The Israeli Economy: Current Trends, Strength and Challenges

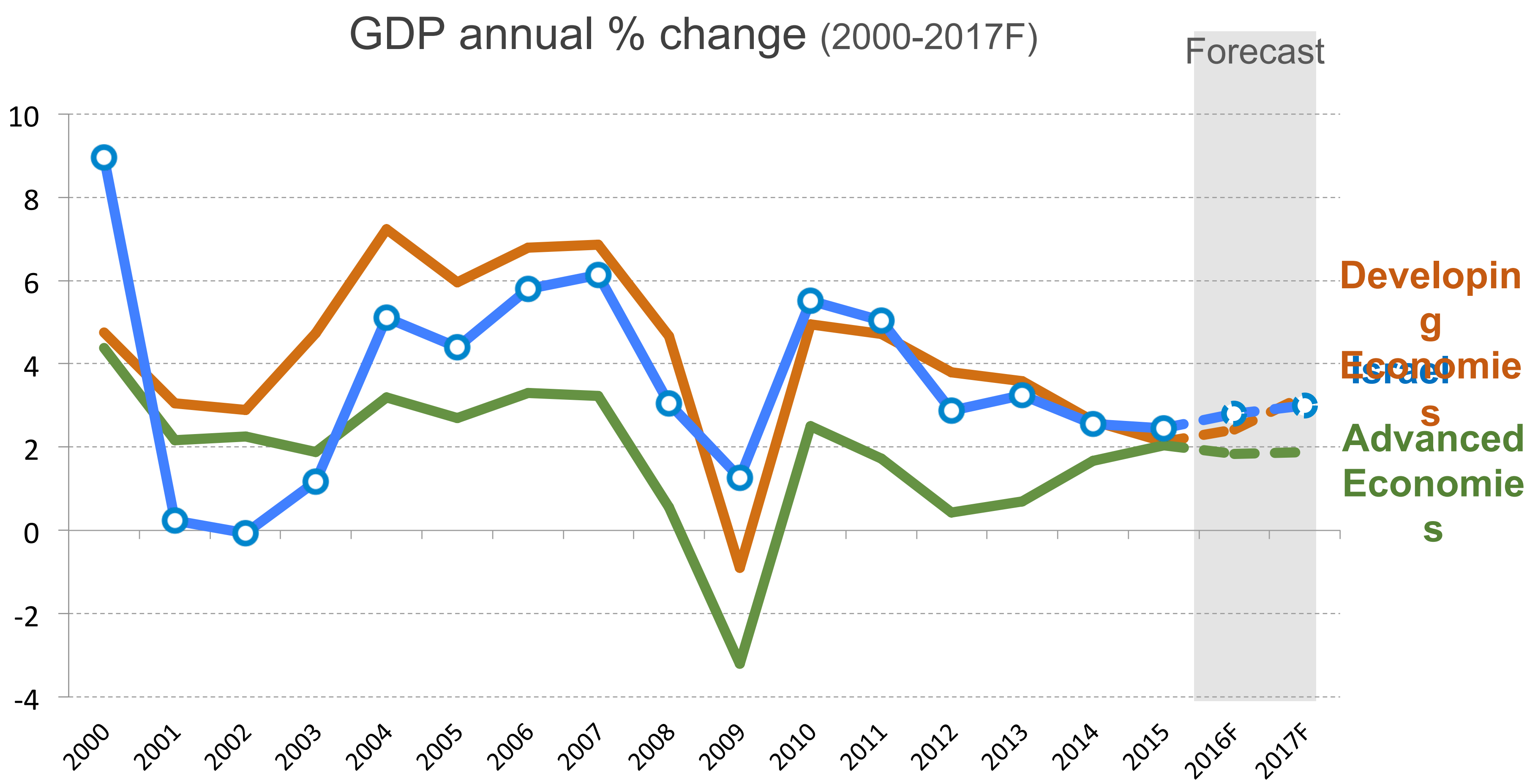
IRMC Conference

Dr. Karnit Flug

Governor of the Bank of Israel

13.06.2016

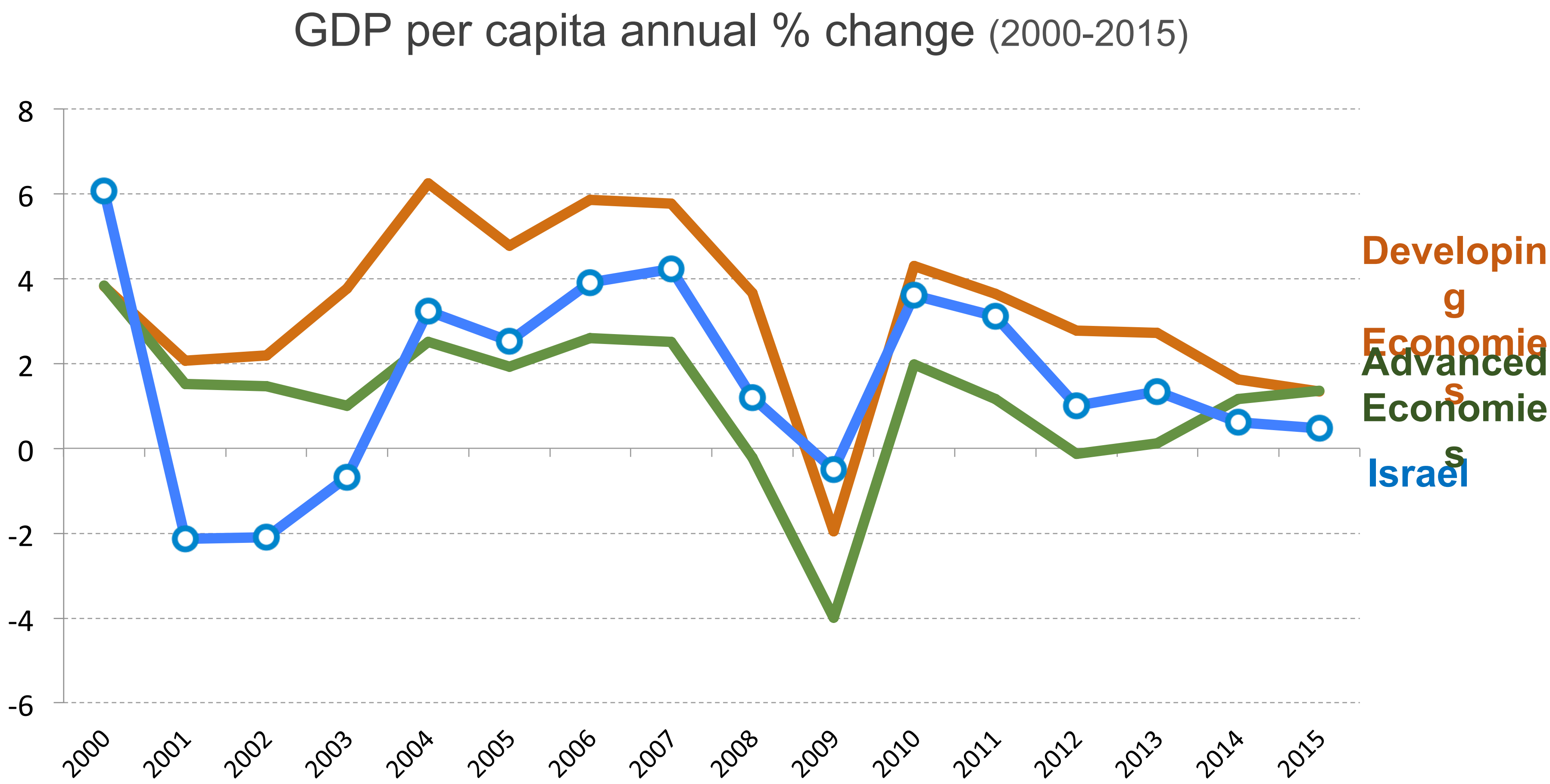
GDP Growth Rates



*Simple average for 21 rich OECD countries and emerging markets according to IMF definition

Source: IMF

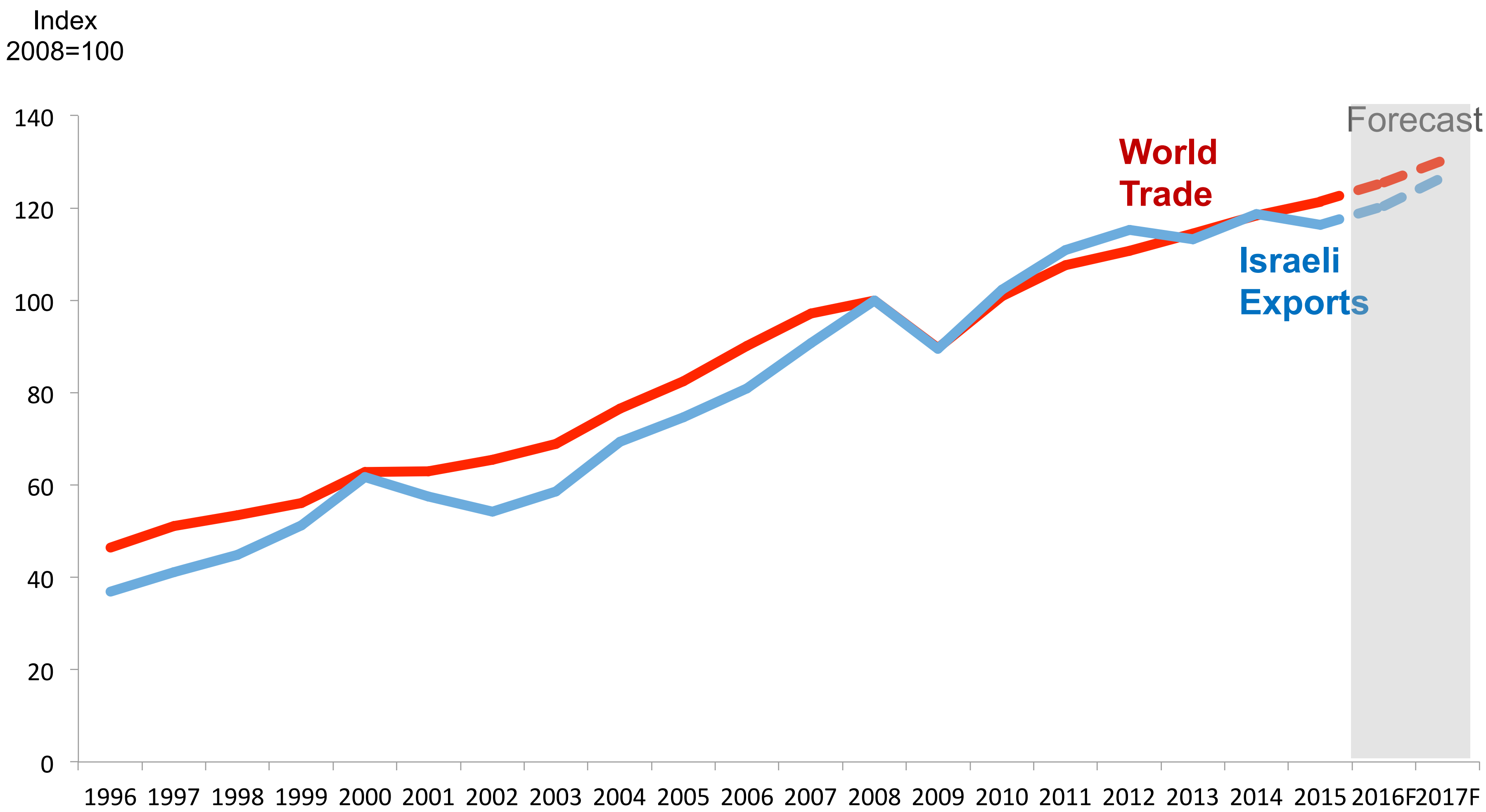
GDP per capita Growth Rates



*Simple average for 21 rich OECD countries and emerging markets according to IMF definition

Source : IMF

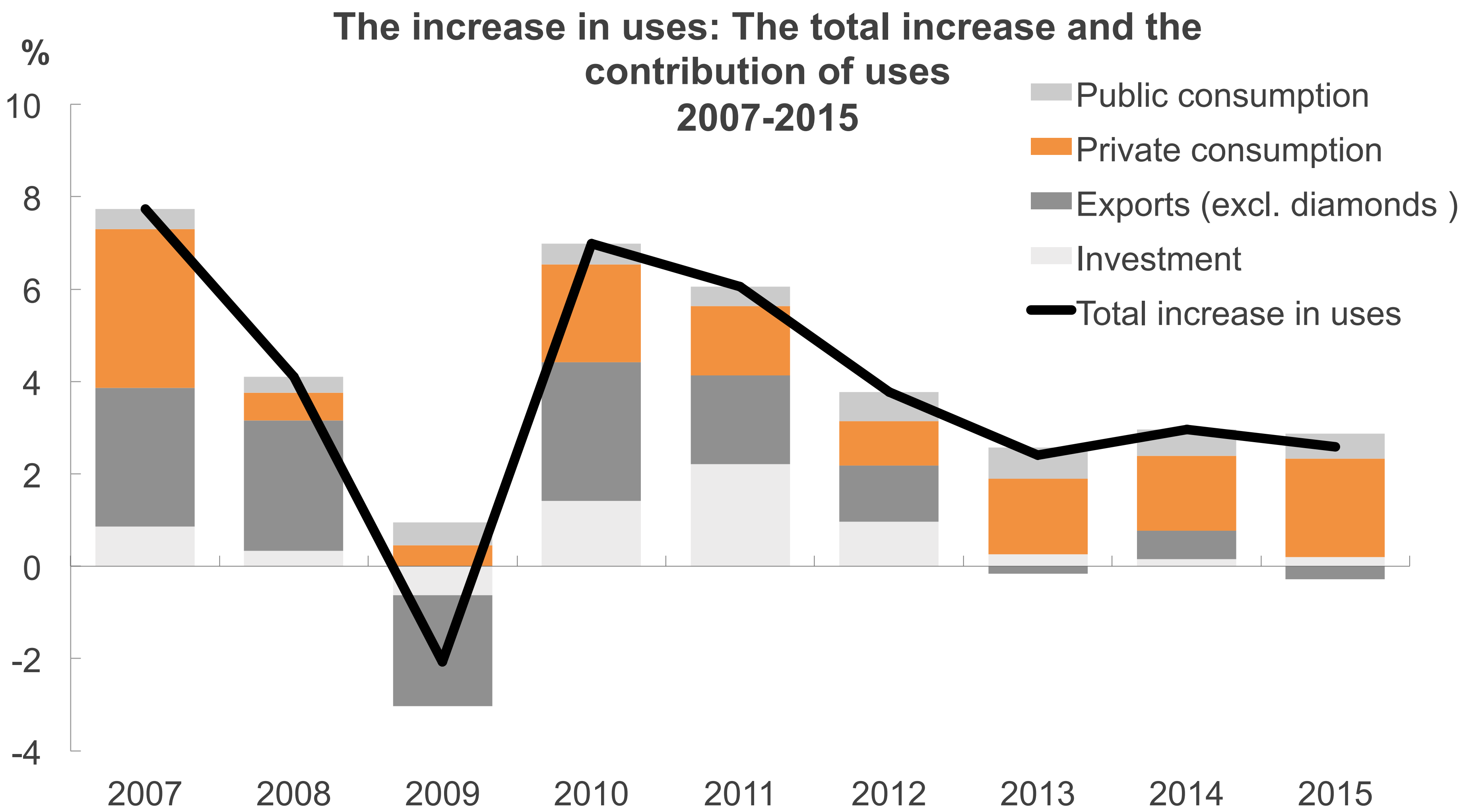
Israel's Goods and Services Exports and World Trade, 1996-2017F



*Excl. diamonds and start-ups

Source : BoI and IMF

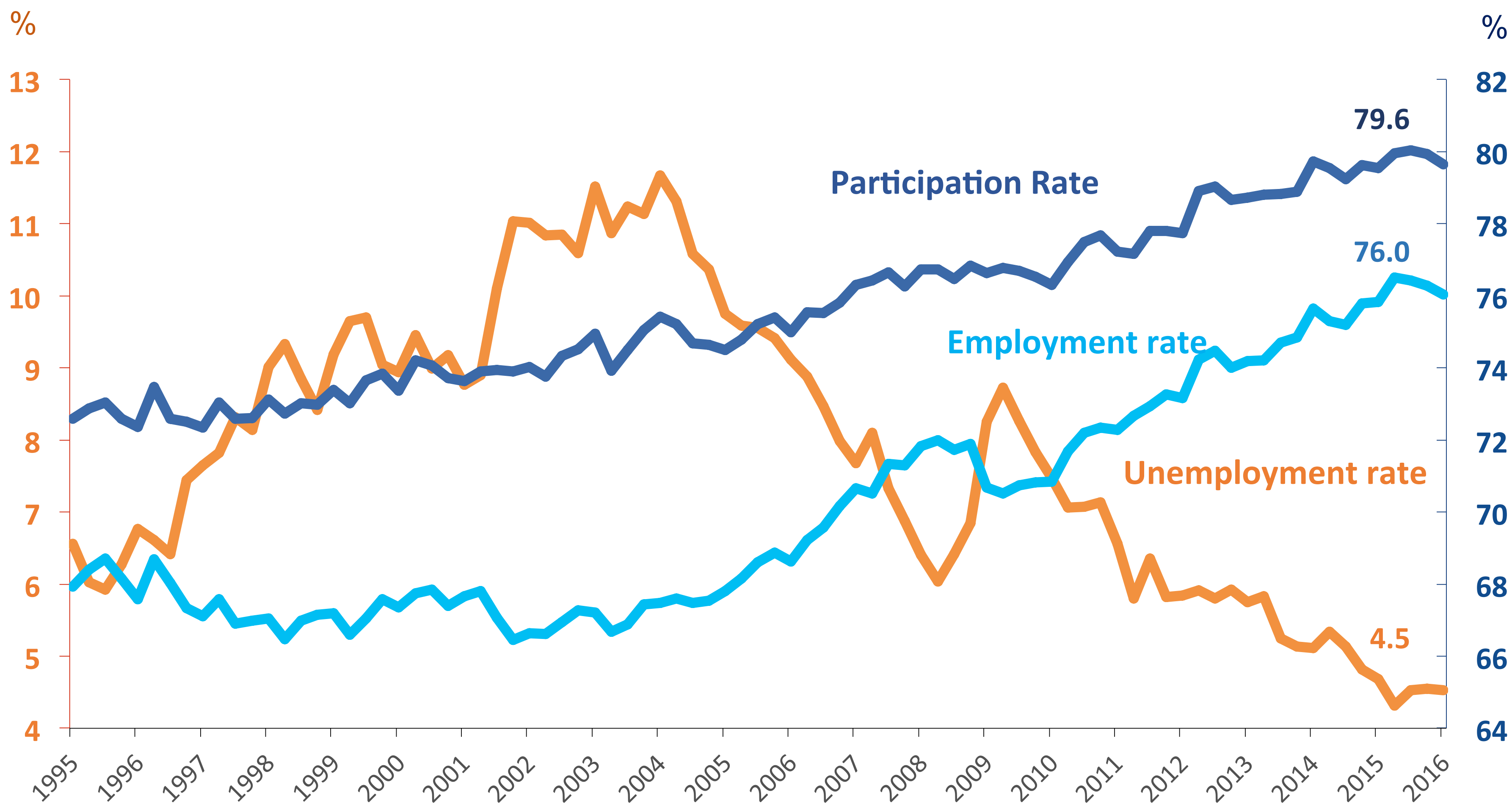
Structural Change in the Composition of Growth – Private Consumption is Leading While Exports are in Stagnation



Source: BoI Report 2015, CBS

Labor Market

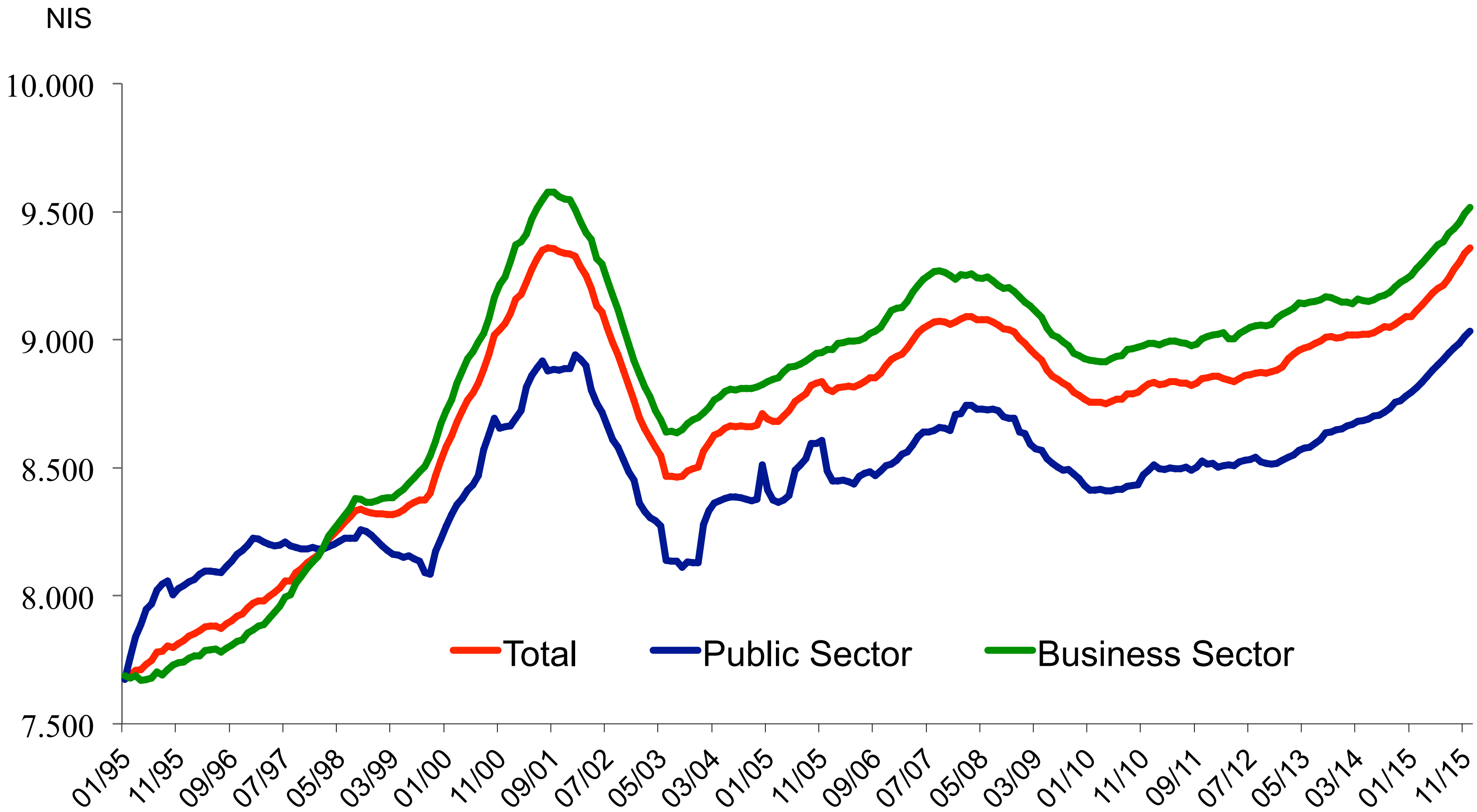
Quarterly, 1995-2016, 25-64



Source : Central Bureau of Statistics Labor Force Survey

Real Wage per Employee Post*

1995-2015



*Seasonally adjusted, 12 months moving average, 2015 prices

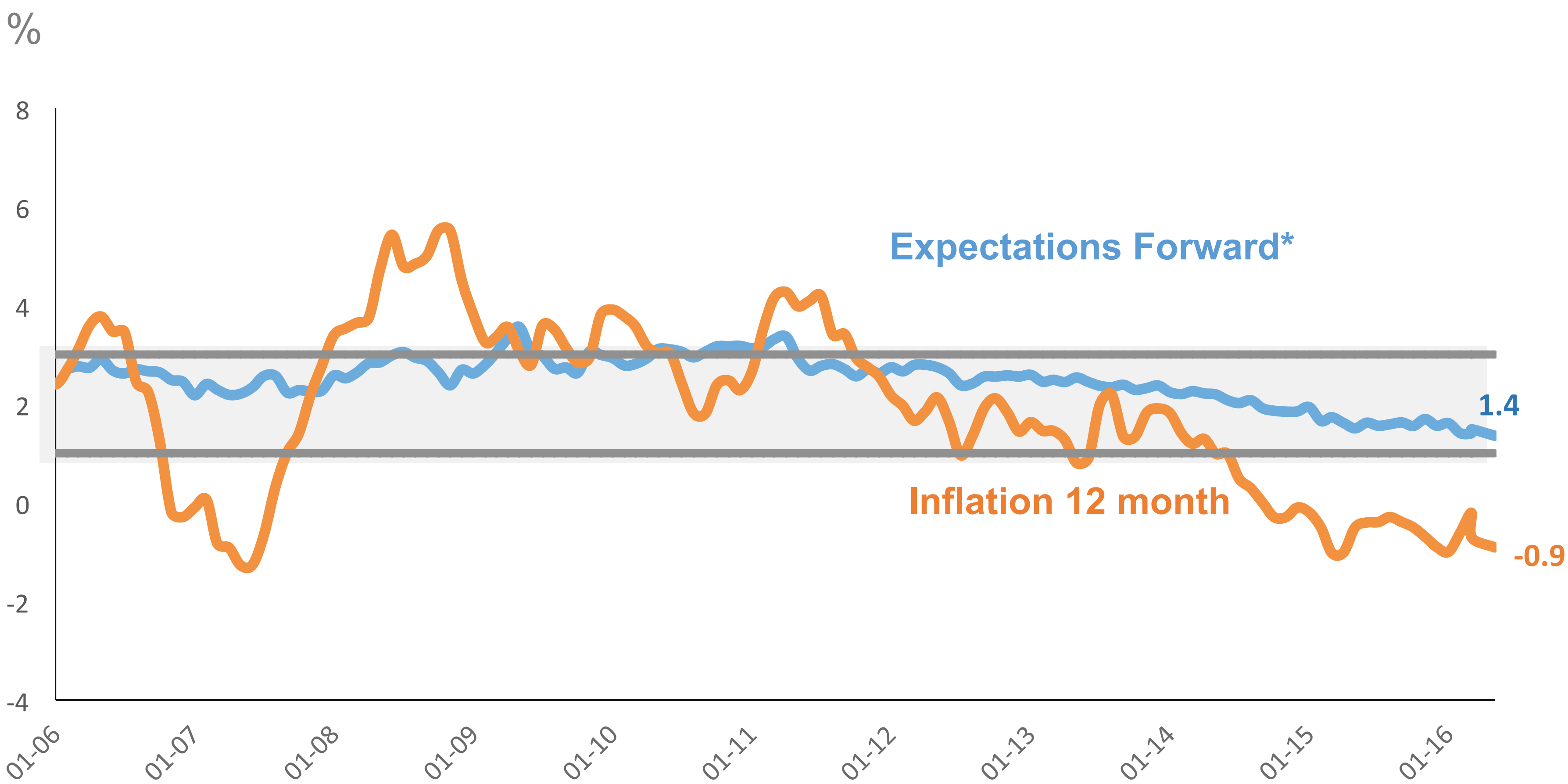
Source : Central Bureau of Statistics Data

Bank of Israel Policy

BOI's Policy Objectives

- Maintain price stability, as the central goal.
- Support economic policy, primarily growth, employment and reducing social gaps.
- Support the stability and orderly activity of the financial system.

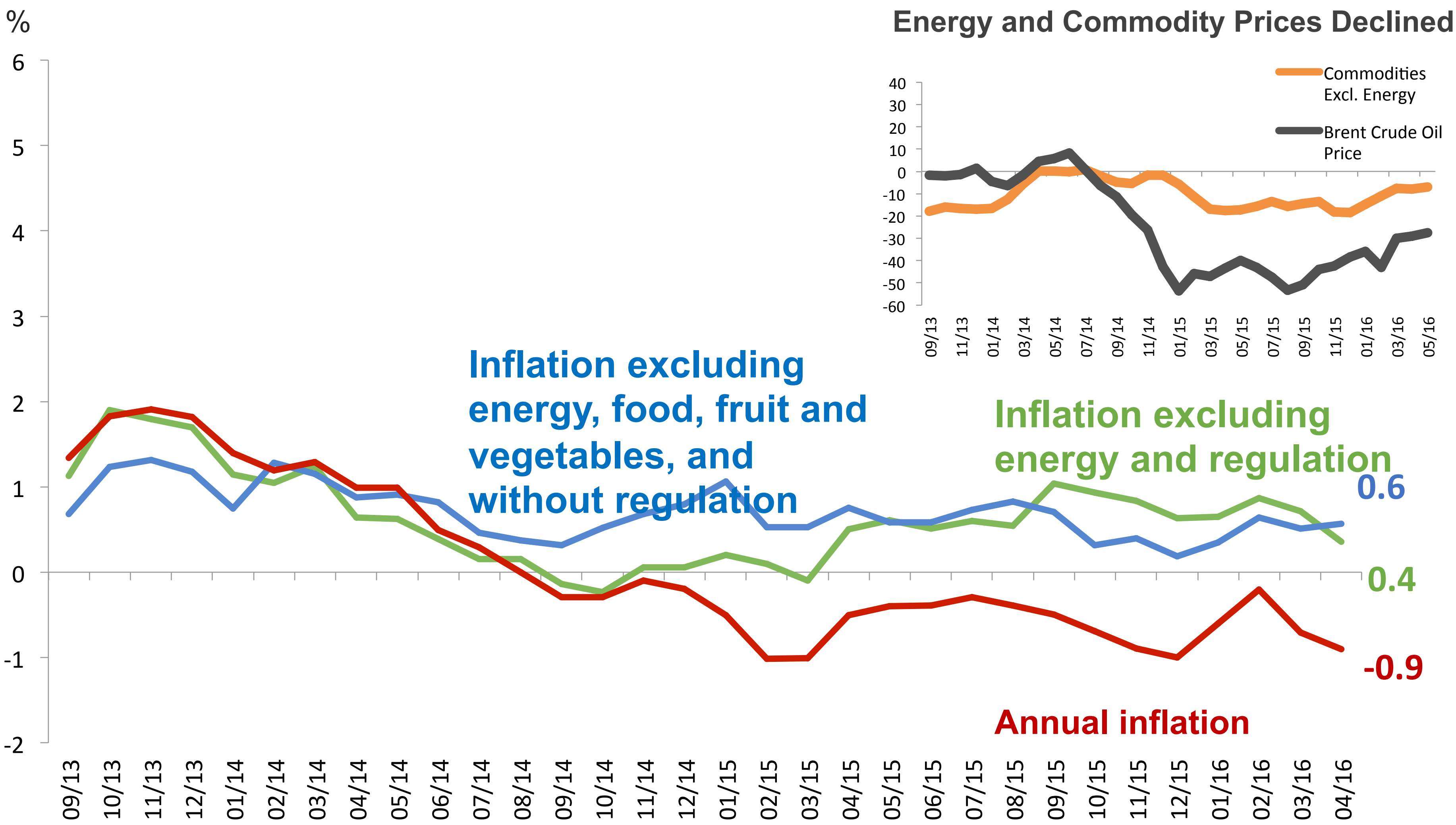
Actual Inflation and Inflation Expectations
2006-2016



* Forward inflation expectations 3-5 years

Source: BoI

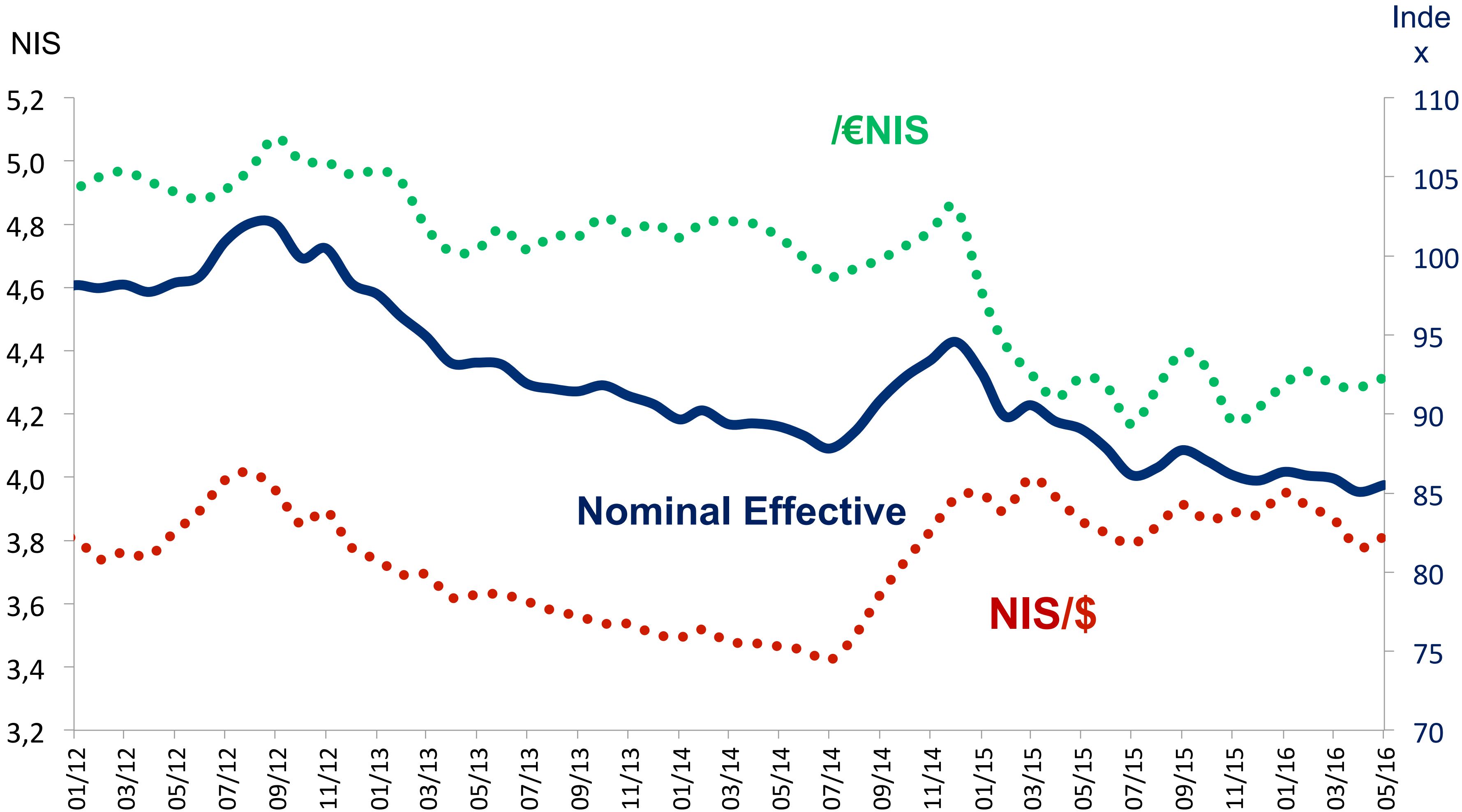
Factors of a One-Off Nature and Energy Prices Contribute to the Low Inflation



*12-month % change

Source : CBS (Israel) & BoI

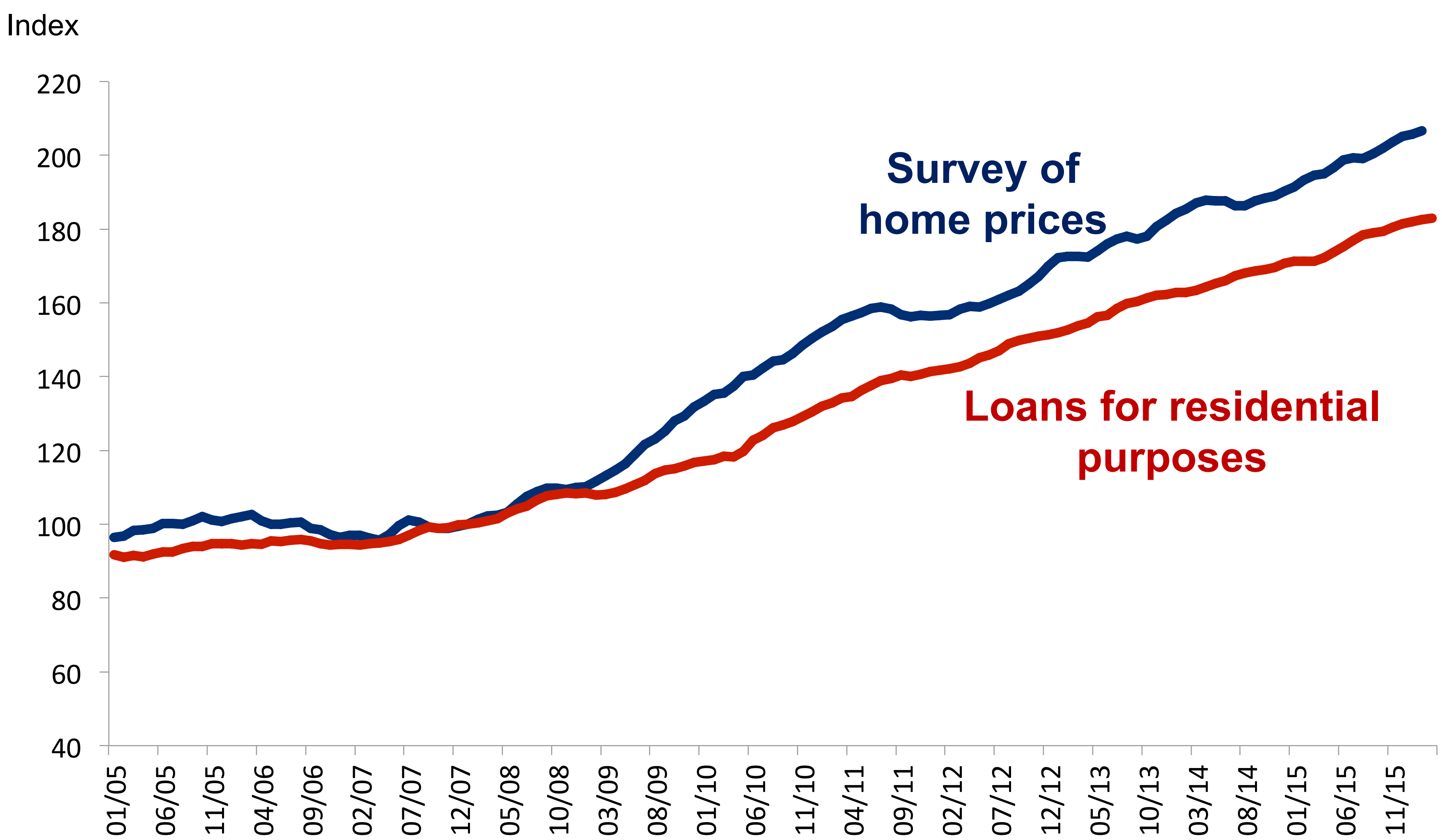
Exchange Rates
2012-2016



Source : BoI

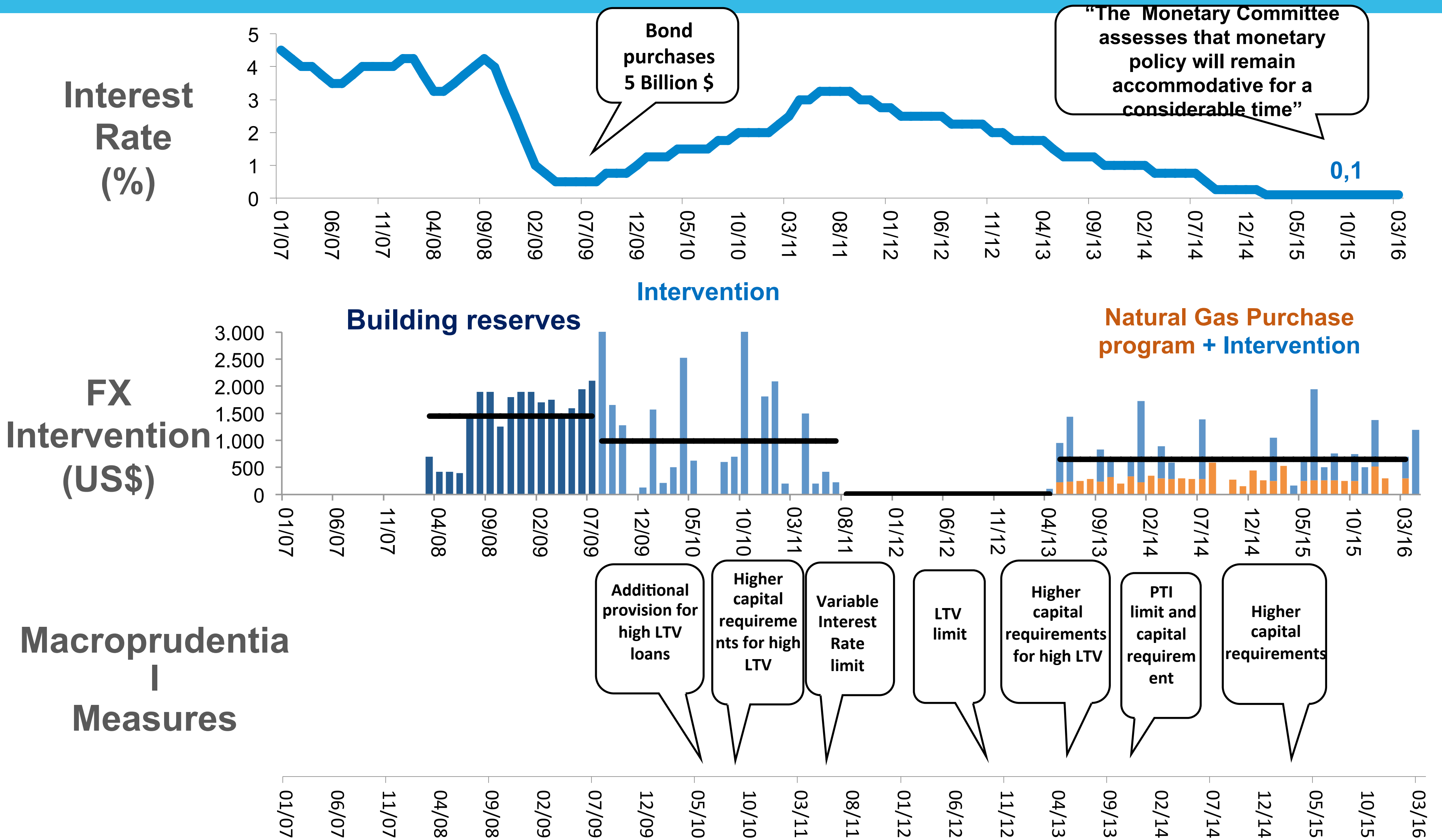
Survey of Home Price and Loans for Residential Purpose

2005-2016, Monthly



Source : Bank of Israel, Banking Supervision Department

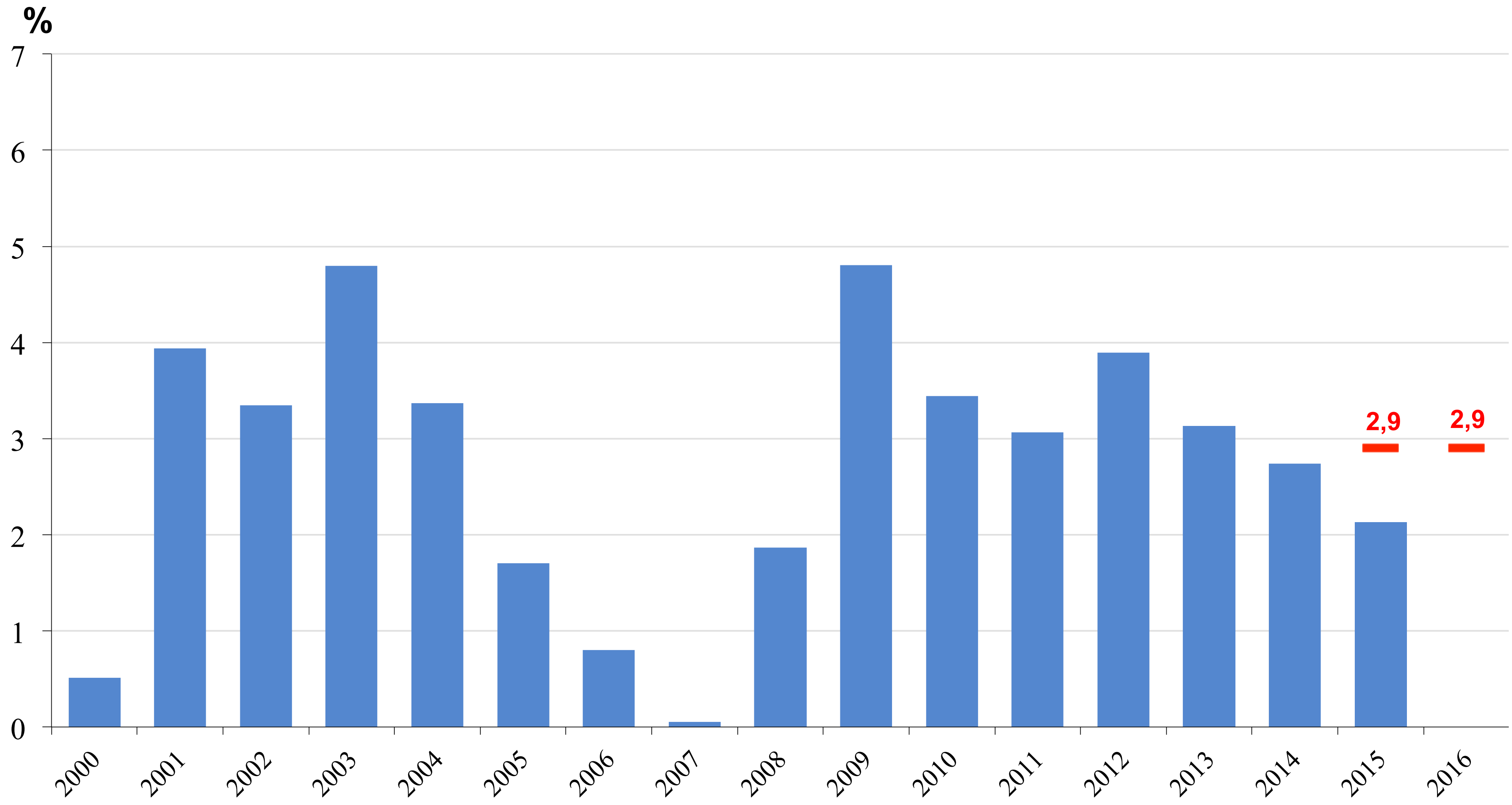
Bank of Israel Policy Tools 2007-2016



Source : BoI

Fiscal Policy

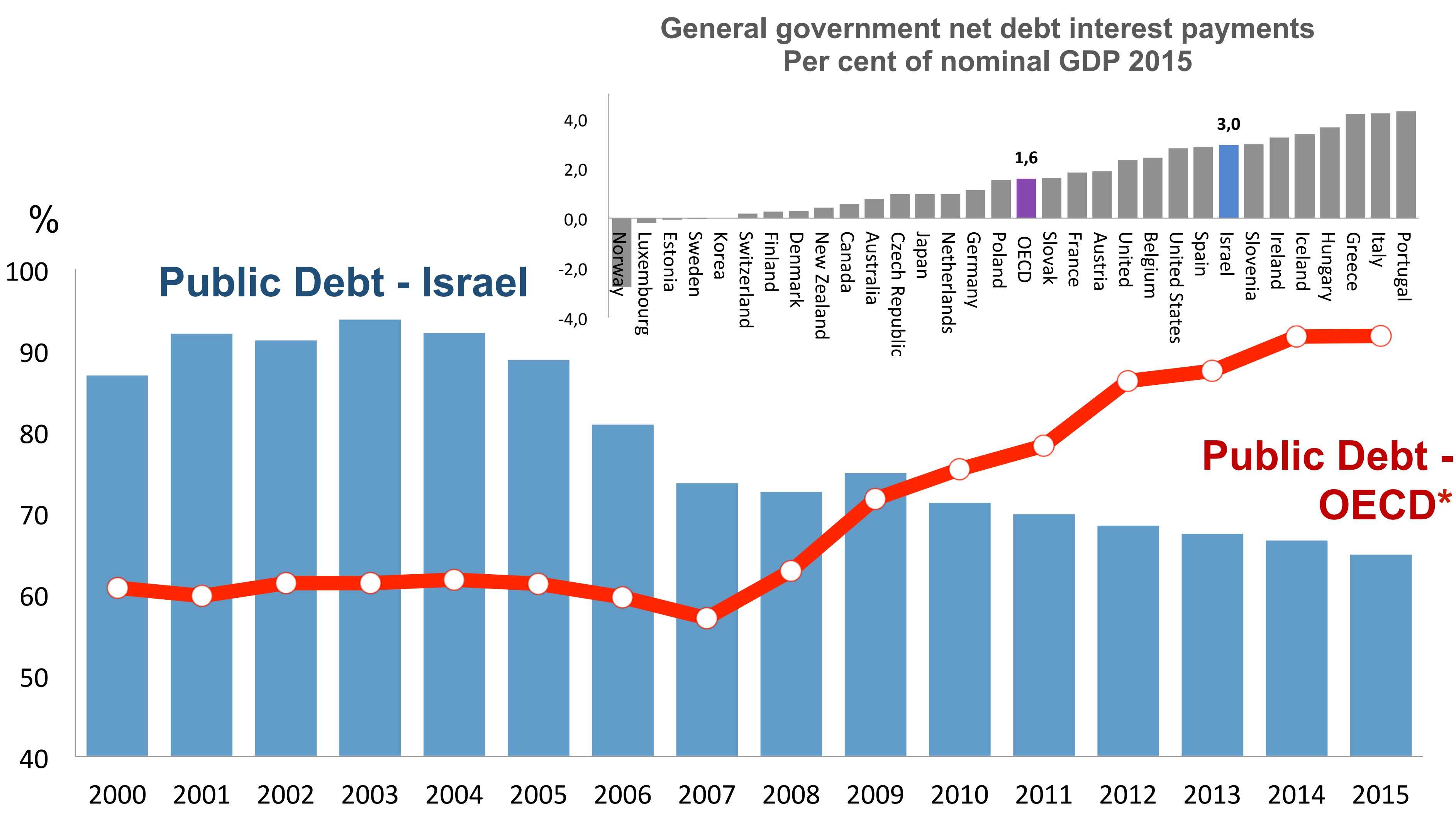
Budget Deficit* and Deficit Target
(Percent of GDP, 2000-2016)



*Percent of GDP; excluding credit extended. The data refers to the deficit excluding the Bank of Israel's profits.

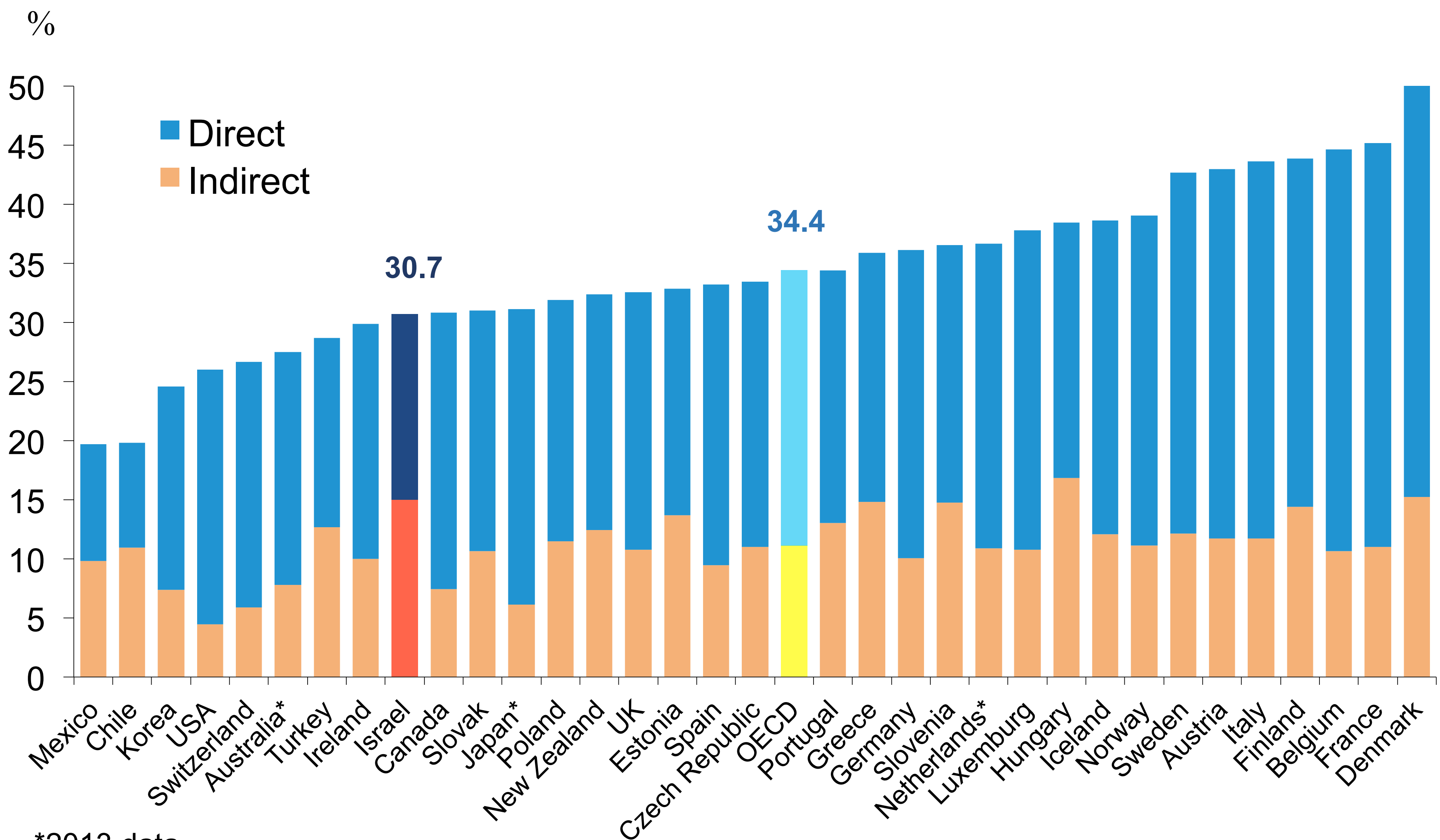
Source : BoI

Public Debt in Israel is Decreasing but Net Interest Payments are Still High in International Comparison



Source : The BoI and the OECD.

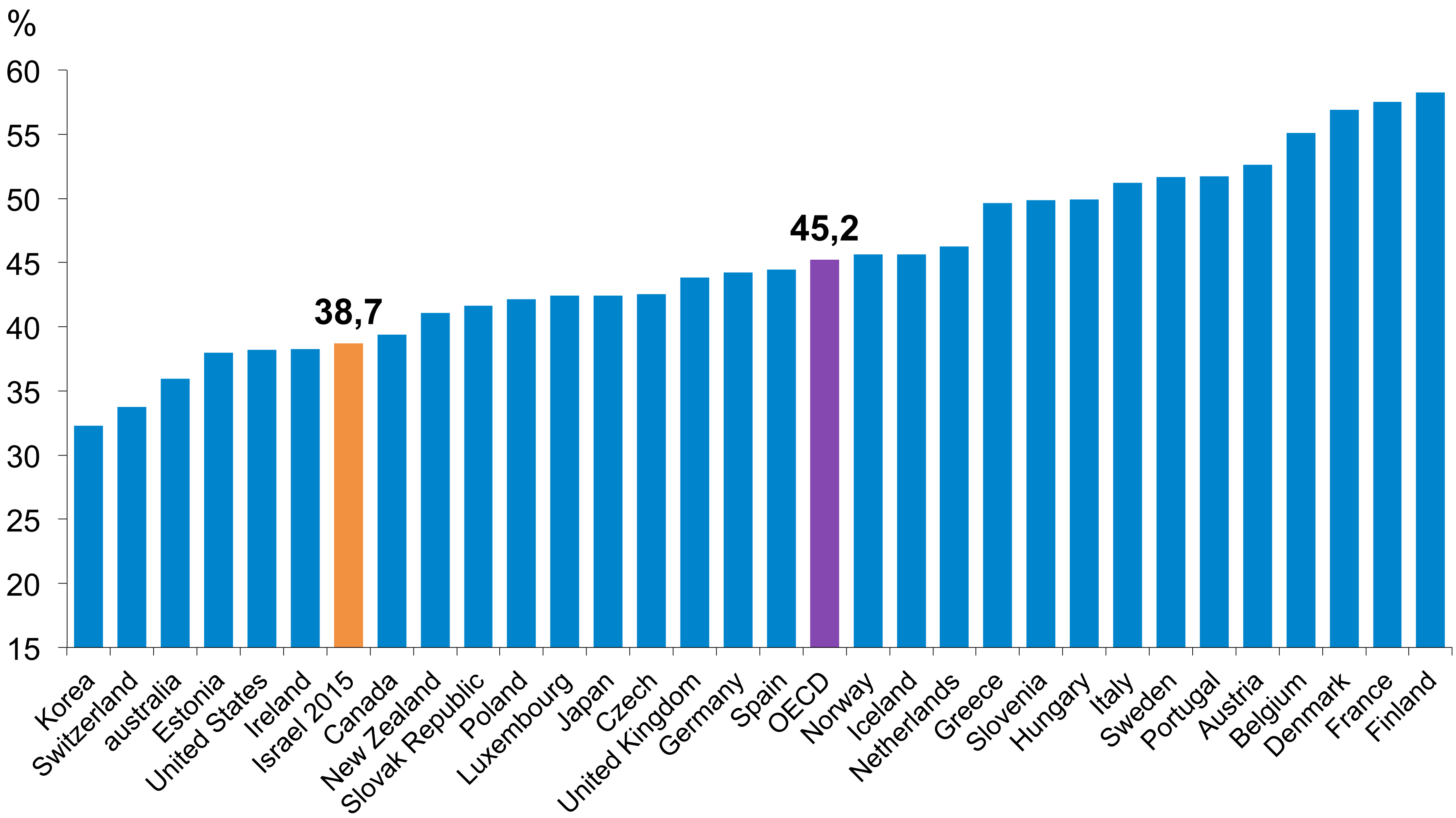
Tax Burden
2014, Percent of GDP



*2013 data

Source : OECD Revenue Statistics 2015

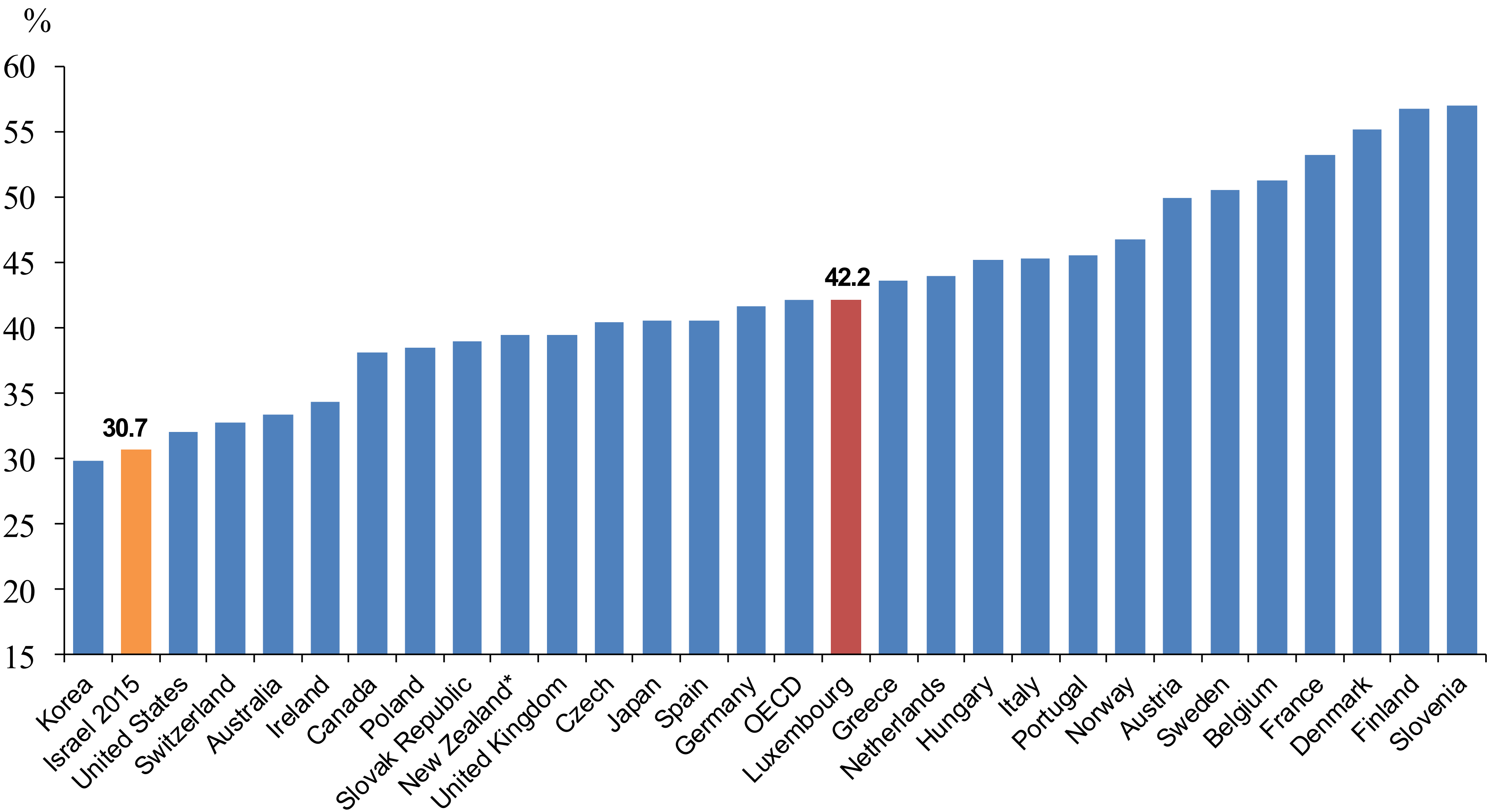
Public Expenditure
Percent of GDP, 2014



Source : OECD

Civilian Public Expenditure Excluding Interest

Percent of GDP, 2014

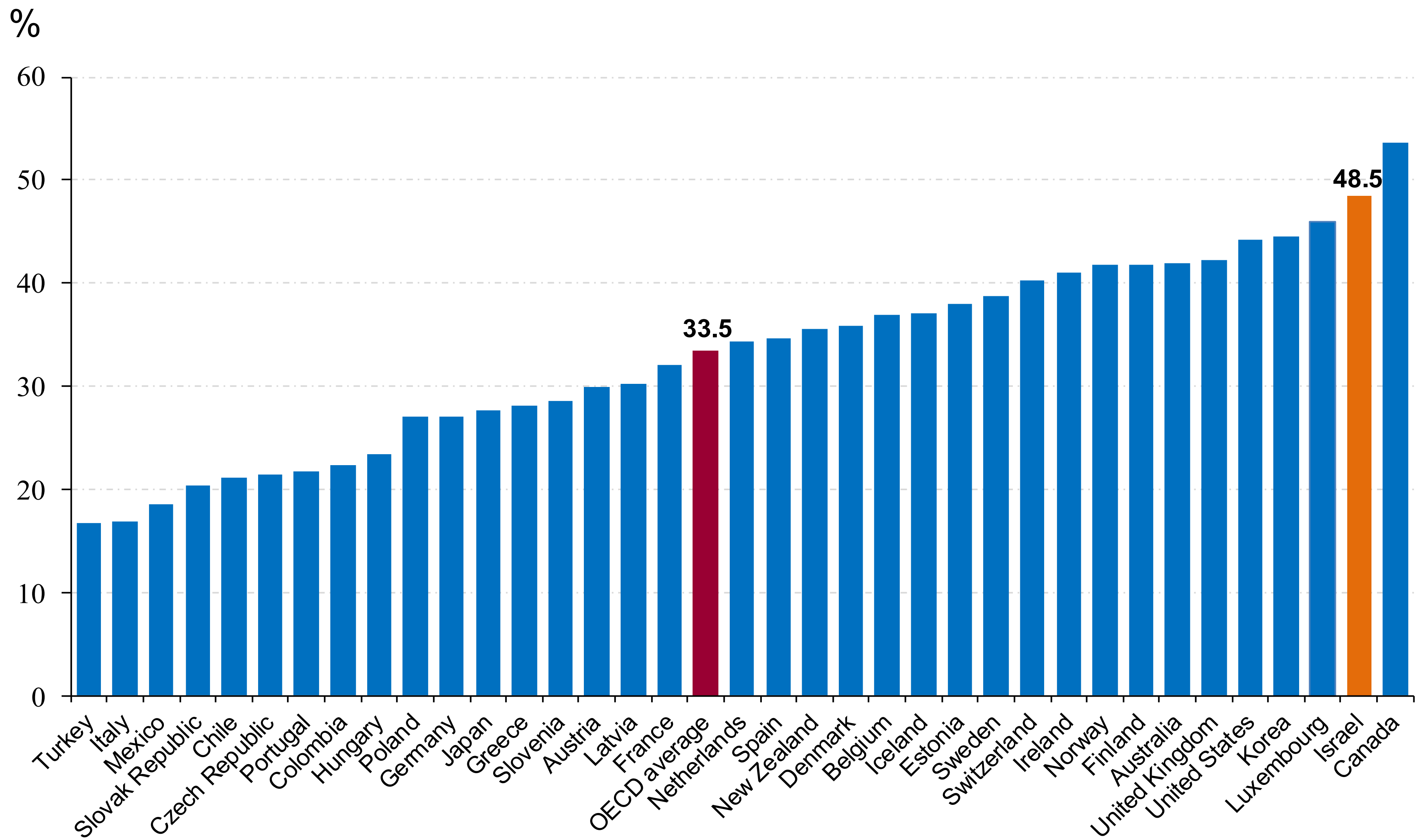


- The data is calculated by decreasing the net debt interest payments and defense expenditure from the general government total outlays

Source :OECD and the BoI

Behind the Engine of Growth - Strengths

Share of the Population Aged 25-64 with Tertiary-Level Education , 2014



Source : OECD Education at a Glance 2015

Israel is Leading in International Innovation Rankings

Index	Bloomberg	WORLD ECONOMIC FORUM
Ranking	5	3

Factors in Israel that encourage innovation

- ✓ Quality universities that provide the economy with human capital, scientific aptitude, and technological abilities
- ✓ Collaboration between the universities and industry
- ✓ Government support for commercial R&D
- ✓ Developed venture capital industry

Source: World Economic Forum 2015& Bloomberg

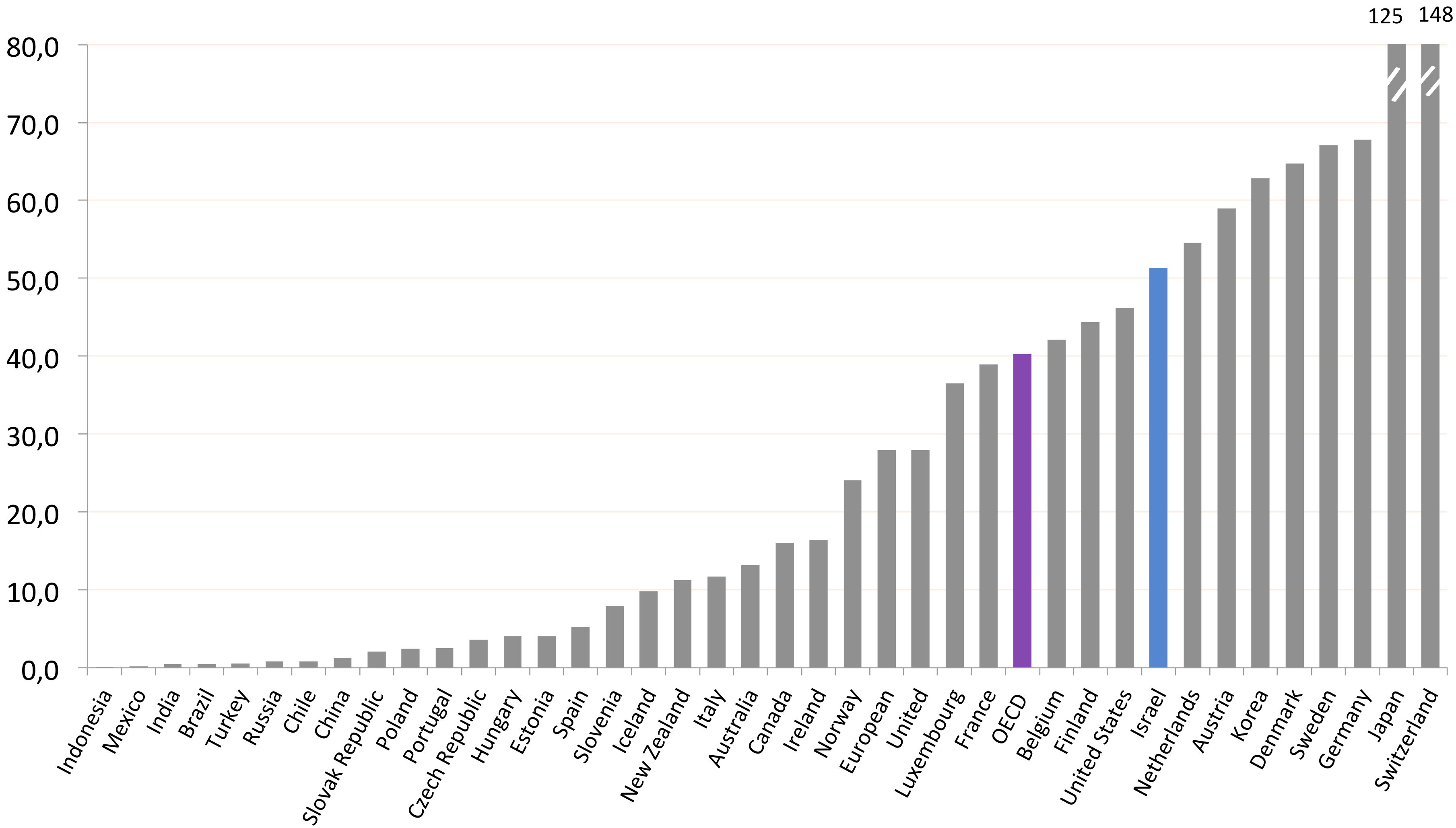
Israel's Relative Advantages - Technology

- **73 Israeli companies are listed on Nasdaq**
- Over **300 international companies** established Israeli R&D centers
- More than **4,000 startups** : The world's greatest concentration of high tech companies outside Silicon Valley
- Leading in cyber security: **430 cyber security companies and startups**. In 2015, Israel's share of private investment in the field was nearly 20% (second only to the US).

Source: IMF WEO April 2014, Israel innovation authority, Nasdaq, The National Cyber Bureau

Triadic patent families

Number per million inhabitants, 2013



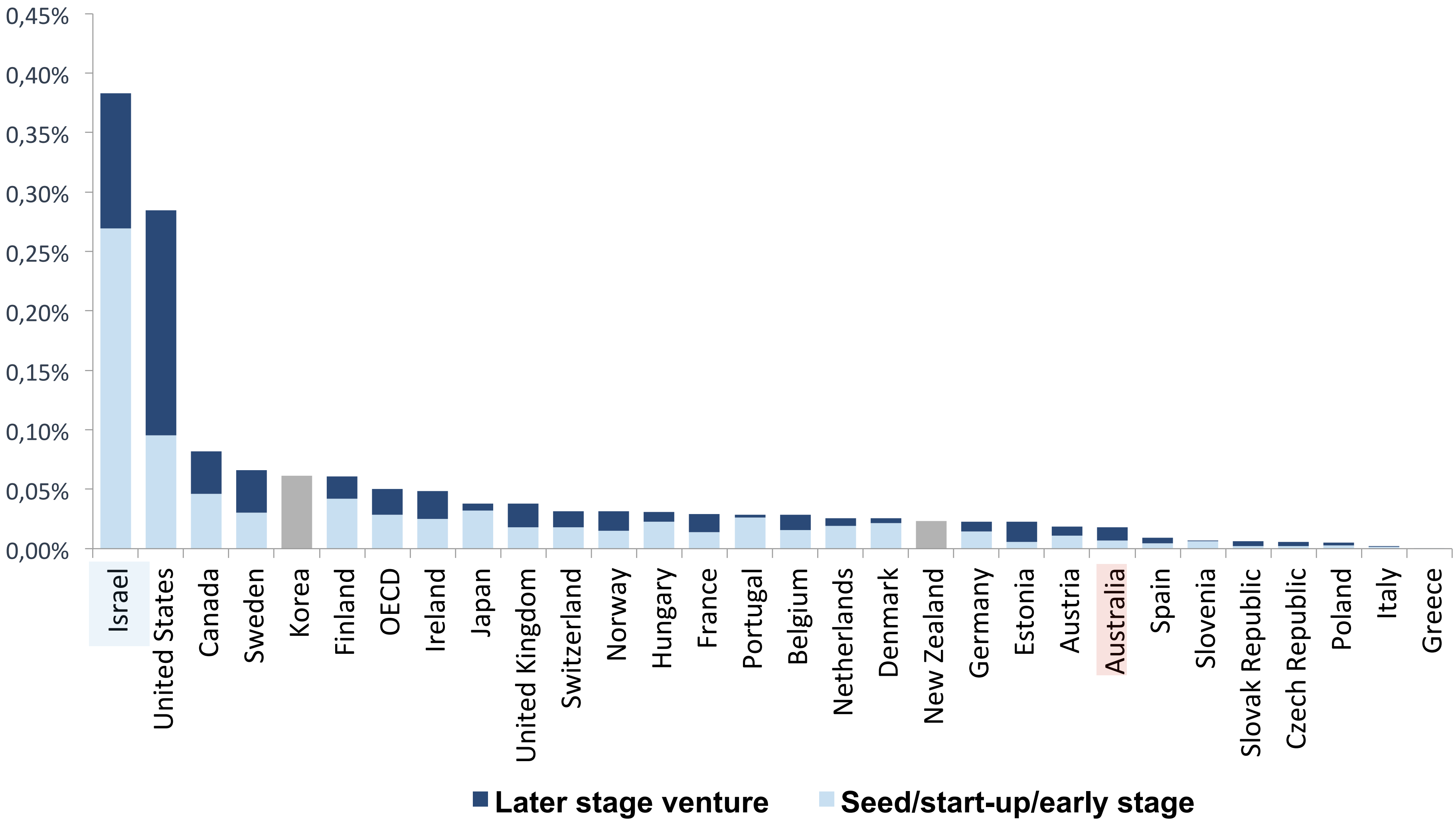
Source: OECD Factbook 2015-2016

Israel's Relative Advantages – Water Innovation

- **World leader in desalination**; With a network of five coastal desalination plants, which together produce 75% of all water supply to households.
- Leading in **Waste-Water Recycling** with a rate of 80%.
- Israel developed and patented the **"Drip Irrigation",** that has not only produced huge reduction in agricultural water use, but has also vastly increased yields, and it is used worldwide.

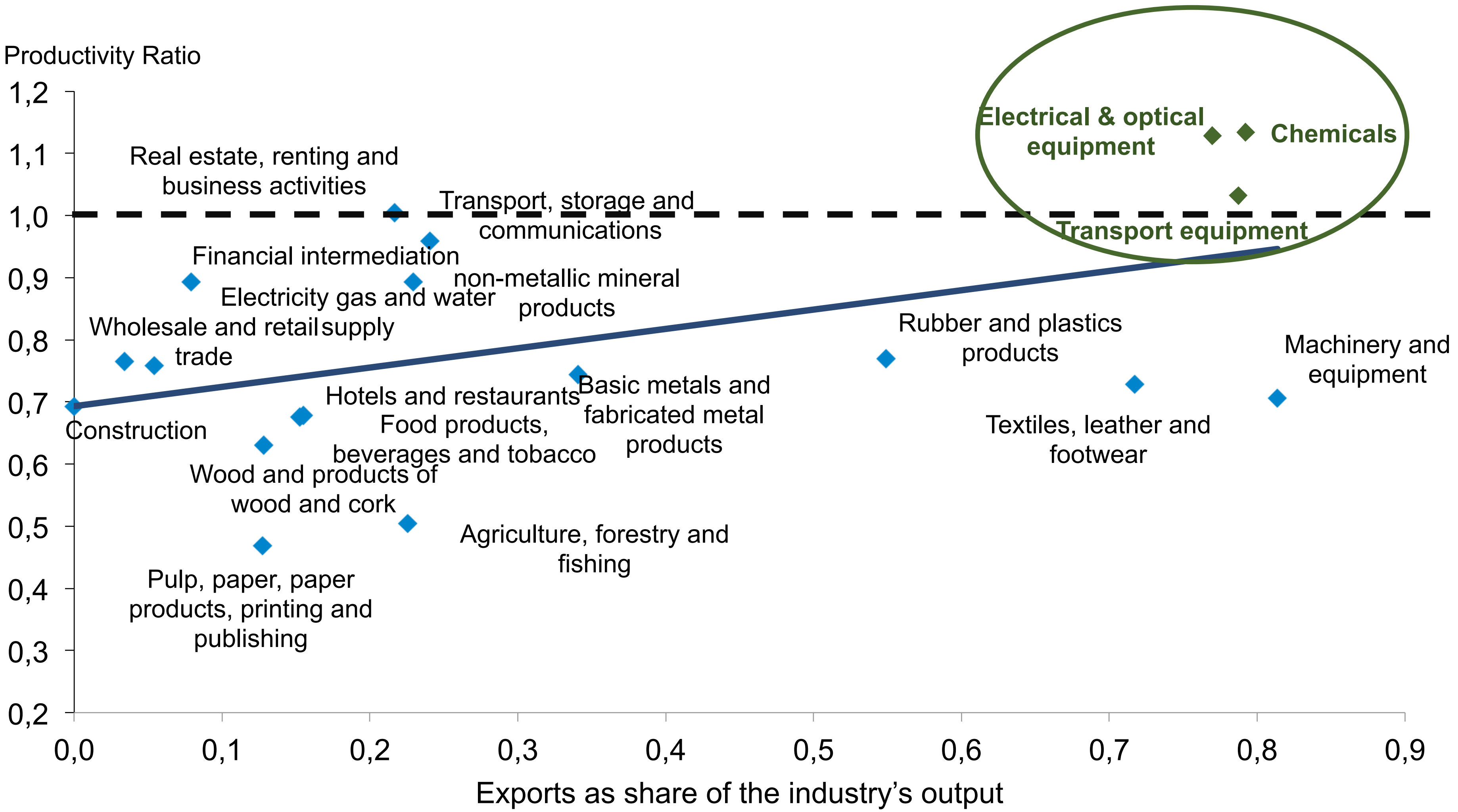
Source: The Israel water authority , "Natafim", "Mekorot".

Venture Capital Investment as % of GDP, 2014



Source : OECD

Productivity Gap—Israel vs. OECD Average, and Exports' Share of Output in Israel, by Industry, 2010

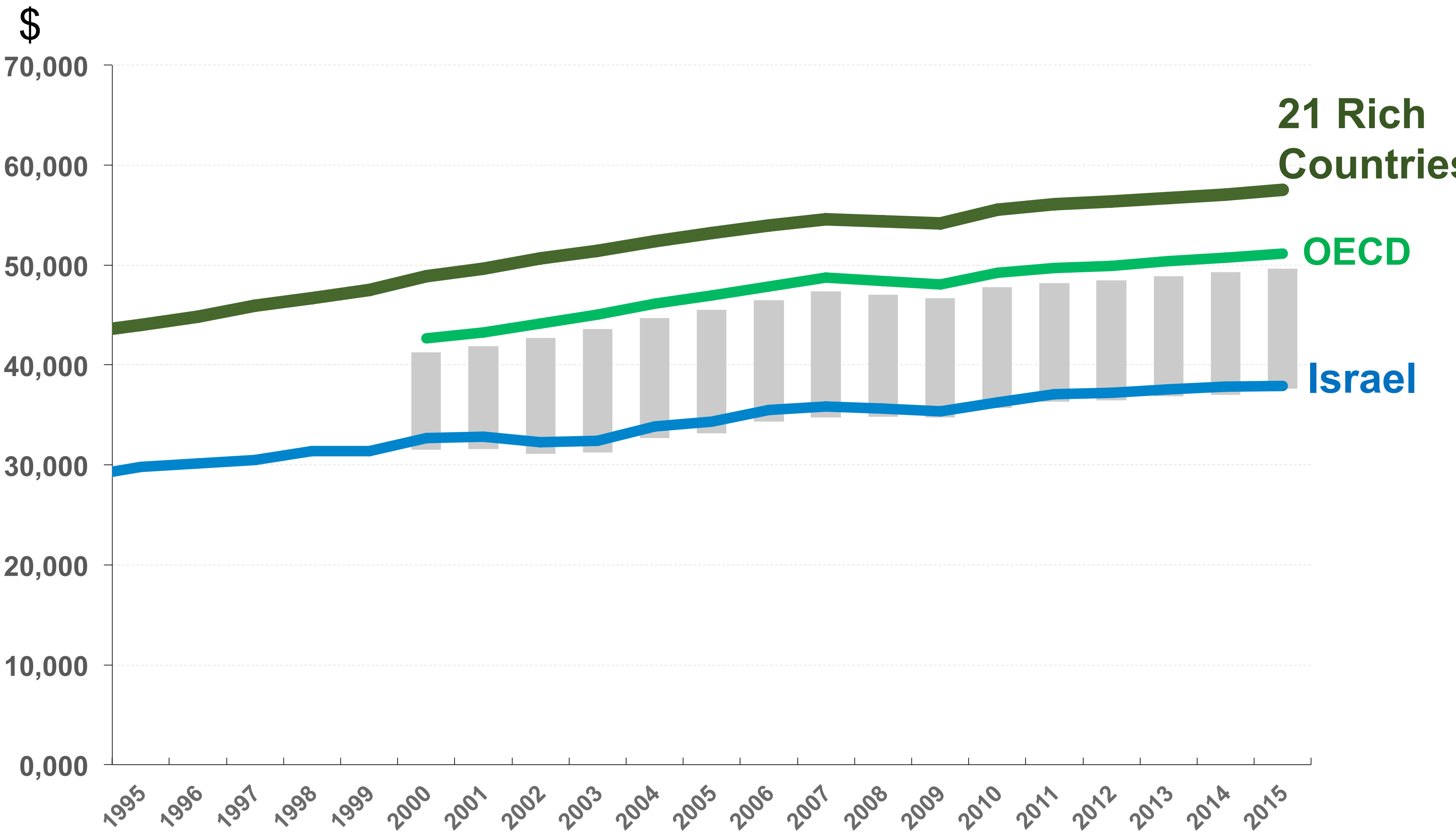


Source : Eurostat, OECD, BoI, CBS (Israel)

Long Term Challenges

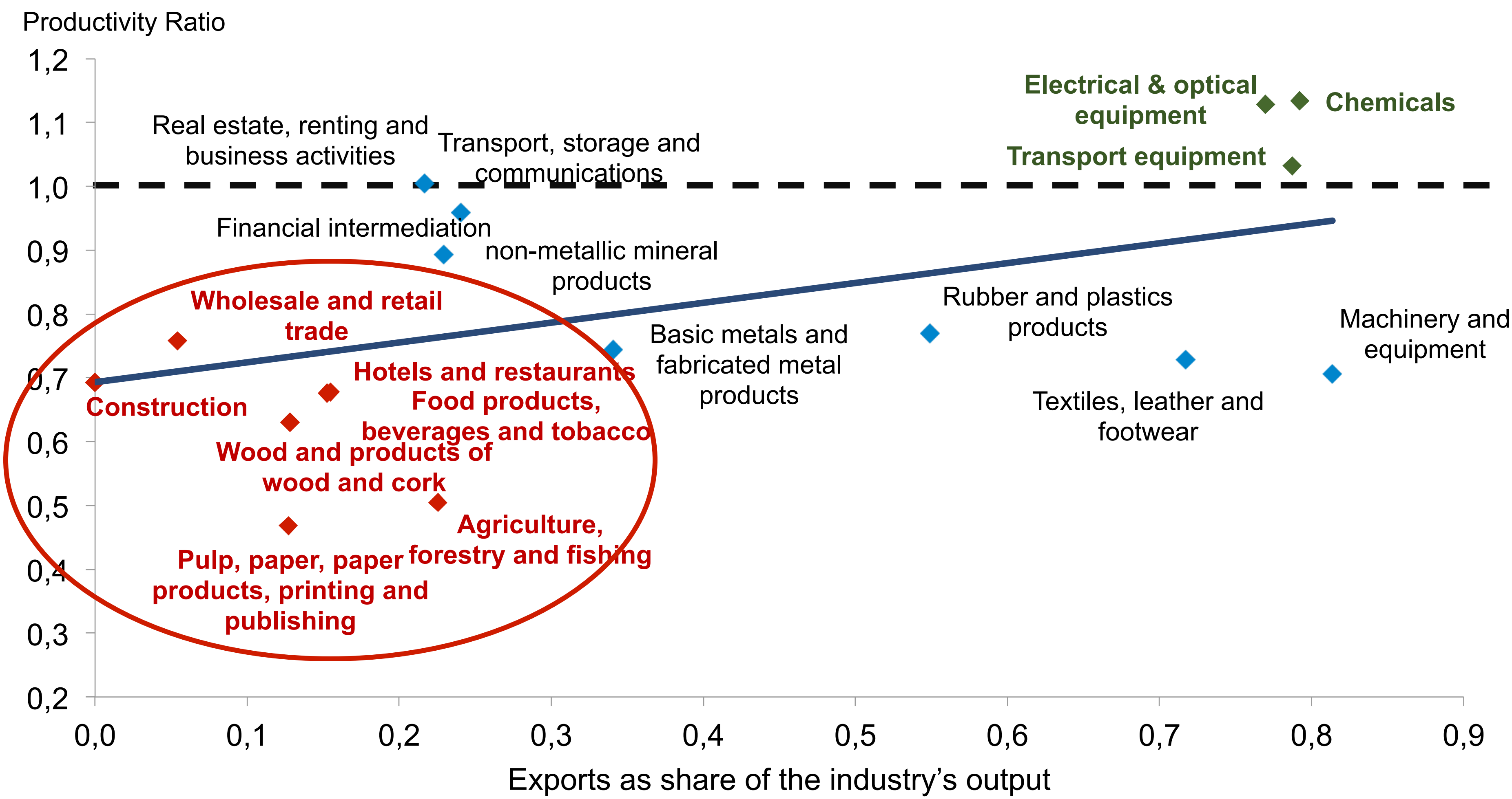
Output Per Hour Worked

1995-2015,$ PPP, 2015 Constant Prices



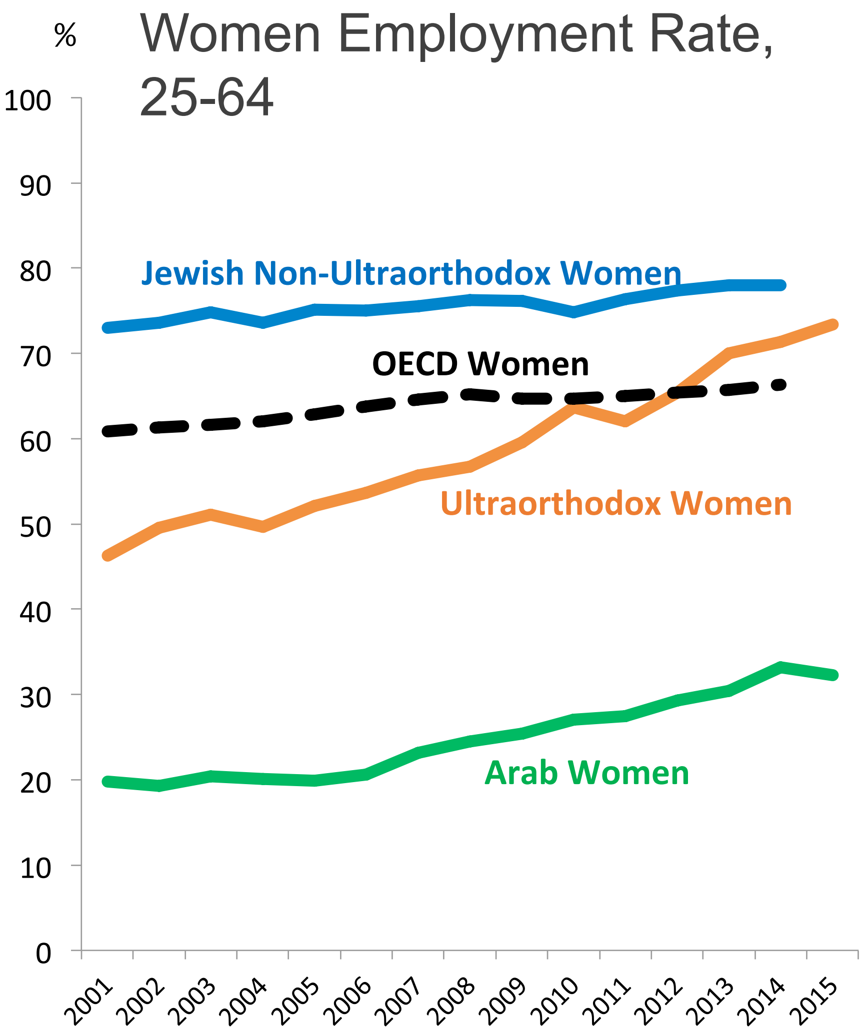
Source : The Conference Board Total Economy Database 2015

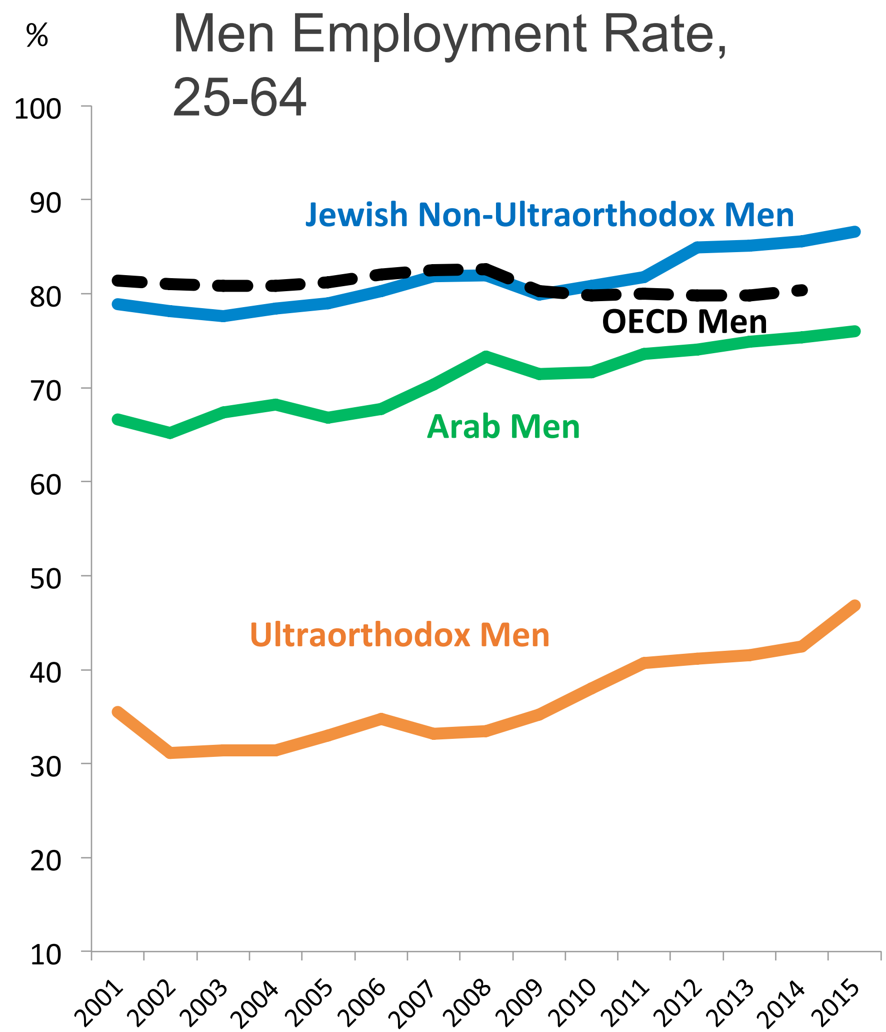
Productivity Gap—Israel vs. OECD Average, and Exports' Share of Output in Israel, by Industry, 2010



Source : Eurostat, OECD, BOI, CBS (Israel)

Employment Rate by Population Groups

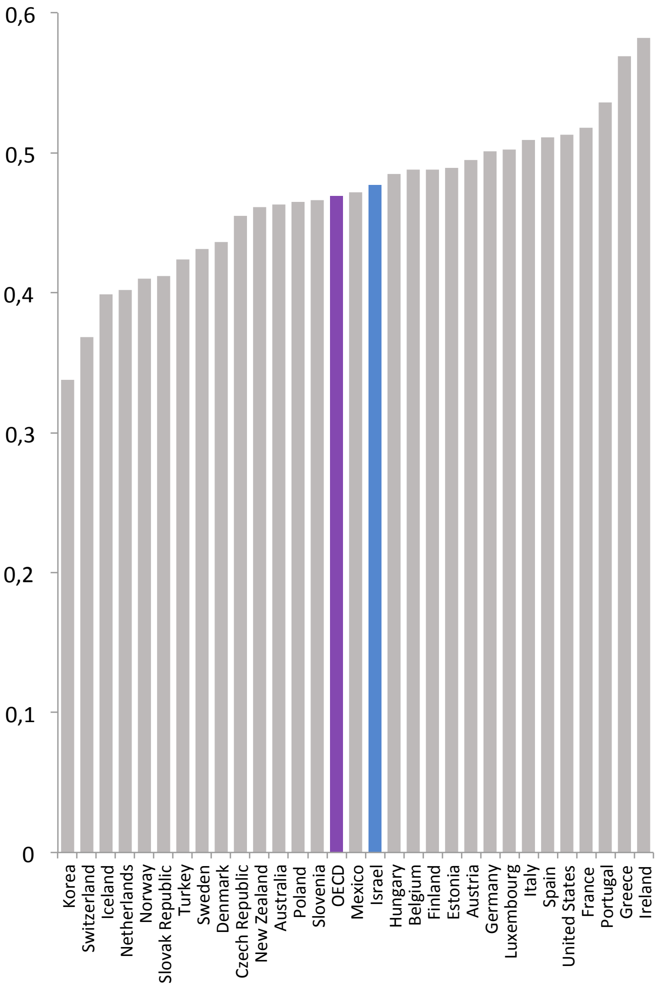




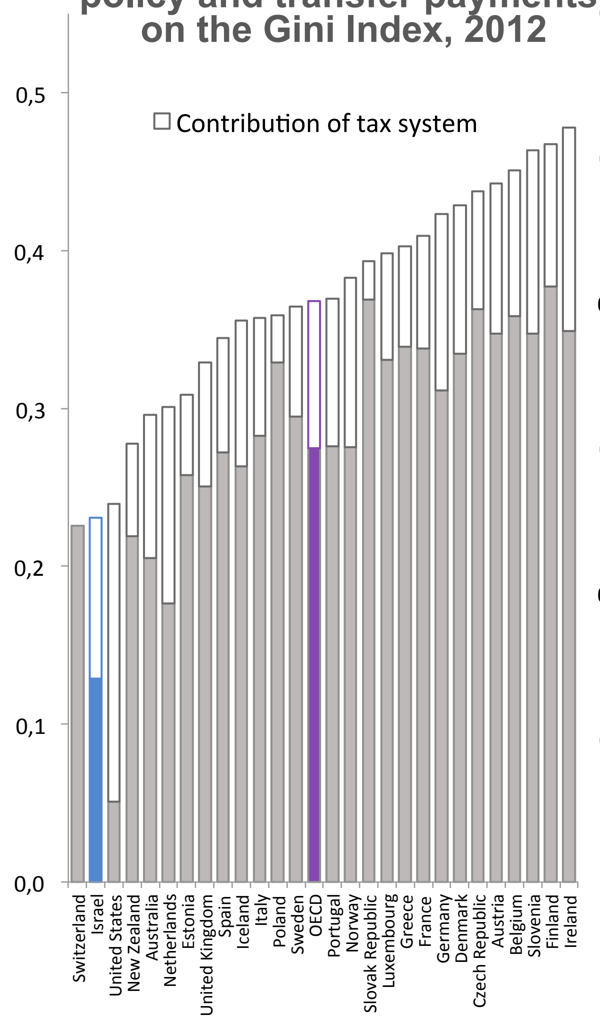
Source : Based on Central Bureau of Statistics Data

Economic Income Inequality is Similar to the OECD Average, but the Effect of Policy, Particularly Transfer Payments, is Low in International Comparison.

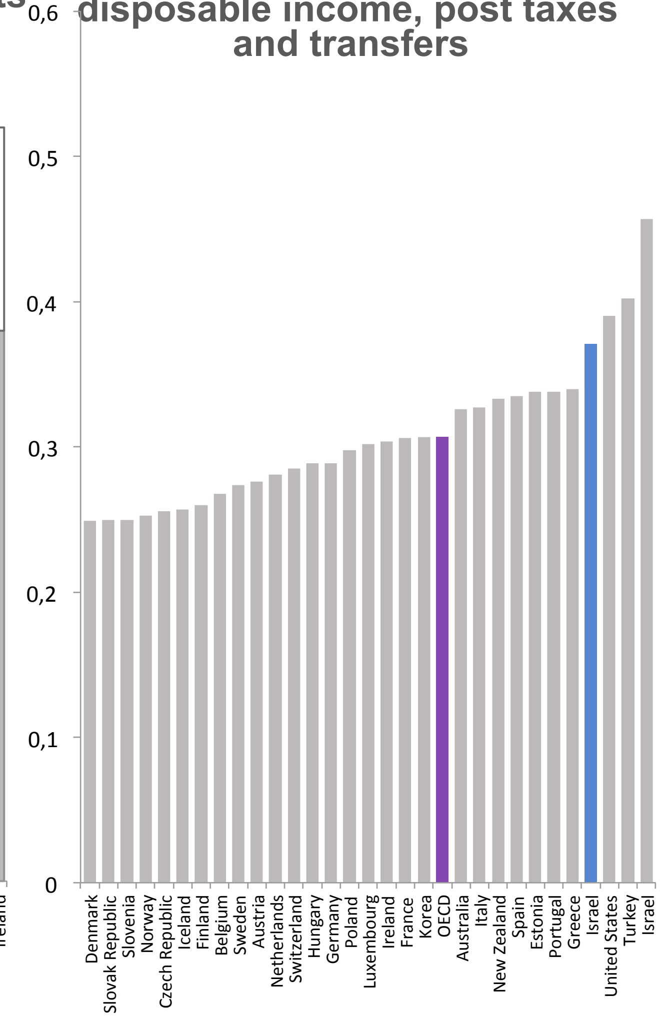
Gini Index, 2012*, at market income, before taxes and transfers



Strength of the effect of tax policy and transfer payments on the Gini Index, 2012



Gini Index, 2012*, at disposable income, post taxes and transfers



*Israel data for 2014

Source : Based on Central Bureau of Statistics Data and OECD

The Need to Formulate a Focused Strategic Plan:

- **Integrate population sectors into the labor market: Active labor market policy**
  - Ultra-Orthodox (men)
  - Arab (women)
  - Older workers (around retirement age)
- **Increase human capital: Education and professional training**
- **Remove obstacles to growth and productivity**
  - Infrastructure
  - Business environment
  - Competitiveness
  - Promote reforms (ports, electricity, and the natural gas and energy industry)
  - Research and development
- **Increasing quality and efficiency of public service systems (health, long-term care, welfare, pension, etc.)**
- **Diversify trade geographically and by industry**

Thank You