



STATE OF ISRAEL
MINISTRY OF FINANCE
INTERNATIONAL AFFAIRS DEPARTMENT

January 2008

Economic Highlights

4th QUARTER 2007

Dear Friend,
Once again we are distributing our "Economic Highlights."
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S&P has raised its long-term foreign currency sovereign credit rating on the State of Israel to 'A' from 'A-', and its long-term local currency credit rating to 'AA-' from 'A+'

→ For more details see next page

Israel's gross debt is expected to drop to roughly 80% of GDP by the end of 2008 – a 20% decline in four years only (2003 – 102%)

→ See page 7

▶ The Bank of Israel has begun conducting Repo auctions from October with financial institutions and banks

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▶ A sharp rise in private car purchases: 200,000 new cars in 2007.

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[For up-to-date economic figures – Page 6](#)

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Latest News

S&P: Israel Raised to 'A/A-1', LC 'AA-/A-1' On Reduced Debt, Improved Resilience; Outlook Positive

Roni Bar-On, the Minister of Finance: "This is a break through the glass ceiling which has restrained Israel's economy from upgrading."

Bank of Israel: The improvement in Israel's credit rating by S&P reflects the success of the macroeconomic policy pursued by the Government and the Bank of Israel in order to sustain the upward trend of Israel's economic growth and its economic and financial stability.

Ratings list: **Foreign Currency Sovereign Credit Rating**

To: A/Positive/A-1

From: A-/ Positive/A-1

Local Currency Sovereign Credit Rating

To: AA-/Stable/A-1+

From: A+/ Positive/A-1

T&C Assessment

To: AA

From: AA-

For information regarding other credit rating firms please visit:

www.mof.gov.il/debt/gov/rating.asp

The Bank of Israel has begun conducting Repo auctions in October

The Monetary Department at the Bank of Israel has announced that the Bank will begin Repo auctions in the capital market, in the framework of which buying government bonds and Treasury bills from financial institutions and banking corporations, and then will sell these back one week later at a predetermined price.

A rise in credit to the business sector and in issues of corporate bonds in the first half of 2007 – reaching an unprecedented annual rate of 21 percent. The rate of increase in the last few years exceeds the rate of growth of real economic activity.

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Recent Tax Reductions

Two Major Tax Reductions have been Authorized by the Knesset

Negative Income Tax

- The maximum amount entitled 45% of minimum wage (approx. \$430) additional pay is granted to employed parents. Self employed are also entitled to benefits.
- Employed persons more than 55 years old are entitled to benefits of younger persons with children.
- Benefits will be transferred directly to private accounts to prevent employers from receiving them.
- The program only will be applied in areas in which the "Wisconsin" program operates.

Income Tax

The income tax reductions are aimed especially for the low middle-class income.

The reduction will begin in 2008 and continue gradually into 2009, where it is planned to finish.

Tax Level (NIS)	Taxation before the reduction	Authorized reduction by the Knesset
Up to 4,270	10%	10%
4,271-7,600	17%	14%
7,601-11,410	25%	21%
11,411-16,380	30%	28%
16,381-35,270	32%	32%
over 35,271	44%	44%

"European Champions"

Deloitte has given Israeli hi-tech the first three places in an event in which the 500 fastest growing technology companies were ranked:

Rank	Company	Area of Expertise	Country	Growth Rate*
1st place	Voltaire	Communications	Israel	50,612%
2nd place	Celltick	Communications	Israel	29,627%
3rd place	Runcom	Semi-Conductors	Israel	27,950%
4th place	TomTom Nv	Software	Holland	17,193%
5th place	ByBox Holdings	Software	GB	15,272%
6th place	Red Band	Software	Israel	14,347%

*In the past 5 years

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Other Current News

Treaty for Avoidance of Double Taxation with Moldova, to enter into force on January 1, 2008

The treaty is based mainly on the OECD model treaty and is establishes, among others, tax withholding rates in the source country regarding: Interest, Dividends, Royalties, Capital gains, Permanent establishment and a residence test for companies.

An R&D cooperation agreement has been signed between MERCK (Germany) and the Chief Scientist. According to the agreement, both parties will support Israeli companies developing pharmaceutical and chemical products for high-tech and life-sciences fields.

Israel signed a free-trade agreement with MERCOSUR – The first time ever that the South-American trade group subscribes with a country outside Latin America. (Dec 18).

It is expected that the agreement will enhance significantly Israeli– Latin American trade.

The Chief Scientist's Research Committee has approved General Motor's Request to establish a project center in Israel.

The purpose of the project center will be to execute an industrial technological R&D program in cooperation with Israeli partners, which will receive funding grants from the center. The center will also:

- Spot and contact Israeli industrial companies and/or academic research centers with whom GM wished to cooperate in R&D.
- Accompany projects by GM's R&D staff.

2.3 million entrances to Israel from abroad in 2007 – a 25% increase compared to 2006 – Out of which: 2.27 million tourists, a 24% increase.

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The NASDAQ Stock Market, Inc. and the Tel Aviv Stock Exchange (TASE) have signed a Memorandum of Understanding (MOU) to formalise the relationship between the two markets. Under the agreement, NASDAQ and TASE will develop the channels of communication between the two markets and work to facilitate the stronger trading of company shares admitted on both markets.

Entering 2008, Israel's population is estimated at 7.2 million

Israel's population consists of 75.6% jews, 20% muslim and 4.4% other. Population growth in 2007: 1.7%, slightly less than 2006 (1.8%). During 2007, 18,000 people have immigrated to Israel.

Current Infrastructure development

Beginning construction of the Tel-Aviv subway. (\$2.5 billion, completion estimate: 2014).

Construction of the Light Rail in Jerusalem. (\$750 million, completion estimate: 2010).

Five-year plan for intercity highways. (\$4 billion, Time frame: 2006-2010)

Natural gas – laying the Ashkelon-Dead Sea pipeline.

Investments in desalination's infrastructure – The Hadera site totals 100 million cubic meters, Ashkelon site 105 million and Palmahim site 30 million, totaling 235 million cubic meters. There is a planned expansion of an additional 300 million cubic meters. (All of the above – per year)

Israel Railways – further implementation of a multi-year plan. (\$6.5 billion) Completion estimate: 2010.

Carmel Tunnel – Connecting the Haifa shoreline with its center. (\$250 million, completion estimate: 2010).

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ECONOMIC FIGURES

Demand and Output

Data from previous editions is constantly being updated.
All projections are done by the Economics and Research Department

GDP growth:

2007 estimate: **5.3%**
2006: **5.2%**; 2005: **5.3%**
Growth expected for 2008: 4.2%
OECD forecast for 2008: **2.7%**

Private Consumption Growth:

2007 estimate: **7.2%**
2006: **4.5%**; 2005: **4.0%**
OECD forecast for 2007: **2.7%**
Growth expected for 2008: 4.3%

Business GDP growth:

2007 estimate: **6.3%**
2006: **6.5%**; 2005: **6.5%**
Growth expected for 2008: 4.9%

Public Consumption Growth:

2007 estimate: **2.6%**
2006: **2.3%**; 2005: **2.9%**
Growth expected for 2008: 2.0%
OECD forecast for 2007: **2.2%**
OECD forecast for 2008: **2.1%**

GDP per Capita, based on PPP: \$28,169 (2006) – 21st place in a descending list including Israel and OECD members. OECD Average: **\$32,098**

Foreign Trade

Goods and Services

Import growth:

2007 estimate: **12.8%**
2006: **3.3%**; 2005: **3.5%**
Growth expected for 2008: 4.6%

Export growth:

2007 estimate: **8.6%**
2006: **5.9%**; 2005: **4.3%**
Growth expected for 2008: 4.7%

Balances

Current account surplus:

4th Quarter 2006 – 3rd Q' 2007: **3.7%**
2006: **5.6%**; 2005: **3.3%**

Gross Debt: (% of GDP)

(General government gross financial liabilities)
2007 projection: **81.5%**;
2006: **87.7**; 2005: **97**; 2004: **100.7**

Budget deficit

(Central Government):
2007: **0.02%** (100 million NIS)
(Planned deficit was **2.9%**)
2006: **0.9%**; 2005: **1.9%**;
2004: **3.7%**

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Investments

Total Gross Local Investment:

2007 estimate: **13.4%**
 2006: **5.3%**; 2005: **11.1%**
 2004: **3.1%**
Growth expected for 2008: **7.1%**

Investment in Fixed Assets:

2007 estimate: **13.6%**
 2006: **10.1%** ; 2005: **2.3%**
Growth expected for 2008: **5.5%**

Israeli Investments abroad: (B\$)

2006: **30**; 2005: **18**; 2004: **13**.
 ↑ Growing trend.

Foreign investments: (B\$)

Jan-Nov 2007: **9.6**;
 2006: **25.8** (including TEVA-Ivax deal)

Foreign direct investments (B\$):

Jan-Nov 2007: **8.9**; 2006: **14.2**;
 2005: **9.9**; 2004: **9.1**.

Challenges

- **Maintain the budget framework.** Implementing a sound, responsible fiscal policy, **narrowing socio-economic gaps and reducing poverty.**
- **Maintaining monetary stability** – Israel has an Inflation-Targeted monetary regime. The target is 1-3%.
 2007 CPI change: **3.4%**. (2006: **-0.1%**)
- **Continuation of the reduction of the public debt to GDP ratio:**
 2006: **87.7%**; projected debt in 2007 is: **81.5%**.
 OECD 2007 projection (all countries): **76.8%**;
- **Reducing the rate of unemployment** is still a challenge even though it is in a downtrend. Expected average rate in 2007: **7.5%**; 2008: **7.2%**
 Unemployment rate in the 2nd quarter was **7.5%**; 3rd quarter: **7.3%**
 → November registered a rate of **6.6%** - the lowest in 11 years.
 2006: **8.4%**; 2005: **9.0%**; 2004: **10.4%**; (OECD, 2007: **5.4%**).
- **Increasing participation rate in labor force:**
 Expected participation rate for 2007: **56.6%**. (3rd quarter: **56.7%**)
 (2006: **55.6%**; 2005: **55.2%**) (OECD: **70.0%**).

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[Continue reforms](#)

- **Continue reducing corporate tax** – from **29%** in 2007 to **25%** by 2010.
(Plan is: 2008 – **27%**; 2009 – **26%**)
 - Introducing **negative income tax (EITC)**. **Pension benefits for all.**
→ *See page 3*
 - **Reducing tax burden** on low and medium income levels
(Increasing the disposable income which in turn may increase private consumption). → *See page 3 as well*
 - **Privatization processes, combined with structural changes:**
 - Splitting and sale of Oil Refineries – US **\$2.3 billion** (2006-7)
 - Sale of the controlling core of Bezeq – US **\$919 million** (2005)
 - Privatization of ZIM – US **\$112.5 million** (2004)
 - Privatization of Pi–Gllioth (terminals only) – US **\$197 million** (2007)
* The Governments share – approximately 50%.
- Total income from privatization of government, mixed companies & banks between 2000-7: **US \$6.5 billion**

Sources: Ministry of Finance – Department of Economics and Research, Central Bureau of Statistics, Bank of Israel, Tel Aviv Stock Exchange, Government Companies Authority, Standard and Poor's.

We welcome your feedback!

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