GOVERNMENT OF ISRAEL MINISTRY OF FINANCE
OFFICE OF THE ACCOUNTANT GENERAL

Investor Newsletter

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- Israel sets records with largest bond issuance
- 2018 GDP grows 3.2 percent
- 2018 deficit target met at 2.9 percent of GDP

Issuance

On January 9, 2019, the Government of Israel raised €2.5 billion, its largest ever, in the global debt capital markets. Demand for the bonds was roughly €15 billion, the most for a euro-denominated issuance. More than 300 high-quality institutional investors from 30 countries participated in the deal. Israel was the first sovereign in 2019 to announce a mandate for a euro-denominated issuance.

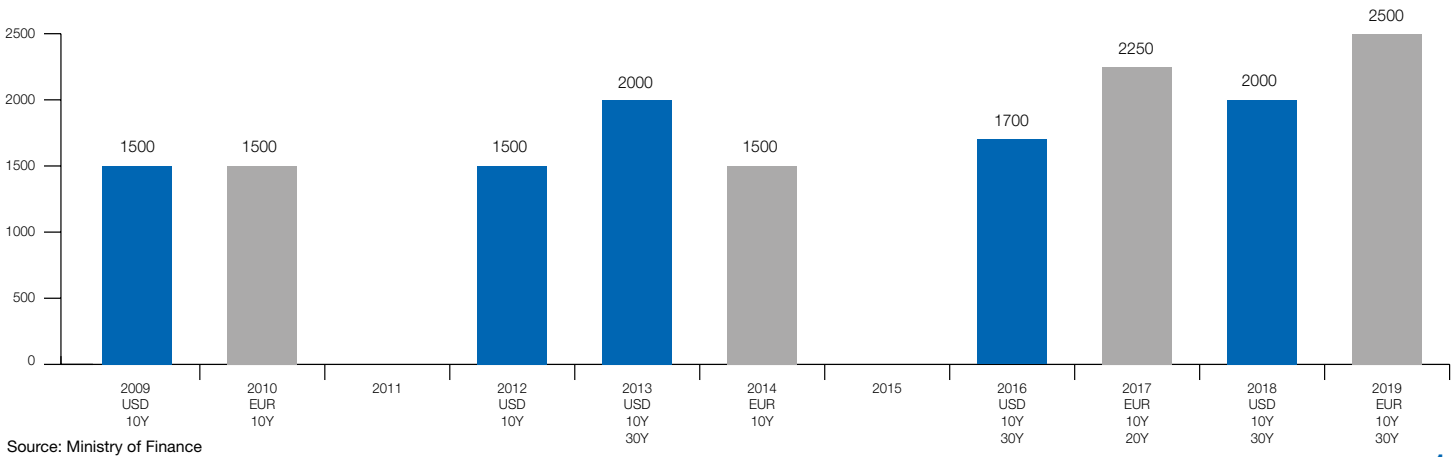
The deal was divided into two tranches: a 10-year and a 30-year maturity. The 10-year tranche raised €1.25 billion with a coupon of 1.5 percent. It was issued at a spread of just 75 basis points above mid-swaps, Israel's lowest-ever cost of funding for a euro issuance. The 30-year tranche raised €1.25 billion with a coupon of 2.5 percent. It was issued at a spread of 115 basis points above mid-swaps. This is the first time the government has executed a 30-year maturity in a euro-denominated issuance. Israel is one of just a handful of non-EU countries to issue euros with a 30-year maturity.

This follows Israel's previous euro deal in 2017, where Israel was the first non-EU country to issue a 20-year maturity. The deal underwriters were Barclays, BNP Paribas, and Goldman Sachs International.

Following the issuance, Accountant General Rony Hizkiyahu said, *"The success of the offering as expressed by the high volume of demand and low margins stems from Israel's economic soundness, which resulted in the raising of Israel's credit rating last summer. The long-term of the bond, the 10-year series and the 30-year, issued for the first time in euros, is a testimony to foreign investor confidence in the Israeli economy."*

Additionally, Israel's Minister of Finance Moshe Kahlon said, *"This successful offering is an expression of confidence in the Israeli economy by international financial institutions, and is further proof of global recognition of Israel's responsibly-managed economy. I congratulate the Accountant General and his team on this success and I am certain there are many more successes yet to come."*

Historical Sovereign Issuances
(USD/EUR, millions)

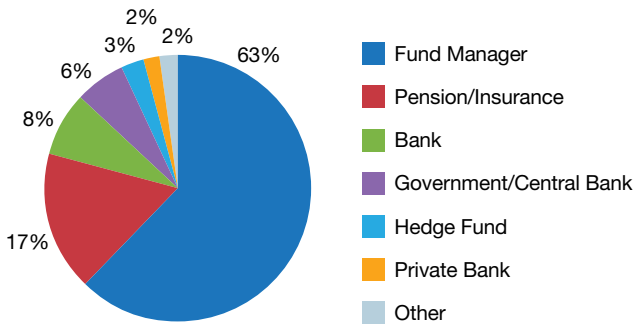


Source: Ministry of Finance

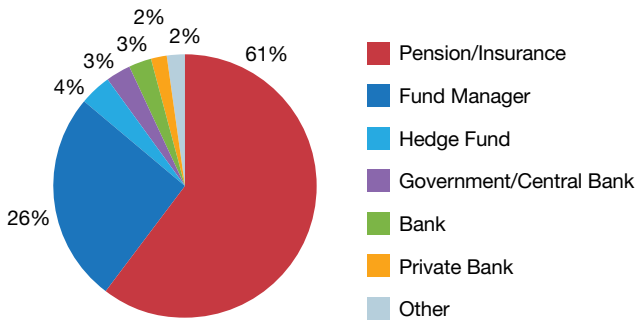
Issuance Breakdown

Source: Ministry of Finance

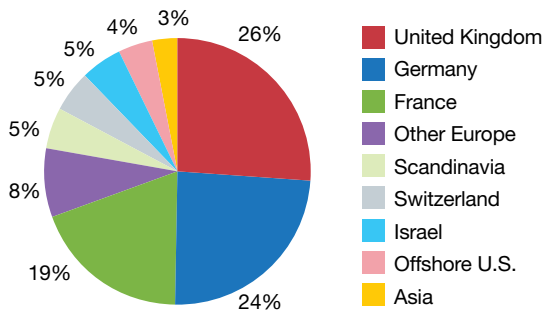
10-Year Investor Type



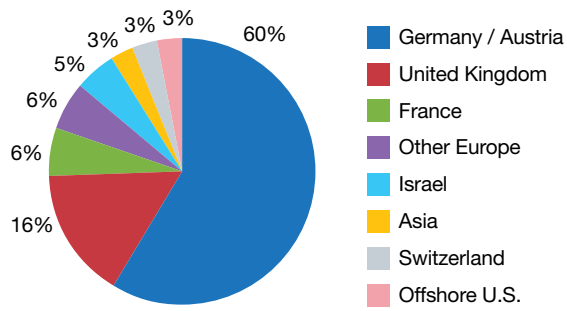
30-Year Investor Type



10-Year Investor Region



30-Year Investor Region



Macro

Israel finished 2018 with an annual GDP growth rate of 3.2 percent.[1] In fact, its annual GDP growth rate has averaged more than 3 percent since the year 2000. Over the same period, the OECD has averaged less than 2 percent annual GDP growth. During the past five years, Israel has averaged just over 3.4 percent; whereas the OECD averaged just over 2 percent.

Of the total 3.2 percent growth, roughly 2.3 percent can be attributed to private consumption. The growth of private consumption results from a strong economic foundation consisting of record low unemployment of 4.1 percent (as of November 2018) with a steady participation rate; real wages rising more than 2 percent per year; a strong shekel; a current account in its 16th year of surplus; a strengthening net creditor position, and a GDP per capita of more than $40,000 and rising. It is most impressive that GDP per capita rose more than $6,000 over the course of the past five years given its annual population growth rate of nearly 2 percent. Israel's GDP per capita is higher than that of the OECD average, Korea, Japan, the UK, and France.

Israel's Central Government debt-to-GDP ratio has been on a long-term downward trend. It declined from 78.4 percent in 2006 to 67.2 percent in 2012, 58.8 percent in 2017, and, as of the first estimate, a slight pickup to 59.7 percent in 2018.[2]

(continued)

1 According to preliminary estimates
2 Preliminary estimate; Press Release: https://www.gov.il/he/departments/news/press_30012019

Macro (continued)

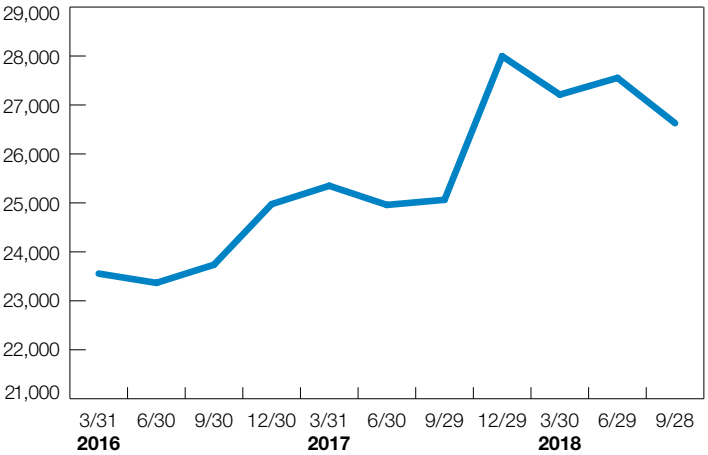
Maintaining a low debt-to-GDP ratio has been a significant goal of the government's fiscal policy-making. From 2008 to 2018, Israel led advanced countries in the reduction of debt-to-GDP. During this time, this important ratio was reduced by 10.9 percentage points. Keeping an economy growing by more than 3 percent annually, however, requires finding innovative paths to growth and improving productivity. These priorities are exemplified in specific government spending programs, such as infrastructure. The budget for the Ministry of Transportation, for example, has increased 80 percent since 2010.

While raising expenditure in the near term, along with a depreciation of the shekel and a rise in inflation, resulted in a slight uptick in debt-to-GDP in 2018, the ratio remains below its 2016 level. Israel's policy makers are mindful of the tradeoff of using expenditure to fuel long-term growth while simultaneously trying to keep the government debt burden under control. The government's goal of growing the economy, concurrent with a downward trend of debt-to-GDP has had positive results in recent years. This continues to be a goal for the future as well.

Imports, rising faster than exports, narrowed Israel's trade balance surplus in 2018. In addition to low oil prices and the strength of the shekel, imports were strong due to the increase in investments for natural gas field development and expansion of a large multi-national company's R&D center. As a result of these investments, we expect to see exports accelerate in the coming years.

Israel Trade Balance

(Goods and Services, USD Millions,
Not Seasonally Adjusted)



Source: Central Bureau of Statistics

Deficit

Israel's budget deficit hit its target of 2.9 percent of GDP in 2018. The Government of Israel has met or beaten its deficit target in each of the past six years by closely adhering to two fiscal rules. First, it establishes an annual budget deficit target that takes into account expenditure and expected revenues. Second, the government employs an expenditure rule. This rule limits the amount of additional spending the government can make year-over-year. It is derived from an equation that is implemented with the creation of a budget.[3]

When calculating deficits, both revenues and expenditures are taken into account. On the revenue side, it can be challenging to forecast future revenues as no one can predict if large transactions will be conducted in any given year. This can be doubly challenging with Israel's biennial or early budget planning. The past few years have seen many large "one-off" transactions including Google's acquisition of Waze and Intel's acquisition of Mobileye. These were positive surprises that brought in larger-than-expected revenues, allowing the government to come in soundly under the deficit target. While there were also major acquisitions in 2018, such as PepsiCo's purchase of SodaStream and IFF's purchase of Frutarom, the revenues from these acquisitions, if any, were not realized in 2018. Given there were no significant surprises, revenues came in more or less at expectation.

On the expenditure side, Israel continues to be fiscally conservative. To ensure strict enforcement of expenditures, each ministry's Controller is an employee of the Accountant General's Department, from the Ministry of Finance, and all spending is closely monitored. In 2018, as was the case in previous years, expenditure was fully executed in line with the planned budget. This, along with expected revenues, resulted in Israel meeting its target.

In the past few years, when revenues came in higher than expected and Israel found itself below the deficit target, questions arose about why the government does not spend more to meet the target. The answer again speaks to the fiscal conservatism of the government. Even when revenues are unexpectedly high, fiscal prudency remains paramount. In such cases, the expenditure rule is followed and the extra proceeds are used to pay down outstanding debt, contributing to the lowering of debt-to-GDP over the long term.

3 Real growth of government expenditure may not exceed: the average population growth rate of the last three years + (50 percent / debt-to-GDP ratio)

Monetary

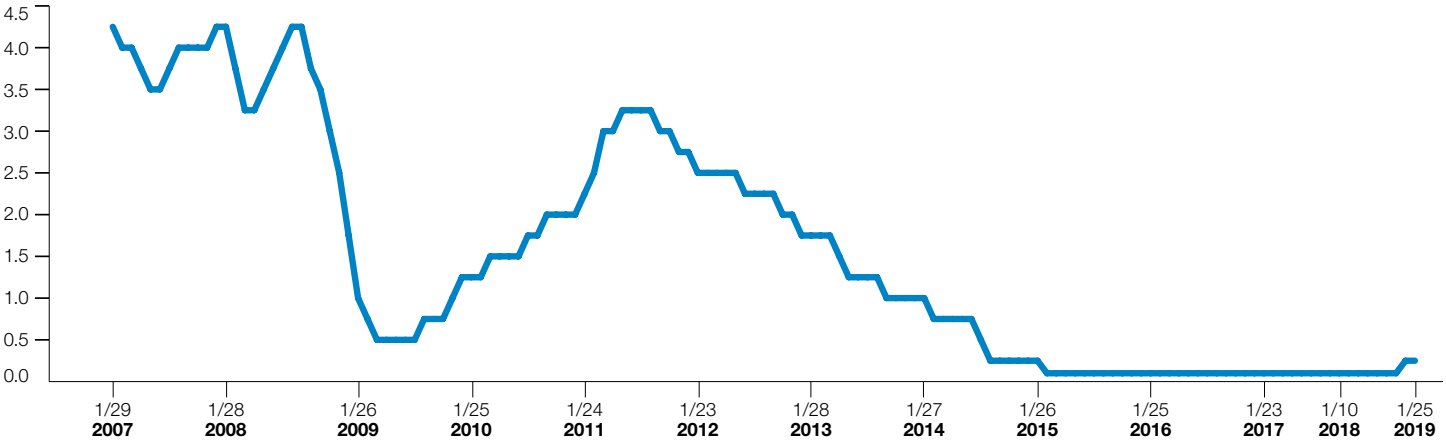
On January 7, 2019, the Bank of Israel announced the decision to keep the base interest rate unchanged at 0.25 percent. During the prior meeting, on November 26, 2018, the interest rate was raised from 0.1 percent to 0.25 percent. This was the first interest rate move since 2015 and the first rate hike since 2011. The inflation rate at the end of 2018 stood at 0.8 percent, just below the Bank of Israel's target range of 1 to 3 percent.

In December 2018, the Bank of Israel announced the end of its foreign exchange purchasing program that was implemented to offset the exchange rate effects of Israel's emerging natural gas production. The program, beginning in 2013, comes to a close as Israel's sovereign wealth fund, The Fund for Israel's Citizens, is expected to begin operating next year. The Fund will invest in non-shekel assets abroad with the proceeds that the state receives from levies on profits from natural gas, oil, and other national resources.

The Bank of Israel, however, maintains the right to be active in the foreign exchange market. This important monetary tool may be used in cases of exchange rate fluctuations that are not in line with fundamental economic conditions or when they view conditions in the foreign exchange market are disorderly.

Also in December 2018, Professor Amir Yaron became Israel's tenth Governor of the Bank of Israel. Born in Israel in 1964, Governor Yaron earned his doctorate in Economics from the University of Chicago. His thesis advisor was Lars Peter Hansen, recipient of 2013 Nobel Prize for Economics. Governor Yaron earned his bachelor and master's degree (both in Economics) from Tel Aviv University. Governor Yaron has held numerous academic appointments and has been published widely in fields such as asset pricing, risk-return strategies, and macroeconomics and finance. From 2009 until his Governorship, he was the Robert Morris Professor of Banking and Finance at the Wharton School of Business at the University of Pennsylvania. His inaugural address from his appointment ceremony may be found **here**.[4]

Bank of Israel Base Rate



Source: Bank of Israel

4 https://www.boi.org.il/en/NewsAndPublications/PressReleases/Pages/24-12-18.aspx

Elections

In April 2019, Israel will hold elections for the 21st Knesset. In Israel, governments operate on four-year terms, although elections may be called early. In December 2018, the Government called for early elections. Although the current coalition will have governed for four calendar years, the original date for elections was scheduled for November 2019.[5]

Israel holds closed-list proportional elections. The Knesset is comprised of 120 seats; the current minimum threshold for a party to enter the Knesset is 3.25 percent of the state-wide vote. A government is formed when a majority coalition of 61 or greater seats is achieved.

The outgoing government was the fourth led by Prime Minister Benjamin Netanyahu of the Likud Party. Other governing coalition parties included: Jewish Home, Kulanu, Shas, and United Torah Judaism.

5 This is due to the law that elections take place in the Hebrew month of Kislev (which generally falls toward the end of the calendar-year).

Other News

Israeli High-Tech Firms Raise Record $6.47 Billion in 2018

Israeli private high-tech companies raised a record $6.47 billion in 2018, up 17 percent from 2017, according to the Israel Venture Capital Research Center (IVC) and ZAG law firm. In the fourth quarter, high-tech firms raised $1.82 billion, an increase of 8 percent from the third quarter, the IVC report showed.

“Most of the capital was raised by well-established software companies with annual revenues of up to $10 million in the verticals of AI (artificial intelligence) and cyber security,” said Marianna Shapiro of IVC.

2018 was a strong year, in particular, for cyber security companies, which raised $1.08 billion. Life science companies raised $1.2 billion.

“Over the course of 2018, there was a noticeable trend of foreign funds and investors, whose investments in Israel rose by more than $1 billion compared to last year,” said Shmulik Zysman, managing partner at Zysman, Aharoni, Gayer & Co.

— *Jerusalem Post*

https://www.jpost.com/Israel-News/Israeli-hi-tech-firms-raise-record-64b-in-2018-576828

Other News

Egypt to Begin Importing Israeli Gas in 2019

Egypt's Dolphinus Holdings has announced plans in 2019 to start importing gas from Israel. Under the agreement, Egypt will buy $15 billion worth of gas over ten years.

According to Reuters, "Imports will start in small quantities and will gradually increase to reach their climax in September 2019." Partners in Israel's Tamar and Leviathan offshore gas fields, which include Delek Group, Isramco and Ratio, said that they will supply Dolphinus with close to 64 billion cubic meters of gas over a decade.

— *Haaretz*

https://www.haaretz.com/israel-news/egypt-to-begin-importing-israeli-gas-in-2019-1.6343222

More Than 4 Million Tourists Visited Israel in 2018

More than 4.1 million tourists visited Israel in 2018, eclipsing last year's record by 14 percent. Revenue from tourism reached close to $5.8 billion.

Israel Tourism Minister Yariv Levin attributed the historic high to new "marketing strategy, infrastructure development, the opening of direct routes from new destinations, and creating collaborations with some of the largest travel agents in the world."

This is the second consecutive year Israel has broken tourism records and the tourism ministry is forecasting another record-setting year in 2019. Several global events are scheduled to take place in Israel this year as well as the opening of a new international airport.

In other tourism related news, the leading international market research firm, EuroMonitor, named Jerusalem as the fastest-growing tourism destination in the world.

— *E Turbo News*

https://www.eturbonews.com/242426/over-4-million-tourists-visited-israel-last-year

Amazon to Purchase Israel Startup CloudEnsure for $250 Million

Amazon, the world's largest supplier of cloud services, has announced that it will be buying Israeli startup company CloudEnsure for $250 million. Founded six years ago, CloudEnsure is a cloud computing company that creates business software for disaster recovery, backup and live migration, in the event of a system crash. It places data on multiple clouds operated by providers such as Amazon.

CloudEnsure has raised more than $18 million from leading venture capital firms and strategic investors, including Dell EMC, VMware, Mitsui & Co., Infosys and Magma Venture Partners.

— *Jewish Telegraphic Agency*

https://www.jta.org/quick-reads/amazon-buys-israeli-start-up-cloudendure-for-250-million

Chinese Investment in Israeli Tech is Growing

The vast majority of investment in Israel still originates from the U.S. and Europe, but money from China and the broader Asian region has grown. Companies from Singapore, South Korea and Japan are all, "establishing some beachhead," according to Steven Schoenfeld, founder and CIO of BlueStar Indexes, a firm that develops Israel-focused indexes and exchange-traded funds.

The scope of Chinese investment in Israel covers "pretty much every major disruptive tech sector," Schoenfeld said, including the autonomous and electric vehicle spaces. Many of the major Chinese auto manufacturers currently maintain research and development centers in Israel.

— *CNBC*

https://www.cnbc.com/2018/07/19/chinese-investment-in-israel-technology-is-growing-expert-says.html

Other News

JVP, SOSA Partner with New York on Cyber Initiative

New York City Economic Development Corporation (NYCEDC) announced a new cybersecurity initiative with Israeli venture capital firm Jerusalem Venture Partners (JVP) and startup network SOSA. New York University, Columbia University and Cornell Tech, a joint venture between Cornell University and the Technion Israel Institute of Technology, will also take part in the initiative.

The global cyber center, Cyber NYC, will receive a $30 million investment from the city of New York and will be backed by $70 million in private sector commitments. It will "grow the cybersecurity sector, leverage a roster of world-renowned partners to launch a global cyber center, provide an innovations hub for startups, initiatives to fuel commercialization and research, and new talent pipelines to train the workforce of the future," NYCEDC said in a statement.

"We've convened a world-class roster of partners to help us execute this essential plan, which will help protect the industries and people that make NYC the economic powerhouse that it is today," said NYCEDC President and CEO James Patchett.

SOSA, the global innovation platform connecting Israeli startups, will establish the center in the Chelsea neighborhood. The 15,000 square-foot center will foster collaboration and innovation with corporations, investors, startups, and talent from around the world.

— Reuters

https://www.reuters.com/article/us-usa-cyber-jvp/israeli-vc-jvp-to-partner-in-new-york-city-cyber-center-idUSKCN1MC1OB

— Jerusalem Post

https://www.jpost.com/Israel-News/Israeli-companies-to-lead-establishment-of-New-York-cyber-innovation-hub-568472

Binational Fund to Invest $7.3 Million in Joint U.S-Israel Innovation Projects

The U.S.-Israel Binational Research and Development Foundation (BIRD) Foundation announced that it plans to invest $7.3 million in eight new American–Israeli innovation projects.

The BIRD Foundation was established by the United States and Israeli governments in 1977 and has invested close to $350 million in 974 projects since its creation. The sales of products developed by companies receiving funding have exceeded $10 billion.

New investments include projects in educational and agricultural technology, energy, digital health, medical devices, and homeland security.

The BIRD Foundation funds up to half a project's budget, starting from research and development and ending with the beginning stages of marketing. If the product is successful the foundation gets repaid through royalties.

— CTECH - Calcalist

https://www.calcalistech.com/ctech/articles/0,7340,L-3753815,00.html

Relevant Links

Israel Government Portal
https://www.gov.il/en

Israel's Ministry of Finance
http://mof.gov.il/en/pages/default.aspx

Israel's Government Debt Management Unit
http://mof.gov.il/en/PolicyAndBudget/GovernmentDebt/Pages/default.aspx

Bank of Israel
http://www.boi.org.il/en/Pages/Default.aspx

Central Bureau of Statistics
http://www.cbs.gov.il/reader/cw_usr_view_Folder?ID=141

Tel Aviv Stock Exchange
https://www.tase.co.il/Eng/Pages/Homepage.aspx

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