ISRAEL*

The 2016 pick-up in growth should continue, reaching 3¼ per cent in 2017-18. Support from slight budgetary easing, very low interest rates and measures to support the low-paid should continue to stimulate domestic demand and employment. However, the ongoing weakness of the international environment and the impact of exchange rate appreciation on foreign trade are projected to hold back export growth.

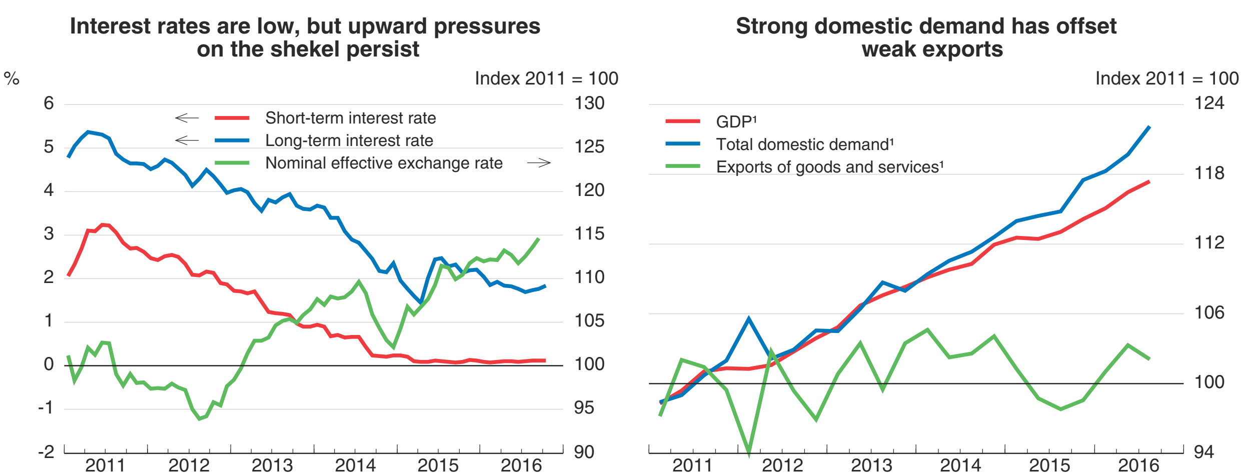
So long as inflation remains low, an accommodative monetary policy remains appropriate to damp currency appreciation. The rise in mortgage rates induced by the macro-prudential measures adopted by the Bank of Israel to stabilise the property market is welcome. Reforms designed to increase competition in banking should be extended to other sheltered sectors (such as farming) to enhance supply and productivity and foster catch-up. Lowering the regulatory burden on businesses by simplifying complex administrative and licensing procedures should be further promoted.

With the economy close to full capacity, the mild budgetary expansion planned for 2017 should only have a small positive and temporary effect on activity without excessively reducing the budgetary leeway achieved through the consolidation of previous years. Public finances could nevertheless play a greater role in stimulating growth and making it more inclusive, by shifting the structure of spending towards boosting investment and promoting efficiency in public transport and education.

Growth has recovered, largely under the impetus of domestic demand

Growth has gathered pace since 2015, as consumer spending was boosted by the strong labour market and credit conditions remained favourable. Business investment was

Israel



1. In real terms.
Source: OECD Economic Outlook 100 database.

StatLink http://dx.doi.org/10.1787/888933437730

* The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Israel: **Demand, output and prices**

	2013	2014	2015	2016	2017	2018
	Current prices NIS billion	Percentage changes, volume (2010 prices)				
GDP at market prices	1 059.1	3.2	2.5	3.3	3.4	3.3
Private consumption	585.3	4.2	4.2	5.8	3.7	3.5
Government consumption	238.4	3.6	3.3	4.2	4.0	2.8
Gross fixed capital formation	215.4	0.0	0.0	10.6	7.6	4.3
Final domestic demand	1 039.1	3.2	3.1	6.4	4.6	3.5
Stockbuilding[1]	- 3.9	0.6	0.6	-1.4	0.2	0.0
Total domestic demand	1 035.2	3.8	3.8	4.9	4.8	3.5
Exports of goods and services	353.6	1.5	-4.1	3.3	3.1	4.0
Imports of goods and services	329.7	3.8	-0.5	9.1	8.0	4.8
Net exports[1]	23.9	-0.7	-1.2	-1.5	-1.3	-0.2
Memorandum items						
GDP deflator	_	1.1	2.8	1.7	1.4	1.5
Consumer price index	_	0.5	-0.6	-0.5	0.7	1.1
Private consumption deflator	_	0.6	-0.4	-0.2	0.7	1.2
Unemployment rate[2]	_	5.9	5.2	4.9	4.8	4.7
General government financial balance[3,4]	_	-3.2	-2.1	-2.5	-2.9	-3.1
General government gross debt[3]	_	66.0	64.1	62.7	62.2	61.9
Current account balance[3]	_	3.9	4.4	4.0	3.0	2.7

1. Contributions to changes in real GDP, actual amount in the first column.
2. Employment and unemployment data prior to Q1 2012 are derived from a quarterly labour-force survey that has since been replaced by a monthly survey, which included a number of methodological changes. The data prior to Q1 2012 have been adjusted to be compatible with the new series.
3. As a percentage of GDP.
4. Excluding Bank of Israel profits and the implicit costs of CPI-indexed government bonds.

Source: OECD Economic Outlook 100 database.

StatLink http://dx.doi.org/10.1787/888933439094

also vigorous. Despite the appreciation of the shekel and weak foreign demand, exports also picked up, driven by a dynamic hi-tech industry. With unemployment at a historic low level below 5%, increasing shortages of skilled labour, and a revaluation of the minimum wage that is set to continue until the end of 2017, wage increases have strengthened. Consumer prices, however, fell by 0.3% year-on-year in October 2016, because of lower import prices.

There has been a slight relaxation of budgetary policy, but supply conditions need improving

The Bank of Israel has kept its policy rate at 0.1% since March 2015. Despite intervention, the shekel appreciated by 3½ per cent in effective terms in 2016. Notwithstanding a significant pick-up in mortgage rates, linked to the adoption of macro-prudential measures, house price increases have remained strong at around 8% in recent months.

The general government budget deficit, which will probably rise from 2.1% to 2.5% of GDP between 2015 and 2016, is set to reach around 3% of GDP in 2017 and 2018. According to the government's budget proposal for these two years, public spending will rise quite rapidly, especially in the areas of housing, health care and transport. There are plans to cut corporate taxes, but also to raise taxes on property investors. This limited budgetary expansion should provide only slight and temporary support to the economy. However, to offer more lasting and significant backing for growth, and make it more inclusive, the composition of public spending would need to shift towards training for marginal groups and investment in public transport. In combination with heightened competition in sheltered sectors, these structural reforms should stimulate supply and productivity.

The resilience of domestic demand should shore up the economy

Despite the appreciation of the currency and ongoing weakness of foreign demand, growth is projected to be robust in 2017 and 2018. The accommodative monetary stance and higher wages for the low-paid will bolster consumption, while investment will benefit from the launch of projects by major hi-tech firms and government measures to promote housing and transport. The current account surplus should shrink, unemployment remain low, and inflation increase steadily within the targeted range of 1-3%, driven by pay rises.

The international outlook remains fragile both at the global and regional levels due to persistent geopolitical tensions, and a weaker-than-expected external environment would undermine growth. On the other hand, if unemployment were to continue to fall and exacerbate wage pressures, domestic demand could be stronger than expected. The adoption of a budget for the two coming years further heightens budgetary risks because of the difficulties in forecasting tax revenues over a two-year timeframe.