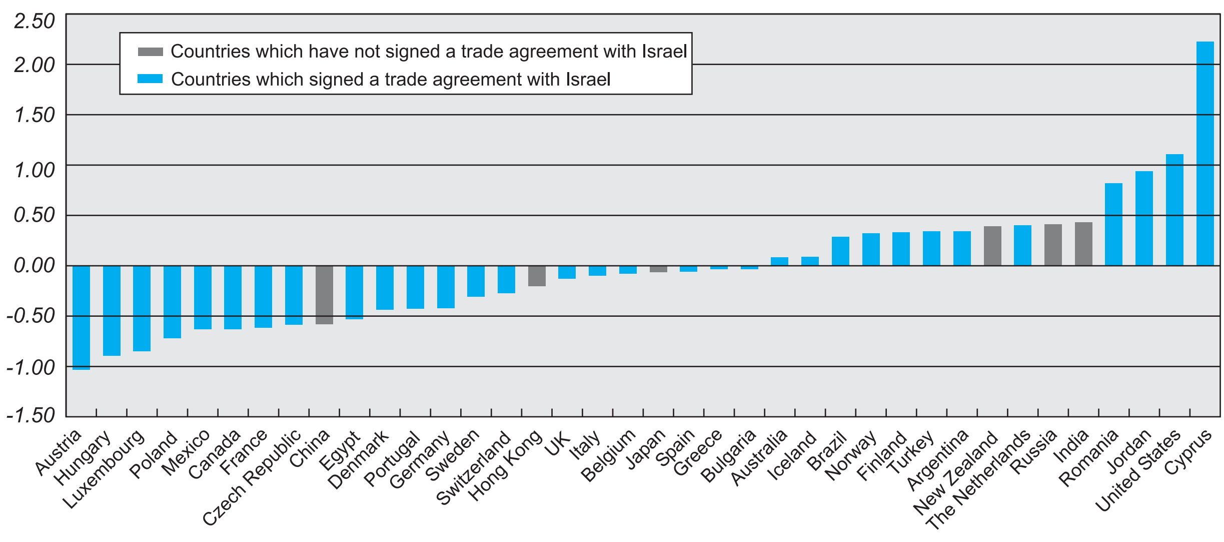


Figure 2.2

Israel's Surplus Market Share in the Imports of Selected Countries (average), 1990-2008[a]



[a] The figure shows the average annual difference between Israel's predicted and actual shares in target countries' imports (0 indicates that the actual and predicted shares are the same), and ranks Israel's surplus shares in the imports of those countries.

Figure 2.3

The surplus of Israeli exports by country, 2007-08 (average)

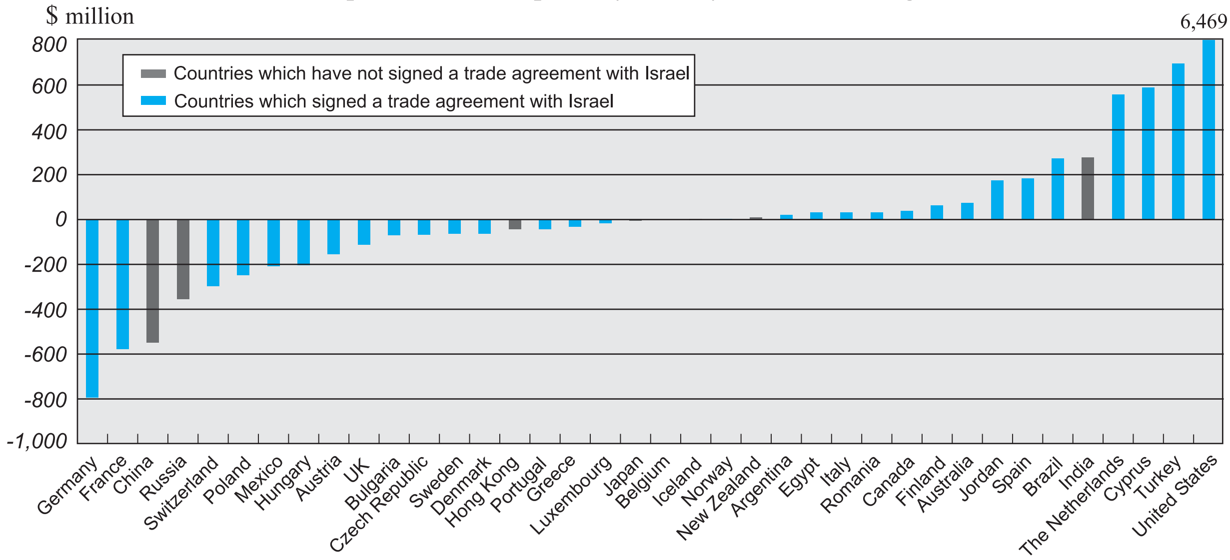
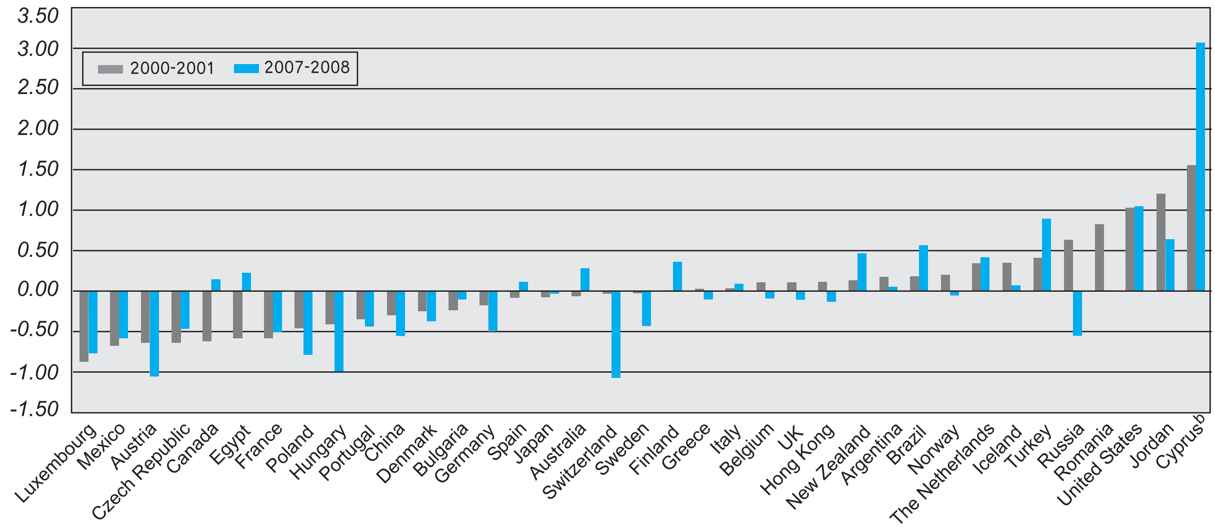


Figure 2.4

Surplus market share of Israeli exports to selected countries, 2000–01 compared with 2007–08[a] (averages)



[a] The figure shows the average annual difference between Israel's predicted and actual shares in target countries' imports (0 indicates that the actual and predicted shares are the same), and ranks Israel's surplus shares in the imports of those countries.

[b] The high surplus share of Israel's exports to Cyprus may reflect Cyprus's status as a transshipment point for goods destined for countries with which Israel does not have direct trading relations.

Figure 2.5

Israel's market Share in the imports of selected countries (excluding oil), average of 5–6 years after a trade agreement became effective compared with 1–2 years before the agreement

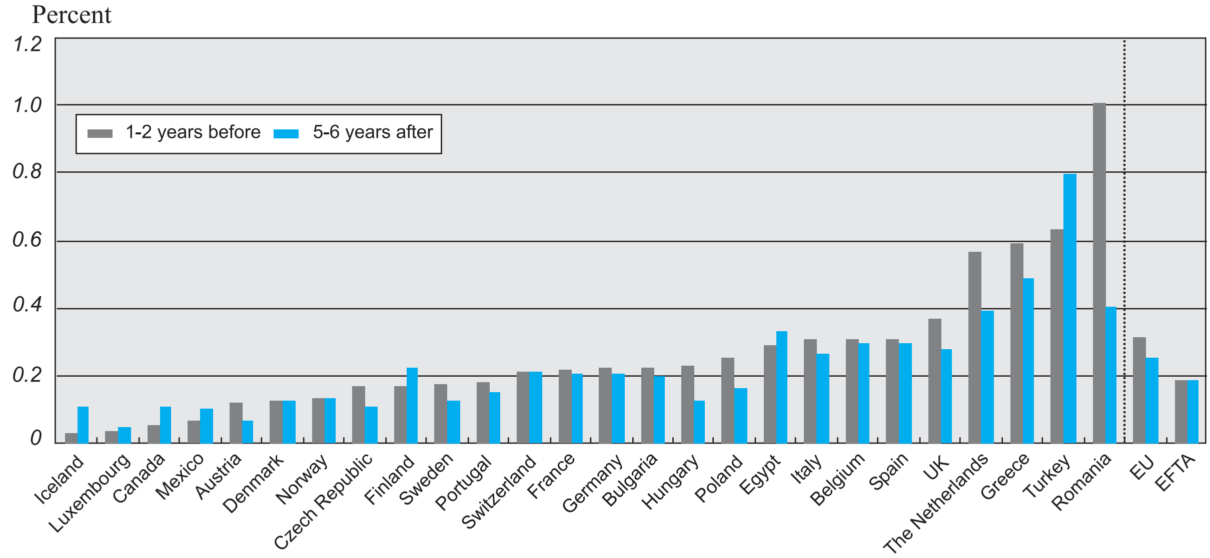
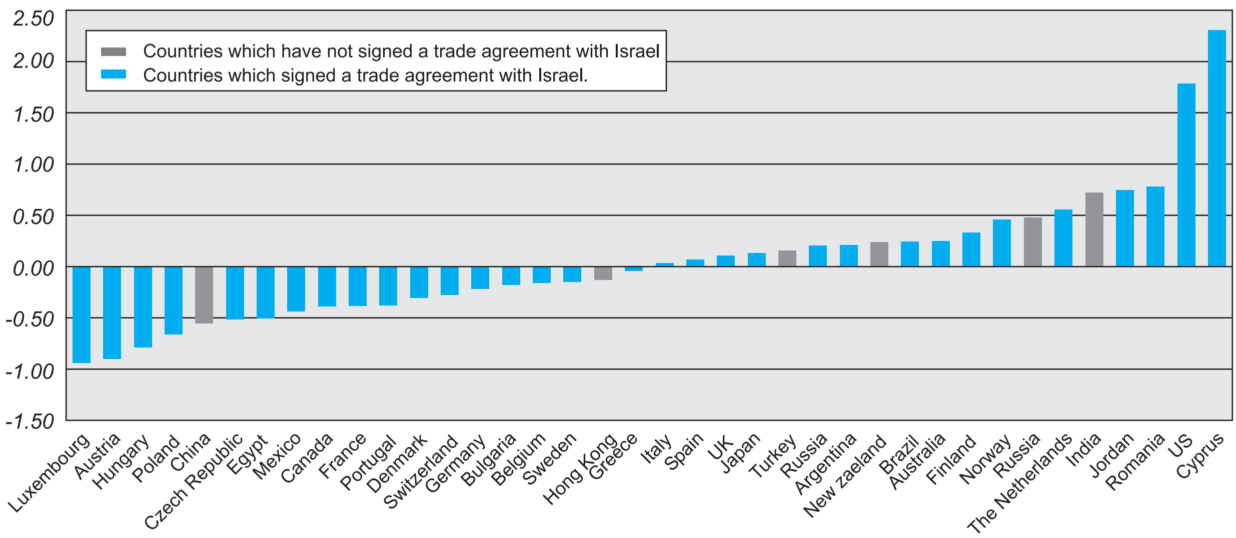


Figure 2.6

Israel's surplus market share in the imports of selected countries, 1990-2008[a] (average, with the addition of a dummy variable for the US)



[a] The figure shows the average annual difference between Israel's predicted and actual shares in target countries' imports (0 indicates that the actual and predicted shares are the same), and ranks Israel's surplus shares in the imports of those countries.

Appendix A

Table 2.2

Trade Agreements with Israel

Agreement with	Year the agreement was signed	Year the agreement went into effect
EU	1995	2000
EFTA	1992	1993
US	1985	1985
Bulgaria	2001	2002
Turkey	1997	1997
Mexico	2000	2000
Canada	1996	1997
Romania	2001	2001
Egypt	2004	2004
Jordan	1995	1995
Mercosur	2007	

SOURCE: Ministry of Industry, Trade and Labor.

EU (27 countries): Austria, Belgium, UK, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, The Netherlands, Hungary, Ireland, Italy, Luxembourg, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden.

EFTA: Iceland, Lichtenstein, Norway, Switzerland.

Mercosur: Argentina, Brazil, Paraguay, Uruguay, Venezuela.

Appendix B

Table 2.3

Dependent variable: Market share of Israeli exports of goods within total imports (excluding oil) by country: A Selection of Versions Used to Choose the Model[a]

Variable	Regression 1	Regression 2	Regression 3	Regression 4
GDP[b]	0.05	0.15	0.15	0.08
	(0.41)	(0.01)	(0.01)	(0.06)
GDP per capita[b]	-0.07	-0.13	-0.12	-0.05
	(0.21)	(0.03)	(0.05)	(0.28)
Distance	-0.38	-0.56	-0.56	-0.60
	(0.01)	(0.00)	(0.00)	(0.00)
Dummy for date that trade agreement went into effect	-0.17	-0.18	-0.12	-0.30
	(0.26)	(0.41)	(0.60)	(0.14)
Imports of chemicals	-	-	0.84	1.23
			(0.01)	(0.00)
Imports of office and communication equipment	-	-	1.12	1.25
			(0.02)	(0.01)
Dummy for US	-	-	-	1.79
				(0.00)
All industries	-	+	-	-
Selected industries[c]	-	-	+	+
Number of observations	1,309	957	957	957
R^2	0.13	0.36	0.36	0.40

[a] The numbers in parentheses are the levels of significance of the coefficients.

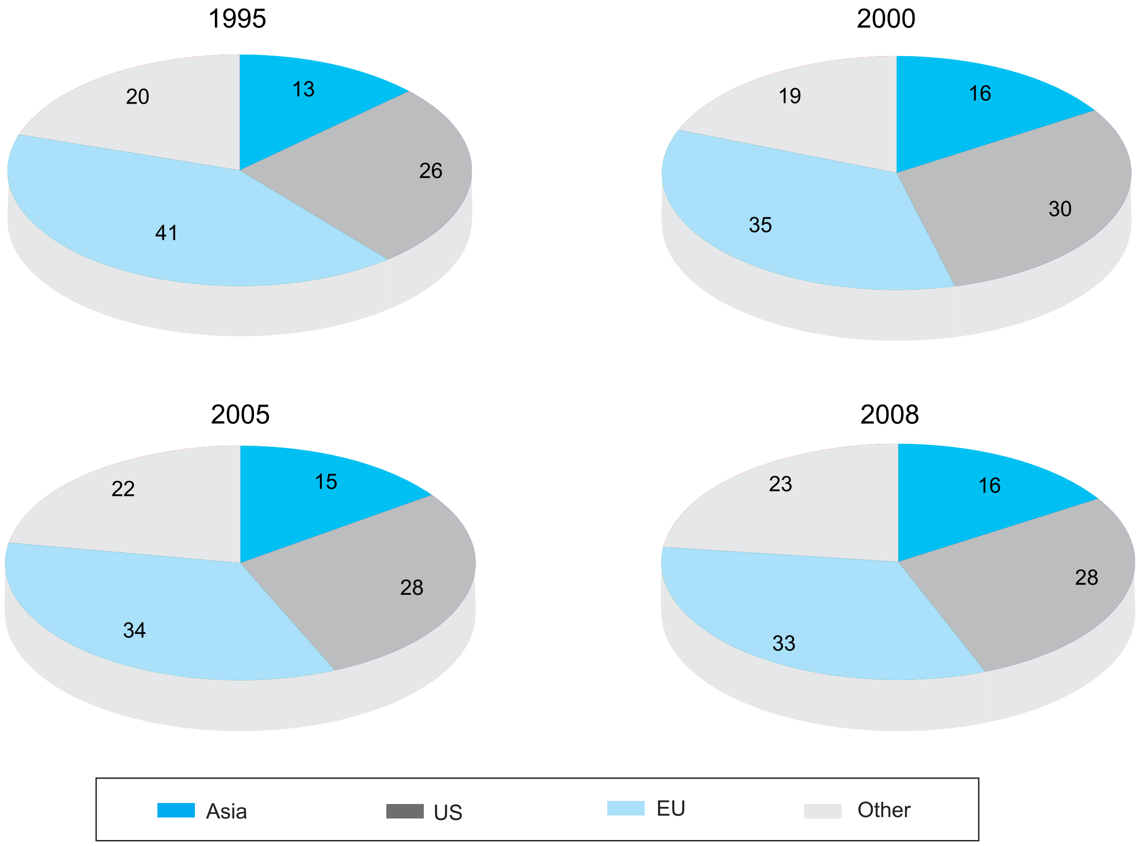
[b] GDP and per capita GDP are expressed in ratios to the corresponding global variables.

[c] Industries that did not reach a threshold level of significance of 0.35: clothing, textiles, motor vehicles and drugs. [a] The numbers in parentheses are the levels of significance of the coefficients.

Appendix C

Distribution of Israel's goods exports by target country groups, selected years

Percent



First Year of the Earned Income Tax Credit

- In its first year of implementation, the earned income tax credit (EITC) program disbursed grants to 28,800 eligible persons. The average annual grant was NIS 2,600 per worker and the total sum paid out was NIS 74 million.
- About half of those eligible for the grant received NIS 2,000–NIS 4,000 in annual terms.
- Sixty-five percent of grant sums accrued to especially low-income workers—those whose wage-labor income per standard person was in the lowest third.
- Forty-five percent of persons potentially eligible for the EITC in 2008 (as determined on the basis of their income in 2007) exercised their eligibility—a relatively high takeup rate by the standards of similar programs abroad in their initial stages of implementation.
- According to the 2007 data, 64,000 persons were assessed to be eligible for the EITC; 85 percent of them had children up to age 18, had been in the labor market for years, and had low but stable incomes.

Since 2008, Israel has been piloting an earned income tax credit (EITC) program that seeks to mitigate income-distribution inequality and encourage labor-force participation by subsidizing low-wage workers in order to increase their income. In the first year of implementation, workers who met the terms of the law (on the basis of their income in the 2007 tax year) received grants of up to NIS 840 per month (for households with two eligible persons with at least three children up to age 18). The program focuses on two groups: working people with children up to age 18 and older low-wage workers (aged 55+) who have no children up to age 18; it is applied in areas where the Orot la-Ta'asuka (welfare-to-work) program is also being implemented (hereinafter: "combined-program areas"). The grant is disbursed in several installments during the year on the basis of income in the previous tax year and claims presented by those eligible. Claims are submitted in an expedited and simple procedure via post offices in the combined-program areas. To facilitate the application process, the Israel Tax Authority sent notices to all people whom it found eligible on the basis of its records (pertaining to their income in 2007) and encouraged them to apply for the grant if they were found to meet the criteria. In 2008, only employees were included in the program, but starting in 2009 (on the basis of income in 2008) the self-employed have been included as well. The nationwide rollout of the program was deferred, under the 2009 and 2010 Economic Arrangem Laws, from 2010 to 2012 (on the basis of income in 2011). Under the Caregivers Law, however, the program will already be implemented countrywide for mothers of young children (up to age two)[12] in 2010 and 2011 (on the basis of income in 2009 and 2010).

This survey presents main findings relating to the first year of the implementation of the EITC Law: the main characteristics of the population of eligible persons, the size of the grant and its distribution among those eligible, the main trends in the takeup of eligibility, and the effect of the program on its recipients' welfare.

1. Description of the population of persons eligible[13]

The EITC Law focuses on low-wage earners and is meant to support two main population groups: households of wage-earners with children up to age 18 (85 percent of those eligible) and older low-wage earners (55+). Among households with children, 12 percent are single-parent.[14] Twenty-six percent of those eligible immigrated to Israel in the 1990s, as against 23 percent of wage-earners countrywide who did so.[15] The rate of Arabs who were eligible, 20 percent, far surpassed their share in the wage-earning population (14 percent).

Most of those eligible worked for a protracted period in 2007 (ten months on average) and earned slightly more than the minimum wage[16] (Table 2.4).

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[12] The law also applies to single fathers with young children.

[13] The analysis pertains to a file of wage-earners and was prepared on the basis of computerized Form 126. This form, submitted to the Israel Tax Authority by the employer, gives a condensed presentation of all payments and withholdings, credit points, a breakdown of months worked, etc., for each person on the employer's payroll in annual terms. The file contains 10 percent of all wage-earners countrywide and sampled 303,000 persons in 2007. Data on eligibility, grant size, and actual takeup were added to the database. Supplemental characteristics—number and age of children, date of immigration and place of residence—were added on the basis of data obtained from the Ministry of the Interior.

[14] Studies in the United States show that the American EITC law had a major effect on this group and that the extent of employment of single mothers is positively correlated with the payment of an EITC. See, for example, N. Eissa and J. Leibman, "Labor Supply Response to the EITC", 1996; B. Meyer and D. Rosenbaum, "Welfare, the EITC and the Labor Supply of Single Mothers", 2001.

[15] The analysis is based on administrative data, which are slightly different from those of the Central Bureau of Statistics labor-force and income surveys due to differences in defining the wage-earner population: the administrative database defines every individual who worked at least one day in the tax year as a wage-earner; the surveys use a narrower definition.

[16] The average minimum wage in 2007 was NIS 3,679 per month.

Table 2.4 Main Characteristics of Eligible Persons' Employment Patterns in 2007

	Workers aged 23+ with 1–2 children		Workers aged 23+ with 3+ children		Older workers (55+)	
Characteristics	Eligible	Ineligible*	Eligible	Ineligible*	Eligible	Ineligible*
Gross monthly wage, NIS	3,735	8,932	3,866	8,674	3,661	9,315
Months worked	10	11	10	11	10	10
Age	36	40	38	40	61	62
Monthly wage-labor income per standard person in household with 2 breadwinners, NIS	3,019	6,422	2,125	4,652	3,884	9,460
Monthly wage-labor income per standard person in household with 1 breadwinner, NIS	1,437	2,974	928	1,874	2,315	4,743

* Ineligible wage-earners who live in combined-program areas

The data in the table emphasize the focus of the EITC Law on very-low-income workers: their average wage was 42 percent of the wage of other wage-earners who had similar demographic characteristics and lived in the combined-program areas. The wage-labor income per standard person of those eligible fell short of half of that of ineligible persons with similar characteristics in any eligibility group.

Analysis of the employment of eligible persons in the five years preceding 2007 shows clearly that this population is firmly integrated into the labor market: more than half of those eligible worked continuously in 2002–06 (Table 2.5) and 70 percent worked at least three years during this time.

Table 2.5
Percent of Eligible Persons Who Worked Continuously as Wage-Earners in 2002–06

	Pct. of eligible persons who worked continuously				
	1 yr	2 yrs	3 yrs	4 yrs	5 yrs
	2006	2005–06	2004–06	2003–06	2002–06
All persons eligible	88	77	69	61	56

Additional characteristics that indicate steady presence in the labor market are an average of ten months worked per year over the years and consistency in the size of posts held[17] (Table 2.6).

The stability that was found in the annual average wage originates, among other factors, in the fact that the wages of about half of those eligible (in 2008) who worked in 2002–06 (for most of that time) remained constant over the years: more than 30,000 eligible persons who reportedly had three or more years of employment experience during this time earned NIS 2,000–NIS 4,000 per month and most of them earned at a steady level.[18] In 2005–06, about two-thirds of eligible persons worked more than eight months on annual average (Table 2.7). However, the large number of workers who did not work during this entire period is indicative of the difficulty in maintaining stable employment at the low end of the labor market.

Table 2.6
Employment Patterns of Eligible Persons in 2002–07*

	2002	2003	2004	2005	2006	2007
Avg. monthly wage, current prices, NIS**	3,579	3,558	3,558	3,591	3,686	3,782
Minimum monthly wage, NIS	3,267	3,335	3,335	3,335	3,501	3,679
Deviation from minimum wage (pct.)	10	7	7	8	5	3
Months worked, on annual avg.	9.8	10	10	10	10.3	10.2

* Among those eligible who worked as wage-earners in the relevant years.
** Wage is calculated on the basis of actual months worked.

[17] Since the data in our file do not include hours worked, we estimated the extent of employee post on the basis of the average monthly wage data.

[18] The annual average wage (calculated commensurate with the number of months actually worked) was defined as stable if its deviation from the worker's average wage in the five years from 2002 to 2006 did not exceed 20 percent.

Table 2.7
Distribution of Eligible Persons by Months Worked, 2005–06 Average

Average number of months worked	Weight of group (pct.)
1–4	11
5–8	22
9–11	24
12	43
Total	100

We examined wages earned in 2005 and 2006 by workers who were eligible for the EITC in 2008. Even though they had been steadily employed in the preceding five years, the wages of most of these people remained low or close to the minimum (e.g., in 2005 and 2006—Table 2.8). It follows that the EITC Law is indeed supportive of workers who, despite being steadily employed, earn low wages for years.

Table 2.8
Distribution of Eligible Persons by Wage Levels, 2005–06 Average

Range of monthly wage (NIS)	Weight of group (pct.)
0-1,000	2
1,001-2,000	10
2,001-3,000	23
3,001-4,000	30
4,001-5,000	23
5,001-6,000	8
6,001-7,000	2
7,001-8,000	2
Total	100

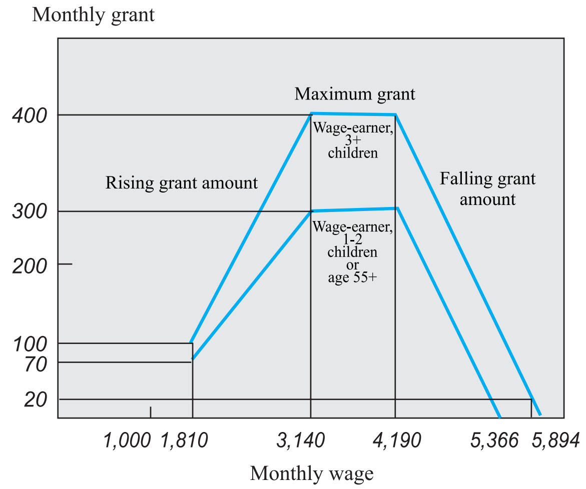
2. Level and distribution of EITC grants among those eligible

The relation of the EITC to the average income level has a trapezoid shape pattern: it initially rises in tandem with wage, peaks at a certain income range, holds steady at that level, and declines gradually at higher income ranges (Figure 2.7).

Thirty-five percent of persons eligible who have children fall within the flat range of the trapezoid, i.e., they earn incomes that entitle them to the highest possible grant (NIS 290 per month for eligible persons with up to two children and

Figure 2.7

Distribution of EITC Grants by Eligibility Type (NIS), 2007



NIS 420 per month for those with three or more children). This population shows a perceptible upward trend in the proportion of those eligible commensurate with the increase in their monthly wage, as well as a large share of these eligible persons (36 percent) in the declining segment of the trapezoid. In contrast, the share of the group of older workers who qualified for the maximum grant was smaller (30 percent) and a large portion of them (39 percent) fell into the rising part of the trapezoid.

The distribution across the trapezoid shows an evident gender difference among those eligible. Due to wage differences, the proportion of eligible men rises steadily—from 23 percent at low income levels to 35 percent in the flat part of the trapezoid and 43 percent in the falling segment—whereas the share of women is highest at low wage levels (36 percent) and then declines steadily, to 33 percent in the flat segment and 29 percent in the falling segment.

An eligible person's position on the trapezoid affects his or her employment behavior: the progressivity of the EITC on the rising part of the trapezoid encourages those eligible to increase their labor supply in order to obtain a larger grant, whereas eligible persons in the declining segment of the trapezoid have an incentive to reduce their work hours in order to limit the decrease in the grant.

3. Takeup of entitlement to an EITC

In 2008–09, more than 52,000 claims for EITC grants were submitted on account of income in 2007. Among them, 28,800 claims were approved, around 20,000 were rejected, and the rest are pending.[19] Overall, the program paid out NIS 74 million and the annual average grant was NIS 2,560. In 1,140 households, both spouses received the grant, at the average of NIS 4,700, and the largest annual grant came to NIS 9,000. About half of those who exercised their eligibility for the program received annual grants in the range of NIS 2,000–NIS 4,000 (Table 2.9).

Table 2.9
Distribution of Grant Recipients, by Size of Grant

Range of annual grant (NIS)	Recipients	Share of group among all Recipients (pct.)
0-999	4,742	16
1,000–1,999	5,925	21
2,000–2,999	6,745	23
3,000–3,999	7,503	26
4,000–4,999	1,826	6
5,000+	2,075	7
Total	28,818	100

Among the 490,000 wage-earners who lived in the combined-program areas, an estimated 64,000 were found potentially eligible—13 percent of all wage-earners in those parts of the country.

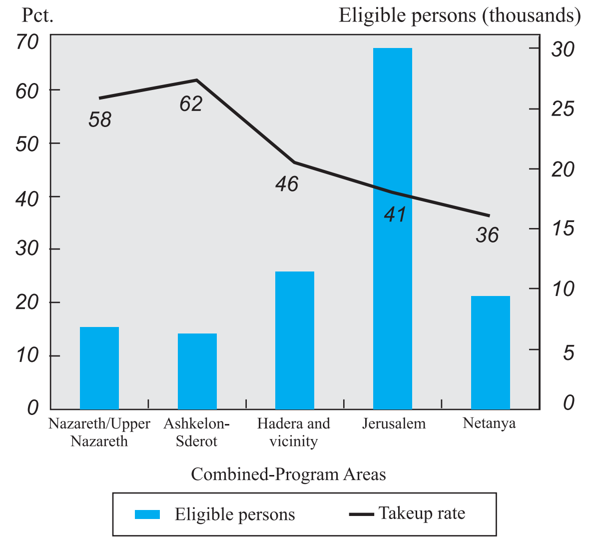
Forty-five percent of those who took part in the program exercised their eligibility, with slightly above-average takeup rates found among 1990s immigrants (48 percent) and Arabs (49 percent).[20] Israel's takeup rates are higher than those in the U.S. federal program in its initial years of implementation.

Takeup by regions

The takeup rates varied considerably from one region to the next[21]: in Nazareth/Upper Nazareth and Sderot-Ashkelon, more than half of those eligible took up the grants, while in Netanya the takeup rate was only about one-third (Figure 2.8).

Figure 2.8

Distribution of Eligible Persons for Grants and Takeup of Grants, by Combined-Program Areas



Takeup by employment history

The takeup rate correlates with the number of years of employment experience in the five years preceding the year of eligibility: among eligible persons who worked up to three years in 2002–06, it rose from 38 percent to 44 percent, and among those eligible who worked four and five years during this time, it was higher—46 percent and 47 percent, respectively.

Takeup by size of grant

As expected, the takeup rate rose steadily commensurate with the size of the annual grant (Table 2.10)—from 18 percent at the low grant levels to 51 percent at higher levels. At the maximum grant level, however, the takeup

[19] The main reason for the lengthy time needed to process claims is employers' failure to submit Form 126, which provides information about total payments and withholding in the tax year, to the Tax Authority. Although employers are required to submit this form by the end of March in respect of the previous year, they are often given an extension. In cases where the form was not submitted, the claimant was allowed to submit Form 106, which the employer is required to present to every employee. (Form 106 and Form 126 provide the same data.)

[20] Not including residents of East Jerusalem.

[21] The distribution of those eligible in the combined-program areas was as follows: 47 percent of all persons eligible in Jerusalem; 18 percent in Hadera and vicinity; 15 percent in Netanya; 10 percent in Nazareth/Upper Nazareth; and 10 percent in Sderot/Ashkelon.

rate declined slightly, in contrast to international experience showing that the takeup rate is highest at the point where the grant is largest. The explanation for this is that the large number of persons in Israel who qualify for the maximum grant (workers with three or more children who earn close to the minimum wage) live in eastern Jerusalem,[22] where the takeup rates are very low—evidently due to lack of awareness of the existence of the program.[23]

Table 2.10
EITC Takeup Rate by Size of Annual Grant

Range of annual grant (NIS)	Number of persons eligible	Number of recipients	Takeup rate (pct.)
20–100	229	42	18
101–600	6,929	2,221	32
601–2,100	22,479	9,267	41
2,101–4,600	28,640	14,497	51
4,601+	5,724	2,792	49
Total	64,000	28,818	45

4. Effect of the program on workers' welfare

The largest portion of grants disbursed under the auspices of the program—the total, as stated, added up to NIS 74 million—accrued to members of cohorts of workers whose labor income was at the bottom of the distribution scale (based on wage-labor income per standard person—Table 2.11); this is consistent with the goal of the EITC Law to narrow social disparities. Analysis of the income distribution of all wage earners in the combined-program areas shows that 65 percent of total support (NIS 48 million) was received by workers in the two lowest distribution cohorts. More than 60 percent of payments to workers at higher income levels (more than NIS 4,000 per standard person) accrued to workers aged 55+ in small households—a group that constituted only 15 percent of grant recipients.

The EITC payments had a substantial upward effect on the monthly average wage-labor income per standard person of recipient households that belonged to the two lowest quintiles of recipients (Table 2.12). The increase in income was 12 percent in the lowest quintile and 7 percent in the next-to-lowest quintile. In contrast, for recipients in the higher rungs of the income-distribution scale—mainly those aged 55+ without children—the increase in income was found to be very slight.

Table 2.11
Distribution of EITC Payments in Combined-Program Ereas, by Cohorts of Monthly Wage-Labor Income per Standard Person*

Range of monthly income (NIS)	Share of cohort (pct.)	Share of total recipients (pct.)	Grant amount disbursed (NIS ,1000s)	Distribution of grant by income cohorts (pct.)
0–1,000	19	24	19,957	27
1,001–2,000	19	38	28,351	38
2,001–3,000	16	21	14,808	20
3,001–4,000	13	12	7,850	11
4,001–5,000	9	5	2,438	3
5,001–6,000	6	1	648	1
6,001–7,000	4	0	78	0
7,001+	13	0		0
Total	100	100	74,130	100

* The number of individuals in the household was calculated on the basis of the individual's marital status and number of children up to age 18.

Table 2.12
Distribution of EITC Recipients by Income Quintiles

	Quintiles				
	1	2	3	4	5
Monthly income per standard person (NIS)	656	1,136	1,600	2,331	3,710
Monthly grant per standard person (NIS)	79	83	84	84	87
Grant per standard person as pct. of income per standard person (pct.)	12	7	5	4	2

[22] Residents of eastern Jerusalem account for more than half of all persons eligible for the maximum grant (NIS 400–NIS 420 per month).

[23] In contrast, a relatively high takeup rate was recorded among Arab eligible persons who live in other combined-program areas, where information activity about the program took place. In the Nazareth area, there was a joint project among the Yedid association, Agam-Mehalev (operator of the welfare-to-work program in that area), and the Israel Tax Authority, in which Tax Authority officials gave the Yedid volunteers and the Agam-Mehalev counselors instruction about the details of the program.

Diary of Events: September to December 2009

Month	Date	**Event**	**Details**
September 2009	3	The European Central Bank leaves the rate of interest at 1 percent—its lowest ever	
	9	The ministerial committee approves the privatization of Haifa and Ashdod ports	The ministerial committee on privatization decided to privatize Haifa and Ashdod ports by selling the state's holdings in them. In the first stage, starting in mid-February 2010, 15 percent of the state's holdings will be sold. In the second stage, 12 months after completion of the first stage, up to 49 percent of the state's holdings in the companies will be sold. As long as the state holds 51 percent or more of the company's issued share capital, all the directors in the company will be appointed by the state. In the third stage the balance of the state's holdings in each of the companies will be sold or will be depleted through private auction, beginning from mid-February 2020.
	13	Trade tussles in the world intensify against the background of the crisis	The President of the United States, Barack Obama, announced the imposition of 45 percent customs duties on motor car and light truck tires imported from China. Imports of tires from China to the United States grew threefold from 2004-2008, and led to the closure of tire factories in the United States.
	22	The EIB will finance up to 50 percent of the desalination project in Ashdod	The investment bank of the European Union (EIB) announced its intention to participate in financing up to 50 percent of the cost of the investment in the desalination project in Ashdod—NIS 1.5 billion. The low interest rate that the European bank is expected to offer, which is lower than that of commercial banks, is likely to reduce the price of the desalinated water.
	23	Israel Aerospace Industries will supply advanced radar systems to South Korea at a price of 280 million dollars	The IAI won two contracts in South Korea to supply radar systems at an overall price of 280 million dollars.
	23	Reform of regulation of the banking sector and the financial markets in the European Union	The European Union has presented a program for reforming the regulation of the banking sector and the financial markets, with the aim of preventing another global economic crisis. The program includes the establishment of a supra-regulator of the banking sector and a pan-European supervisory mechanism, whose function will be to warm about systemic threats to financial stability in the 27 countries of the European Union. The European Systemic Risk Board (ESRB), which will be established as part of the reform in order to warn about future crises, will comprise representatives of the central banks, headed by the President of the European Central Bank (ECB). The council will be responsible for local supervision of banks and financial organizations on the continent. The council will not have direct authority, but will convene on a regular basis and report to treasury heads and finance ministers of the European Union.

	25	Heads of the G20 agree to limiting bankers' salaries and to regulating the financial sector	During the summit the heads of the G20 agreed to take steps to limit bankers' salaries, to tighten the regulation on risk-taking in the financial sector, and to change the supervision of the financial system. In an attempt to deal with global warming, the leaders agreed to gradually reduce subsidies to oil and coal companies, as well as to energy resources whose plants emit large amounts of carbon.
	28	The Bank of Israel interest rate for October 2009 will remain unchanged at 0.75 percent	
October 2009	1	Reform in the operation of the cash flow system in Israel	A large part of the handling of cash in the economy will be transferred from the Bank of Israel to the banks, for which purpose they will set up "cash centers". The "cash centers" will be required to use high quality cash-counting and sorting machines—which will considerably reduce the possibility of transferring counterfeit money or low quality currency from the banking system to the public.
	6	Israel and Russia are strengthening their relationship: they will invest jointly in a global food project	Israel and Russia are strengthening their strategic cooperation in the economic sphere, in addition to strengthening their political relationship. In a meeting between Russia's Deputy Prime Minister, Viktor Zubkov, and President Shimon Peres, it was agreed that the countries would promote the Food for Peace project in the Third World, as well as cooperation between business people from Israel and Russia in a variety of fields—including R&D and projects, mainly those dealing with agriculture and water.
	7	Australia precedes the G20 by raising the interest rate by 0.25 percent	For the first time in more than a year and a half, the Reserve Bank of Australia surprisingly raised the interest rate to 3.25 percent, following a reduction in the rate of interest to its lowest level in 49 years in the wake of the economic crisis. The bank also announced that it would soon raise the interest rate again.
	14	New tax benefits for investors in Israeli films	The Knesset Finance Committee approved regulations submitted by the Minister of Finance, Dr. Yuval Steinitz, granting tax benefits to investors in Israeli films. The regulations are based on recommendations of a committee appointed by the Director General of the Ministry of Finance, Yoram Ariav. The new regulations include, among other things, a quick, non-bureaucratic "green channel", in which anyone who chooses to invest in Israeli films and their production will enjoy a full tax allowance on the expenditure for tax purposes to the extent of the investment in the film. The benefit relates also to the commercial television channels and the cable and satellite franchisees: they too will enjoy a full tax allowance for their investments in Israeli films.
	26	The Bank of Israel interest rate for November 2009 will remain unchanged at 0.75 percent	
November 2009	2	The 2008 poverty report: one in every four Israelis is poor	The dimensions of poverty remain stable, with a slight decline in the number of poor elderly people.

	4	A debt settlement was achieved with Zim	Following Zim's announcement on September 10, 2009 that the company is liable to not meet its repayments on time, the bondholders reached a settlement with the company, which includes postponement of the repayment of the 2012-2015 bonds to at least 2016, and possibly even to 2020 if the ratio between the debt and the company's operational profit flow exceeds 3. If the debt is not discharged by 2016, the interest to be paid to bondholders will be increased by 1.2 percent a year. Bondholders will also obtain options to realize Zim's shares according to the value of the company of 770 million dollars, as well as an option to convert a third of the debt to shares in the company.
	8	Israeli food will be sold in Europe without tariffs	From January 1, 2010, food products exported to Europe will be exempt from tariffs and other levies. This implies a lowering of prices of Israeli products in European markets and their greater competitiveness. The exemption from tariffs and other levies was achieved as part of a new agricultural trade agreement signed between Israel and the European Union.
	9	Fitch ratified Israel's rating—"A" stable	
	13	The Drought Levy is put on hold. The price of water will be increased in two steps	According to a draft compromise worked out by the Prime Minister's Office and the Ministries of Finance and National Infrastructures, the price of water in Israel will increase on January 1, 2010 by 25% and again on June 1, 2010 by 15%. The price increase is meant to replace the one-time increase of 50% that was planned for January 1 as part of the water tariffs' reform. The Drought Levy that was introduced at the beginning of August 2009 will be put on hold between January 1 and April 15, 2010.
	16	Ministerial committee approves the draft bill for setting up an economic court	The Ministerial Committee for Legislative Affairs approved the draft bill for an economic court, paving the way for establishing a special court for economic matters, which was initiated by the chairman of the Israel Securities Authority, Prof. Zohar Goshen. According to the proposal, an economic department will be set up in the Tel Aviv District Court. The department will include a panel of professional judges, and will conduct most of the judicial procedures concerning securities and companies. The proposal aims to streamline criminal, administrative and private enforcement in these areas.
	19	The establishment of the private prison is annulled	In a rare step, a panel of nine High Court justices decided to annul Amendment 28 to the Prisons Ordinance in terms of which a prison was would be managed and operated in Israel by a private corporation.
	22	More than one thousand subsidized apartments will be rented to young people in the Negev and the Galilee	The Ministry for the Development of the Negev and the Galilee is embarking on a campaign in conjunction with the Amidar company: more than one thousand apartments in the Negev and the Galilee will be offered for rent at half the price to young families and students on the basis of long-term, 3-5 year contracts. The campaign will be conducted on a "first come first served" basis.
	22	An economic cooperation agreement was signed between Israel and Poland	

	24	The Bank of Israel interest rate for December 2009 was raised by 0.25 percent and stands at 1 percent	
	24	The Industrial Development Bank is purchased	Businessman Zvika Barenboim purchased the Industrial Development Bank from the state through B.G.I. Investments for NIS 572 million.
	25	Changes in vehicle taxation	The Knesset Finance Committee approved the reduction of purchase tax on new cars (released from customs after November 25, 2009) from 90 percent to 83 percent. The tax credit on electronic stability programs has been abolished. At the same time, the value of the use of company cars has been changed: for new vehicles on the road from 1 January 2010 priced up to NIS 130,000 —2.04 percent of the price of the car in the first year; for more expensive vehicles—2.48 percent of the price of the car in the first year.
	27	The investments company of Dubai announced that it would have difficulty in repaying its debts on time	The Emirates government company, Dubai World, requested a six-month postponement of the repayment of 60 billion dollars of its debts. The request sent shock waves through the capital markets, and led to sharp falls on European stock exchanges. The fear is greatest in countries whose banks are more exposed to companies from the Emirates.
	30	The Finance Committee approved the order for encouraging capital investments	The Finance Committee approved the extension of validity of the order for encouraging capital investments until the end of 2010. The order enables the Investment Center of the Ministry of Industry, Trade and Labor to offer benefits and grants to enterprises in various parts of the country. The validity of the current map of national priority regions was extended to the end of 2010.
December 2009	2	The European Investment Bank will provide Israel with credit of 141 million euros for financing water-conservation projects	The accountant-general of the Ministry of Finance, Shuki Oren, completed the raising of 141.1 million euros from the European Investment Bank (EIB). The loan was given to the Israeli government for financing water projects—sewage infrastructures and waste-water enhancement. These projects are intended to produce waste water for agricultural irrigation, thereby conserving fresh water, which is more expensive. The loan was granted to the Israeli government on preferential terms, and will save the government a significant amount compared with ordinary overseas borrowing.
	2	The Finance Committee approves benefits for entrepreneurs who will built rental housing	The Finance Committee approved further far-reaching benefits for entrepreneurs who will build rental housing, as part of a bill for encouraging capital investments (up to 2013): reducing the company-tax rate for entrepreneurs from 18 percent to 11 percent; and requiring the entrepreneur to build 50 percent of the apartments in the project for rental, as opposed to 70 percent until now. The current concessions were extended until 2013.
	6	Fall in unemployment in the United States	November data of the American Department of Labor shows a decrease of 0.2 percent in unemployment, to 10.0 percent. Also, the number of people who lost their jobs was the lowest since the start of the recession.

	7	The Israel Electric Corporation will build four power stations for the Palestinian Authority at a cost of NIS 200 million	The project is intended to ensure mutual backup between the electricity networks of seven Arab states, but in practice the Palestinian Authority's total dependence on the Israel Electric Corporation remains unchanged. The power stations will probably be financed by the European Union.
	7	The government approved the appointment of attorney Yehuda Weinstein as attorney general	
	8	Starting in February, the provident funds will no longer be permitted to publish monthly yields	Starting in February 2010, institutional bodies will not be permitted to offer and market provident funds, pension funds and senior employees insurance on the basis of short-term yields—less than a year. This implies cessation of publication of the monthly yields that appear regularly for all long-term-savings products.
	9	Japan: A new 81-billion-dollar incentives package	The Japanese government has announced an additional $81 billion economic incentives package, the aim of which is to prevent a return to recession, against the background of the continuing deflation and the strengthening of the Yen, which adversely affects exports.
	10	Greece's credit rating is lowered	Fitch has lowered the rating of Greek government bonds from A-minus to BBB-plus with a negative outlook, against the background of the ballooning public debt and the high government deficit. This is the lowest credit rating for government bonds in the eurozone.
	13	A new map of national priority regions for encouraging investments in education and housing	A new map for encouraging investments in education and housing has been drawn up. The map includes as national priority regions many Arab communities as well as Jewish settlements in Judea and Samaria. The map will not affect the definition of national priority regions for industry, which serves as the basis for distributing grants from the Investment Center.
	15	The maximum payment period of unemployment benefits has been extended	The Knesset Labor and Welfare Committee has approved the extension of the maximum period of entitlement to unemployment benefits for unemployed people up to age 35 by a further 15-30 days. The aim of the amendment is to give a safety net to young unemployed people in order to enable them to continue their search for work that matches their capabilities. The following are the changes in the maximum period: • Up to age 25: From 67 to 97 days; • Ages 25-28: From 50 to 65 days; • Ages 28-35: From 100 to 125 days. The decision will be valid from January 1, 2010 to December 31, 2010.
	15	The government approves the allocation of NIS 65 million for dental treatment	The government has approved the transfer of NIS 65 million from the "medications basket" in order to finance free preservative dental treatment for children up to age 18.

	15	Abu Dhabi has extricated Dubai from financial crisis by injecting 10 billion dollars	The Abu Dhabi government has come to the aid of its neighbor Dubai by placing 10 billion dollars at the disposal of the government company Dubai World for the payment of debts, 4.1 billion of which is designated for the Nakheel construction company for payment of its bonds. The Dubai government has also announced a new law on bankruptcies, which is designed to regulate the bankruptcy process and to protect creditors in the country.
	16	Israel and the United States agree to broaden their economic cooperation	As part of the JEDG Forum, the director general of the Israeli Ministry of Finance, Haim Shani, and a representative of the ministry have concluded an agreement with the head of the American delegation, Andy Baukol, to widen cooperation in the area of hi-tech, including integrating IT technologies in educational and health systems, and examining the extension of the joint investment funds into research projects.
	19	The Copenhagen climate change conference	The countries participating in the conference signed a draft agreement for dealing with global warming, an agreement that deviated considerably from the original aims of the conference. According to the draft agreement, all countries will submit plans in writing by next month for reducing carbon dioxide, and will also undertake to transfer about 100 billion dollars to developing countries by the year 2020. The President of the United States, Barack Obama, reached agreement on the reduction of greenhouse gasses with the leaders of India, China, Brazil and South Africa. All the agreements, however, are not legally binding. The President of Israel, Shimon Peres, undertook at the conference that by 2020 Israel would reduce its expected growth of greenhouse gas emissions by 20 percent.
	21	A settlement was concluded regarding Africa-Israel	As part of the settlement, holders of short-term Africa-Israel bonds, and particularly holders of Series 9 bonds, will receive the major proportion of the cash part of the settlement—NIS 450 million out of the NIS 550 million that Africa-Israel will distribute to bondholders. The holders of short-term bonds that are designated for redemption in 2009 and 2010, will receive as part of the updated draft settlement NIS 370 million more than was allocated to them in the original draft. This will be at the expense of holders of the long-term series, who will divide among themselves only NIS 100 million in cash. As compensation for the long-term bondholders, Africa-Israel will provide them with added bonds to the value of NIS 76 million, to be shared among them. The owner, Lev Leviev, will inject NIS 750 from his own pocket into the company.

	24	The Senate approves Obama's health insurance reform	The US Senate approved President Barack Obama's plan for comprehensive reform of the health system. The changes in the new law are the most significant in the American health system since the health law for the elderly was enacted in 1965. Among other things, the reform grants, for the first time, medical insurance to 31 million low-income-earning Americans, and determines a mechanism to prevent health expenditures from rising. The Obama administration will allocate 871 billion dollars over the next ten years to implement the reform. Details of the reform will be consolidated in the near future in the House and the Senate.
	28	The Bank of Israel interest rate for January 2010 was raised by 0.25 percent and stands at 1.25 percent	
	30	The state will subsidize the railway system according to its performance	The new subsidy agreement for Israel Railways that was signed with the government, stipulates that the railways will receive compensation on the basis of passengers' satisfaction, and the increase in passenger and cargo traffic. Until now the railways' subsidy was determined according to its operating deficit. In terms of the present agreement, the railways will receive a fixed subsidy, significantly smaller than that needed by the company, and the additional subsidies will be given only subject to increasing the number of regular passengers and the volume of cargo, as well as improving punctuality and the level of service. Failure to comply with the objectives will result in the imposition of fines. A further change mandated by the new agreement is the assurance that all the income derived by the railways from transporting passengers, transporting cargo, and other commercial activities will be used to finance its day-to-day activities.
	30	From January 1, 2010, VAT will be reduced by half a percentage point to 16 percent	