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Expectations for peace in Israel and the value of the Israeli shekel, 1999–2008

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Abstract

This article presents a regression analysis of some of the factors that influenced the value of the Israeli shekel from 1999 to 2008. The regression results show that changes in domestic expectations for peace in Israel had a significant effect on the value of the shekel. These results combined with a review of the political and economic developments in 2002 suggest that the exchange rate crises in the Israeli foreign currency market in the second quarter of 2002 was due to a decrease in expectations for peace. The article also discusses the impact of the 2002 exchange rate crises on the Israeli economy and the value of the shekel.

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Notes

1. See Avi Ben-Bassat, "The Obstacle Course to a Market Economy in Israel," in The Israeli Economy, 1985–1998: From Government Intervention to Market Economies, ed. Avi Ben-Bassat (Cambridge, MA: MIT Press, 2002), 33, 34.
2. S. Brock Blomberg and Gregory D. Hess, "Politics and Exchange Rate Forecasts," Journal of International Economics 43 (1997): 189–205.
3. Kyle Kauffman, and Akila Weerapana, "The Impact of AIDS-related News on Exchange Rates in South Africa," Economic Development and Cultural Change 54, no. 2 (2006): 366.
4. Asaf Zussman, Noam Zussman and Morten Orregaard Nielsen, "Asset Market Perspectives on the Israeli-Palestinian Conflict," Economica 75 (2008): 84–115.
5. Andrew Schein, 'NASDAQ or Nablus: Explanations for the recent fluctuations in the Israeli economy,' Israel Affairs 9, no. 4 (2003): 64–78.
6. Zvi Eckstein and Daniel Tsiddon, "Macroeconomic Consequences of Terror: Theory and the Case of Israel," Journal of Monetary Economics 51 (2004): 971–1002.
7. Gerald Schneider and Vera E. Troeger, "War and the World Economy: Stock Market Reactions to International Conflicts," The Journal of Conflict Resolution 50, no. 5 (2006): 623–45.
8. Tami ... Journal of Finance
9. T ... B'tselem, http://
10. This ... data for 2008 is ... December
27. With regard to Palestinians, 2002 was also the deadliest year with 1032 deaths.



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11. Data from <http://www.mfa.gov.il>, the website of Israel's foreign ministry. The data for 2008 and 2009 do not include the period of Operation Cast Lead.
12. Annual data of Israel's GDP and inflation rates from Israel's Central Bureau of Statistics (CBS), Statistical Abstract of Israel 2011, <http://www.cbs.gov.il>.
13. Quarterly GDP from the Bank of Israel website, <http://www.boi.gov.il>.
14. Press announcement by CBS on August 16, 2011.
15. US data from US Bureau of Labor Services, <http://www.bls.gov>.
16. Data from England from UK's office of National Statistics, <http://www.statistics.gov.uk>.
17. See discussion by Nissan Liviatan and Nathan Sussman, "Disinflation Process in Israel in the Past Decade," in *The Israeli Economy, 1985–1998*, ed. Ben-Bassat, 129–56.
18. Information concerning shekel/dollar exchange rates and interest rates of the Bol are available from the Bol's website, <http://www.boi.gov.il>.
19. Joseph Djivre and Daniel Tsiddon, "A Monetary Labyrinth: Instruments and the Conduct of Monetary Policy in Israel 1987–1998," in *The Israeli Economy, 1985–1998*, ed. Ben-Bassat, 126. Also see Dov Elkayam, "The Long Road from Adjustable Peg to Flexible Exchange Rate Regime: The Case of Israel," Bol Discussion Paper, 2003.
20. See the Bol's Foreign Currency Department Annual Report, 2007, Bol's Market Operations Department Annual Report 2008, 2009 and 2010 and Bol's Recent Economic Developments May–August 2011, p. 13.
21. For surveys of this literature see K.A. Froot and R.H. Thaler, "Anomalies: Foreign Exchange," *Journal of Economic Perspectives* 4, no. 3 (1990): 179–92; Charles Engel, "The Forward Bias Puzzle: Evidence," *Journal of International Money and Finance* 15, no. 1 (1996): 61–72; and Michael Grosche, "The Forward Bias Puzzle: Evidence," *Journal of International Money and Finance* 15, no. 1 (1996): 61–72.
22. Michael Grosche, "The Forward Bias Puzzle: Evidence," *Journal of International Money and Finance* 15, no. 1 (1996): 61–72.
23. Zussman et al., "Asset Market Perspectives," 97.

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24. Aliza Fleischer and Steven Buccola, "War, Terror and the Tourism Market in Israel," *Applied Economics* 34, no. 11 (2002): 1335–43.
25. For announcement of the interest rate reduction, see Bol Press Release, December 23, 2001, and for an example of the disagreement between the Bol and the Finance Ministry, see article by Moti Bassok, "Klein: The Depreciation is Not Likely to Cause Inflation" [in Hebrew], *Haaretz*, March 25, 2001.
26. The Bank of Israel's Monetary Program for June 2002, Press Release of the Bol, May 27, 2002.
27. Nehemia Shtrasler, "The Dollar Dive/No Crisis, No Disaster," *Haaretz*, April 14, 2007, wrote, 'In June 2002 Israel went into panic mode when the dollar climbed to an all-time high of five shekels. Everyone wondered whether it would break the five-shekel psychological barrier and reach six to the dollar.'
28. According to an article in the *New York Times*, "The Markets: Stocks & Bonds; Nasdaq Index Tumbles 3%, to Its Lowest Point This Year," June 20, 2002, even the Dow Jones and Nasdaq indices fell due to the terrorism in Israel. The article reports, 'The selling was accelerated by the second suicide bombing in Israel in as many days. Analysts said the bombing gave investors already skeptical about second-quarter earnings another reason to stay away.'
29. See articles by John Kifner, "Cabinet in Israel Endorses Seizure of the West Bank," *The New York Times*, June 22, 2002, and "Israeli Forces Hit Palestinian Offices in Hebron in Effort to Dislodge Gunmen," *The New York Times*, June 28, 2002.
30. Data on attacks from Israeli army is reported in an article by James Bennet, "Israelis Say Hamas Is Not Able to Mount Major Retaliation," *The New York Times*, May 27, 2004.

31. In the article, "The Israeli Economy: A Tale of Two Cities," *The New York Times*, June 24, 2002, it is noted that the Israeli economy was "shaken" by the events of June 2002, leading to a "sharp decline in the Israeli economy" and a "sharp decline in the Israeli economy" (p. 1).

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