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The Israeli Shekel in its Global Context

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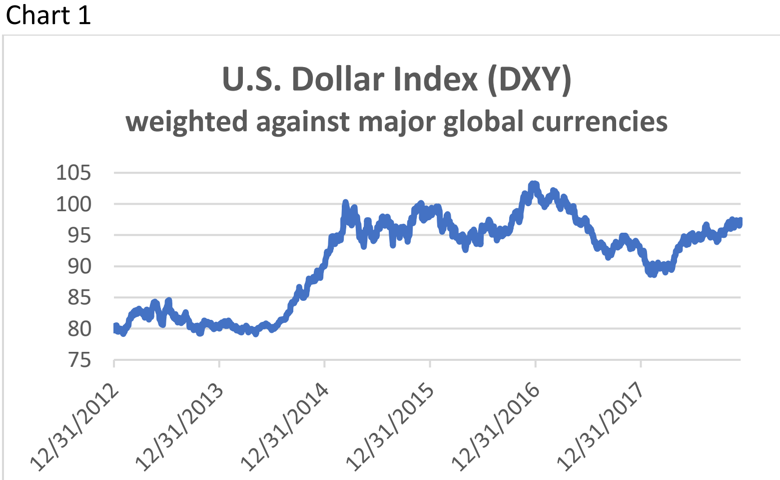
On December 31, 2009, one U.S. dollar purchased 3.8 Israeli shekels. Nine years later, at year-end 2018, one U.S. dollar purchased 3.7 Israeli shekels – remarkable stability during a remarkably unstable period for the global financial system. During the same period, the euro declined 21% from 1.43 per dollar to 1.13. The British pound fell 22.7% against the U.S. dollar, while the Brazilian real and Russian ruble both plummeted 55%.

If world financial markets were the solar system, the U.S. dollar would be the sun, whose immense gravity controls the orbits of other national currencies. Just as the sun burns its fuel, the dollar is fueled by interest rates on U.S. treasury bonds. Higher U.S. interest rates relative to other countries cause the dollar's sun to burn brighter, sometimes scorching fragile financial systems.

By October 2014, the strengthening U.S. economy allowed the Fed to finally end its Quantitative Easing (QE) policies. During the six years of QE, the Fed's balance sheet ballooned by $4.5 trillion in treasury bonds and mortgage-backed securities. As QE ended the U.S. dollar surged relative to global currencies (see chart 1).

Chart 1



Source: Bloomberg, L.P.

The sharply appreciating dollar triggered cascading effects. Commodity prices, such as oil, plummeted; currencies dropped, with commodity-exporting countries receiving particularly severe punishment. After a reprieve in 2016 and 2017, the dollar's rise in 2018 once again triggered currency-related chaos in a host of countries such as Turkey and Argentina (see our September 2018 GHPIA Global Markets newsletter[1]).

Of course, the Israeli economy was not isolated from these global impacts, but you would be forgiven for believing otherwise. Chart 2 highlights cumulative currency depreciation and average economic growth rates since the Federal Reserve started to taper QE in 2013. Israel's combination of strong economic growth and relative currency stability is unique in the world.

Chart 2

FX vs. USD	**2013-2018**	**GDP Growth**	**GDP per capita**
Developed Economies			
Israeli Shekel	-6.4%	3.3%	$40,270
Euro	-17.6%	1.9%	$36,869
British Pound	-31.3%	2.0%	$39,720
Japanese Yen	-9.6%	0.8%	$38,428
Canadian Dollar	-21.0%	1.9%	$45,032
Australian Dollar	-20.6%	2.6%	$53,800
Emerging Economies			
Brazilian Real	-40.3%	-0.9%	$9,821
Russian Ruble	-50.8%	-0.9%	$10,743
Indian Rupee	-15.5%	7.6%	$1,940
Chinese Yuan	-11.0%	7.1%	$8,827
South African Rand	-31.6%	1.1%	$6,161
United States		2.5%	$59,532

Source: Bloomberg, L.P.

At least for now, Israel's income per capita ranks higher than most developed countries when translated into dollars. These numbers overstate Israel's wealth given the higher cost of living experienced by most Israelis. Nonetheless, the Israeli economy was a bastion of stability in an ocean of chaos in recent years. Many people find this reality counterintuitive given Israel's geopolitical neighborhood and security context.

As we discussed in last quarter's newsletter, "Fiscal Discipline and Falling Debt: Israel Gets a Credit Upgrade" [2], Israel was the only developed country to reduce its debt burden following the global financial crisis of 2008. Strong macroeconomic management, infrastructure investment, innovation, and continued deregulation should promote sustained currency stability and economic growth in Israel. This year was a difficult year in global stock markets, but Israel displayed its increasingly characteristic resilience.

[1]. *U.S. Economic Strength Pressures Emerging Markets*, available at: www.ghpia.com
[2] Available at: www.israelinvestmentadvisors.com