BANK OF ISRAEL
Office of the Spokesperson and Economic Information

June 6, 2011

Report to the public on the Bank of Israel's discussions prior to setting the interest rate for June 2011

The discussions took place on May 19 and 23, 2011

General

Before the Governor makes the monthly interest rate decision,[1] discussions are held at two levels—the first in a broad forum, and the second in a narrower one.

In the broad-forum discussion, the relevant background economic conditions are presented, including real, monetary and financial developments in Israel's economy, and developments in the global economy. Participants in this discussion include the Governor, the Deputy Governor, the directors of the Research and Market Operations Departments of the Bank and economists from various departments who prepare and present the material for discussion. The data, estimates and assessments in this report are those that were available at the time of the discussions.

In the narrow forum, the directors of the Research and Market Operations Departments and two other participating members of management (the Deputy Governor and the Head of the Monetary and Finance Division of the Research Department) present their recommendations regarding the interest rate and, following a discussion, the Governor makes his decision.

A. THE BROAD-FORUM DISCUSSION—THE STATE OF THE ECONOMY

1. Developments on the real side

General assessment

Data published last month (between the date of the previous interest rate decision on April 24 and the current decision on May 23) point to continued expansion of economic activities in most sectors of the economy. The preliminary estimate of National Accounts data for the first quarter points to GDP annualized growth of 4.7

[1] When the Monetary Committee is appointed, in accordance with the new Bank of Israel Law, interest rate decisions will be made by the Committee.

POB 780 Jerusalem 91007 Israel
Tel: 972-2-6552712/3 Fax: 972-2-6528812 www.bankisrael.org.il

percent – higher than the previous estimate of the Bank of Israel Research Department of 4.5 percent GDP growth in 2011 - and to growth of business product of 5.8 percent. The macro-economic picture developing until now is that of an economy where the use of resources – domestic and from overseas – is growing rapidly. With that, the level of GDP in the first quarter of 2011, according to the estimate of the Research Department, indicates that the output gap has nearly closed. Labor market figures show that despite the economy's nearing full employment, wage pressures are not yet seen in the business sector. An analysis of sector salary figures shows that in most sectors, the nominal wage is rising at a moderate pace.

National accounts

The preliminary estimate of national accounts figures for the first quarter of 2011 points to continued fast growth in economic activity: GDP grew 4.7 percent, private consumption excluding consumer durables rose 3.7 percent, investment in fixed assets increased 23.7 percent, exports grew 16 percent, and imports grew 15.9 percent. Domestic public consumption, which is generally volatile year round, fell 5 percent, following a 25.3 percent drop in defense spending, and thus somewhat lowered the demand pressure on GDP. Business sector product rose 5.8 percent. It should be noted that looking back over the previous four quarters, there is an outstanding gain of 6.6 percent in business sector product, a rise of 22.7 percent in investment in fixed assets, an increase of 11.5 percent in exports, and a rise of 10.2 percent in imports.

Indicators of real economic activity

Indicators published this month with regard to the pace of expansion in April were mixed. According to monthly figures from a new survey of trends provided by the Central Bureau of Statistics, there was a continued improvement in business activities of the private sector. Overall company expectations in the business sector show great optimism regarding the extent of activity in the coming months – net balances of expectations are high and are similar to those reported in previous months. Two consumer confidence indices increased in April – the Globes index rose 4.2 points and the Bank Hapoalim index rose 2 points – continuing their rise of the previous month. Despite the volatility, these indices are at a relatively high level. In contrast, according to the index of Google searches, there was a slowdown in all branches connected with domestic demand, so that the probability of a slowdown reached 0.7 in April-May, compared with a probability of 0.5 in the previous month. Compared with the situation a month ago, there was a marked slowdown in searches for durable goods, personal care, restaurants and tourism. In addition, despite the fact that the Purchasing Managers Index in industry rose in April, and the fact that most components of the index – including manufacturing capacity, export demand, and employment – are in an expansionary trend, the index is still below the level of 50 points, and so it points to contraction in activities.

The labor market

Labor market data point to continued expansion in employment, and a drop in unemployment, with a moderate increase in wages. According to trend figures for February, the unemployment rate continued to drop, and reached 6 percent of the civilian labor force. The number of jobseekers fell by 1.2 percent in March, compared with February (seasonally adjusted), and was 7 percent lower than the corresponding month of 2010. The nominal wage increased by 1.2 percent in December–February compared with the three preceding months, while the real wage fell by 0.4 percent (seasonally adjusted). Total health tax receipts in April 2011, which provide an indication of wage payments in that month, show an increase of 7.8 percent, in nominal terms, from their level in April 2010. The government recently approved an increase in the minimum monthly wage of NIS 410, to NIS 4,300.

Foreign trade

Goods exports fell 2.1 percent in April, after a rapid and extended increase over the six preceding months. In the three preceding months, exports increased at an average monthly rate of 4 percent. The rapid growth of exports in the second half of the year took place at the same time as rapid growth in world trade. Estimates of world trade (the Triple Trade Index[2]) indicate a continuous growth at the rate of 2 percent per month in the preceding 6 months. Goods imports grew by an average of 6.3 percent, continuing an increase of an average monthly rise of 2.9 percent in the preceding three months. In recent months there has been marked, continued growth in investment products imports, a development which apparently reflects a correction to the drop in their share during the crisis period (approaching closing the output gap).

2. Budget data

Tax revenues in the first quarter of the year were 2.4 percent higher than the seasonal path consistent with the budget forecast. Local expenditures in the first four months of the year were 0.6 percent lower than the seasonal path consistent with the full implementation of the budget. Based on these trends, even assuming full expenditure of the budget, the deficit for 2011 is expected to be lower than the legislated ceiling (which is 3 percent of GDP).

3. Developments on the nominal side

Inflation

[2] The Triple Trade Index measures the total foreign trade of Germany, Japan and the US, and is a leading indicator of world trade.

The CPI increased by 0.6 percent in April, less than the average increase predicted by forecasters. This monthly rate was also below the seasonal path consistent with the achievement of the annual inflation rate target range. It should be noted that this is the second consecutive month that the index was below the path consistent with achieving the inflation target range, after four months that it was above the path. On a seasonally adjusted basis, the CPI fell 0.1 percent in April. In the previous twelve months it rose by 4 percent, above the upper limit of the target range. The April increase in the CPI was influenced, similarly to recent months, by increases in the price of food and energy, and from a continued rise in housing prices (representing rental contracts), and also by the seasonal increase in the prices of clothing and footwear. Price drops were seen only in furniture and equipment.

Expectations and forecasts of inflation and of the Bank of Israel interest rate

Twelve month forward inflation expectations as derived from the capital markets stood at 3.3 percent last month, while expectations for medium and long terms remained steady within the inflation target range. The average of forecasters' inflation expectations for the next twelve monthly CPIs was the same as the average in the previous month, 3.1 percent, slightly above the upper limit of the target inflation range. Based on the Telbor market (Tel Aviv Inter-Bank Offer Rate), the Bank of Israel interest rate in a year’s time is expected to be 4.2 percent, and forecasters’ predictions on average are that it will be 4.3 percent. About half of forecasters predict that the Bank of Israel will leave the interest rate for June unchanged, and half forecast the Bank to raise the interest rate for June by 0.25 percentage points.

The makam and bond markets

During the period surveyed, yields on government bonds (not indexed to the CPI), decreased 5-10 basis points, primarily in the medium range. Along the CPI-indexed government bonds curve, yields fell 7–12 basis points for most maturity terms. There was a mixed trend for *makam* yields with drops in short term returns and an increase of 5-15 basis points in most of the other terms, among other things against the background of foreigners shortening durations and expectations of an interest rate increase.

The interest rate differential and the yield gap between Israel and abroad

As a result of the interest rate for May remaining unchanged, and before the interest rate decision for June, the Bank of Israel interest rate stayed 2.75 percentage points higher than the US federal funds rate and 1.75 percentage point higher than the ECB (European Central Bank) rate. The yield gap between Israeli and US unindexed 10-year government notes widened this month to 210 basis points, primarily against a background of a bigger drop in yields in the US.

The monetary aggregates

In the twelve months up to and including April, the M1 monetary aggregate (cash held by the public and demand deposits) increased by 5 percent, and the M2 aggregate (M1 *plus* unindexed deposits of up to one year) increased by 6.5 percent.

The credit market

In March, there was a drop of 1.2 percent in the balance of credit to the business sector, to a level of NIS 764 billion. Most of the decrease came from the appreciation that was recorded in March, which influenced the shekel value of the balance of credit from abroad. The balance of credit to households rose 1.4 percent in March and reached NIS 345 billion. Within that figure, credit for housing rose by about 1 percent, after a similar rise in February. The overall volume of mortgages granted in the twelve months which ended in April was NIS 50 billion, about 25 percent higher than the previous twelve months. About 47 percent of new mortgages granted in April were not indexed to the CPI, at variable interest rates. On May 5th, a Bank of Israel directive went into effect, which limits the share of variable rate housing credit. The interest rates on mortgages rose in April for all terms.

The housing market

House prices continued to rise. House prices—which are presented in the Central Bureau of Statistics survey of house prices but are not included in the CPI—rose in February–March at a monthly rate of 1 percent, following their increase of 1.4 percent a month in January–February. The annual pace of home price increases continues to be high, though it moderated somewhat. In the last twelve months, house prices increased 13.9 percent. Unlike the increase in house prices, the housing cost price index, which is based mainly on renewed rental contracts and which is included in the CPI, rose by 0.7 percent in March, and in the last twelve months it increased by 6 percent, slightly lower than the increase, from this perspective, in the previous month. Trend figures show somewhat of a drop in sales of new houses in recent months, and in parallel a moderate drop in the inventory of new houses for sale.

The Research Department assessment (staff forecast)

The Bank of Israel staff forecast**,** which was updated this month**,** is that inflation in 2011 will be above the upper limit of the target inflation range, and that it will decline to within the target range in the first quarter of 2012 (this is sooner than in the previous forecast, in which this was expected to occur towards the middle of 2012). The interest rate is expected to increase gradually to about 4.2 percent in a year’s time (compared with 4.4 percent in the previous forecast).

The main factors causing the higher inflation rate were the same as before: the housing component (rentals), which is expected to continue rising rapidly, increased demand, and the increase in energy and commodity prices. The main force acting to reduce inflation is the appreciation reflected in the effective exchange rate, and the lagged effects of recent interest rate increases.

The main factors which could change the forecasts for real activity and inflation in Israel are developments in the global economy, including changes in commodity and oil prices, developments in the local housing market, the realization of geopolitical risks, and a possible increase in wage pressures in the public sector.

4. The foreign currency market and the share market

The foreign currency market

From the previous monetary policy discussion held on April 21 until May 20, the shekel depreciated by 2.4 percent against the dollar, similar to the trend in exchange rates vis-à-vis the dollar around the world; against the euro the shekel remained almost unchanged. The strengthening of the dollar against the major currencies was the result of increased concern over the debt crisis in some European countries and the sharp drop in commodity prices. In terms of the nominal effective exchange rate, the shekel depreciated by about 0.9 percent.

The capital market

Between the previous monetary policy discussion and the current one, most Tel Aviv share price indices fell, in line with the trend in most stock markets around the world. The Tel Aviv 25 index dropped by 3.6 percent, and the Tel Aviv 100 index dropped by 3.9 percent. The slowdown in the extent of new stock issues continued in April, with only some NIS 10 million of shares being issued, mainly in the trade and services industry; this was the lowest monthly figure of new issues in the last two years. This compares with NIS 90 million of issues in March, and NIS 294 million in February.

Corporate bond issues in the last few months stood at about NIS 4 billion a month, compared with a monthly average of about NIS 3 billion in 2010; their average rating rose. The CPI-indexed Tel-Bond indices rose—the Tel-Bond 20 index rose by 1.4 percent, and the Tel-Bond 40, by 1.2 percent, and the Tel-Bond shekel (not indexed to the CPI) index rose by 0.9 percent.

5. Israel’s financial risk, the sovereign risk premium

Israel's sovereign risk premium as measured by the five-year CDS barely changed over the month as a whole, and at the end of the period was 143 b.p.

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6. Global economic developments (see Appendix for further details)

The recovery in the global economy continued this month, although some slowing in its rate was evident, and the level of optimism regarding the global economy, and in particular the US and European economies, declined. Macroeconomic data published during the month present a mixed picture. The IMF expects a global GDP growth rate of 4.4 percent in 2011, and 4.5 percent in 2012, similar to its January forecasts, albeit with greater emphasis on the downside risks in the current forecasts. In the last few months world attention was again focused on the European debt crisis, in particular that of Greece. Commodity prices, mainly food and oil prices, fell during the month, against the background of global macroeconomic data and the strengthening of the dollar, although it is still too soon to determine that this represents a turnaround. Be that as it may, the reductions in commodity prices to date are expected to moderate the rising rate of inflation in emerging market economies. Against this background, the investment houses assess that no increase in the interest rate in the eurozone is expected before July, and as far as the US is concerned, the expected timing of increases in the interest rate was pushed back further. In some emerging market economies the interest rate was increased again this month.

B. THE NARROW-FORUM DISCUSSION—THE INTEREST RATE DECISION FOR JUNE 2011

In the monthly narrow-forum monetary policy discussion, four members of management make recommendations to the Governor regarding the appropriate rate of interest for the economy. At the end of the current discussions on the interest rate for June, three members of management recommended that the Governor increase the interest rate by 0.25 percentage point, to 3.25 percent, and one member recommended that he leave the interest rate unchanged for June.

As stated in previous reports of interest rate decisions, the Bank of Israel is implementing a policy consistent with the process of gradually restoring a more normal interest rate environment—a process aimed at stabilizing inflation within the target range, and supporting further growth of economic activity while maintaining financial stability. The pace of interest rate increases is not fixed, but depends on the inflation environment, growth in Israel and globally, the monetary policies of the major central banks, and the exchange rates of the shekel. An increase of 25 basis points in the rate of interest for June is consistent with that process, and at that level, monetary policy continues to be expansionary.

Several issues were discussed, including the expected path of inflation and inflation expectations, an assessment of the environment of real economic activity including reference to developments around the world, and geopolitical risks.

The first issues discussed were inflation and inflation expectations. It was noted that the inflation environment is still above the upper limit of the target inflation range, the midpoint of which is 2 percent inflation a year. Inflation over the last twelve months was 4 percent, and although inflation, seasonally adjusted, was low in the last two months, it is too soon to conclude that this represents a turning point. Participants also noted that 12-month forward inflation expectations, both those derived from the capital market and those of forecasters, are still above the upper limit of the inflation target. This, despite the fact that various forces are acting to moderate inflation—the recent appreciation of the shekel, and the reduction in world commodity prices, essentially food and crude oil. The point was also made that according to the Research Department forecast, inflation is expected to decline to within the target range in the next twelve months, assuming that the interest rate rises gradually to 4.2 percent. The lower than forecast rate of inflation in the last two months, does not provide a strong enough reason to deviate from the upward-sloping path of the interest rate.

The level of real economic activity was also discussed. The participants agreed that most indicators published this month supported the assessment that in the first quarter of 2011 and in April the rapid increase in real activity, demand and employment continued. The National Accounts data for the first quarter show more rapid growth than that in the previous Research Department forecast, and the updated data and the figures for the last twelve months highlight the increases in business sector product and in the domestic use of resources. Employment data also indicate expansion, although wage increases have been moderate. Participants in the discussion were of the view that the macroeconomic situation is that of an economy with buoyant demand, falling unemployment, an output gap that is closing, and close-to-full employment.

Other issues discussed were the level of activity in the global economy and the risks––including those relating to the debt crisis in Europe and geopolitical risks—confronting the Israeli economy, and their potential economic impact. Participants also expressed concern over a slowdown in US economic activity and over its ability to handle the growing fiscal burden, and spoke of indications of a slowdown in emerging market economies, including in China. Most of the participants thought that although the level of uncertainty regarding the pace of the global recovery had risen, it was not expected to have a significant impact on domestic activity in the short term. The probability of the realization of the current geopolitical risks is unknown.

Taking into account the high rate of growth and the approach to full employment, three members recommended increasing the interest rate in order to reduce the inflation rate. The member who recommended no change in the interest rate quoted the level of uncertainty regarding the continued recovery of global economic activity and the increased geopolitical risks as the main arguments supporting that recommendation.

The recommendation to increase the interest rate took into consideration the fact that central bank interest rates in the advanced economies are at a low level and are not expected to increase in the near future. It was mentioned that the increasing differential between interest rates in those economies and that in Israel makes it necessary to strike a balance between the domestic factors serving to favor an increase in the rate and the effect of such an increase on shekel appreciation and hence on exports and on total economic activity. In light of the latest indicators of economic activity and the shekel depreciation since the last monetary policy discussions, the members recommending an increase in the interest rate did not expect that it would significantly disturb the balance between the above forces.

In addition, it was stated in the discussion that despite the moderation in the pace of increase in house prices in the last few months, it remains high. In the last twelve months house prices rose by 13.9 percent.

Taking all the above points into consideration, the Governor decided to increase the interest rate for June by 25 basis points, to 3.25 percent.

In its announcement of the decision, the Bank of Israel emphasized the following points:

- The inflation environment is still above the upper limit of the target inflation range. Inflation over the previous twelve months was 4 percent. Inflation expectations for the next twelve months derived from the capital market and the average of the forecasters' expectations are still slightly above the upper limit of the range this month. This, despite several background developments that could be expected to moderate inflation, such as the appreciation of the shekel in recent months and the fall in commodity prices.

- Most economic indicators published this month support the assessment that the rapid expansion of activity continued in the first quarter of 2011 and in April, specifically on the export side, but also in domestic demand and employment. National Accounts data for the first quarter are consistent with a growth rate higher than that in the most recent Research Department forecast (4.5 percent GDP growth in 2011). Employment data indicate continued expansion, with the economy approaching full employment. Nevertheless, there are several risks that imply a relatively high level of uncertainty regarding future global growth and its implications for Israel's economy.

- The annual rate of increase in house prices continues to be high, although it has slowed a little—in the last twelve months house prices increased by 13.9 percent.

- Central bank interest rates in the major advanced economies are still low, and are expected to remain so in the next few months. Against the background of the acceleration in inflation in emerging market economies, several central banks increased their interest rates again this month.

The Bank of Israel will continue to monitor developments in Israel's economy and the global economy and in the financial markets. The Bank will use the instruments available to it to achieve its objectives of price stability, the encouragement of employment and growth, and support for the stability of the financial system, including keeping a close watch on developments in the assets market, and especially in the housing market.

The decision was made and published on May 23, 2011.

Participants in the narrow-forum discussion:
Prof. Stanley Fischer, Governor of the Bank of Israel
Prof. Zvi Eckstein, Deputy Governor of the Bank of Israel
Dr. Karnit Flug, Director of the Research Department
Dr. Edward Offenbacher, Member of Management and Head of the Monetary and Finance Division, Research Department
Mr. Barry Topf, Director of the Market Operations Department
Mr. Eddy Azoulay, Chief of Staff to the Governor
Dr. Yossi Saadon, Advisor to the Governor and Bank of Israel Spokesperson
Ms. Esti Schwartz, Secretary of the Monetary Committee
Mr. Konstantin Kosenko, Economist, Research Department

Appendix: Major Global Economic Developments

US

Despite a rise in morale among the American public and a strengthening of its support for the administration, following the killing of Al Qaeda's leader, there was a 10% drop in the investor optimism index with regard to the recovery of the US economy, compared with January. Macroeconomic figures continued to be mixed, and while they pointed to a lower than expected growth rate and a continued drop in home prices in the first quarter, they also showed a higher than expected number of jobs added. During the period that preceded the current interest rate decision, the US Federal Reserve updated its 2011 growth forecast from a range of 3.43-3.9 percent that had been published in January, to a range of only 3.1-3.3 percent, against the background of weak growth figures for the first quarter, as well as its forecast of the unemployment rate from 8.9 percent to 8.5 percent, while noting that it expects slow development of any sort of lowering of the unemployment rate. As far as its quantitative easing plan - QE2 – US Federal Reserve Chairman Ben S. Bernanke said that it will be completed as planned at the end of June, though with that, the Fed will continue to replace all bonds reaching maturity with new bonds, so that in effect the quantitative easing, at this stage, is not expected to influence the markets, in his assessment. It appears that the quantitative easing plan at most moderated the slowdown in growth but did not lead to its strengthening, and in addition it brought about an increase in the level of inflation which eroded the nominal gains. For example, despite a rise of 1.6% in labor productivity in the first quarter, there was a 2.5% drop in the real hourly wage, the sharpest drop in three years. Most of the gain in private consumption reflects higher prices and not a real increase in demand.

Aside from macro economic figures, it appears that the central problem of the US, as Federal Reserve Bank Chairman Bernanke expressed it, is the growing deficit. The International Monetary Fund noted in its Fiscal Monitor quarterly report that Japan (for understandable reasons) and the US (for unjustified reasons) are the only two developed economies which are increasing their fiscal deficit. It should be pointed out that since the crisis broke out, the US chose quantitative and fiscal easing in order to support growth, at a cost of a rise in the level of deficit and debt to GDP. It appears that with the large number of voices calling for fiscal and even monetary constriction, both from within (Walker, Volcker, Geithner) and from without, at the end of the day there will have to be constraints, but this time at a cost of slowdown in growth and a rise in the unemployment rate, as is happening in Greece and Portugal. For example, the fall in growth in the last quarter was very much impacted by the drop in public consumption, and additional fiscal constraints are likely to make it even more difficult. With that, against the background of the concern of the debt crisis in Europe and the dovish speech of ECB president Jean-Claude Trichet in his announcement about leaving the interest rate unchanged (despite a rise in the level of inflation to 2.7 percent in March) and the sharp drop in commodity prices, the dollar strengthened 2.1 percent against the euro since the last monetary policy meeting. A forecast rise in the US interest rate was pushed off form March-April to June.

Europe

During the course of the last month, world attention again was focused on the debt crisis in Europe in general, and in Greece in particular. The hope that consolidation of the €78 billion aid plan for Portugal and the easing of the pace of reducing the fiscal deficit required of it over the coming three years would bring some calm, even if temporary, to the debt crisis in Europe quickly dissipated. The publication by the European statistics office that Greece's deficit in 2010, at 10.5 percent, was significantly greater than forecast (9.6 percent, by the European commissionership) and a rise in the debt level to 142.8 percent of GDP at the end of 2010, led S&P to reduce Greece's debt rating by two levels to B-. The European Union commissioner for monetary policy, Olli Rehn, said that the situation in Greece is especially serious, and that Greece's economy is expected to contract by 3.5 percent this year.

In addition, rumors around Greece's desire to leave the Euro bloc (which were denied by Greece and Germany) again raised questions regarding the ability of countries on the periphery of the Euro bloc to avoid, in the end, bankruptcy. The head of the European division of the International Monetary Fund warned of an expansion of the debt crisis in Europe to its core countries and developing markets in Eastern Europe, and expressed willingness to expand the aid to Greece if that country would ask, but pointed out that Greece has the ability to raise hundreds of billions of euros through privatizing assets held by its government, a step that Greece should have already taken according to the first agreement. Market assessments are that Greece cannot allow itself to actually separate from the euro bloc, and in effect is trying to pressure the major countries in Europe to accept easings in aid – since Greece's abandonment of the euro bloc would hurt not only it but the entire bloc. According to BIS figures, European bank exposure to Greece was about €100 billion. According to investment house estimates, Greek banks hold about €50 billion in Greek bonds and their collapse would put other banks on the continent at risk, and would be liable to create a chain reaction which would jeopardize the stability of the entire banking system in Europe. In addition, a Greek bankruptcy will lead to a significant loss for the ECB, which is exposed to Greece with about €200 billion which are funded primarily by Germany and France, and would raise the cost of raising debt for the other PIGS countries, and as such would be likely to weaken and even threaten the euro and the entire bloc. In light of this, investment houses believe that the threat of Greece leaving will lead to expanding the extent of the aid by an additional €60 billion which should cover Greece's debt payments through the end of 2013. Despite the expectations of expanded aid to Greece, a lack of investor confidence in Greece's ability to rebuild is expressed in the inverted yield curve (with a two-year yield of 25 percent) and the fact that 85 percent of respondents to a Bloomberg survey believe that Greece, at one point or another, will be forced to default. In addition, the gaps between the major economies and peripheral economies of the euro bloc are widening. First quarter growth in the euro bloc surprised to the upside (2.5 percent on an annualized basis, compared with a forecast of only 2.2 percent), but this was due to Germany which surprised with annualized growth of 5.2 percent, which compensated for Greece which contracted 4.8 percent (as opposed to growth of 3.2 percent in the last quarter). The inflation rate in the euro bloc continues to rise, and in April reached 2.8 percent in annual terms. With that, Trichet's speech was seen as crucial and another interest rate hike is not expected before July.

Emerging markets

China also appears to be showing signs of a slowdown this month (relative to its terms of growth) with a drop in industrial production, in consumer sales, and its purchasing managers' index in the manufacturing sector. This slowdown did not show up in a moderation of inflation, which remained high and fell less than expected to 5.3 percent in April. This led the central bank to raise its reserve ratio this month by 50 basis points, the fifth rise this year.

Capital markets

World stock markets were influenced by the debt crisis in Greece much more than by European growth figures which were a pleasant surprise. The falls began after the US announced the elimination of Osama bin Laden, which led to a rise in the level of risk aversion around the world, with the MSCI World Index down 2.3 percent and the emerging market EMCI Index down 6 percent since the last monetary survey. At the same time, bond markets showed a drop in yields against the background of risk aversion and investors seeking a safe haven, and US yields fell 25-30 basis points in the 5-10 year range, and in Germany there was a drop of 15-20 basis points in the same range. The EMBI spread widened during the period surveyed, from 265 to 281.8.