

January 15, 2018

SURVEY OF INDUSTRY EXPECTATIONS FOR JANUARY – MARCH 2018 Final Findings

Based on the answers of ~189 industrial companies which replied to the survey from mid-December 2017 through to mid-January 2018

Manufacturers' reports on the last quarter of 2017:

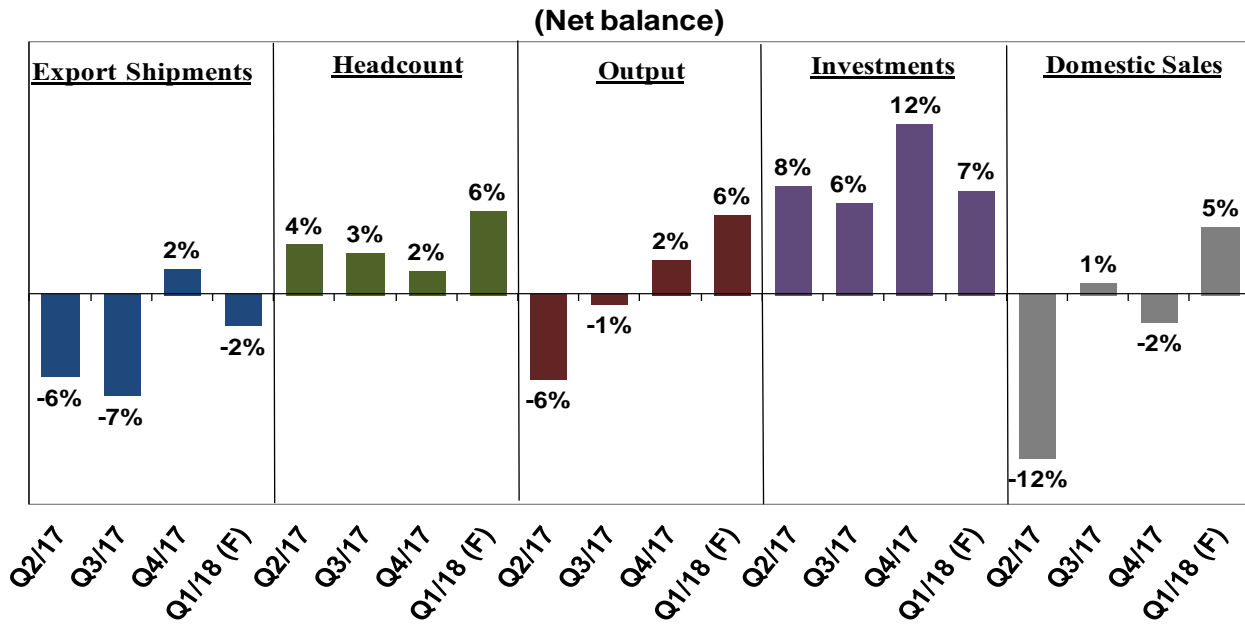
- ❖ Growth in industrial output resumed.
- ❖ Hiring in industry continued.
- ❖ Decline in industry sales to the domestic market.
- ❖ Growth in export shipments resumed.
- ❖ Growth in industry investments in fixed assets continued.
- ❖ Expansion of the operations of multinational industrial companies abroad.

Manufacturers' forecasts for the first quarter of 2018¹:

- ❖ Forecasts for a further increase in industrial output, most likely due to seasonal factors.
- ❖ Forecasts for further growth in industry employee headcount.
- ❖ Forecasts for growth in sales to the domestic market.
- ❖ Forecasts for a decline in export shipments.
- ❖ Forecasts for further growth in industry investments.
- ❖ Forecasts for sharp growth in the operations of multinational industrial companies abroad.

¹ Since 2014 the Division of Economic Research has deducted the bias coefficient from the net balances obtained from the manufacturers' forecasts, since over a lengthy period a bias has been observed in manufacturers' forecasts in the Survey of Industry Expectations versus their actual reports. This analysis refers to the manufacturers' forecasts less the bias coefficient found for each parameter. For further information, see the explanation in the Methodological Appendix.

Manufacturers' Forecasts for the First Quarter of 2018



Net balance = the percentage of those reporting an increase less the percentage of those reporting a decrease, adjusted for the reported intensity of the change.

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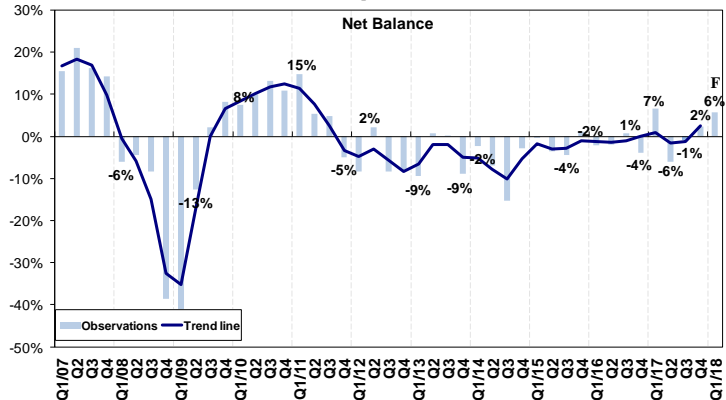
Industrial Output

In the last quarter of 2017 growth in industrial output resumed, with manufacturers reports indicating a positive net balance² of 2%, following a decrease of around 1% in the prior quarter.

In parallel to the growth in industrial output, there was an increase in equipment utilization in industry, with a positive net balance of 2% after a decrease of around 1% in the previous survey. Additionally, raw materials inventory increased, with a positive net balance of around 4% as well as 1% positive net balance in finished goods inventory.

In the first quarter of 2018 manufacturers foresee acceleration of the growth pace in their output, with a positive projected net balance³ of around 6%. In our opinion, the forecast for this increase is most likely influenced by high seasonality in view of preparations for Passover, which falls at the end of March 2018.

Industrial Output, 2007 - 2018



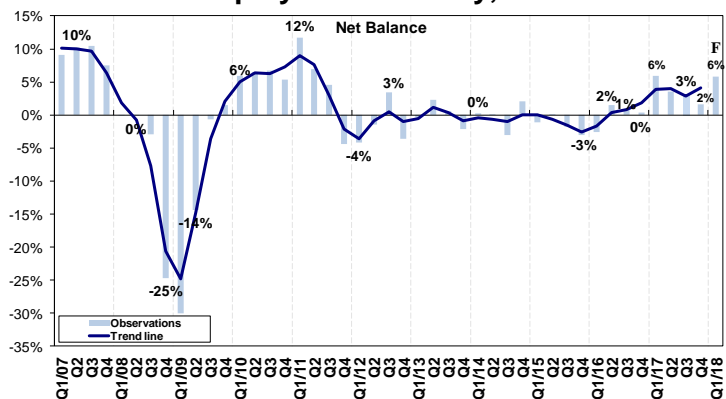
Persons Employed in Industry

In the last quarter of 2017 a further increase was reported in industry headcount: Manufacturers' reports indicate a positive net balance of 2% further to reports of an increase (3% positive net balance) in headcount in the third quarter of 2017.

However, the difficulty in recruiting professionals for industry sectors continued: In the last quarter of 2017 the percentage of manufacturers reporting such difficulty was 85%, following 89% in the third quarter and 91% in the second quarter of the year.

Manufacturers estimate that in the first quarter of 2018 hiring in industry will continue, with a positive projected net balance of 6%.

Persons Employed in Industry, 2007 - 2018



² Net balance = the percentage of those reporting an increase less the percentage of those reporting a decrease, weighted according to the intensity of the change.

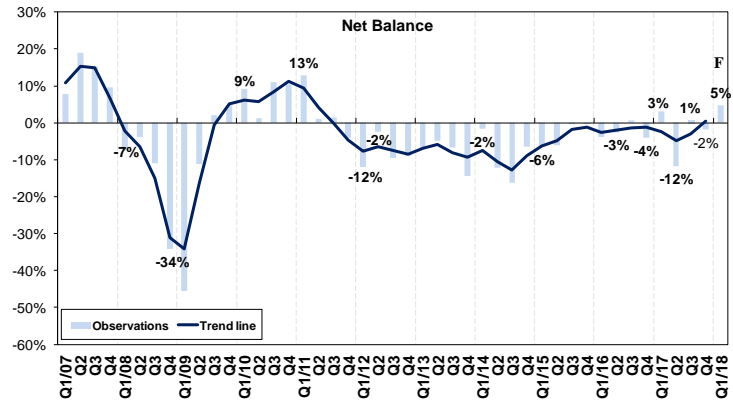
³ Projected net balance, less the bias coefficient, derived from the average differences in the past decade (2004-2013) between the manufacturers' forecasts and their actual reports. For an explanation of the bias coefficient, see the Methodological Appendix.

Sales to the Domestic Market

In the last quarter of 2017 industry sales to the domestic market dropped, with 2% negative net balance after a positive net balance of around 1% in the previous survey.

In the first quarter of 2018, manufacturers predict strong growth in domestic sales with a positive projected net balance of around 5%, which reflects optimism as regards the development of domestic sales. We note that the forecast is possibly the result, among other things, of seasonal factors due to preparations for Passover, which falls at the end of March 2018.

Sales to the Domestic Market, 2007 - 2018

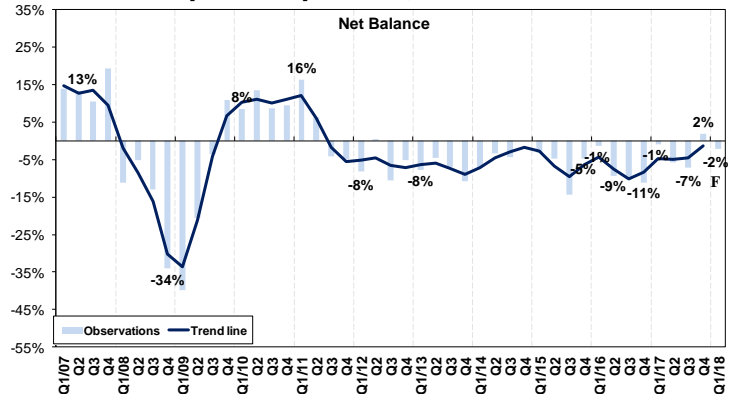


Export Shipments

In the last quarter of 2017 growth in export shipments resumed, with a positive net balance of around 2% following a negative net balance of 7% in the prior quarter.

Nevertheless, **the dramatic erosion of export profit margins continued**, with a negative net balance of about 30% in profitability after a similar negative net balance the third quarter of 2017. We note that in all probability, the erosion of profit margins is due to the cumulative impact of the revaluation of the Shekel against the U.S. Dollar.

Export Shipments, 2007 - 2018



Additionally, **a further drop in export prices in foreign currency was posted in the last quarter of the year**: A negative net balance of 14% further to 12% negative net balance in the previous survey. The decrease in prices is the result, among other things, of the revaluation of the Shekel against the Dollar, combined with the difficulties encountered by exporters in the harsh global competition, which has forced them to continuously lower their prices in foreign currency.

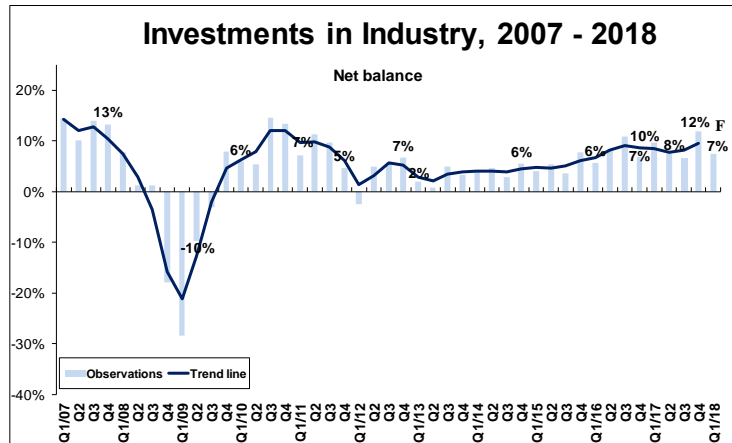
In the first quarter of 2018 manufacturers foresee a downturn in export shipments (2% negative projected net balance), together with a further drop in export prices in foreign currency (6% negative projected net balance).

The major factors inhibiting export growth as ranked by exporters are foreign exchange rates, domestic manufacturing costs and the difficulty in penetrating and marketing in new markets.

Investments in Industry

In the last quarter of 2017 industry investments in fixed assets continued to grow: A positive net balance of around 12% following 6% positive net balance in the previous quarter.

Manufacturers also reported an increase in real financing costs, with 11% positive net balance in the quarter further to a trend of rising expenses, which has persisted for over seven years⁴.



In the first quarter of 2018 manufacturers foresee a further increase in industry investments, with a slowdown in pace: A positive projected net balance of 7%. Manufacturers also expect real financing costs to increase further, with a positive projected net balance of 10%.

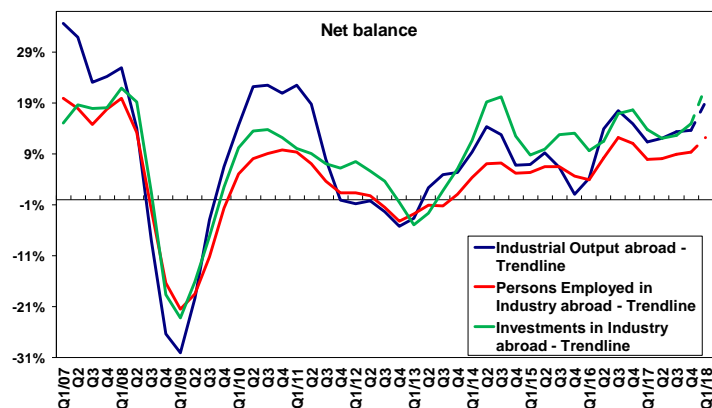
In the last quarter of 2017 the percentage of manufacturers reporting difficulty in obtaining new credit rose, with 45% of manufacturers in need of new credit encountering difficulty in obtaining it, compared to 42% who such reported difficulty in the previous survey. **By contrast, a slight decrease was recorded in the percentage of those experiencing difficulty in maintaining their existing line of credit,** with about 38% of the manufacturers reporting difficulty in maintaining their existing credit line compared to 43% in the third quarter of the year.

Multinational Operations

In the last quarter of 2017 a further increase was posted in the output of Israeli plants abroad: A positive net balance of 11% following a positive net balance of 14% in the third quarter of the year, along with **continued hiring abroad:** 8% positive net balance after a positive net balance of around 10% in the last survey.

In parallel, **an increase in investments by the plants abroad was recorded,** with around 11% positive net balance posted in the last quarter of 2017.

Multinational Activities of Israeli Industrial Companies abroad



In the first quarter of the year, the multinational industrial companies foresee a surge in their operations abroad with a sharp increase in output (19% positive projected net balance), along with expectations for continued hiring (12% positive projected net balance) and forecasts for a sharp rise in investments (a positive projected net balance of 22%).

For explanations and clarifications, please contact our Division of Economic Research:
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⁴ Excluding stagnation in real financing costs in the first quarter of 2015.

Methodological Appendix – The Bias Coefficient

Since 2014 the Division of Economic Research has deducted the bias coefficient from the net balances obtained from the manufacturers' forecasts, since over a lengthy period a bias has been observed in manufacturers' forecasts in the Industry Expectations Survey versus their actual reports. For most parameters this bias was found to be positive, meaning a tendency to over-optimism, while in a small number of parameters a tendency to pessimism was observed.

Bias coefficient: The average difference in the past decade⁵ between the net balance of the manufacturers' forecasts⁶ and the net balance of their actual reports for that quarter.

Bias Coefficients (%)

(Positive coefficient = tendency to over-optimism; negative coefficient = tendency to pessimism)

Parameter	Output	Export	Domestic market	Headcount	Investments
Total industry	4.0	4.0	2.1	-1.6	0.5

⁵ From the first quarter of 2004 through to the last quarter of 2013.

⁶ The percentage of manufacturers reporting growth less the percentage of those reporting a downturn, weighted for the reported intensity of the change.