Weekly — February 24, 2023

Weekly Economic & Financial Commentary

United States: **Mixed Housing Data and Upside Inflation Surprise**

- Existing home sales declined 0.7% in January, while new home sales leaped 7.2%. Real personal spending shot higher in January, and solid growth in discretionary spending suggests continued consumer resilience. The core PCE deflator surprised to the upside, which could compel the FOMC to go higher for longer.
- Next week: Durable Goods (Mon), Construction Spending (Tue), ISM (Wed/Fri)

International: **Improving Sentiment in U.K. and Eurozone, Encouraging Inflation Trends in Canada**

- February's PMI surveys shed some brighter light on sentiment in the U.K. and Eurozone, particularly for the services sector. While we still forecast both economies to fall into recession this year, we expect growth to be more resilient than previously forecast. Meanwhile, Canada's CPI release showed that the trend of lower consumer prices continued in January, with CPI inflation receding more than expected to 5.9% year-over-year.
- Next week: China PMIs (Wed), Canada GDP (Wed), Eurozone CPI (Thu)

Interest Rate Watch: **50 bps at the Next FOMC Meeting?**

- Minutes of the Jan. 31-Feb.1 FOMC meeting show that a "few" FOMC members favored raising rates by 50 bps at that time. Given the run of stronger-than-expected data in recent weeks, could a few more members join them at the next meeting on March 22?

Credit Market Insights: **Increasing Delinquency Rates for Young Borrowers**

- Due to decades high inflation increasing the costs of everything from groceries to discretionary activities, consumers have been facing increasing pressure on household balance sheets. While the increase in credit card and auto loan delinquency rates for all borrowers is similar to that experienced in the previous two quarters, younger age groups experienced comparably stark increases compared to their older counterparts.

Topic of the Week: **Israeli Shekel Detached from Fundamentals**

- We have not said this too often. But, the Israeli shekel is underperforming relative to the rest of the emerging market currency complex. We see merit in entering positions at current levels, and we believe a move toward ILS3.40 by the end of Q1-2023 is imminent.

Wells Fargo U.S. Economic Forecast

	Actual 2022				Forecast 2023				Actual		Forecast	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	2021	2022	2023	2024
Real Gross Domestic Product [1]	-1.6	-0.6	3.2	2.7	-0.6	0.8	-1.9	-1.6	5.9	2.1	0.6	0.5
Personal Consumption	1.3	2.0	2.3	1.4	0.1	0.8	-1.0	-1.7	8.3	2.8	0.7	0.3
Consumer Price Index [2]	8.0	8.6	8.3	7.1	5.5	3.5	2.4	2.2	4.7	8.0	3.4	2.3
"Core" Consumer Price Index [2]	6.3	6.0	6.3	6.0	5.3	4.3	3.3	2.9	3.6	6.1	3.9	2.7
Quarter-End Interest Rates [3]												
Federal Funds Target Rate	0.50	1.75	3.25	4.50	5.00	5.25	5.25	5.25	0.25	2.02	5.19	3.25
Conventional Mortgage Rate	4.27	5.58	6.01	6.36	6.30	6.10	5.65	5.40	3.03	5.38	5.86	5.00
10 Year Note	2.32	2.98	3.83	3.88	3.70	3.60	3.25	3.10	1.45	2.95	3.41	2.94

Forecast as of: February 08, 2023

[1] Compound Annual Growth Rate Quarter-over-Quarter [2] Year-over-Year Percentage Change [3] Annual Numbers Represent Average

Source: U.S. Dept. of Commerce, U.S. Dept. of Labor, Federal Reserve Board and Wells Fargo Economics

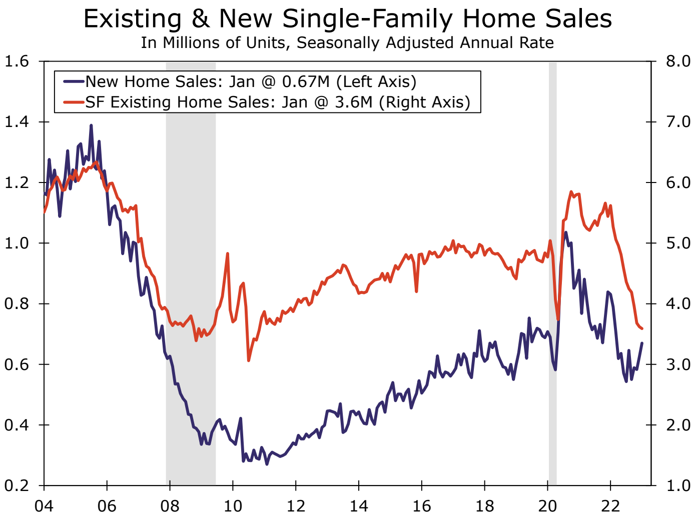
Please see our full U.S. Economic Forecast.

U.S. Review

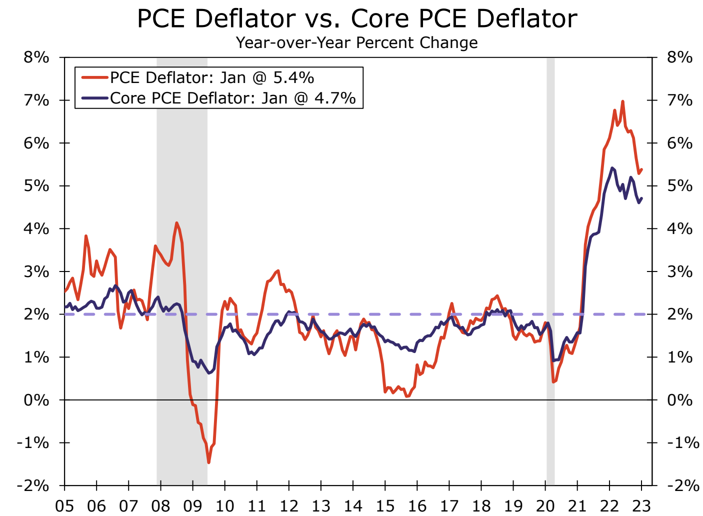
Mixed Housing Data and Upside Inflation Surprise

In a light week for economic data, market participants continued to digest last week's slew of stronger-than-expected reports. Retail sales and manufacturing production surprised to the upside, while the Consumer Price Index rose at its fastest pace since October. While seasonal factors likely boosted some of these headline figures, the string of beats raises the potential for more aggressive moves from the Federal Reserve. As discussed in Interest Rate Watch, the minutes of the last FOMC meeting (released on Wednesday) underscored the Committee's resolve to bring down inflation and suggest more members may be drifting toward the hawkish camp.

One sector that has acutely felt the effects of the FOMC's policy tightening thus far is housing. Existing home sales fell 0.7% to a 4.0 million-unit annualized pace in January. The slip marks the 12th consecutive month that sales have declined and brought the year-over-year change down to an all-time low of -36.9%. The pullback in sales has helped to cool off home price appreciation. The median single-family home price was $363,100 in January, down nearly 14% from its recent peak of $420,900 in June 2022. Inventory remains low by historical standards but edged up slightly in January as the spring selling season starts to get under way. This year will likely be different than last year—to learn more, join a webinar with our real estate economists on Wednesday, March 1 as they discuss the housing market outlook for 2023.



Source: NAR, U.S. Department of Commerce and Wells Fargo Economics



Source: U.S. Department of Commerce and Wells Fargo Economics

Meanwhile, new home sales leaped 7.2% in January to a 670,000-unit annualized pace, the highest since March. The median new home sales price was $427,500 during the month, which is down 0.7% over the year. The price decline likely reflects home builders offering interest rate buy-downs and sale price discounts to move inventory. For-sale inventory totaled 439,000 units at the end of January, down nearly 3% over the month.

Despite the bite of high mortgage rates and still-elevated home prices, brighter days may be ahead for housing demand. Strong labor market conditions have supported real income growth, and recent upward revisions to personal income suggest households have more purchasing power than previously thought. Specifically, fourth quarter personal income was lifted by $185B and the third quarter was revised higher by roughly $108B. The positive revisions meant consumers came into the year with a bit more dry powder, likely driving the 1.1% jump in real personal spending in January. Solid spending in discretionary categories, such as food services & accommodations (+4.6%), recreation services (+1.4%) and transportation services (+0.9%), is a sign of the continued resilience of household spending.

While strength in real consumption is a positive development, it also adds pressure to inflation. The core PCE deflator, which excludes food and energy, rose a higher-than-expected 0.6% in January. The increase bumped the year-over-year percent change to 4.7%, up from 4.6% in December, which is well-above the FOMC's 2% inflation target. (Return to Summary)

U.S. Outlook

Weekly Domestic Indicator Forecasts					
Date	**Indicator**	**Period**	**Consensus**	**Wells Fargo**	**Prior**
27-Feb	Durable Goods Orders (MoM)	Jan	-3.9%	-4.3%	5.6%
27-Feb	Durables Ex Transportation (MoM)	Jan	0.1%	0.2%	-0.2%
28-Feb	Consumer Confidence	Feb	108.4	108.0	107.1
1-Mar	ISM Manufacturing Index	Feb	47.8	47.5	47.4
1-Mar	Construction Spending (MoM)	Jan	0.3%	0.3%	-0.4%
3-Mar	ISM Services Index	Feb	54.5	54.0	55.2

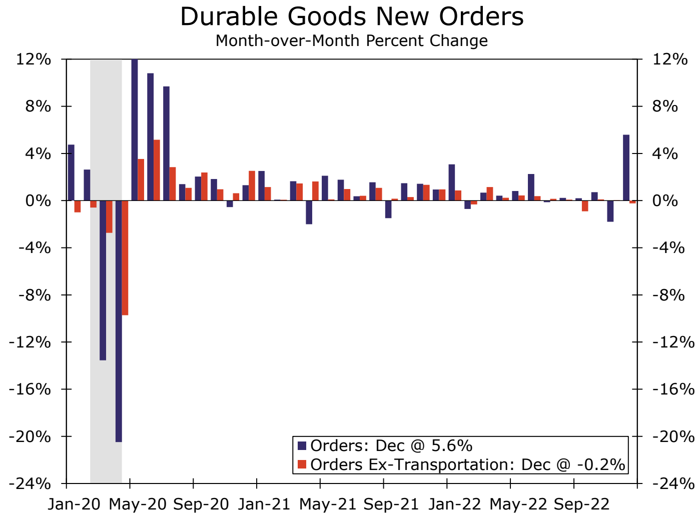
Forecast as of February 24, 2023

Source: Bloomberg Finance L.P. and Wells Fargo Economics

Durable Goods • Monday

January durable goods orders look set to deliver a large-looking blow with a strong downside potential in aircraft. With that in mind, we expect to see durable goods orders fall 4.3% over January. This is likely somewhat due to payback from December, when durable goods orders rose a massive 5.6%, the largest increase since coming out of the pandemic-related lockdowns in July 2020. However, this increase was entirely from aircraft, as nondefense aircraft orders more than doubled over the month, boosting the transportation equipment category to a nearly 17% monthly increase. Data from Boeing suggest this bounce reversed in January and point to aircraft providing a considerable drag. Excluding transportation, we expect durable goods orders rose a modest 0.2%. Nondefense orders, excluding aircraft, also known as core capital goods orders, are slowing, down 0.2% in December, which bodes poorly for the general trend of production.

Not all recent news comes with worse-than-it-looks data on durables. The revisions to fourth quarter GDP were a mixed bag; while headline GDP was revised down, a slight boost to equipment brought it up to a -3.2% annualized rate from a -3.7% rate. Regardless, it still stands that the outlook is negative. Recent industrial production figures imply that as financing costs continue to rise, demand for capital expenditures is dropping and sapping new orders.

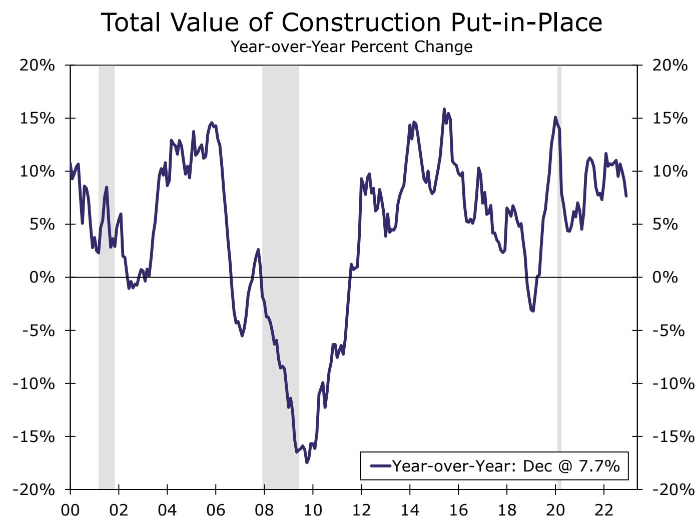


Source: U.S. Department of Commerce and Wells Fargo Economics

Construction Spending • Wednesday

While elevated input prices and financing costs have hampered the construction industry, construction spending still has room to rise. We expect construction spending rose 0.3% in January. Construction on the nonresidential side of the ledger appears to be holding up a little stronger in this tough environment for builders. The Architecture Billing Index showed mild improvement in December, but remained in contractionary territory. On the other hand, building contracts went from steady to growing. Interest rate hikes continue to hammer demand, with firm comments including a "wait-and-see" mindset as the industry awaits the terminal fed funds rate.

On the residential side, housing starts fell 4.5% and building permits rose only 0.1% in January. The rate of home completions rose 1.0% however, showing some signs of life even as rising rates dampen the prospects for construction across the board.



Source: U.S. Department of Commerce and Wells Fargo Economics

ISM Manufacturing/Services Indices • Wednesday / Friday

Both the ISM manufacturing and services purchasing manager indices for February are released next week, with manufacturing out on Wednesday and services on Friday.

To start, we expect to see that ISM manufacturing spent another month in contractionary territory, with only an improvement of one-tenth of a point to 47.5. Last month, new manufacturing orders fell to 42.5, the lowest reading since mid-2020. Orders are expected to continue to dry up and production is expected to slowly contract. At least prices paid fell and employment remains steady in the face of these issues. We will look for more disinflationary pressures and challenges to the labor market in this upcoming report.

We expect to see ISM services show a slight deterioration though remaining in expansionary territory at 54.0 in the wake of the massive bounce in headline and new orders indices in January after a contraction in December. Ten of 18 industries reported growth last month, and the industries that showed declines—retail and wholesale trade, transportation & warehousing, construction and information, among others—reflect a gradual adjustment to the overall economic slowdown and the new higher rate environment. On the demand side, new orders and supplier deliveries improved, to growth and steady-state, respectively, and provide evidence that there can be near-term growth despite broader challenges.

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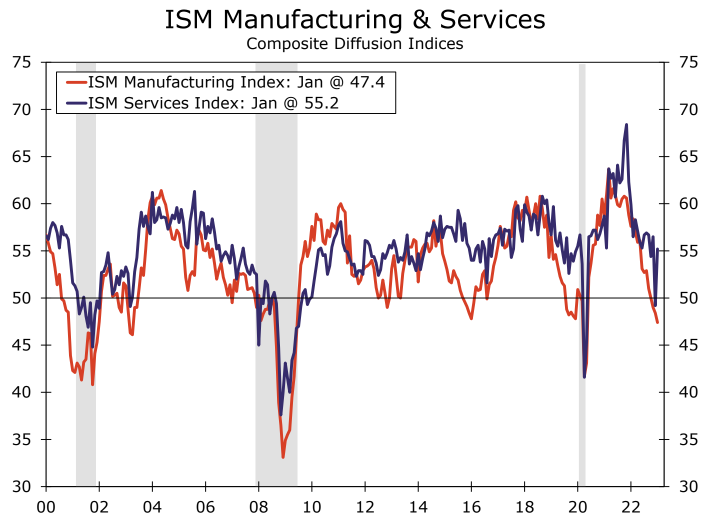


Source: Institute for Supply Management and Wells Fargo Economics

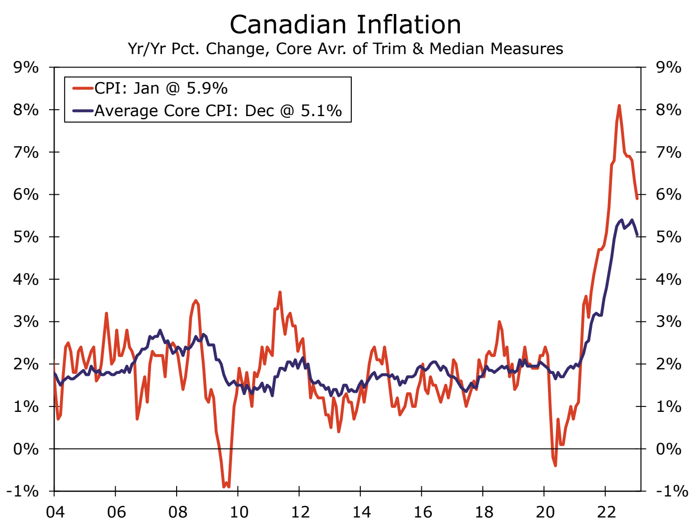
International Review

Improving Sentiment in U.K. and Eurozone, Encouraging Inflation Trends in Canada

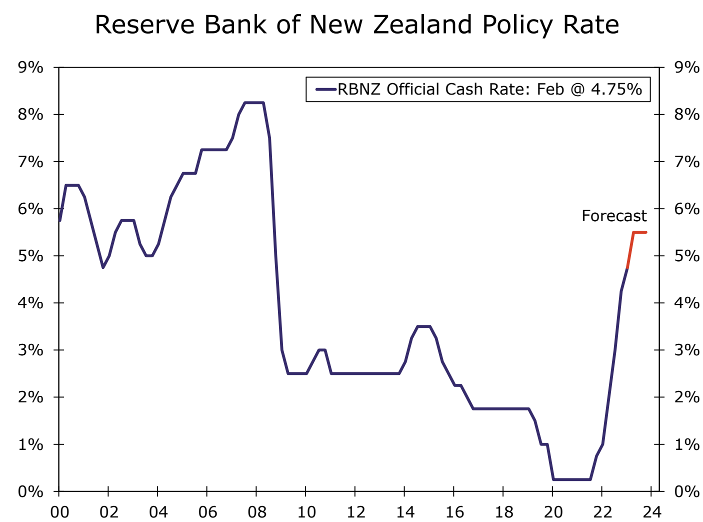
February's PMI surveys shed some brighter light on sentiment in the U.K., in line with our expectation for growth trends to be more resilient than previously forecast. Recent trends in the U.K. PMI surveys have been mixed, with the manufacturing and services readings in contraction territory for the past several months. However, in encouraging news for February, the services PMI was a bright spot, accelerating more than consensus expectations to 53.3 and back into expansion range, while the manufacturing PMI ticked up to 49.2. Services sector respondents saw an increase in business activity, and reported stronger demand amid an improving economic outlook. Even with an upgraded growth outlook for the U.K., we still expect the economy to fall into recession and contract by 0.6% in 2023.

In the Eurozone, growth trends this year may be better than originally expected as well. The Eurozone economy managed to avoid contraction in the last quarter of 2022, and February business activity accelerated much faster than expected to a nine-month high. Much of this strength came from the services sector, where the services PMI rose for the second month in a row to 53.0, sitting comfortably in expansionary territory. While the manufacturing PMI dipped slightly to 48.5, a silver lining was a further cool down in input cost inflation, particularly noticeable in the manufacturing sector. A somewhat brighter growth outlook combined with still-high inflation may add fuel to further rate hikes from the European Central Bank (ECB) this year. Overall, February PMI data are consistent with the Eurozone economy growing in Q1, and although we still forecast a recession to materialize this year, we expect the downturn to be short and shallow. For 2023 as a whole, we expect Eurozone GDP to edge up 0.1%.

Meanwhile, Canada's January CPI data showed that inflation receded more than expected to 5.9% year-over-year. Recent inflationary trends in Canada have been encouraging, with the overall CPI inflation rate continuing to trend lower from its peak of 8.1%. As for underlying inflation, two important measures called the trim and median core inflation rates trended slightly lower, averaging 5.1%. January's encouraging inflation report provides scope for the Bank of Canada (BoC) to continue holding policy rates steady at the current level of 4.50%. After a cumulative 425 bps of rate hikes, BoC policymakers said they prefer to see the effects of cumulative tightening on the economy before adjusting policy rates further. In our view, the Bank of Canada will remain on hold for the next few quarters before being among the first central banks to start cutting policy rates. Our forecast sees the BoC beginning its easing cycle in Q4 of this year as recessionary conditions start to crystallize.



Source: Bloomberg Finance L.P. and Wells Fargo Economics



Source: Bloomberg Finance L.P. and Wells Fargo Economics

RBNZ Signals Further Tightening Ahead

The Reserve Bank of New Zealand (RBNZ) delivered a 50 bps rate hike at its February monetary policy meeting, bringing the Official Cash Rate to 4.75% and signaling further rate hikes ahead. Overall, the language of the statement was still committed to bringing inflation down, but fairly balanced in tone and not overly hawkish. The RBNZ clarified that it considered either a 50 or 75 bps rate hike, but settled on 50 bps because, while the balance of risks to inflation remains skewed to the upside, the extent of that risk had moderated. Furthermore, 50 bps would balance bringing core inflation down and early signs of moderating demand.

Within the details of the announcement, the RBNZ acknowledged that although it has seen early signs of easing price pressures, core CPI remains too high, employment is still beyond its maximum sustainable level, and near-term inflation expectations remain elevated. In its updated economic projections, policymakers see a slightly lower peak for annual CPI at 7.3% in Q1-2023, with inflation receding faster over this year and next. As for growth trends, the RBNZ continues to expect a recession this year, recognizing that a reduction in aggregate demand is necessary to bring inflation back to target. While the slower global outlook is contributing to weaker demand for key commodity exports such as dairy and meat, a rebound in tourism and easing of travel from China could potentially offset these losses. In addition, the RBNZ cited that historical evidence suggests risks are tilted toward a more concentrated period of contraction, and members agreed that the sooner supply and demand are matched, the overall lower cost of reducing inflation. In our view, this suggests a recession this year won't prevent the RBNZ from embarking on further rate hikes.

The RBNZ's updated economic projections showed no change in the forecasted peak in the Official Cash Rate (OCR) at 5.50%, but now the central bank expects a slower path to that terminal rate. In line with this, we now forecast a 50 bps rate hike in April, followed by a final 25 bps rate hike in May to 5.50%.

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International Outlook

Weekly International Indicator Forecasts

Date	Indicator	Period	Consensus	Wells Fargo	Prior
28-Feb	China Manufacturing PMI	Feb	50.7	--	50.1
28-Feb	China Non-Manufacturing PMI	Feb	55.0	--	54.4
28-Feb	Canada Quarterly GDP Annualized	Q4	--	1.6%	2.9%
2-Mar	Eurozone CPI (YoY)	Feb	8.2%	--	8.6%
2-Mar	Eurozone Core CPI (YoY)	Feb	5.3%	--	5.3%

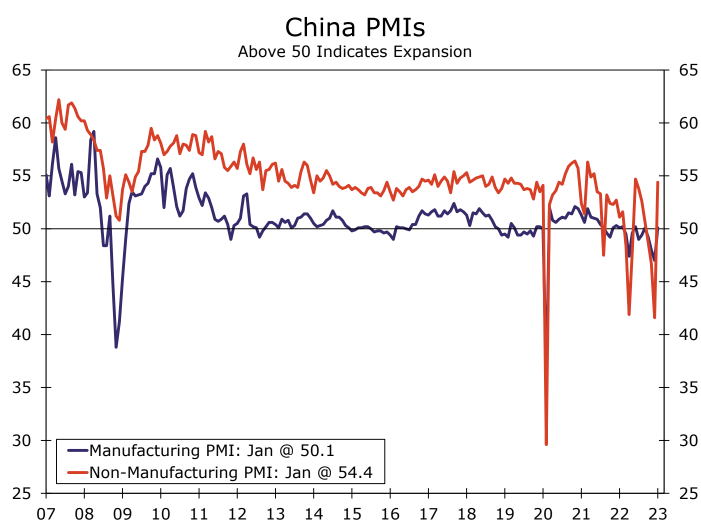
Forecast as of February 24, 2023

Source: Bloomberg Finance L.P. and Wells Fargo Economics

China PMIs • Wednesday

Our outlook for China's economy has improved in recent months. We suspect that as the end of China's Zero-COVID policy allows for unrestricted mobility to return, this should improve China's growth prospects and, in turn, boost the global growth outlook as well. As a result, we now forecast the Chinese economy to expand 5.2% this year. February PMI survey results released next week should reflect this more optimistic outlook for the Chinese economy.

In January, both the manufacturing and non-manufacturing PMIs moved back into expansionary territory after spending the past three months in contraction. The details of the January report pointed to an improvement in the manufacturing sector, with increased production and market demand, as well as shorter delivery times. Meanwhile, the non-manufacturing PMI surged a whopping 12.8 points to 54.4, suggesting optimism ahead for the services sector. PMI trends for both manufacturing and non-manufacturing sectors are expected to show continued improvement in February. The consensus expectation is for the manufacturing PMI to tick up to 50.7, with the non-manufacturing PMI moving up to 55.0.

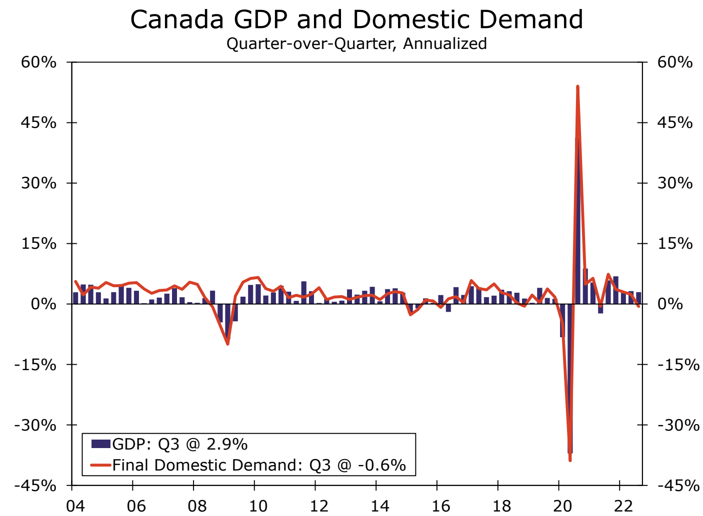


Source: Bloomberg Finance L.P. and Wells Fargo Economics

Canada GDP • Wednesday

Now that inflation has begun to trend lower and the Bank of Canada (BoC) has paused rate hikes to see how the economy is reacting to an extended period of monetary tightening, market participants will likely be paying close attention to how growth in the Canadian economy fared at the end of last year. We expect Canada's GDP release next week to show that the economy remained resilient in the last quarter of 2022, with quarterly GDP (annualized) growth of 1.6% in Q4-2022.

Heading into 2023, however, we expect that growth trends may begin to downshift. Despite a strong labor market that has resulted in five consecutive months of job gains all led by increases in full-time employment, the outlook for the Canadian consumer in particular may signal a slowdown in growth ahead. While recent inflation trends have been encouraging, inflation is still elevated, weighing on real household disposable incomes and consumer spending. In addition, the current elevated level of interest rates should weigh on the housing market and consumer activity. Taken together, we forecast a mild recession in Canada in the first half of 2023.



Source: Datastream and Wells Fargo Economics

Eurozone CPI • Thursday

February inflation numbers for the Eurozone released next week are expected to show a further decline in consumer prices against a backdrop of receding global energy prices and improvements in supply chains.

For context, headline inflation receded to 8.6% year-over-year in January from a recent high of 10.6%. Meanwhile, core CPI (excluding volatile line items such as food, energy, alcohol and tobacco) remains somewhat more stubborn. With food and energy prices now respectively up "only" 14% and 19% over the year, all signs point to headline inflation having already peaked and now trending lower. On the other hand, it is less clear when underlying inflation will begin to recede substantially. Indeed, consensus expects headline CPI to decline to 8.2% year-over-year, but with core inflation remaining steady for another month at 5.3%.

In response to still-present inflation pressures, we do not think the European Central Bank (ECB) is finished monetary tightening quite yet. We expect the ECB to follow through on its guidance for another 50 bps rate hike in the Deposit Rate in March, and expect two additional 25 bps increases in May and June, which would see a peak at 3.50% for the current cycle.

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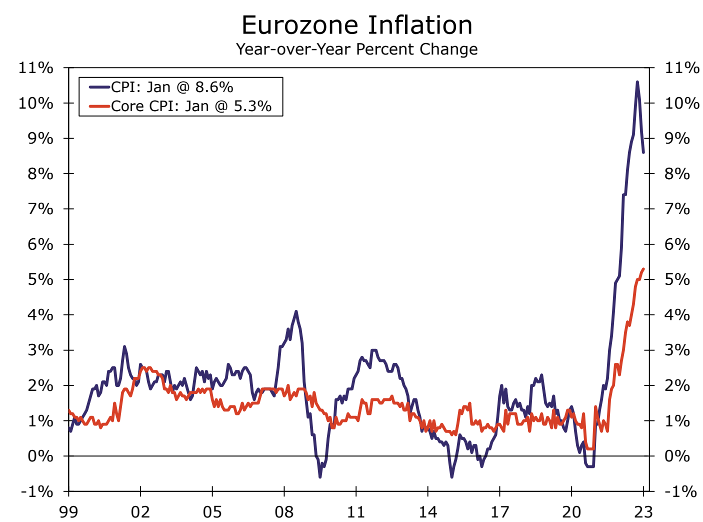

Source: Bloomberg Finance L.P. and Wells Fargo Economics

Interest Rate Watch

50 bps at the Next FOMC Meeting?

The minutes of the FOMC meeting that was held on Jan. 31-Feb. 1, which were released this week, shed some more light on the current thinking of Fed policymakers. The statement that was released at the conclusion of that meeting indicated that all 12 voting members of the Committee agreed to raise the target range for the federal funds rate by 25 bps. However, there are a total of 19 members of the FOMC, and the minutes show that "a few" Committee members favored raising rates by 50 bps at that meeting. (In any given year, seven district bank presidents do not vote at the policy meetings, but all 19 members participate in those meetings and each member gets an opportunity to speak.) Cleveland Fed President Loretta Mester and St. Louis Fed President James Bullard, both of whom are not voting members this year, recently acknowledged that they each favored raising rates by 50 bps on Feb. 1.

The economic data since the last FOMC meeting have generally been stronger than expected. For example, employment surged by 517K in January, and retail sales and industrial production both rose more than expected in January. Revised data show that consumer prices have not decelerated as much previously thought. Therefore, a few more Committee members other than Mester and Bullard may be drifting into the more hawkish camp. As of this writing, the market is pricing a probability of roughly 25% of a 50 bps rate hike at the March 22 FOMC meeting with a terminal range for the fed funds rate of 5.25%-5.50%, which is 75 bps above its current setting. We do not have a great deal of conviction around the exact amount of further tightening that lies ahead. Our current forecast looks for only 50 bps of further tightening, but we acknowledge that 75 bps is a clear possibility. The exact amount of tightening will depend on incoming data. But we have a strong conviction that the FOMC will not be easing policy anytime soon. Fed policymakers have been crystal clear in their desire to return inflation to the central bank's 2% target, and we expect the FOMC to refrain from cutting rates until early 2024.

As we wrote in this space last week, yields on U.S. Treasury securities have risen in recent weeks as market participants have started to anticipate more Fed tightening than they expected earlier this month. As shown in the following chart, the yield on the two-year Treasury note is more or less back to the 15-year high that it reached in November. The yield on the 10-year note has not returned to its October high, but it has risen nearly 60 bps since early February. This back-up in long-term Treasury yields has put upward pressure on mortgage rates. As shown below, the 30-year fixed rate mortgage have risen from 6% in early February back toward 6.5%, which has led to a 10% decline in mortgage applications for purchase over the past two weeks. Consequently, we look for the housing market to remain soft for the foreseeable future.

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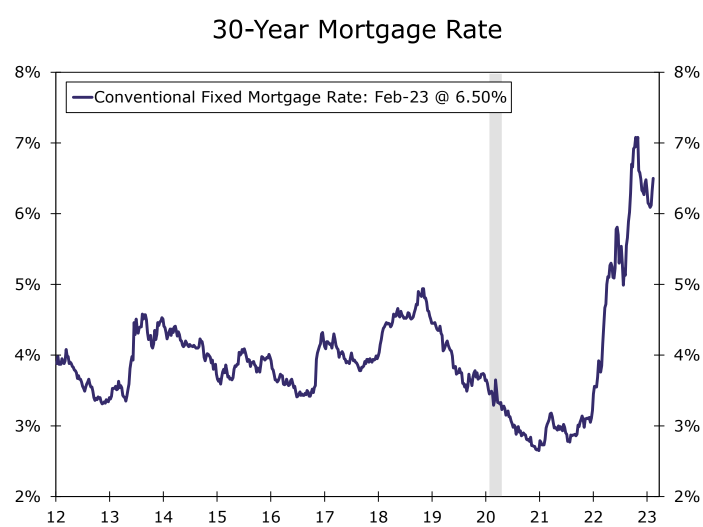
Source: Bloomberg Finance L.P. and Wells Fargo Economics



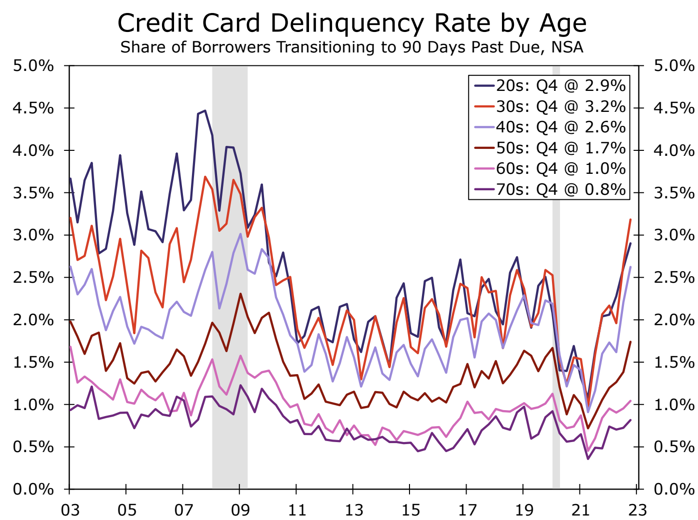
Source: Freddie Mac and Wells Fargo Economics

Credit Market Insights

Increasing Delinquency Rates for Young Borrowers

A recent research note from the New York Fed regarding their latest Quarterly Report on Household Debt and Credit shows an increasingly worrying trend in credit card and auto loan delinquency rates for younger borrowers. Due to decades high inflation increasing the costs of everything from groceries to discretionary activities, consumers have been facing increasing pressure on household balance sheets. All told, credit card balances increased by $61 billion in Q4-2022 and by $130 billion total in 2022. In addition, rising interest rates leave consumers little respite in auto purchases, as higher financing costs place additional strain on household transportation budgets. Auto loan balances in Q4-2022 increased by $28 billion, in line with a decade-long upward trend.

The rise in balances and higher costs of paying down debt have played significant roles in credit card and auto loan delinquency rates rising through the fourth quarter. Across the board, credit card and auto loan delinquencies for all borrower age groups increased. While the increase for all borrowers is similar to that experienced in the previous two quarters, younger age groups experienced the largest increases. Delinquency rates on credit cards for the 20s, 30s and 40s age groups now stand at 2.9%, 3.2% and 2.6%, respectively. Particularly significant is that the rates for these groups are now higher than their pre-pandemic rates, and this is a far cry from the lows experienced during the pandemic.



Source: New York Fed Consumer Credit Panel, Equifax and Wells Fargo Economics

Some of the rise can be chalked up to a return to pre-pandemic norms in delinquency rates, but the staggering pace at which they have risen over the past year could be cause for concern to the consumer outlook. Seasonality is a large factor at play in delinquency rates for credit cards, with rates typically reaching a seasonal peak around Q4 of any given year and declining in the following quarter. Even so, the year-over-year percentage point growth in delinquency rates for the fourth quarter reached its largest increase yet for the 30s and 40s age groups, rising 1.1% and 1.0% respectively since Q4-2021. It was the second-largest year-over-year percentage point gain in the fourth quarter for the 20s age group at a 0.9% increase over Q4-2021, with the largest being in Q4-2006, notably near the start of the Great Recession.

The rise in credit card and auto loan delinquencies for this group is concerning for younger consumers; however, personal income and spending data released this morning indicate consumers as a whole are still incredibly resilient. The next release of the Quarterly Report on Household Debt and Credit in May will be an important gauge of this uncanny staying power, as continued growth in delinquency rates for these age groups would be both historically and seasonally elevated.

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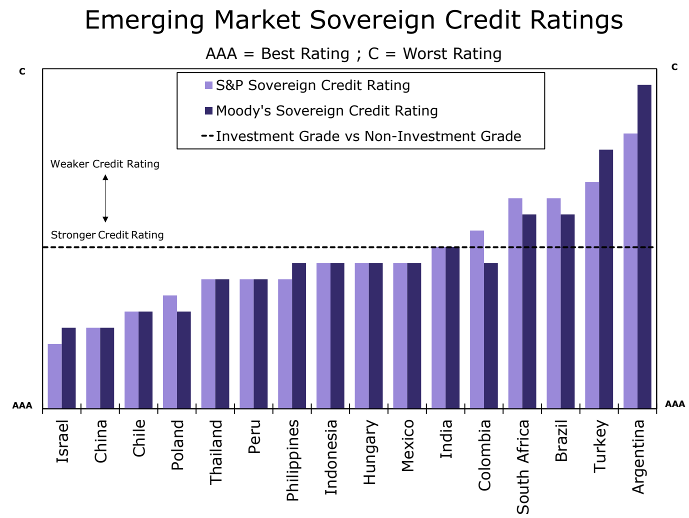
Topic of the Week

Israeli Shekel Detached from Fundamentals

We have not said this too often. But, the Israeli shekel is underperforming relative to the rest of the emerging market currency complex. Typically, the emerging market currencies that underperform are found in Turkey or Argentina. However, the shekel's recent weakness is noteworthy and understandable. For context, the Likud party won the 2022 legislative election. In Israel, the winning party's representatives nominate and recommend a leader in the Knesset (Israel's Congress). Late last year, following the Likud victory, Benjamin Netanyahu was recommended and eventually appointed by Israel's president to lead the nation's policy agenda. While he is no stranger to political office, Netanyahu's policy proposals are generating local political risk and acting as the primary driver of the shekel's underperformance. The proposals that have shaken local financial markets are centered around reforming the country's judicial system, specifically the Supreme Court of Israel. At a high level, Netanyahu and his alliance parties have proposed, and advanced through early stages of parliamentary approval, a law that would allow the governing coalition to override any Supreme Court ruling with a simple majority vote, which the Netanyahu alliance has. Should this law be passed, the ability of the Supreme Court to strike down legislation would be severely limited. In addition, the proposal gives the government an increased ability to select Supreme Court judges.



Source: Bloomberg Finance L.P. and Wells Fargo Economics

As concerning as the latest political developments are, Israel's underlying fundamentals are some of the strongest across the emerging markets and can act as foundation for a near-term shekel recovery. Israel maintains a solid investment grade sovereign credit rating by both Moody's (A1) and S&P (AA-). Relative to other credit in the Europe, Middle East and Africa (EMEA) region such as Poland, Hungary, South Africa and Turkey, Israel's fundamentals are the strongest. In fact, relative to other large emerging markets across all regions, S&P rates Israel's creditworthiness the strongest, while Moody's rates Israel quite strongly and has a "positive outlook," indicating a rating upgrade could be imminent. While local politics now represent a downside risk to the rating, a downgrade out of investment grade territory or toward the lower end of the investment grade spectrum is unlikely. It is these sound fundamentals that historically has led to subdued Israeli shekel depreciation, even during periods of extreme stress in global financial markets.

To that point, we believe Israel's currency can experience a strong rebound in the coming weeks as sound underlying fundamentals and lack of an external driver suggest the recent bout of weakness may have run its course. We also note that the independence of the Bank of Israel (BOI) was recently questioned by Israel's foreign minister Eli Cohen. Following a 50 bps rate hike at BOI's March meeting, Cohen commented how additional policy rate hikes were unjustified and asked Israel's finance minister to develop a framework to prevent a further tightening of monetary policy. These comments exacerbated shekel weakness this week; however, Cohen has since walked back his remarks while Prime Minister Netanyahu publicly defended the competence and independence of Israel's central bank, a move that stemmed the shekel's slide. In addition to Netanyahu's defense, the Bank of Israel called an emergency meeting of the Financial Stability Committee to discuss risks to Israel's financial system as a result of the latest volatility in local currency markets. We view an off-cycle meeting of the BOI Financial Stability Committee as another lever of support for the shekel. In the coming days, we would not be surprised if BOI policymakers announced an FX intervention program to provide additional support to the currency and manage outsized volatility. Historically, the Bank of Israel has not been hesitant to intervene in currency markets—to push the shekel in either direction—and given the central bank's more-than-adequate FX reserve position, policymakers certainly have the firepower to execute an effective currency management program.

Netanyahu defending BOI independence and the increasing likelihood of BOI FX intervention to support the shekel reinforces our view that the shekel is on the verge of a strong rebound and can recover most of recent losses by the end of Q1-2023. Thus, while the progress of Netanyahu's judicial reform proposal through parliament could potentially see some further depreciation in the very shortterm, current USD/ILS levels are still attractive for investors to gain ILS exposure and for corporates to hedge ILS-denominated expenses. We see merit in entering positions at current levels, and we believe a move toward ILS3.40 by the end of Q1-2023 is imminent. (Return to Summary)

Market Data • Mid-Day Friday

U.S. Interest Rates	Friday 2/24/2023	1 Week Ago	1 Year Ago
SOFR	4.55	4.55	0.05
3-Month LIBOR	4.96	4.90	0.50
3-Month T-Bill	4.82	4.79	0.30
1-Year Treasury	4.96	4.92	1.16
2-Year Treasury	4.82	4.62	1.58
5-Year Treasury	4.23	4.03	1.86
10-Year Treasury	3.96	3.81	1.96
30-Year Treasury	3.95	3.87	2.28
Bond Buyer Index	3.75	3.65	2.51

Foreign Exchange Rates	Friday 2/24/2023	1 Week Ago	1 Year Ago
Euro ($/€)	1.055	1.070	1.119
British Pound ($/£)	1.195	1.204	1.338
British Pound (£/€)	0.883	0.889	0.837
Japanese Yen (¥/$)	136.330	134.150	115.530
Canadian Dollar (C$/$)	1.361	1.347	1.282
Swiss Franc (CHF/$)	0.939	0.925	0.926
Australian Dollar (US$/A$)	0.673	0.688	0.716
Mexican Peso (MXN/$)	18.389	18.372	20.557
Chinese Yuan (CNY/$)	6.958	6.869	6.329
Indian Rupee (INR/$)	82.749	82.831	75.654
Brazilian Real (BRL/$)	5.186	5.163	5.118
U.S. Dollar Index	105.233	103.856	97.137

Foreign Interest Rates	Friday 2/24/2023	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	-0.58	-0.59	-0.57
3-Month Sterling LIBOR	4.26	4.19	0.88
3-Month Canada Banker's Acceptance	5.00	4.99	0.92
3-Month Yen LIBOR	-0.03	-0.03	-0.08
2-Year German	3.03	2.88	-0.42
2-Year U.K.	4.03	3.79	1.26
2-Year Canadian	4.30	4.15	1.53
2-Year Japanese	-0.02	-0.03	-0.03
10-Year German	2.54	2.44	0.17
10-Year U.K.	3.66	3.52	1.45
10-Year Canadian	3.43	3.29	1.92
10-Year Japanese	0.50	0.51	0.20

Commodity Prices	Friday 2/24/2023	1 Week Ago	1 Year Ago
WTI Crude ($/Barrel)	76.37	78.49	92.81
Brent Crude ($/Barrel)	83.14	83.00	99.08
Gold ($/Ounce)	1811.87	1842.36	1903.89
Hot-Rolled Steel ($/S.Ton)	1020.00	804.00	994.00
Copper (¢/Pound)	396.10	413.55	445.60
Soybeans ($/Bushel)	15.37	15.29	16.60
Natural Gas ($/MMBTU)	2.46	2.39	4.57
Nickel ($/Metric Ton)	25,176	26,268	24,887
CRB Spot Inds.	565.09	566.76	653.29

Source: Bloomberg Finance L.P. and Wells Fargo Economics

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