Financial Immunities

Market Insights

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Global Economy

- More than a decade after the 2008 financial crisis, policymakers are left with very few good tools to fight the next downturn. The fact that historically low interest rates and huge 12 trillion $ bond purchases failed to accelerate growth and revive inflation, raises two questions: Does the global economy face a process similar to Japan's since the early 1990s, and what will be the effects of the prolonged use of unconventional means
- One of the obvious side effects that a decade of easy money has brought is a record 250 trillion $ of government, household and corporate debt. Zero interest rates and high credit availability have allowed the debt mountain to continue to grow to an unprecedented scale of three times global GDP
- Now that monetary policy is losing its influence and heresy thoughts arise as to the benefit of the negative interest rate, the expectation that the burden will pass to governments, embarking with massive fiscal spending, is exaggerated, given the high level of debt, the budget deficits and political disagreements
- Despite the ongoing economic downturn, China's decision makers refuse to join the wave of monetary incentives that characterize all major economies. A long-term conservative approach that seeks to avoid financial risks stemming from credit risk and asset bubble development is at the heart of this policy
- The US and China are negotiating the latest details of “Phase 1” of the trade agreement. The apparent agreement appears to be closer to a ceasefire or non-war agreement than to resolving the conflict, and is likely to allow the parties to bridge until the US election in November, without bringing about an escalation that could lead the global economy to recession

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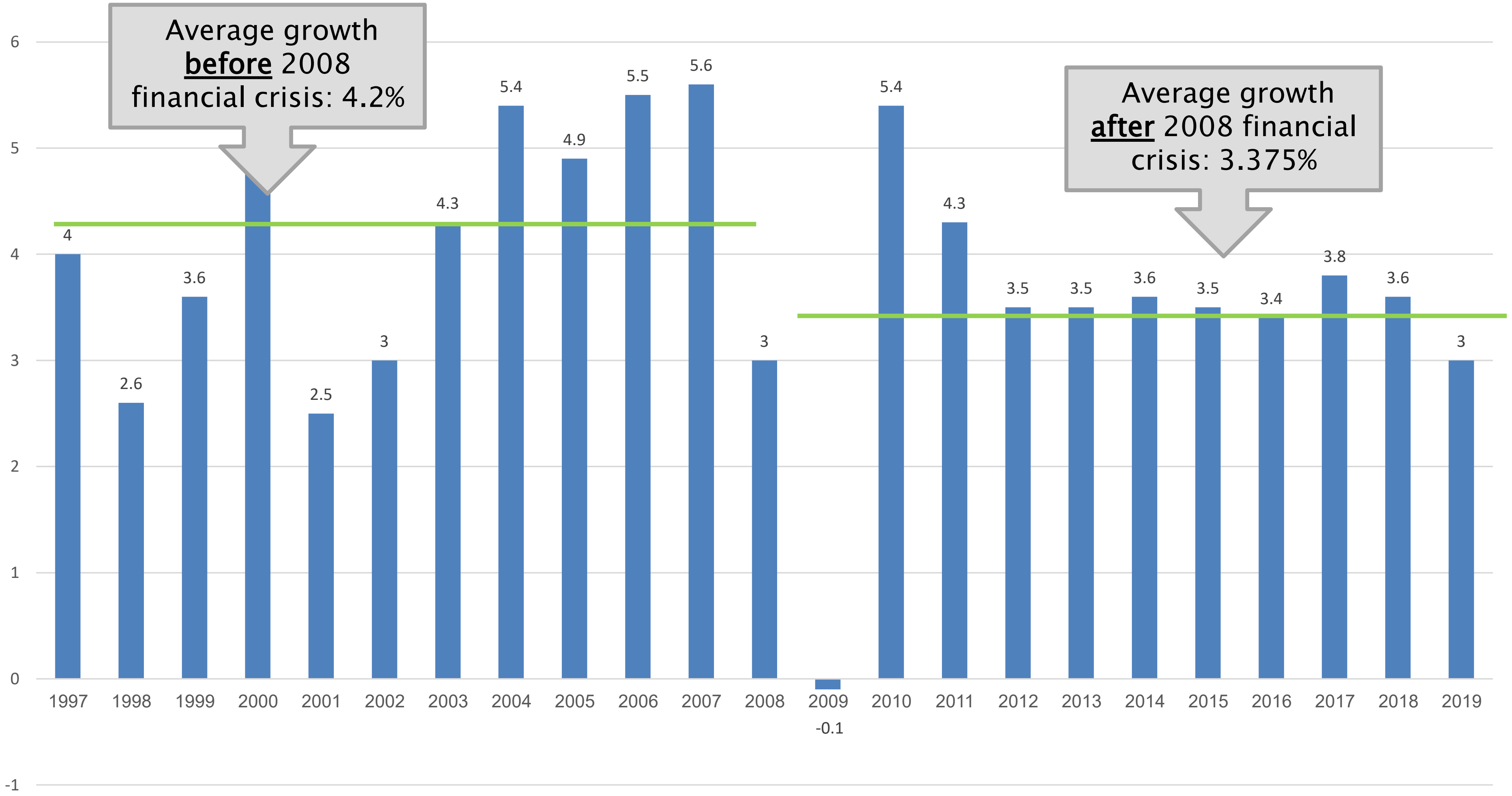
Global GDP



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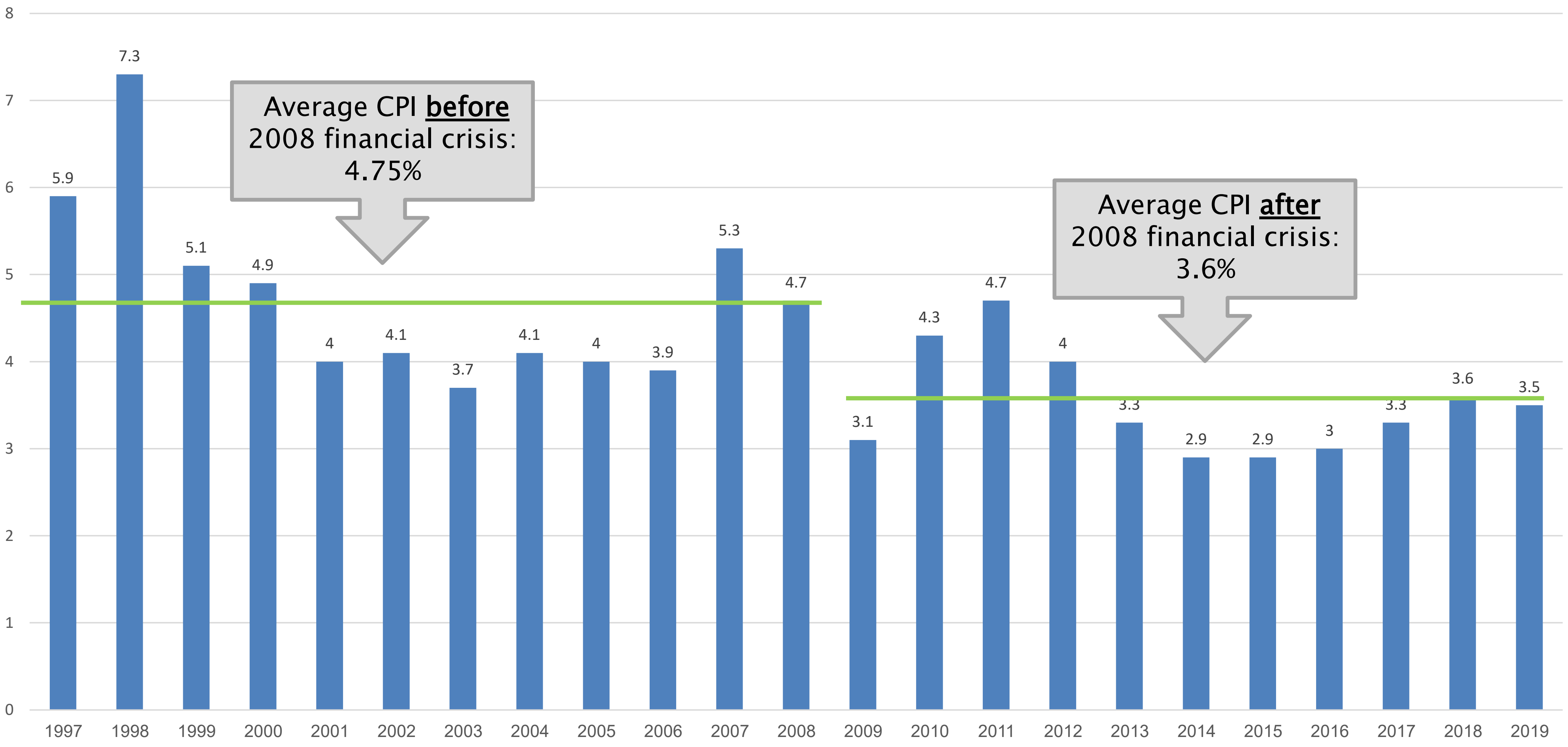
Global CPI



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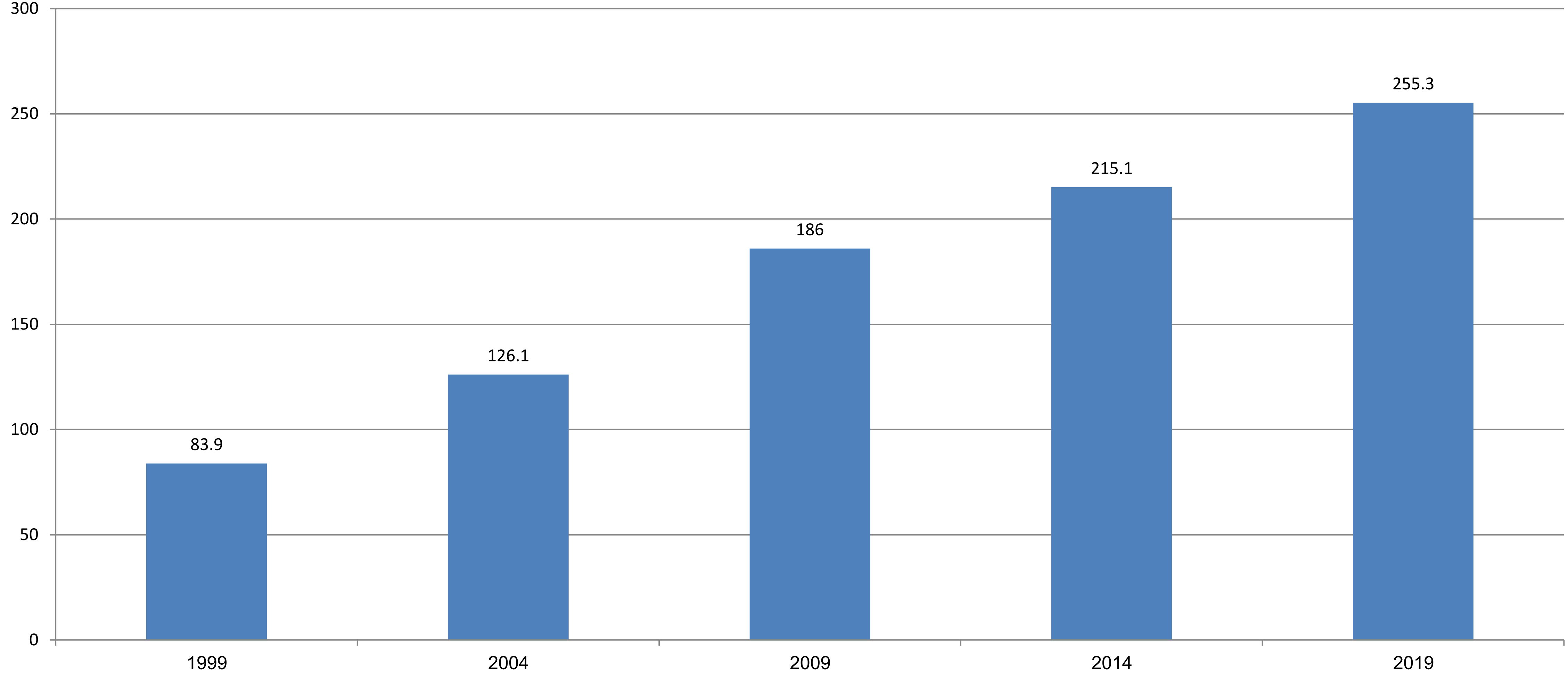
Global Debt

In Trillions USD



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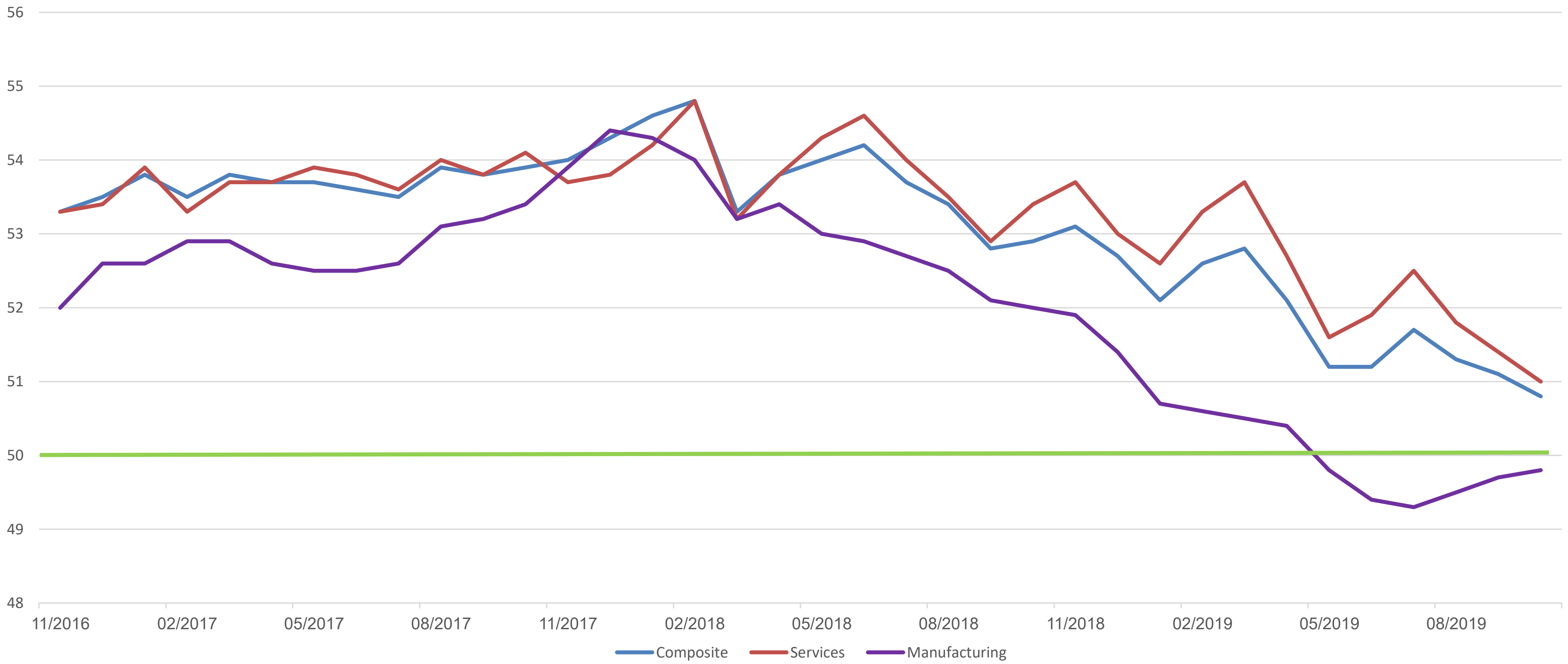
Global PMI



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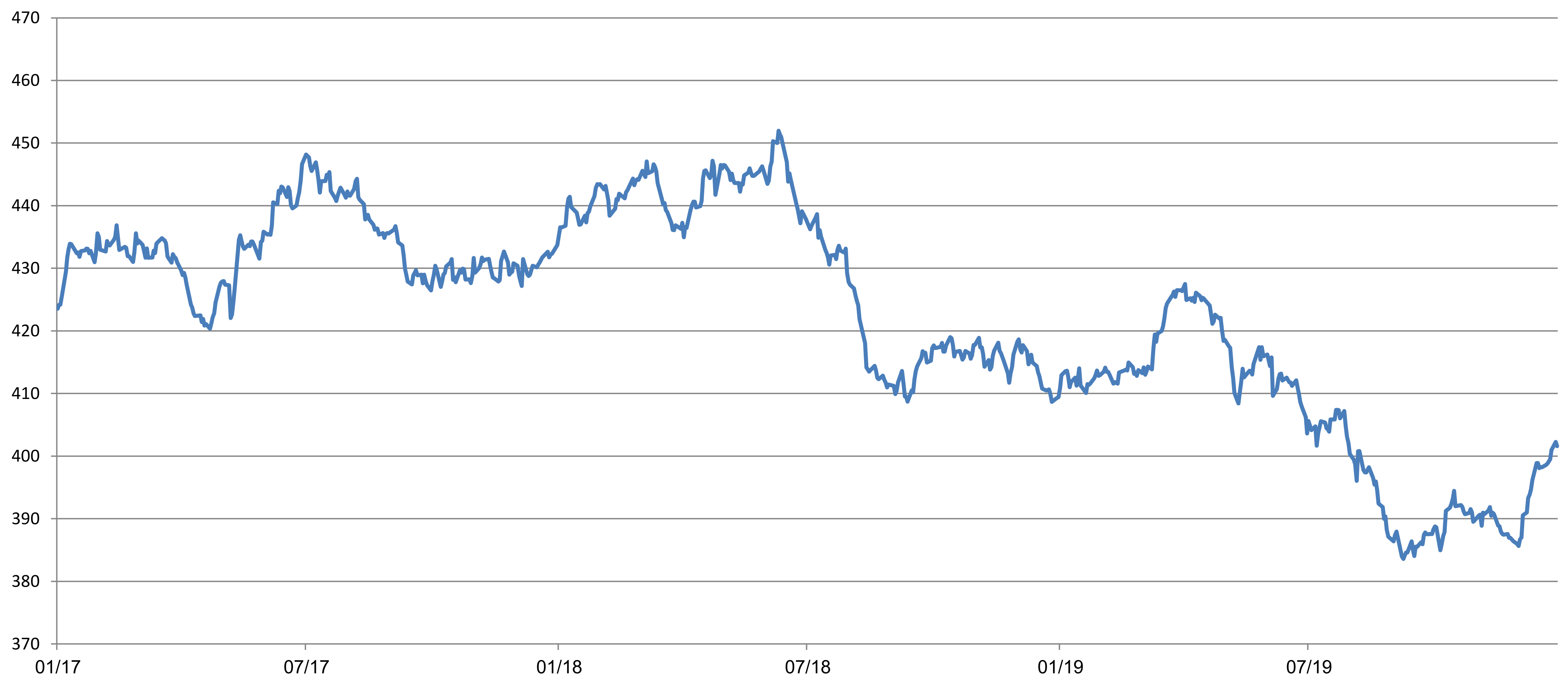
Commodities Index (CRB)



United States

- The US economy is outperforming expectation as the strong labor market and accommodative financial conditions support consumers and small businesses sentiment, which are within reach of the best levels of the economic cycle
- A sector that has made a positive contribution to GDP after a long period of halting is the real estate sector. Homebuilders Index has soared to 20 year high. Housing starts top forecast and permits increased to the highest level since 2007. Indeed, a strong labor market and low mortgage rates push the real estate market forward, while creating a sense of wealth that supports consumer buying intentions
- In another powerful display, the labor market added 266K new jobs in November, with revisions adding 41K jobs for the prior two months. The average monthly job creation pace for the past year stands at 184K, slightly lower than 2018, but still a robust one. The unemployment rate dropped to 3.5%, a 50-year low, and wages rose 3.1% in the past year. All this data back the Fed view that the labor market is strong but not enough to generate wage inflation
- After reducing interest rates three times since the beginning of the year and entering the election year with an economic outlook that remains favorable, the Fed has left interest rates unchanged at 1.5%-1.75% and said that "As long as incoming information about the economy remains broadly consistent with this outlook, the current stance of monetary policy likely will remain appropriate"
- Money market disruptions, which began in September, have since forced the US Central Bank to inject hundreds of billions of dollars of liquidity, a phenomenon that has led to low volatility and increased appetite for risk, but has not solved the fundamental problem. Now the question is whether the Fed can stop intervening without causing chaos to return

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Core Economic Indicator

USA

Economic Indicator	Latest Figure	Reference Period
Growth Rate	2.1%	Q3-2019
Unemployment Rate	3.5%	November-2019
Inflation Rate (Core PCE, YoY)	1.6%	November-2019
Central Bank Interest Rate	1.5%-1.75%	December-2019
10 Years Yield	1.92%	December-2019
Ratio of Surplus in Current Account to GDP	-2.46%	Q3-2019
Ratio of Public Debt to GDP	105.47%	July-2019

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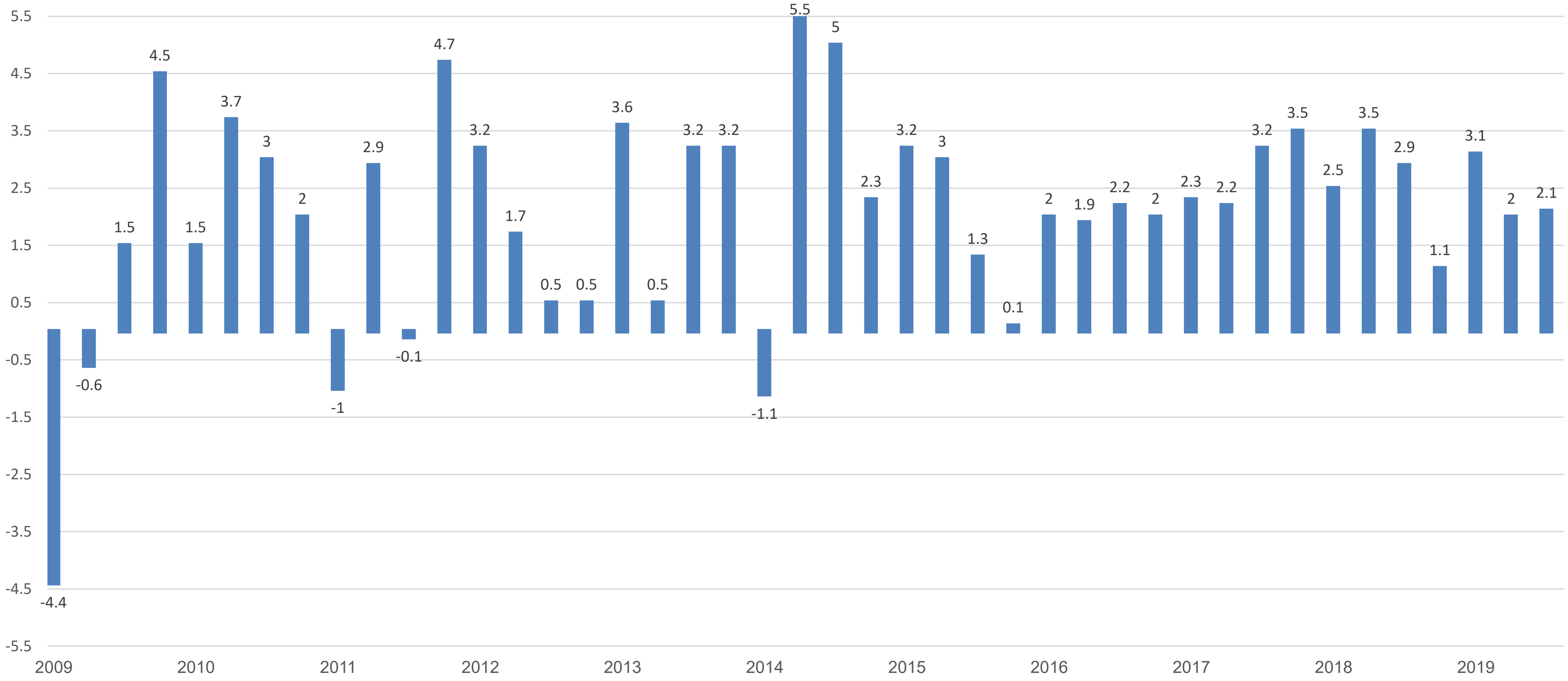
Economic Growth

GDP (Annualized)



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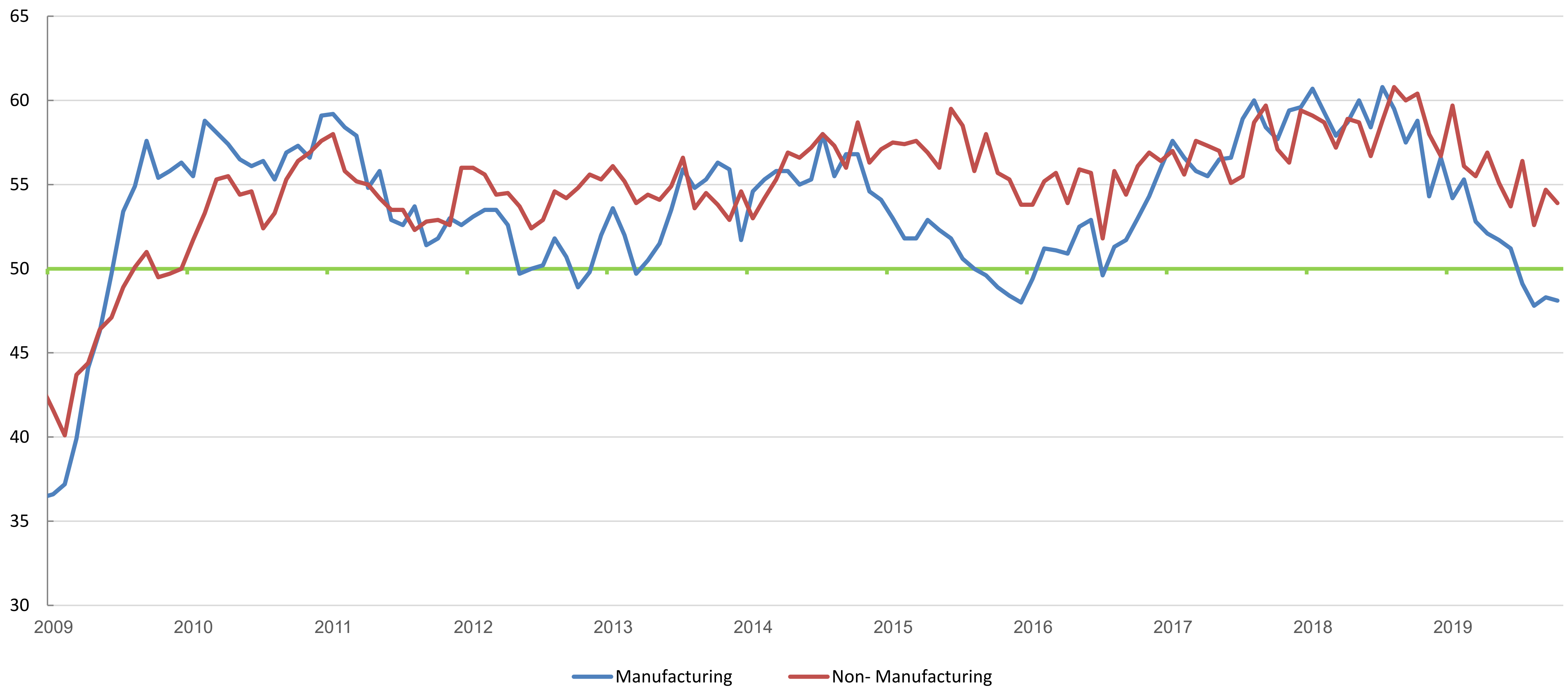
Economic Sentiment

Manufacturing and Non-Manufacturing ISM



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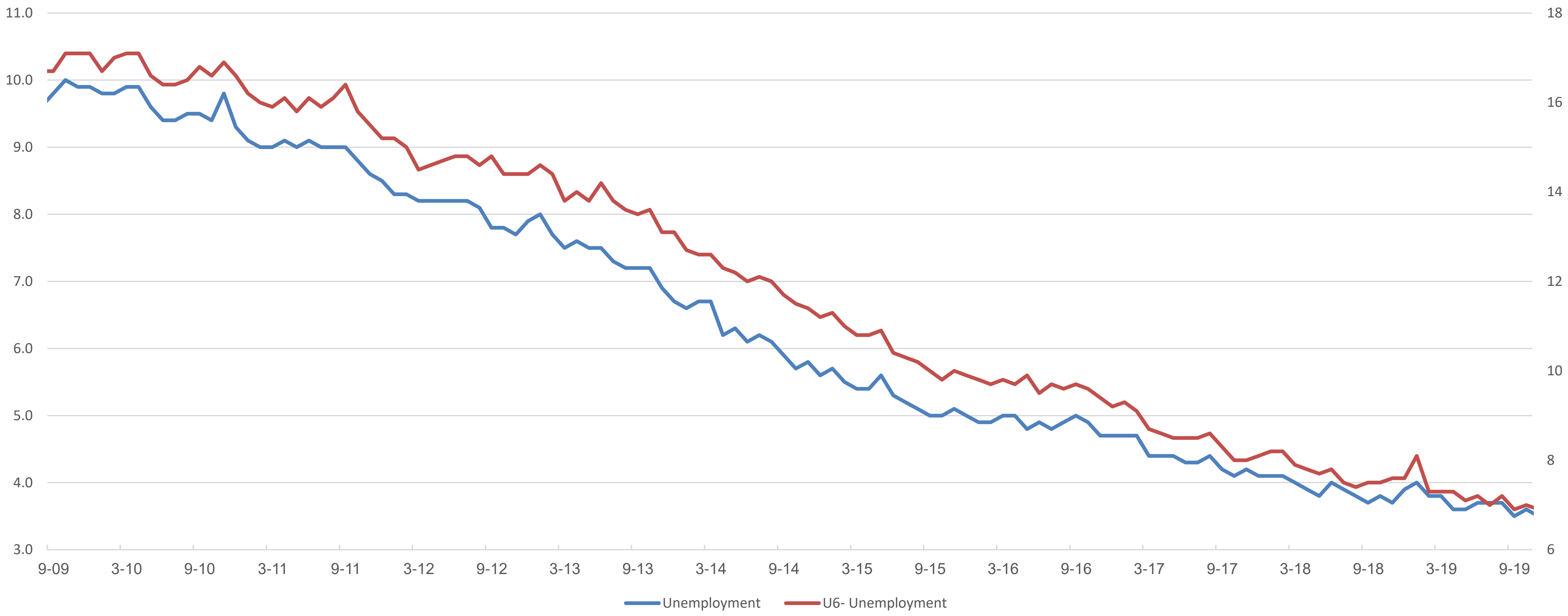
Labor Market

Unemployment Rate (Left) and Under Unemployment Rate, U6 (Right)



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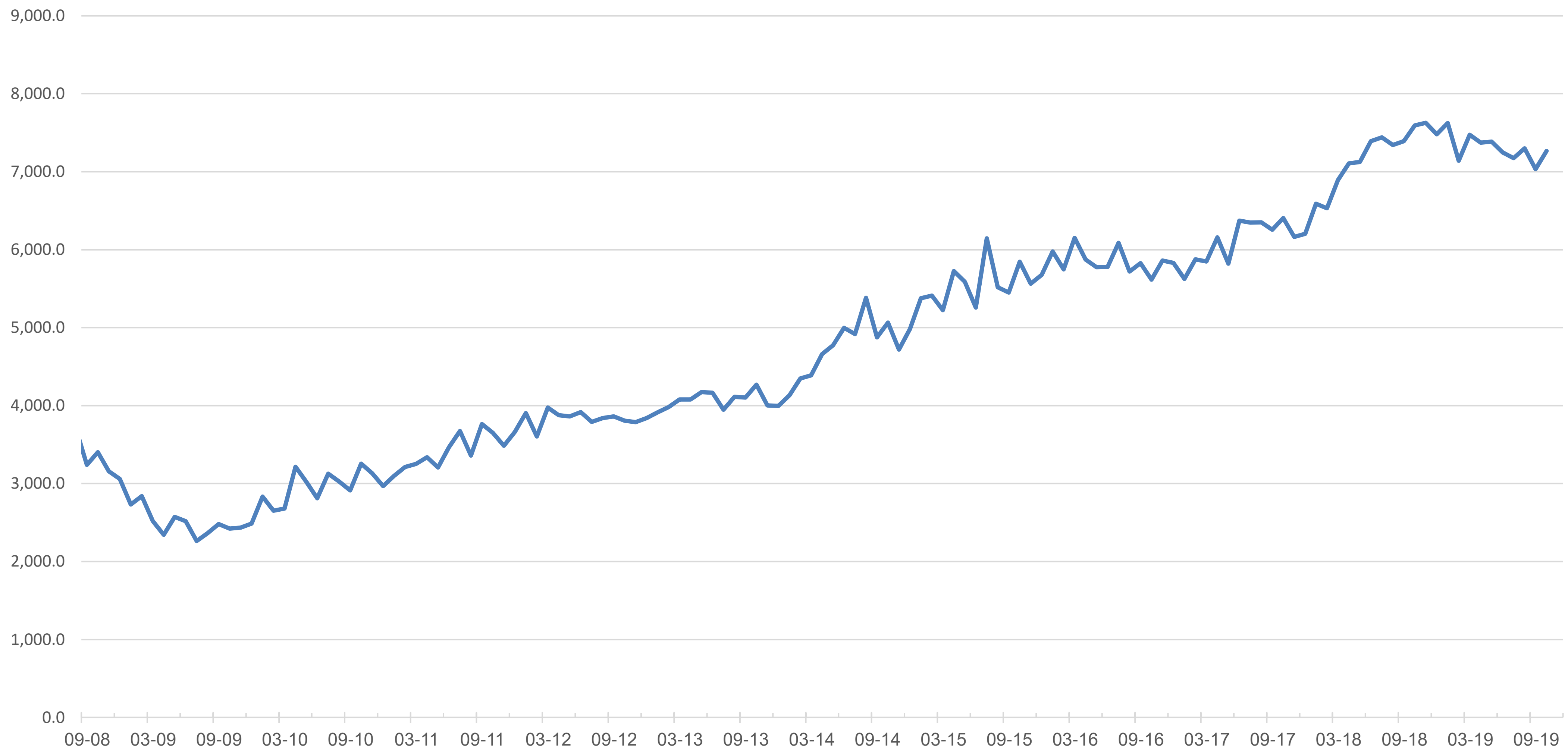
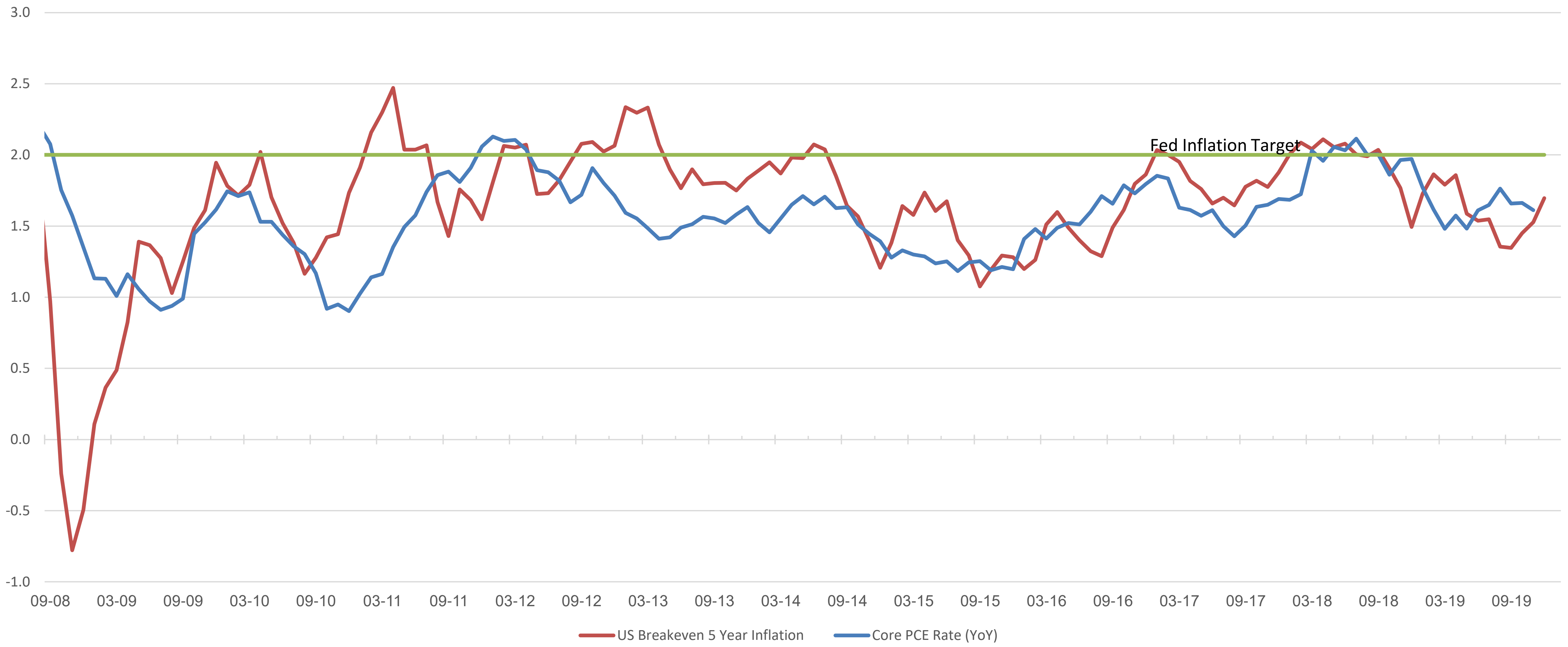
Labor Market

Job Openings



Inflation

Core PCE (YoY) and 5Y Inflation Forecast



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10YR Treasury Yield to Maturity

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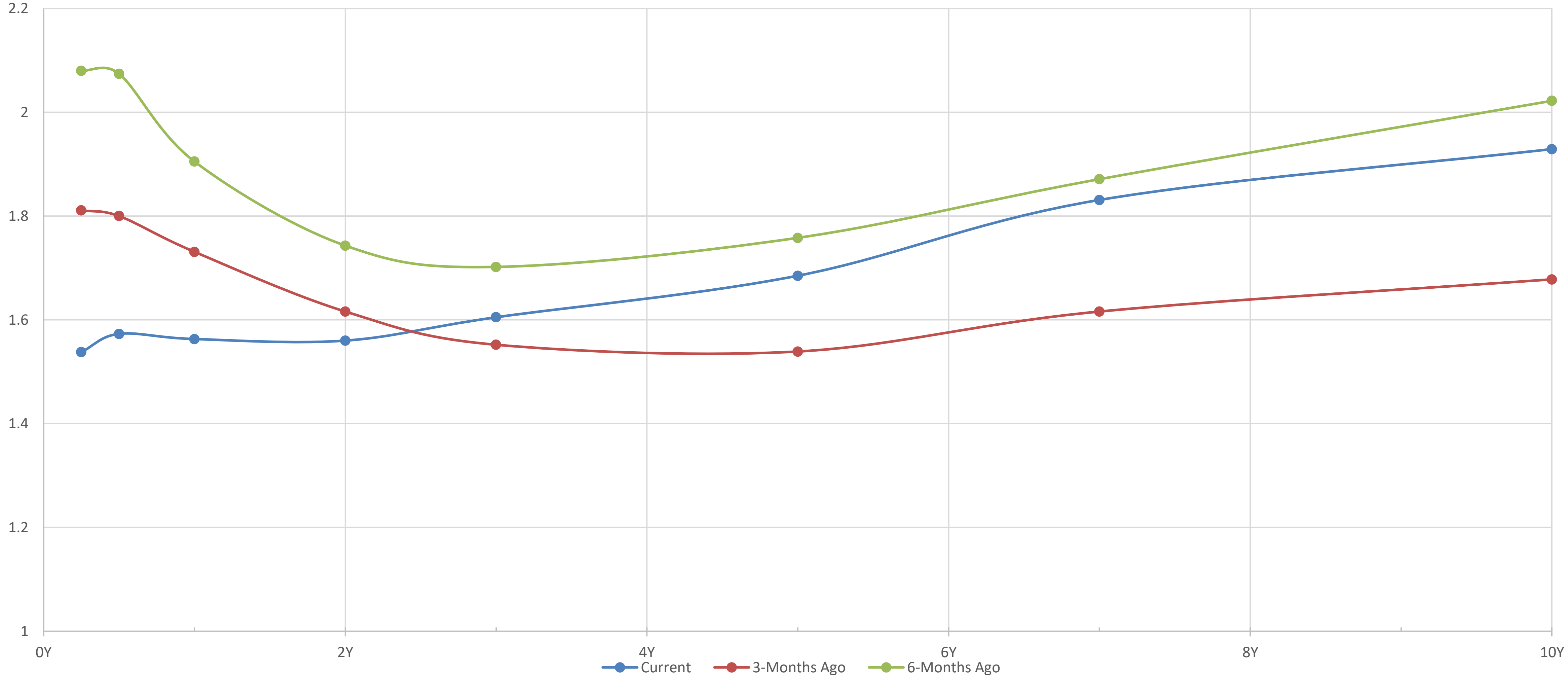
US Treasury Yield Curve



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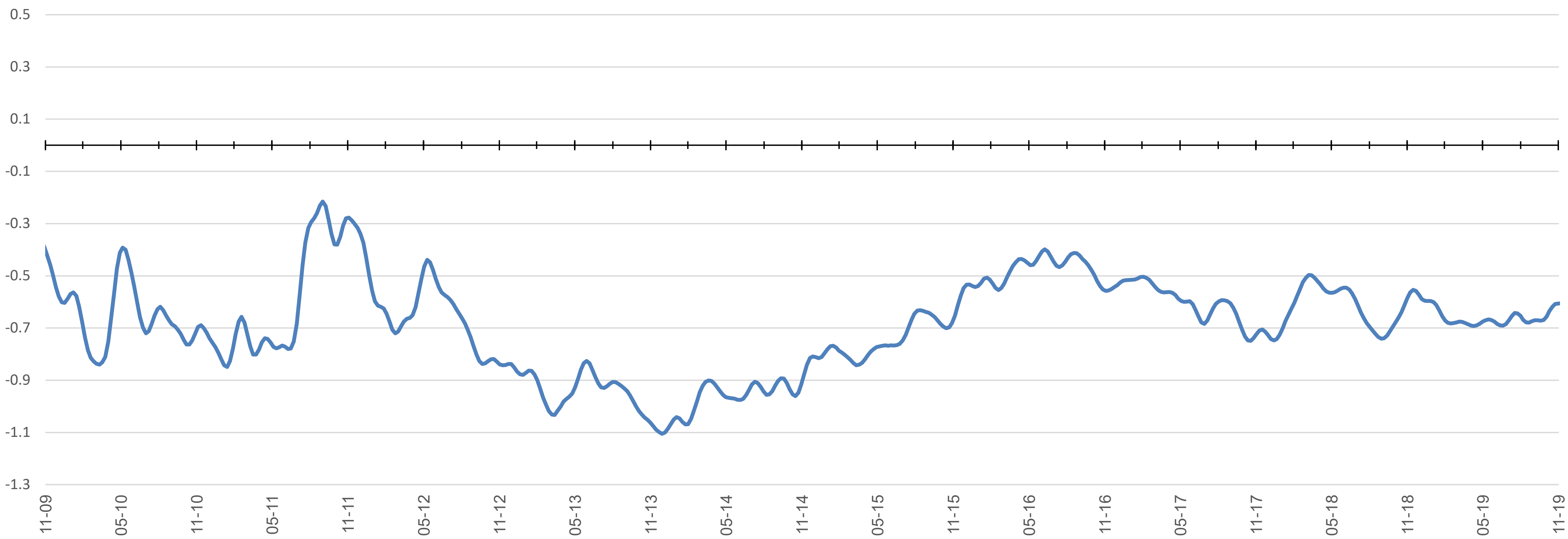
Chicago Feds National Financial Condition Index (NFCI)



The NFCI provides a comprehensive weekly update on U.S. financial conditions in money markets, debt and equity markets and the traditional and "shadow" banking systems. Negative values have been historically associated with looser-than-average financial conditions

US Dollar Index (DXY)

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Citi Economic Surprise

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Eurozone

- After stabilizing at a low level the economic activity in the Euro area is improving mildly as more and more economic indicators are beating early expectations, to an extent that has not been seen for a year and a half

- Despite the slowdown in the economy, the labor market remains strong and unemployment has stabilized at 7.5% since June, the lowest since 2008. Wage growth continues to improve, reaching 2.5%, the highest since the financial crisis

- Despite rising inflation in the Eurozone, it is still well below the inflation target (2%), after rising 1% in the past year and 1.3%, excluding food and energy. For now, there isn't any evident for price pressures as inflation remain persistently weak, however the rise in commodity prices alongside the wage growth might create a price pressures later

- Having provided initial signs of life lately, the European manufacturing sector is signaling that the slump may be bottoming out. The German industry, the biggest in the Eurozone, show signs of stabilization as orders rising, driven by a solid pickup in investment and consumer goods with demand from outside the euro area providing a particular boost

- In her first decision the new ECB president, Christine Lagarde, clung to the path the ECB had set in September and said that she wouldn't reopen the decisions to reduce interest rates and restarting bonds purchases. She also said that she doesn't see negative interest rates as a problem at their current level and initiated a yearlong review of the ECB policy

- A different approach, that cannot be overstated, to the issue of negative interest rates and its impact on the economy can be seen in the decision of the Swedish Central Bank to raise interest rates. The surprising decision to abandon negative interest rates model, that had been in use for 5 years, mainly reflects the concern for the undesirable consequences and damages for the banking and pension systems, arising from the use of

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Core Economic Indicator

Eurozone

Economic Indicator	Latest Figure	Reference Period
Growth Rate	0.9%	Q3-2019
Unemployment Rate	7.5%	October-2019
Inflation Rate (Core, YoY)	1.3%	October-2019
Central Bank Interest Rate	0%	December-2019
10 Years Yield (Germany)	-0.19%	December-2019
Ratio of Surplus in Current Account to GDP	2.67%	Q3-2019
Ratio of Public Debt to GDP	86.4%	Q2-2019

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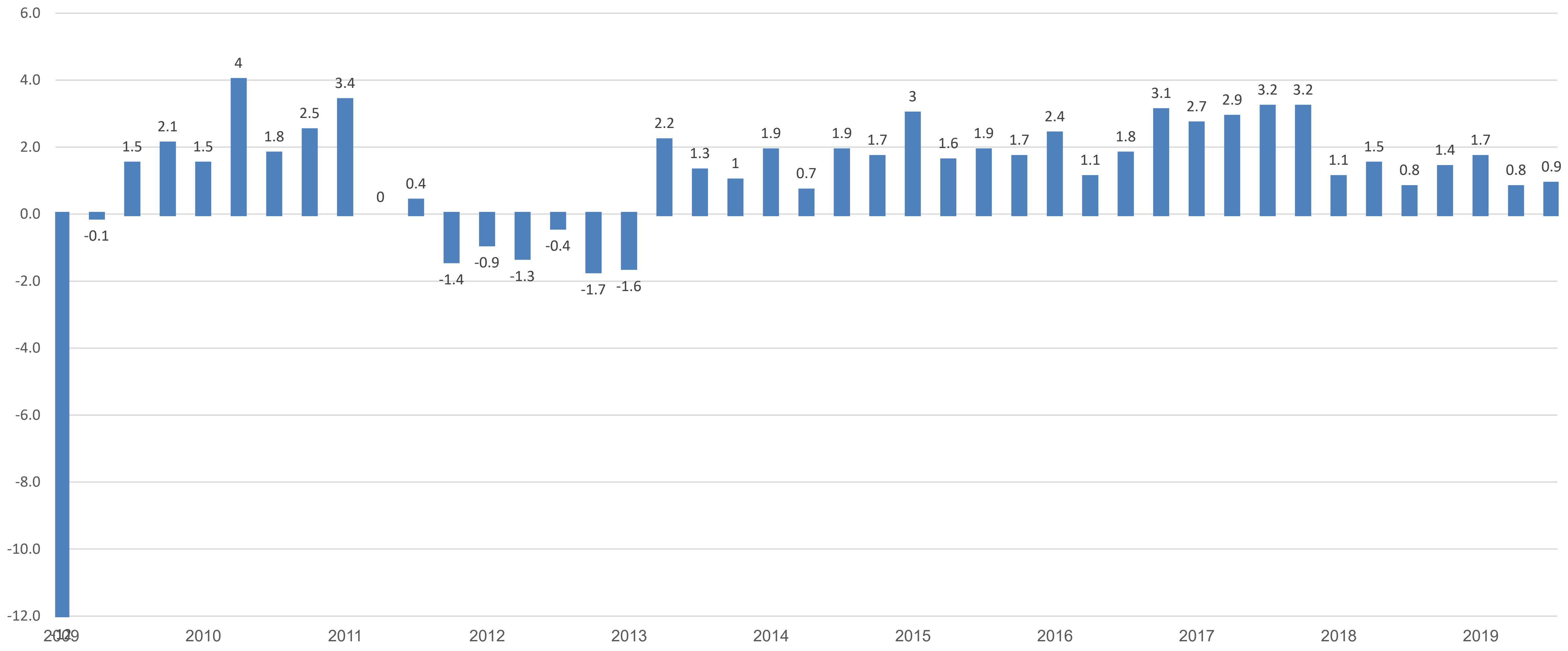
Economic Growth

GDP (Annualized)



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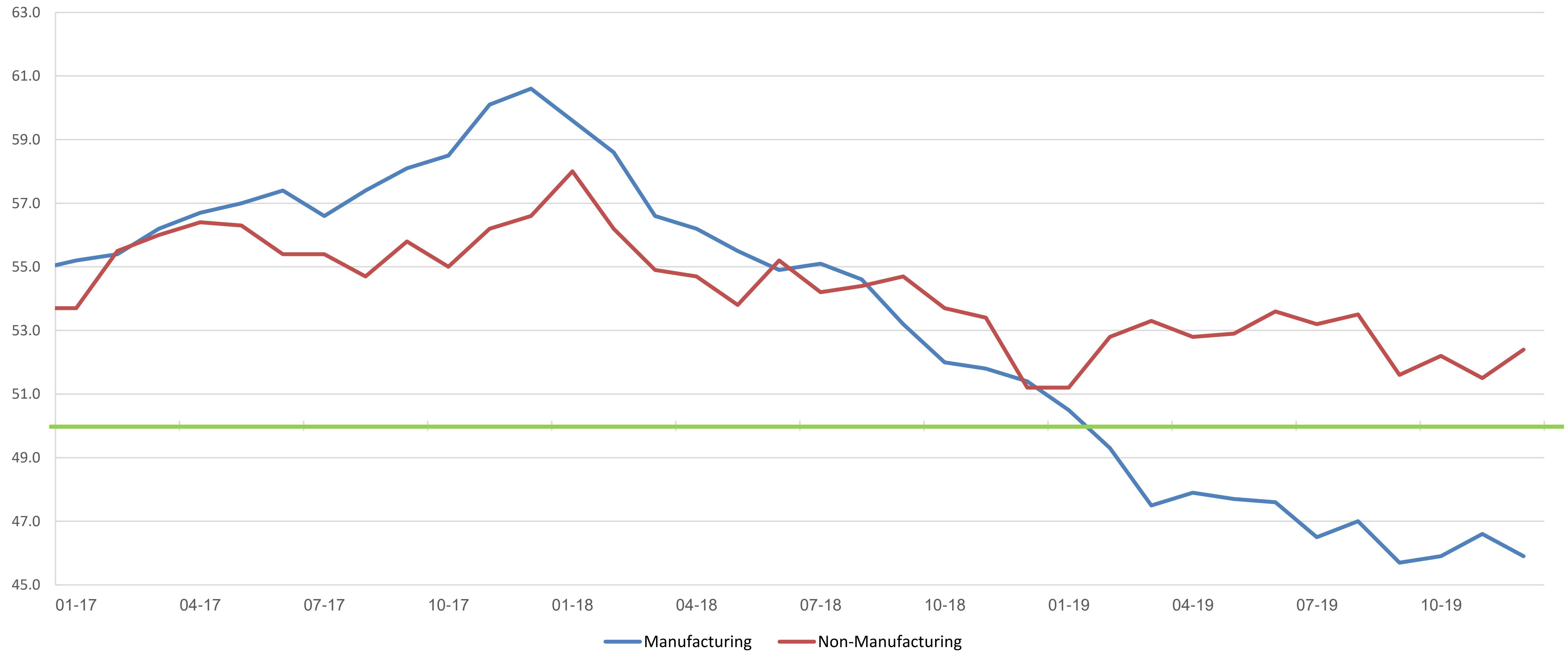
Economic Sentiment

Manufacturing and Non-Manufacturing PMI



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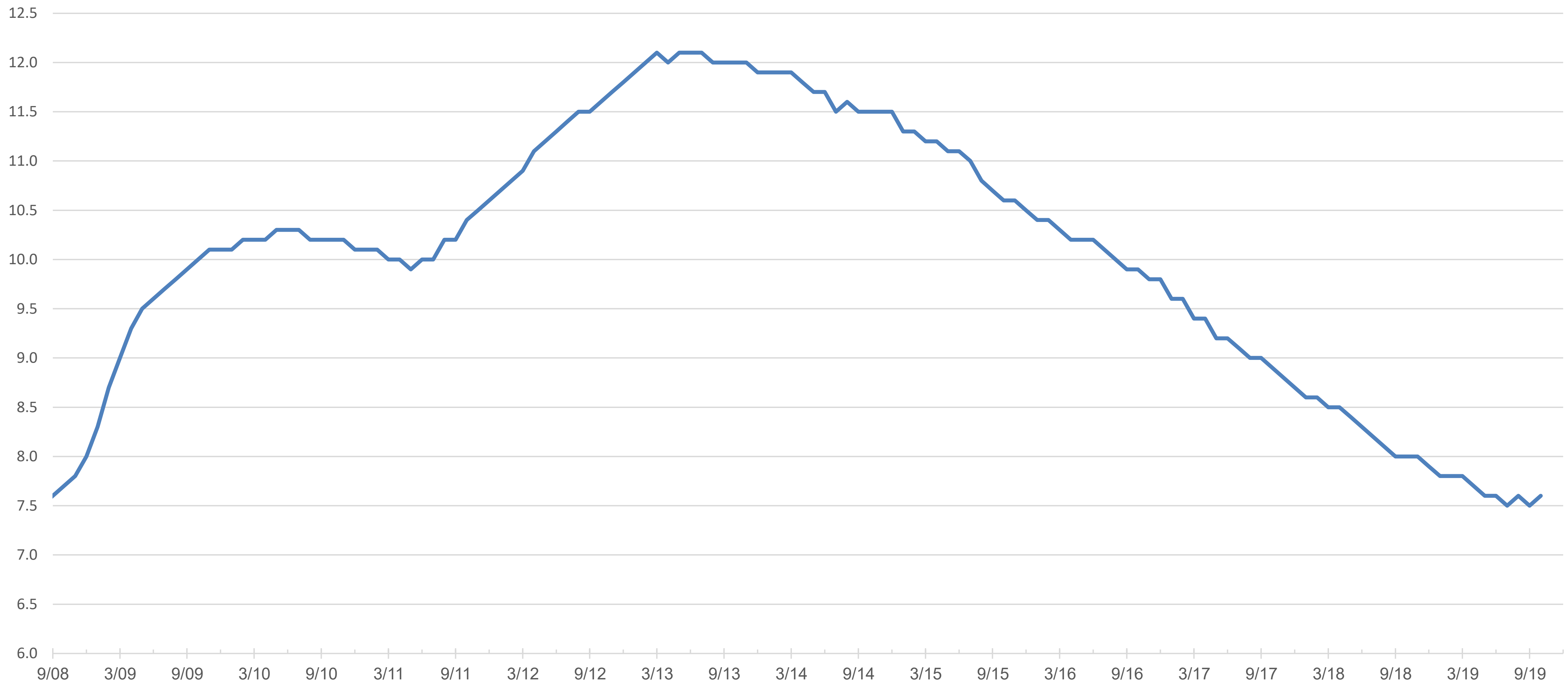
Labor Market

Unemployment Rate



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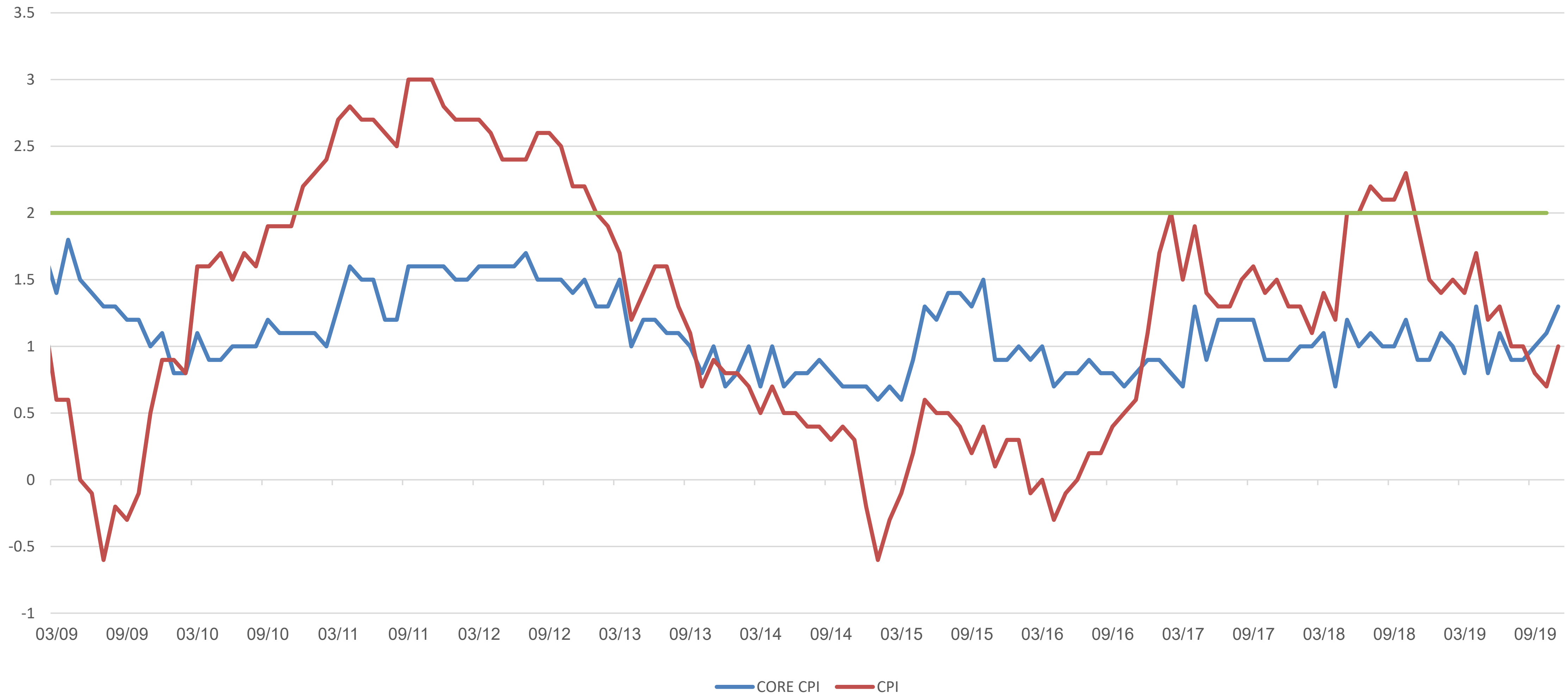
Inflation

CPI and Core CPI (YoY)



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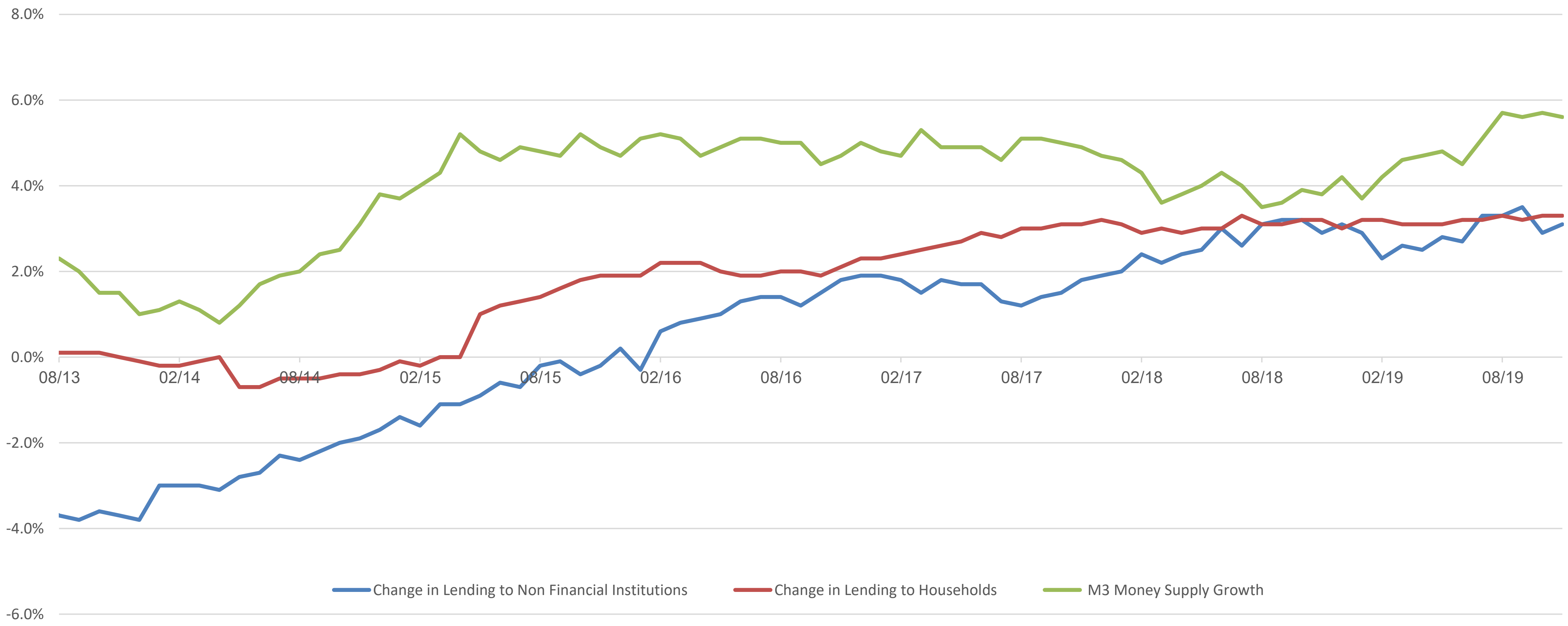
Money Supply and Credit

Growth in Money Supply, Loans to Real Sector



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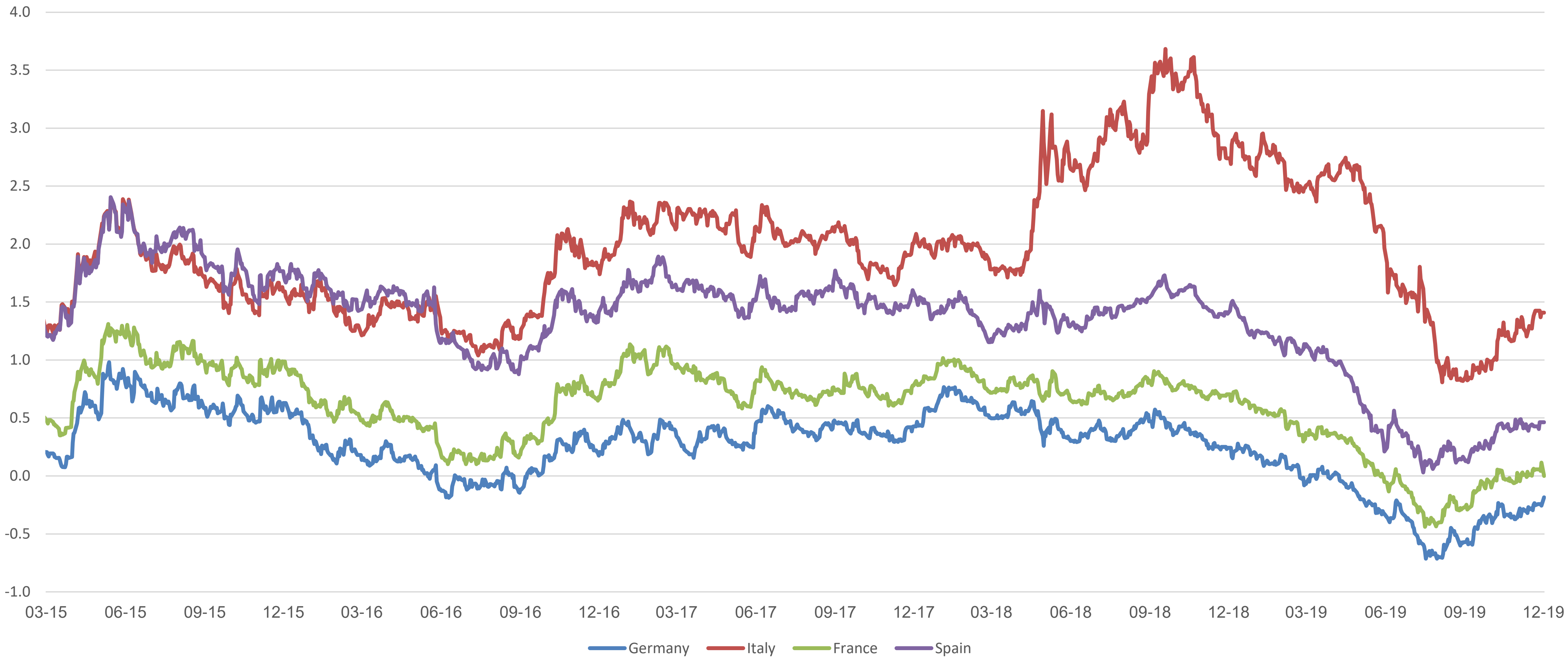
10YR Government Bond Yield



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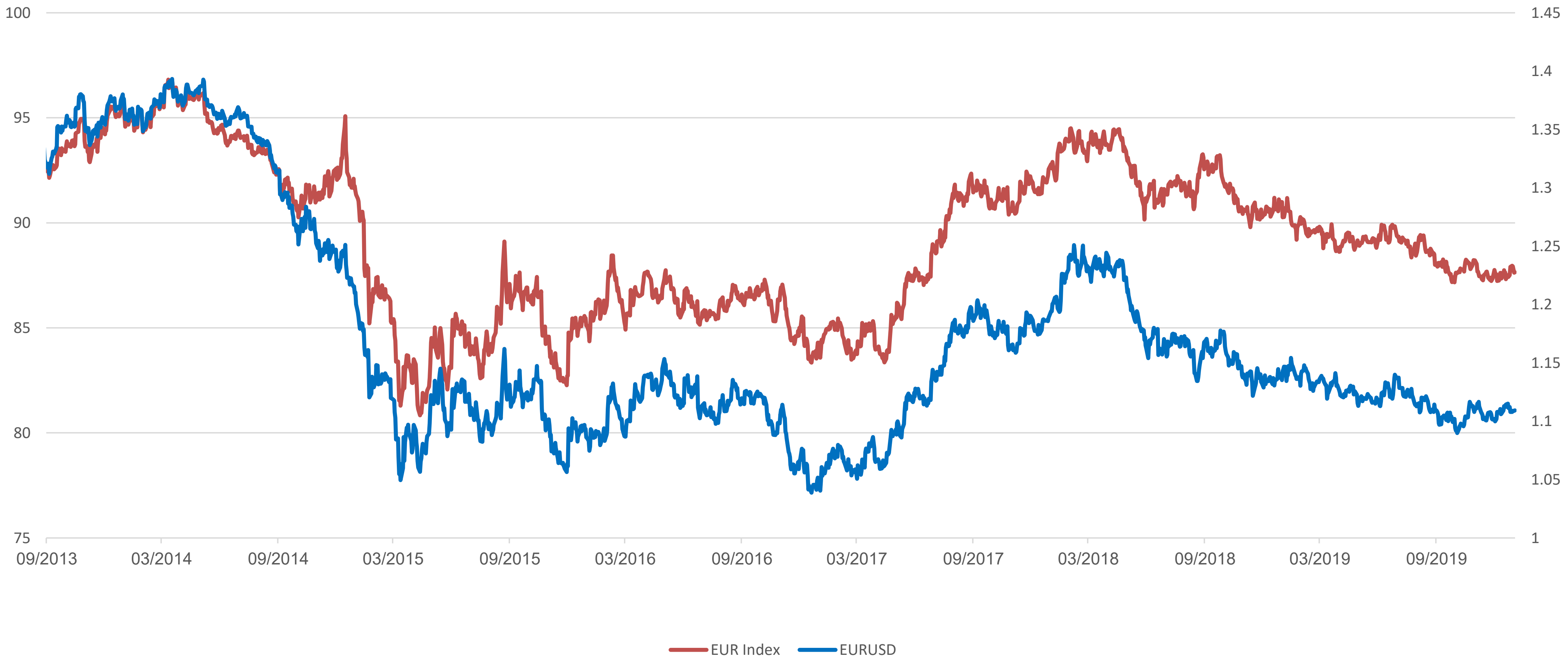
Exchange Rate

EUR Index (Left) EURUSD (Right)



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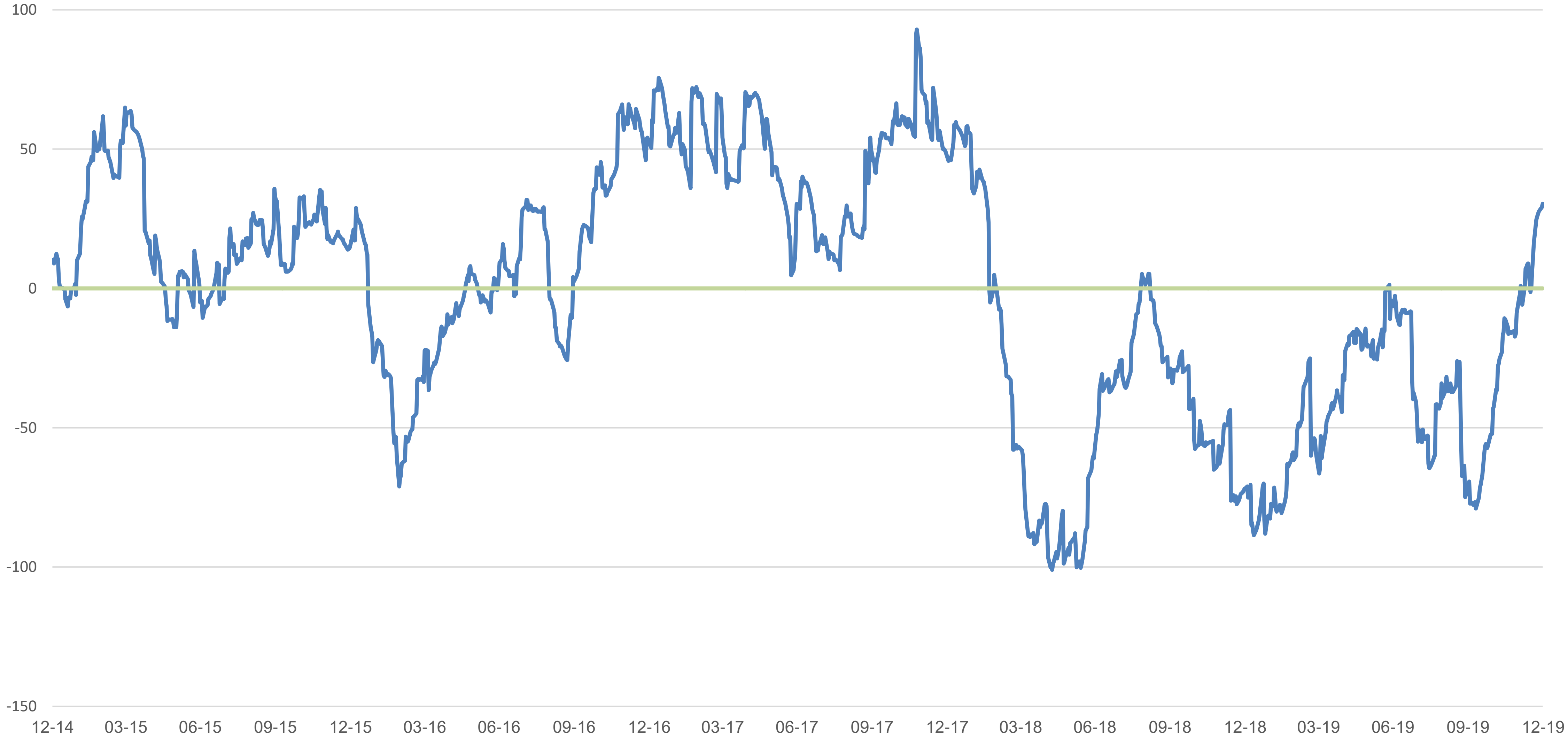
Citi Economic Surprise



Israel

- Ahead of the third round of elections in early March, the government is expected to run from January on the basis of a continuing budget, which would mean a cut of more than 10 billion ILS, with no discretion and no impact on priorities. This reality is expected to hit domestic demand and make it harder for the local economy to exploit its growth potential

- Meanwhile, investors and ratings agencies stay calm, assuming that the economy is strong enough to absorb uncertainty, and that the next government will stick to the principle of budgetary discipline and will succeed in bridging the fiscal gap. Respectively, domestic financial markets are also keeping calm, as reflected in the ongoing decline in government bond yields

- Mounting signs of weakness in the labor market, as the unemployment rate rose sharply to 3.9%, the pace of jobs creation slows, the percentage of open jobs decline, and the workforce participation rate is dropping over time. In addition, the employment component of the PMI Index has recently dropped to 48.7, which reflects a contraction in the labor market

- Low inflation is the name of the game in the Israeli economy as long as the Shekel appreciation trend continues. Recent findings indicate an increase in the transmission of prices in Israel and abroad, in episodes of Shekel appreciation, as a result of increased competition, mainly because of online shopping

- Last year, inflation rose 0.3% ,below the inflation target, and 2019 is expected to be the sixth consecutive year that the BOI will not meet its inflation target (1%-3%), mainly due to the Shekel appreciation. This explains the connection that the Bank of Israel creates between the shekel and inflation and its strong desire to prevent further appreciation of the Shekel

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Core Economic Indicator

Israel

Economic Indicator	Latest Figure	Reference Period
Growth Rate	4.0%	Q3-2019
Unemployment Rate	3.9%	November-2019
Inflation Rate (YoY)	0.3%	November-2019
Central Bank Interest Rate	0.25%	December-2019
10 Years Yield	0.83%	December-2019
Ratio of Surplus in Current Account to GDP	3.58%	Q3-2019
Ratio of Public Debt to GDP	61%	Q4-2018

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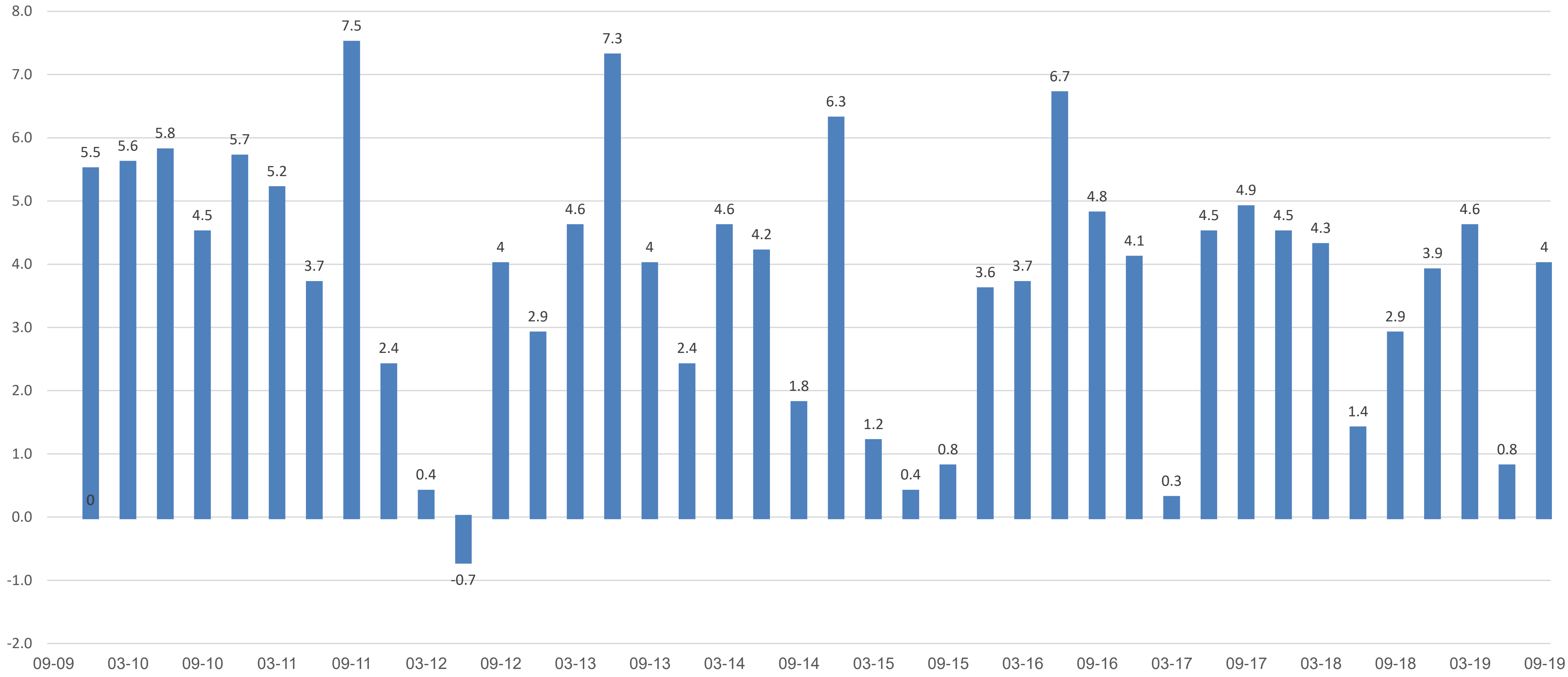
Economic Growth

GDP (Annualized)



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Labor Market

Unemployment Rate

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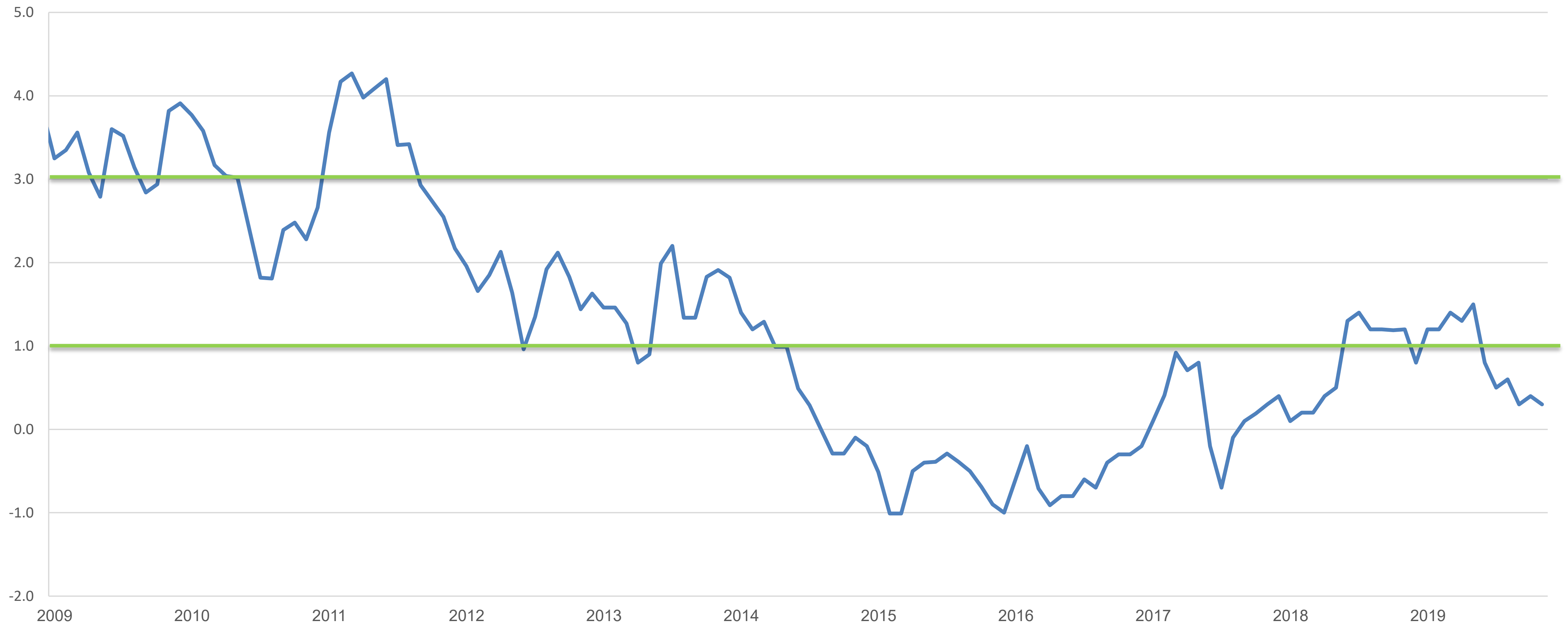
Inflation

CPI (YoY)



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10YR Government Bond Yield

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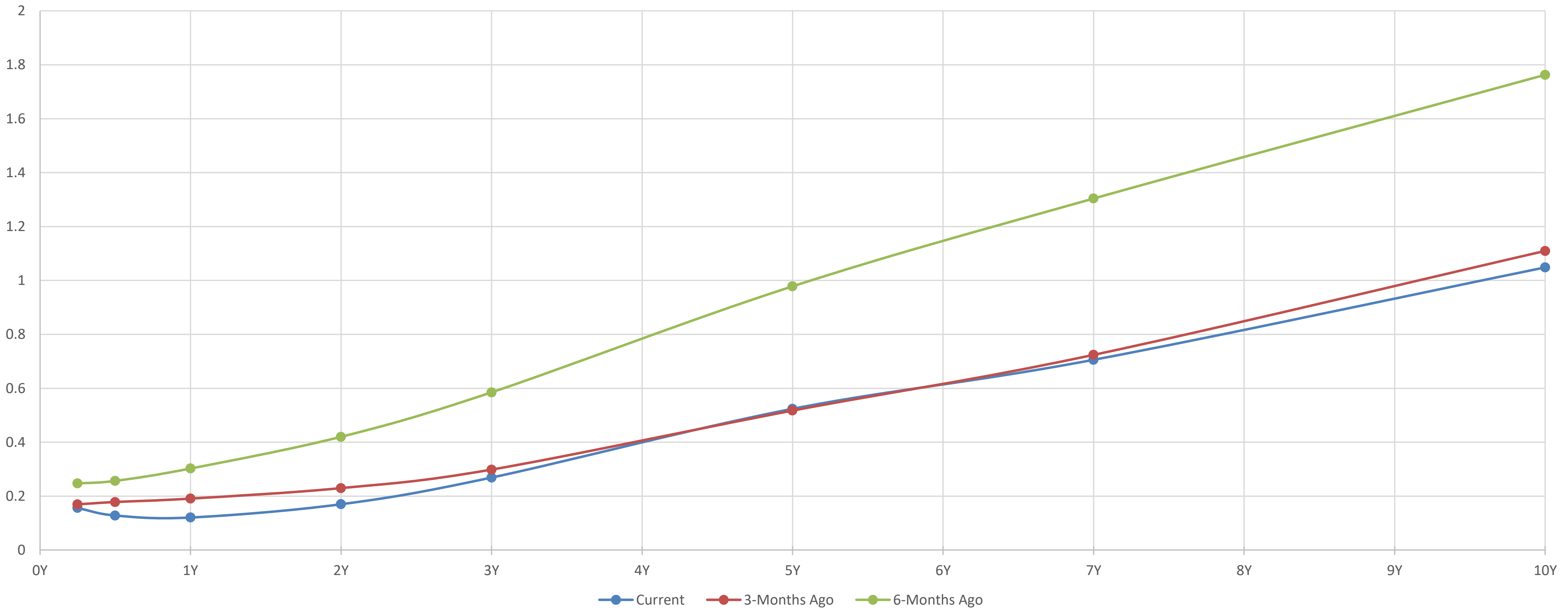
Government Bond Yield Curve



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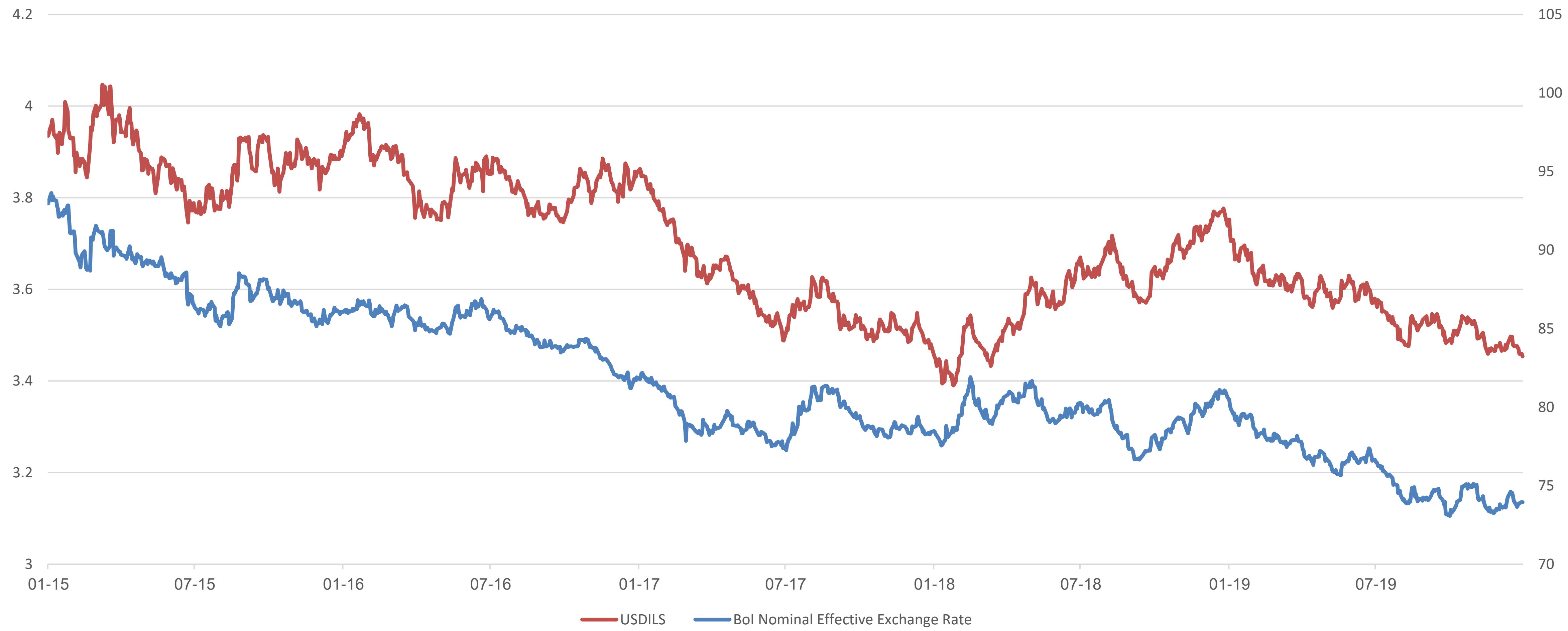
Hedging Costs

USDILS 1YR Forward Premium

Exchange Rate

USDILS (Left) BOI Nominal Effective Rate (Right)



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