



BANK OF ISRAEL
Office of the Spokesperson and Economic Information

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Governor Amir Yaron

G30 Panel: Global Economic and Monetary Challenges

I am unable to be with you today in view of the war that has been launched on Israel. However, it is important for me to deliver a few statements and comments that I prepared dealing with the current situation in Israel and more broadly with issues related to the conduct of monetary policy.

Let me start with the situation in Israel and to explain the economic measures taken so far by the Bank of Israel.

As was reported, early this past Saturday morning, while Israel was in the midst of holiday celebrations, thousands of terrorists belonging to Hamas in the Gaza Strip launched a murderous attack on many communities and towns in the southern part of in Israel, breaking every elementary law of humanity and morality. Their rampage of murder included the killing of children in front of their parents, the killing of parents in front of their children, the murder of elderly people, of entire families, beheading of babies, the slaughter of hundreds of young people celebrating at a music festival focused on peace, setting houses on fire with their owners inside, the desecration of bodies, and the kidnapping into the Gaza Strip civilians, babies, children and elderly. These actions are nothing but terrible inhuman crimes.

So far, the number of murdered victims stands at more than 1,300. Several of the murdered are relatives of Bank of Israel employees. And there are thousands of wounded and many kidnapped.

There is no way to soften the awful shock that we all face. This is the reason that Israel has now gone to war against the terrorist organizations – a war that is likely to persist in the coming period. I have no doubt that, like always, Israel will prevail and that we will rapidly reassert what the Israeli public constantly strives for – calm and quiet.

Every war has a considerable economic dimension that includes the impact to the financial markets, and of course with so many reserve soldiers at the front-lines as well as civilians in shelters due to rocket attacks, there is an effect on real economic activity.

The Israeli economy is strong and stable. It has robust and healthy economic foundations. We are a global leader in innovation and technology. The Israeli economy has known how to function and to recover from difficult periods in the past and to return to prosperity rapidly. During Covid we contracted only 1.5% and in 2021 and 2022 we grew by 9.3 and 6.5 percent respectively and were on target to 3+ percent in 2023.

Moreover, Israel entered this event with a very solid fiscal position. Our debt to GDP ratio is just under 60% and a budget deficit of around 1.5% with similar projections for 2024. At this point it is difficult to put exact numbers, but there is no doubt this war will have fiscal implications that will depend on its intensity and duration. However, with the appropriate budget adjustments, ones that I believe are manageable, there should be no major changes to our fundamental fiscal position.

Past experience has demonstrated the resilience of Israel's public finances to military conflicts. During previous conflicts over the last 30 years, the government was able to absorb the cost of additional military and civilian support expenditures within responsible fiscal frameworks, returning rapidly to a declining debt to GDP ratio on the back of strong rebounds of the domestic economy. For example, during the Second Lebanon war in Q3-2006 economic activity slowed but it was followed by a strong recovery in the following two quarters. The fiscal cost, on the expenditure side, amounted to about 1 percent of GDP, the budget was already balanced in 2007, and the debt to GDP ratio resumed its decline. While military excursions are never exactly alike, I have no doubt that the case will be the same this time.

Since the beginning of this terrorist attack, the Bank of Israel is conducting on-going assessments of all economic aspects of the situation. We are monitoring what is

happening in the financial markets, and we are using a variety of policy tools that are available to us to assure the continuing functioning of the markets.

On Monday morning we declared and activated a program to sell up to \$30 billion in foreign exchange and in addition provide up to 15 billion dollars of swap lines. As part of this program, the Bank will act in the market in the near future in order to moderate the fluctuations of the shekel exchange rate and to provide the necessary liquidity for the continued proper functioning of the markets. We don't have a target exchange rate but want to make sure there are no unnecessary fluctuations or overshooting and that markets function well and in an orderly manner.

The high level of the Bank of Israel's foreign exchange reserves—about \$200 billion—and close to 40% of GDP provides us with ample capacity to support the Israeli economy. We have chosen to act early and decisively in order to reduce uncertainty in the financial markets.

Inflation in Israel has declined for the most part in the last several months. It is currently at 4.1% after it peaked at 5.4% in January 2023. The BOI has raised interest rates from 0.1% in April 2022 to their current level of 4.75%. Prior to Saturday market expectations were that inflation will enter the BOI target of 1-3% sometime in Q1-2024 and they have not changed significantly in the past days. It is too early to tell how supply and demand dislocations from the terror attacks will impact immediate inflation—yet in the medium term it is reasonable to expect some slowdown. The biggest risk to inflation in the past nine months and now even more so is the depreciation of the Shekel. The aforementioned programs that we activated are also consistent with supporting meeting the inflation target.

Needless to say, the Bank of Israel will continue fulfilling its function in managing monetary policy and stabilizing the markets, and we will act with all the tools at our disposal in order to achieve these goals.

Acts of violence that target civilians is a global threat that we must confront. All terrorist activities require funding and involve monetary transactions. From this aspect, it is a global responsibility and a necessity to act against the countries that provide cover for terrorist entities, countries that violate basic international norms, to impose severe sanctions and to exclude them from the global economy and world trade. We must

encourage all countries to do more to prevent using their payments systems to finance terror activities. Therefore, I am using this esteemed platform, to call on the leaders of the global economy that are here with us –to stop the money routes and sources of countries and organizations that sponsor terrorism, and act decisively to eliminate the financial flows that are harmful to ourselves and to our global system. This is our moral and ethical obligation.

Professor Amir Yaron , 14/10/23

Governor of the Bank of Israel