2012 Annual Report

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This translation of the financial statement is for convenience purposes only. The only binding version of the financial statement is the Hebrew version

Report of the Board of Directors to the General Meeting of Shareholders

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Report of the Board of Directors to the General Meeting of Shareholders

At the meeting of the Board of Directors held on March 17, 2013, it was resolved to approve and publish the consolidated financial statements of Mizrahi Tefahot Bank Ltd. and its investees as of December 31, 2012.
The financial statements were prepared in accordance with the directives and guidelines issued by the Supervisor of Banks.

The General Environment and Effect of External Factors on the Bank Group

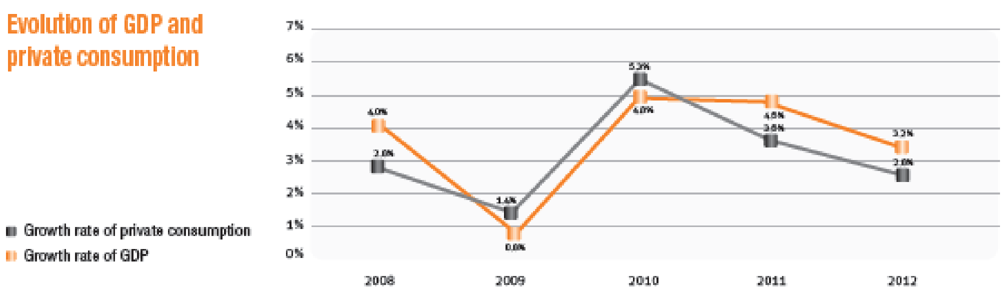
Developments in Israel's Economy in 2012

Real Developments

Economic growth continued in 2012, but at a more moderate pace compared to the previous year. According to estimates by the Central Bureau of Statistics, GDP growth in 2012 was at 3.2%, following a 4.6% growth rate in the previous year. Business GDP grew in 2012 by 3.2%, compared to 5.1% growth in 2011.

The growth rate slowed down during the year, impacted by lower growth rate of private consumption and of exports of goods and services - against the backdrop of the global slow-down. The lower growth rate was particularly noticeable in the fourth quarter of 2012, in which GDP grew at an annualized rate of 2.5%.

Total uses (export, private and public consumption and gross domestic investment) increased in 2012 by 3.2%, compared to 6.3% growth in 2011. Imports of goods and services grew by 3.2%, compared to 11.1% growth last year. Exports of goods and services slowed down, with only 0.5% growth in 2012, compared to 5.5% growth in the previous year.



In 2012, the trade deficit grew by 24.9% in USD terms, primarily due to a USD 4 billion decrease in exports. Private consumption growth slowed down to 2.8% in 2012, compared to 3.6% growth in the previous year. Total domestic investments slowed significantly in 2012, to 10.4% - compared to 23.5% in the previous year - primarily due to slower growth of investment in fixed assets, from 16.0% in 2011 down to 3.4% in 2012.

Unemployment remained stable during the year: In the fourth quarter of 2012 unemployment was at 6.9%, compared to 6.8% in the previous quarter and to 6.8% in the year-ago period.

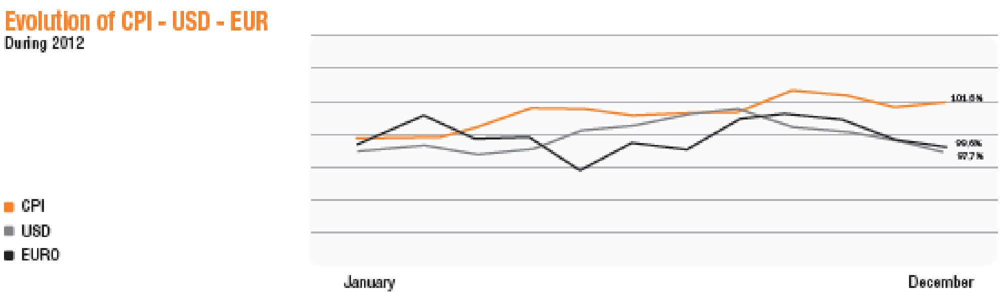
Inflation and exchange rates

In 2012, the Consumer Price Index increased by 1.6%, compared to an increase of 2.2% in 2011. The increase was primarily due to housing and house maintenance prices and to food prices. In the fourth quarter of this year, inflation was further moderated.

In 2012, the USD was devalued by 2.3% against the NIS, reaching NIS 3.733 per USD 1 at the end of 2012, compared to NIS 3.821 at the end of 2011. During the year, the trend was mixed. The devaluation trend, which started in February, reached a zenith in July, with the USD trading at NIS 4.084. Since the end of July, the NIS was revalued vs. the USD.

The Euro was devalued against the NIS in this period by 0.4%, reaching NIS 4.921 per Euro at the end of 2012, compared to NIS 4.938 per Euro at the end of 2011. On March 11, 2013, the USD/NIS exchange rate was 3.690 and the EUR/NIS exchange rate was 4.796.

In 2012, the Bank of Israel avoided buying foreign currency, after buying foreign currency valued at USD 4 billion in 2011 and at NIS 12 billion in 2010.



Monetary and fiscal policy

In 2012, the Bank of Israel lowered its interest rate three times, from 2.75% at year start to 2.00% at year end. This against the backdrop of expectations of relatively stable inflation. The Bank of Israel interest rate for January 2013 was once again lowered, to 1.75%.

In 2012, the Government budget deficit amounted to NIS 39.0 billion, or 4.2% of GDP, compared to a NIS 28.6 billion deficit last year (3.3 of GDP). Tax revenues increased in 2012 by only 3.5% over 2011, and were 6.3% lower than expected. Expenditures by Government ministries increased in this period by 7.1%, compared to planned increase of 4.9%.

In late January 2013, the Governor of the Bank of Israel, Professor Stanley Fisher, announced his intended resignation on June 30, 2013, after more than 8 years in office.

Residential construction and the mortgage market

According to data from the Central Bureau of Statistics, in 2012, demand for new apartments (apartments sold and apartments constructed not for sale) was 39,370 apartments - similar to demand in 2011 - a decrease of 2.7% compared to 2010. The Jerusalem region posted a 28% increase, and the Central District, with the highest demand compared to other regions, decreased by 7.5%. The stable demand for housing was reflected by a modest 4.4% increase in housing loan origination; in 2012, housing loans to the public amounted to NIS 47.2 billion, compared to NIS 45.0 billion in 2011. Mortgage origination in the second half of 2012 was 27% higher than in the first half of this year.

The pace of housing construction starts slowed down, with construction started on an annualized 37,500 residential units in January-September 2012, compared to 45,600 residential units in 2011. However, this is still a high pace compared to the annual average over the past decade, which was 34,500 housing construction starts. The slow-down in housing construction starts resulted in stable inventory of new apartments for sale from private development, which at the end of December was at 15,300 apartments, similar to the end of 2011. Based on the average pace of sales in the six months ended December 2012, this inventory would account for 11.8 months' sales - compared to 12.9 months at the end of 2011.

According to data from the Central Bureau of Statistics, in 2012 housing prices continued to rise and at a faster pace. Housing prices, on nation-wide average basis, were 5.6% higher in October 2012 compared to the end of 2011, following 4.0% growth for all of 2011.

On November 1, 2012, the Supervisor of Banks issued a letter instructing banking corporations to limit the loan-to-value ratios approved for housing loans. For details, see the chapter on Legislation and Supervision of Bank Group Operations.

Capital market

In 2012, markets were higher, as opposed to the sharp declines in 2011, along with lower trading volumes. Support from international markets on the one hand, and concerns about a slow-down and sharply larger Government deficit on the other hand, eventually resulted in the Israeli stock market lagging behind overseas equity markets. The picture at the outset of 2013 is similar.

Equity market - The leading benchmarks, Tel Aviv 25 and Tel Aviv 100, were higher in 2012 by 9.2% and 7.2%, respectively, compared to decrease of 18.2% and 20.1% in 2011. The Tel Aviv 75 Index was up 4.8%, compared to an increase of 25.9% in 2011. The Real Estate 15 Index was up by 14.1%, compared to a decrease of 23.2% in 2011. The

YETER Stock Index rose by an impressive 21.6%, compared to a 25.7% decline in the previous year. Financials sector shares were also sharply higher: The Banking and Financials 15 indices were up by 22.9% and 23.1%, respectively, compared to decreases of 34.6% and 34.0% in 2011.

Average daily trading volume in equities and convertible securities in 2012 amounted to NIS 1.1 billion, compared to NIS 1.7 billion in 2011. In the final quarter of 2012, average daily trading volume was NIS 1.2 billion, compares to NIS 1.4 billion in the final quarter of 2011.

Share issuance (excluding shares issued overseas) dropped significantly, amounting to NIS 3.8 billion, compared to NIS 5.9 billion in 2011.

Debenture market - the Government debenture market was higher across the board in 2012 due to lower interest rates, low inflation in Israel and low interest and yield environments overseas. Debentures with longer terms were up more sharply than those with shorter terms. Corporate debenture benchmarks were up by similar rates to those of Government debentures, with higher increases than in 2011, inter alia due to the stronger equity market. Concerns about increasing budget deficit and the start of an upward trend in yield to maturity of US Government debentures both moderated the increases early in the year.

The General Debenture Index was up by 8.8% in 2012, compared to 2.5% in 2011. The CPI-Linked Government Debenture Index rose in 2012 by 9.4%, after rising by 4.3% in 2011. The Non-Linked Debenture Index was up by 7%, following last year's 5.2% increase. The leading Tel Bond benchmarks were also higher. In 2012, the Tel Bond 20 Index was up by 7.9%, compared to an increase of 0.7% in the previous year, and the Tel Bond 40 Index rose in 2012 by 9.1%, compared to a decrease of 1.6% in 2011.

The low interest rate environment was reflected by corporate debentures, with lower spreads of their yield to maturity compared to Government debentures: Debentures rated AA traded at the end of 2012 at a yield spread of 0.8 percentage points, compared to 1.4 percentage points at the end of 2011; debentures rated A traded at the end of 2011 at a yield spread of 2.75 percentage points, compared to 3.5 percentage points at the end of 2011. In the past year, the AAA rating only included debentures of Israeli Electric Company - guaranteed by the State of Israel.

Overall, the business sector raised debenture debt from the public and from institutional investors, valued at NIS 40 billion in 2012, similar to 2011. The average daily trading volume in corporate debentures in 2012 amounted to NIS 4.1 billion, compared to NIS 3.8 billion in 2011 - an increase of 9.0%.

Global economy

In 2012, the economic slow-down in Europe continued, and even reached core countries (Germany, France). According to the Euro Zone Central Bureau of Statistics, based on preliminary estimates of GDP growth in 2012, the Euro Zone GDP is expected to shrink by 0.4% in 2012, following growth of only 1.4% in 2011. Moreover, unemployment in the Euro Zone continued to rise this year, reaching 11.8% in November. Monthly inflation, in annualized terms, was also lower at 2.2% in December 2012, compared to 2.6% in January 2012.

The EU reached some understandings on support for PIIGS[1] countries, including a more flexible approach to providing monetary assistance and intervention in the debenture market, refinancing and capital infusion to banks troubled by liquidity issues and high concentration of troubled assets, directly by assistance funds and unified supervision over banks in Europe.

Signs of recovery were evident in the USA. GDP growth in 2012 was 2.2%, compared to 1.8% in 2011. The labor market also showed signs of improvement, with the unemployment rate declining from 8.3% in 2011 to 7.8% at the end of 2012. In addition, the average number of new jobs created per quarter in 2012 was 622 thousand jobs, compared to a quarterly average of 526 thousand jobs in 2011. Other indicators, including various real estate benchmarks, also indicated improvement in the US economy during the year.

Signs of recovery were also evident in emerging markets. In China, GDP growth in 2012 was 7.8%, compared to 9.3% growth in 2011, but growth accelerated during the year. In order to promote growth, the Central Bank of China took some monetary stimulus steps in the second quarter: lower interest rates in this country and reduced capital adequacy ratio required of banks. The Central Bank of China recently indicated it was considering further monetary measures to stimulate the economy.

During the year, many countries around the world started to take action to create a competitive advantage in global trade over other countries, inter alia by devaluation of their own currency through significant monetary expansion, lower domestic interest rates and lower capital adequacy ratios for domestic banks.

The Dow Jones Index rose by 5.7% in 2012, compared to 6.2% in 2011. The S&P 500 Index was up by 12.9% in 2012, compared to an increase of 0.4% in the previous year; the NASDAQ 100 Index was up by 16.4% in 2012, following an increase of 2.7% in 2011.

In the UK, the FTSE 100 Index was up by 5.9%, after declining 6.8% in 2011; the German DAX and French CAC benchmarks were higher by 30.2% and 16.4%, respectively, in 2012 - compared to being down by 15.4% and 18.8%, respectively, in 2011. In Japan, the Nikkei Index was up by 23.4%, compared to a decrease of 18.6% in 2011.

(1) Portugl, Italy, Ireland, Greece and Spain

Key data for Bank group

Evolution of income and expenses

	For the year ended December 31,			Change compared to	
	2012	2011	2010	2011	2010
					NIS in millions
Profit and Profitability					
Interest revenues, net	3,214	3,099	2,888		
Non-interest financing revenues (expenses)	95	18	(25)		
Commissions and other revenues	1,478	1,491	1,465		
Total revenues	**4,787**	**4,608**	**4,328**	**3.9%**	**10.6%**
Expenses with respect to credit loss	276	338	473	(18.3%)	(41.6%)
Operating and other expenses	2,786	2,667	2,566	4.5%	8.6%
Profit before provision for taxes	1,725	1,603	1,289	7.6%	33.8%
Provision for taxes	599	522	469	14.8%	27.7%
Net profit(1)	**1,076**	**1,044**	**801**	**3.1%**	**31.3%**

	For the year ended December 31,			Change compared to	
	2012	2011	2010	2011	2010
					NIS in millions
Balance sheet - key items					
Balance sheet total	162,242	150,246	133,304	8.0%	21.7%
Loans to the public, net	128,651	(2) 119,293	(2) 107,003	7.8%	20.2%
Securities	9,041	8,432	7,449	7.2%	21.3%
Deposits from the public	128,499	119,236	105,991	7.8%	21.2%
Debentures and subordinated notes	14,039	12,202	9,813	15.1%	43.1%
Equity(1)	8,811	7,666	7,130	14.9%	23.6%

	2012	2011	2010
Key financial ratios (in percent)			
Net profit return on equity	13.1	14.6	11.8
Net loans to the public to deposits from the public	100.1	100.0	101.0
Capital to total assets	5.43	5.10	5.35
Ratio of Tier I capital to risk elements	8.55	7.77	7.91
Total ratio of capital to risk elements	13.35	13.4	13.96
Cost income ratio	58.2	57.9	59.3
Expenses with respect to credit loss to loans to the public, net for the period	0.21	0.28	0.44
Basic net earnings per share	4.77	4.65	3.63
Diluted net earnings per share	4.74	4.57	3.58

(1) Any mention of "net profit" or "equity" in this Board of Directors' Report refers to net profit and equity attributable to equity holders of the Bank.

(2) Reclassified.

Evolution of income and expenses

	For the three months ended				
	31.12.2012	30.9.2012	30.6.2012	31.3.2012	31.12.2011
	NIS in millions				
Profit and Profitability					
Interest revenues, net	643	900	(1) 871	(1) 800	(1) 734
Non-interest financing revenues (expenses)	229	(98)	(1) (22)	(1) (14)	(1) 52
Commissions and other revenues	373	385	(1) 355	(1) 365	(1) 366
Total revenues	**1,245**	**1,187**	**1,204**	**1,151**	**1,152**
Expenses with respect to credit loss	48	116	45	67	62
Operating and other expenses	740	676	676	694	689
Profit before provision for taxes	457	395	483	390	401
Provision for taxes	176	121	174	128	93
Net profit[(1)]	**270**	**260**	**295**	**251**	**299**

	31.12.2012	30.9.2012	30.6.2012	31.3.2012	31.12.2011
	NIS in millions				
Balance sheet - key items					
Balance sheet total	162,242	157,810	155,311	150,244	150,246
Loans to the public, net	128,651	(1) 126,566	(1) 123,386	(1) 120,369	(1) 119,293
Securities	9,041	7,966	9,565	11,230	8,432
Deposits from the public	128,499	124,322	122,284	119,501	119,236
Debentures and subordinated notes	14,039	14,186	13,873	12,722	12,202
Equity [(1)]	8,811	8,514	8,231	7,933	7,666

	31.12.2012	30.9.2012	30.6.2012	31.3.2012	31.12.2011
Key financial ratios (in percent)					
Net profit return on equity [(2)]	13.1	13.0	15.4	13.6	16.9
Net loans to the public to deposits from the public	100.1	101.8	100.9	100.7	100.0
Capital to total assets	5.43	5.40	5.30	5.28	5.10
Ratio of Tier I capital to risk elements	8.55	8.23	8.03	7.94	7.77
Total ratio of capital to risk elements	13.35	13.11	12.93	13.24	13.40
Cost income ratio	59.4	57.0	56.1	60.3	59.8
Expenses with respect to credit loss to loans to the public, net for the period [(2)]	0.15	0.37	0.15	0.22	0.21
Basic net earnings per share	1.19	1.15	1.31	1.12	1.33
Diluted net earnings per share	1.17	1.14	1.29	1.11	1.32

(1) Reclassified.
(2) Quarterly on annualized basis.

Bank Group Operations and Description of its Businesses Development

Forward-looking information

Some of the information in the Report of the Board of Directors, which does not relate to historical facts, constitutes “forward-looking information”, as defined in the Securities Law, 1968 (hereinafter: “the Law”).

Actual Bank results may materially differ from those provided in the forward-looking information due to multiple factors including, inter alia, changes in local and global capital markets, macro-economic changes, geo-political changes, changes in legislation and regulation and other changes outside the Bank's control, which may result in non-materialization of estimates and/or in changes to business plans.

Forward-looking information is characterized by the use of certain words or phrases, such as: "we believe", "expected", "forecasted", "estimating", "intending", "planning", "readying", "could change" and similar expressions, in addition to nouns, such as: "plan", "goals", "desire", "need", "could", "will be". These forward-looking information and expressions involve risk and lack of certainty, because they are based on management's assessment of future events which includes, inter alia: forecasted economic developments in Israel and worldwide, especially the state of the economy, including the effect of macroeconomic and geopolitical conditions; changes and developments in the inter-currency markets and the capital markets, and other factors affecting the exposure to financial risk, changes in the financial strength of borrowers, the public’s preferences, legislation, supervisory regulations, the behavior of competitors, aspects related to the Bank’s image, technological developments and human resources issues.

The information presented here relies, inter alia, on publications of the Central Bureau of Statistics and the Ministry of Finance, on Bank of Israel data and on various forecasts and assessments on various topics with regard to the future.

Bank Group

Mizrahi Tefahot Bank Ltd. ("the Bank") was among the first banks established in the State of Israel. The Bank was associated as a public company on June 6, 1923, under the name Mizrahi Bank Ltd., and it was issued the license to commence business on May 13, 1924. The Bank was founded at the initiative of the World Mizrahi Center, in order to facilitate the financing of settlement, construction, manufacturing, labor and commercial activities of the new settlers in the Land of Israel. In 1969, upon the merger of the businesses of the Bank with the businesses of Hapoel Hamizrahi Bank Ltd., the Bank’s name was changed to United Mizrahi Bank Ltd. In 1983, within the framework of the arrangement formulated between the Israeli Government and the Banks, the shares of the Bank were transferred to the control of the State through a securities company that was established for this purpose. In the years 1995 and 1997, the Bank was privatized in two stages, and was transferred to control of the present controlling shareholders. Following the merger between United Mizrahi Bank Ltd and “Tefahot” Israel Mortgage Bank Ltd. (“Tefahot”), the merged bank's name was changed on November 7, 2005 to its present name, Mizrahi Tefahot Bank Ltd.

The Bank Group operates in Israel and overseas. The Bank Group is engaged in commercial banking (business and retail) as well as mortgage activities in Israel, through a nation-wide network of 175 branches and business centers. Furthermore, business clients are supported by business centers and professional departments at Bank headquarters, which specialize by sector.

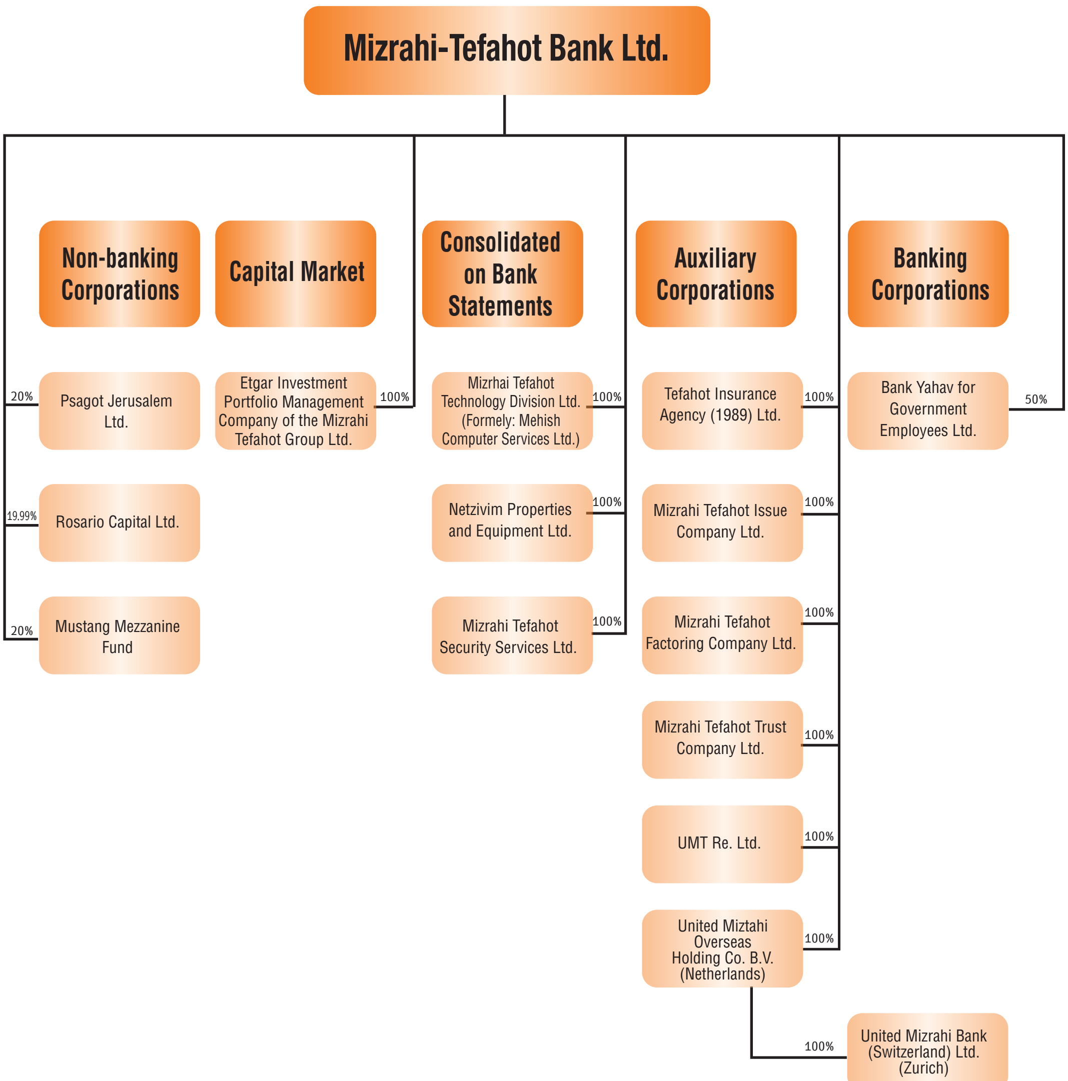
The Bank's overseas operations are conducted via 4 bank affiliates (three branches and a subsidiary) and 4 representative offices in Europe and Latin America.

In addition to its banking activities, the Bank Group is engaged in various activities related to the capital market, including: consultancy for capital market activities, management of securities portfolios for clients, pension advisory service, trust services, distribution of mutual funds and provident fund operation.

The Bank is one of the five largest bank groups in Israel. Below is the Bank Group's share out of the five leading groups, (According to the financial statements for September 30, 2012):

Loans to the public	16%
Deposits from the public	14%
Balance sheet total	13%
Shareholders' equity	11%

Holding Structure - Major Companies [1]:



For further information about organizational changes in the Group, see Note 6 to the financial statements.

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[1] The Bank has holdings in other companies which are not material to Bank operations.

Control of the Bank Group

To the best of the knowledge of the Bank and the Board of Directors, the holding stakes of controlling shareholders of the Bank, as of December 31, 2012 [1], are as follows:

	Holder	No. of shares	Share of equity and voting rights
Wertheim Group	M.W.Z. (Holdings) Ltd.[2]	20,743,785	9.13
	F & W (Registered Partnership) [3]	29,475,441	12.98
	Total Wertheim Group	50,219,226	22.11
Ofer Group	C.A.B.M. Ltd.[4]	7,066,264	3.11
	L.A.B.M. (Holdings) Ltd.[5]	12,862,041	5.66
	A.A.B.M. Ltd. [6]	15,175,631	6.68
	Ofer Investments Ltd.[7]	14,591,953	6.43
	Ofer Sahaf Ltd. [8]	7,477,642	3.29
	Total Ofer Group	57,173,531	25.18
	Total holding stake of controlling shareholders	107,392,757	47.29
Total shares issued by the Bank		[9] 227,099,500	100.00%

(1) For information about changes in holding stakes of controlling shareholders after the balance sheet date, see below under Shareholder Agreements.

(2) A private company, the shares of which are held by Mr. Moshe Wertheim (99.2%) and in trust for Mr. Moshe Wertheim by Attorney Binyamin Rothenberg (0.8%).

(3) A registered partnership held by Mr. Moshe Wertheim (1%) and by M.W.Z. (Holdings) Ltd (99%).

(4) A private company wholly-owned and controlled by Ofer Development and Investments Ltd., a private company, the shares of which are held by Ofer Sahaf Ltd. (89.1%) and by Nazareth Industrial Properties (10.9%). Nazareth Industrial Properties Ltd. is a private company wholly-owned and controlled by Ofer Development and Investments Ltd. Ofer Sahaf Ltd. is a private company wholly-owned and controlled by Ofer Development and Investments Ltd.

(5) A private company wholly-owned and controlled by L.I.N. (Holdings) Ltd., which is a private company owned by a foreign trust whose main beneficiaryr, with regard to Bank shares, is Mr. Eyal Ofer (95%) and a foreign-resident company (5%). The foreign trust has given Mr. Eyal Ofer power-of-attorney to vote at General Meetings of L.I.N. with regard to issues concerning the control permit of the Bank, Bank shares directly and indirectly owned by L.I.N., appointment of Board members at the Bank and all matters concerning the Bank. The power-of-attorney gives Eyal Ofer full authority to act on these matters as he sees fit.

(6) A private company wholly-owned and controlled by Ofer Brothers Holdings Properties Ltd., a private company wholly-owned and controlled by Ofer Investments Ltd.

(7) A private company, the shares of which are held by Leora Ofer (15%), Doron Ofer (15%), Yehuda (Yuli) Ofer RIP (36.67%), and L.I.N. (Holdings) Ltd.(33.33%), which is a private company owned by a foreign trust whose main beneficiary, with regard to Bank shares, is Mr. Eyal Ofer (95%) and a foreign-resident company (5%) (see also footnote 5 above).

(8) A private company wholly-owned and controlled by Ofer Investments Ltd.

(9) Excludes 2,500,000 dormant shares bought back by the Bank in 2009.

Shareholder agreements

Between A.A.B.M. Ltd., C.A.B.M. Ltd., and L.A.B.M. (Holdings) Ltd. as the first party (hereinafter: (“Ofer Group”) and between Feinberg-Wertheim (Registered Partnership) as the other party ("Wertheim Group") for cooperation in exercising rights associated with Bank shares ("voting agreement"). The aforementioned voting agreement stipulates, inter alia, rules for joint voting of controlling shareholders at General Meetings, for each party's right of refusal upon sale of controlling shares by the other parties, for rights to appoint Board members and for rights to appoint the Chairman of the Board of Directors.

Ofer Group

On August 22, 2011, Ofer Investments Ltd. (hereinafter: "Ofer Investments") reported to the Bank concerning a letter that it had received from the Supervisor of Banks concerning the permit to acquire control and means of control over the Bank (hereinafter: "the Supervisor's letter"). Ofer Investments informed the Bank, inter alia, that the Supervisor's letter is based on the long-standing demand by the Supervisor of Banks that recipients of the Control Permit over the Bank should modify the holding structure of controlling Bank shares, such that these shares would be separate from other operations of Ofer Investments, including holding real estate properties.
Furthermore, on January 17, 2013 the Bank received notice from Ofer Investments, with regard to a permit dated January 17, 2013 given by the Governor of the Bank of Israel, for holding control and means of control over the Bank by the Ofer Group (as defined in the control permit - i.e. Eyal Ofer, Doron Ofer, Liora Ofer and the estate of Juli Ofer RIP managed by temporary estate administrators, Attorneys Zvi Efrat and Reuven Bachar) and by the Wertheim Group (i.e. Mr. Moshe Wertheim), pursuant to the Banking Act (Licensing), 1981 (hereinafter: "the new permit"). On this matter, see the report issued by the Bank on January 17, 2013 (reference 2013-01-016320). This citation constitutes inclusion by way of reference of all information provided in the aforementioned report.

Through the receipt date of the new permit, the Ofer Group held Bank shares (controlling interest shares and non-controlling interest shares) through Ofer Investments and its subsidiaries, and through L.I.N. (Holdings) Ltd. (hereinafter: "L.I.N") and its subsidiary. Upon receiving the new permit, the outline of change in the Bank holding structure came into effect, referring only to the holding of Bank shares by Ofer Investments, to separation of the holding of controlling interest shares of the Bank from other operations of Ofer Investments, including holding of real estate properties (hereinafter: "new structure change"). The new structure change includes transfer of controlling interest shares of the Bank (indirectly held by Ofer Investments) to be indirectly held by a sister company of Ofer Investments, Ofer Holdings (1989) Ltd. (hereinafter: "Ofer Holdings"). As a result of the new structure change, Ofer Investments would continue to hold ordinary Bank shares (not part of the controlling interest), directly and through a subsidiary.

New cooperation agreement between individuals of Ofer Group and corporations under their control

As Ofer Investments informed the Bank, upon receiving the new permit and implementing the new structure change, a new cooperation agreement became effective between individuals of Ofer Group and corporations under their control, who hold Bank shares directly and indirectly. The new cooperation agreement replaces previous agreements between the parties. In the aforementioned agreement, the parties agree that relations with regard to Bank holdings, control over the Bank and management rights between the Juli Group (recipients of the control permit from the family of Juli Ofer RIP, including temporary or permanent administrators of his estate, pending distribution of shares owned by Juli Ofer RIP) (hereinafter: "the Juli Group") and L.I.N (in which Eyal Ofer has power of attorney to act with regard to Bank business), would be shared on a 50-50 basis, so that the Board member quota of the Ofer Group would be equally divided between L.I.N and the Juli Group, and no decisions would be made by the Ofer Group with regard to any Bank-related matter without the mutual consent of L.I.N and the Juli Group. For more information, see section 3 in the Bank's Immediate Report dated January 17, 2013 (reference 2013-01-016320). This citation constitutes inclusion by way of reference of all information provided in the aforementioned report.

The notice from Ofer Investments to the Bank further indicated that Ofer Investments and Ofer Sahaf Ltd. (which would continue to hold non-controlling interest Bank shares) have committed, in the new cooperation agreement, to act pursuant to provisions of the control permit, as these may be from time to time, if applicable to them, including to only exercise voting rights with respect to Bank shares they hold in accordance with the decision made with regard to exercise of voting rights with respect to controlling interest Bank shares. Moreover, these companies committed that, should their shares be offered in future to the public, their aforementioned commitment would be reflected in the prospectus to be made public.

Wertheim Group

On February 17, 2013, Mr. Moshe (Mosie) Wertheim informed the Bank that he had gifted to his children his shares and holdings of corporations holding Bank shares which are part of the controlling interest in the Bank, M.W.Z (Holdings) Ltd. and F&W (Registered Partnership), as follows: to Mr. David Wertheim - 63% of his holding stake, and to Ms. Drorit Wertheim - 37% of his holding stake.

According to Mr. Moshe Wertheim's notice to the Bank, this transfer of shares is subject, inter alia, to obtaining a control permit from the Governor of the Bank of Israel, pursuant to the Banking Act (Licensing), 1981.

Investments in Bank Capital and Transactions in Bank Shares

The Bank holds 2,500,000 of its shares bought back in 2009, as approved by the Bank of Israel, for consideration of NIS 76 million. On January 30, 2013, the Bank of Israel allowed the Bank to use the shares held by the Bank for its 2013 stock option plan. See Note 13 to the financial statements for additional information.

On February 1, 2009, the Bank allotted to the trustee, on behalf of Mr. Eliezer Yones, 5,571,381 options, not listed for trading on the stock exchange, pursuant to provisions of the option allotment plan in accordance with a private offering approved by the Bank Board of Directors on November 30, 2008 - which is an integral part of the president's employment terms. The ordinary shares, of NIS 0.1 par value each, to be allotted upon exercise of the options, would be listed for trading on the stock exchange. These options are in addition to Bank securities owned by the President in person and through the Trustee.

See further information see Note 16.A.1. to the financial statements.

Board of Directors' decision with regard to capital adequacy ratio

Pursuant to directives of the Supervisor of Banks dated June 30, 2010, according to which the Bank must adopt a target core capital ratio as of December 31, 2010, in reference to core capital net of all deductions required under Tier I, pursuant to provisions of Proper Banking Conduct Regulation 202 ("Measurement and Capital Adequacy - Capital Components") (hereinafter - "core capital ratio"), the Bank's Board of Directors resolved on October 25, 2010 to determine that the target core capital ratio (original Tier I capital adequacy ratio) shall be no less than 7.5%. Further, the Board of Directors resolved to direct Bank management to act so as to maintain appropriate safety margins, in order to ensure that the core capital ratio shall be no less than the foregoing. The Bank Board of Directors further resolved that the overall capital adequacy ratio shall be no less than 12.5%.

On March 28, 2012, the Supervisor of Banks issued a directive to all banking corporations, citing a higher minimum core capital ratio than the one currently required. According to the directive, all banking corporations would be required to achieve a minimum core capital ratio of 9% by January 1, 2015. In addition, large banking corporations, whose total consolidated balance sheet assets exceed 20% of total balance sheet assets for the Israeli banking sector, would be required to achieve a minimum core capital ratio of 10% by January 1, 2017. The directive with regard to a minimum core capital ratio of 10% does not apply to the Bank. The core capital ratio should be calculated in conformity with Basel III provisions.

On July 23, 2012, the Bank's Board of Director instructed Bank management to advance implementation of the Supervisor of Banks' directive dated March 28, 2012 - so as to implement it, if possible, as from January 1, 2014. Moreover, the Board of Directors has resolved to instruct Bank management to maintain, in as much as possible, appropriate safety margins to this end. On December 31, 2012, the Advisory Committee on Banking Business received draft amendments to Proper Conduct of Banking Business Regulations 201-211 (concerning adoption of Basel III directives with regard to supervisory capital and with regard to risk assets).

Proper Conduct of Banking Business Regulation 202 (Capital measurement and adequacy - supervisory capital) adopts the Basel III recommendations in Israel.

The Bank is reviewing the effect of anticipated changes on its capital, pursuant to the new draft directives on application of Basel III directives, as described above.

For details of these draft directives and the anticipated effect on the Bank's capital adequacy, see chapter "Legislation and Supervision of Bank Group Operations".

For further information about the Bank's capital adequacy ratio and the expected impact of implementation of Basel III directives, see reference under section "Capital adequacy" in the chapter "Risk Management" – "Basel II: Pillar 3 - Market Discipline". For details of the risk adjusted capital ratio, see Note 14 to the financial statements.

Raising of capital sources

In conjunction with the Bank's work plan, which is set by the Board of Directors and includes growth objectives for different operating segments, an assessment is made of the impact of achieving these objectives on total risk assets for the Bank, and therefore on its capital adequacy ratio. Accordingly, along with business and profitability objectives, a plan is set to raise capital sources in order to maintain capital adequacy, in accordance with instructions of the Board of Directors for purposes of capital adequacy, as described above.

Bank management believes that no capital needs to be raised over the next 12 months for purposes of compliance with the minimum capital ratio requirement pursuant to Proper Conduct of Banking Business Regulations No. 202. This information is forward-looking information, as defined in the Securities Act, 1968, based on assumptions, facts and data (hereinafter jointly: "assumptions") brought to the attention of the Board of Directors. These assumptions may not materialize due to factors not all of which are under the Bank's control.

For details of raising funds by means of obligatory notes and debentures, see the chapter on Sources and Financing.

Dividend Distribution

Dividend distribution policy

On April 3, 2006, the Bank's Board of Directors adopted a resolution on a dividend distribution policy, whereby, provided that the Bank's capital ratio is not less than 10% (in terms of Proper Conduct of Banking Business Regulation 311 - Basel I), dividends will be distributed every year at the rate of 40% of the net operating profit and 80% of the profit from extraordinary items of that year. The dividend distribution policy is in effect as from the year 2006. On July 23, 2012, the Bank Board of Directors determined, in conjunction with approval of the new strategic five-year plan for 2013-2017, that during the plan term, the Bank's adopted dividend distribution policy would be maintained.

In addition to the aforesaid, the distribution of dividends by the Bank is subject to the provisions of law and additional limitations, as provided in Note 13 to the financial statements.

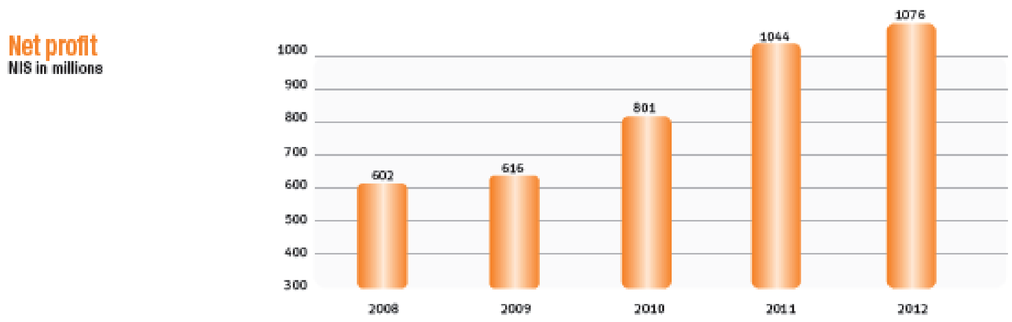
Distributed Dividends

Below are details of dividends distributed and declared by the Bank since 2010 through the publication date of these financial statements (in reported amounts):

Payment date	Dividend per share (in Agorot)	Total dividends paid (NIS in millions)
September 08, 2010	89.59	200
April 17, 2011	53.65	120

Profit and Profitability

Net profit for the Group in 2012 amounted to NIS 1,076 million, compared to NIS 1,044 million in the corresponding period last year - an increase of 3.1%.



Net profit for the Group in the fourth quarter of 2012 amounted to NIS 270 million. Net profit in the corresponding period last year amounted to NIS 299 million (including the non-recurring effect of a NIS 45 million decrease in tax expenses, as follows). Excluding this non-recurring effect, an increase of 6.3% to the corresponding period last year.

In accordance with the Bank of Israel directive on capital adequacy in the banking system, the Bank's Tier I capital adequacy ratio increased to 8.55% at the end of 2012. This increase, due to a 15% increase in capital compared to end of 2011, naturally impacts the return on capital.

The rate of return on capital for 2012 was 13.1% (in terms of 2011 capital – 14.2%). In the corresponding period last year, return on equity was 14.6%.

The rate of return on capital in the fourth quarter of 2012, in annualized terms, was 13.1% (in terms of 2011 capital – 14.8%). In the corresponding period last year, the return on equity was 16.9%.

The target for return on equity in 2017, in the new five-year strategic plan for 2013-2017 (based on Tier I capital adequacy of 9%) is 14.5%.

The following key factors affected Group profit in 2012, compared to 2011:

- Financing revenues (net interest revenues and non-interest financing revenues) increased in 2012 by NIS 192 million, to NIS 3,309 million - compared to NIS 3,117 million in 2011 - an increase of 6.2%.
- Expenses with respect to credit loss decreased in 2012 by NIS 62 million compared to 2011 - a decrease of 18.3%.
- Commission and other revenues in 2012 amounted to NIS 1,478 million, compared to NIS 1,491 million in 2011 - a decrease of 0.9%, primarily impacted by lower revenues from customer activity in the capital market: The average daily trading volume in shares and convertible securities declined by 35% over the corresponding period last year.
- Operating and other expenses amounted to NIS 2,786 million in 2012, compared with NIS 2,667 million in 2011, an increase of 4.5%.
- The rate of provision for taxes on profit in 2012 increased to 34.7%, compared to 32.6% in the corresponding period last year. The corresponding period last year includes a NIS 45 million reduction in tax expenses with respect to deferred taxes, following recommendations of the Trachtenberg Commission.

Change in format of statement of profit and loss

Starting with financial statements for the first quarter of 2012, the profit & loss statement has been compiled in conformity with the new format specified in the Supervisor of Banks' Public Reporting Regulations. Accordingly, data for previous periods was restated to allow for comparison to data for the current period. The major change in format of the statement of profit and loss relates to presentation of profit from financing operations, previously listed on a single line, which as from these financial statements is included under the following items:

	For the year ended December 31,		For the quarter ended December 31,	
	2012	2011	2012	2011
Profit from financing operations before expenses with respect to credit loss - as previously presented	3,433	3,242	886	818
Less:				
Non-interest financing revenues (presented as a separate item under "Total non-interest revenues")	95	18	229	52
Less:				
Profit from investment in shares (now included under "Non-interest financing revenues")	(29)	(6)	(24)	(2)
Financing commissions (included under "Commissions")	153	131	38	34
Interest revenues, net	**3,214**	**3,099**	**643**	**734**
Interest revenues	6,591	6,840	1,179	1,453
Interest expenses	(3,377)	(3,741)	(536)	(719)
Total	**3,214**	**3,099**	**643**	**734**

Commissions now include amounts previously included under "Operating commissions", as well as financing commissions, previously included under "Profit from financing operations":

	For the year ended December 31,		For the quarter ended December 31,	
	2012	2011	2012	2011
Operating commissions - as previously presented	1,299	1,343	329	325
Financing commissions (previously included under "Profit from financing operations", now under "Commissions")	153	131	38	34
Commissions	**1,452**	**1,474**	**367**	**359**

Evolution of income and expenses

Net interest revenues and non-interest financing revenues [1] for the Group in 2012 amounted to NIS 3,309 million, compared to NIS 3,117 million in the corresponding period last year, an increase of 6.2%. In the fourth quarter of 2012: NIS 872 million, compared to NIS 786 million in the corresponding period last year - an increase of 10.9%.

Below is an analysis of the development of financing revenues from current operations (NIS in millions):

	For the year ended December 31,			For the quarter ended December 31,		
	2012	2011	Change rate	2012	2011	Change rate
Interest revenues, net	3,214	3,099	3.7%	643	734	(12.4%)
Non-interest financing revenues [1]	95	18		229	52	
Total financing revenues	**3,309**	**3,117**	**6.2%**	**872**	**786**	**10.9%**
Less:						
Income from collection of interest on troubled debt	155	100		35	24	
Linkage differentials (in 2011 only) and exchange rate differentials with respect to impaired debt	1	52		(13)	4	
Gain from realized debentures available for sale and from debentures held for trade, net	146	18		82	12	
Effect of accounting treatment of derivatives at fair value and others[2]	(79)	18		32	22	
Total financing revenues from current operations	**3,086**	**2,929**	**5.4%**	**736**	**724**	[3] **1.7%**

(1) Non-interest financing revenues include the effect of fair value and others, gain from debentures (see below) and an expense with respect to linkage differentials on CPI derivatives, where the corresponding revenue is recognized as interest revenues, in conformity with accounting rules.

(2) The effect of accounting treatment of derivatives at fair value is due to the difference between the accounting treatment of balance sheet instruments, charged to the profit and loss statement on the accrual basis (interest, linkage differentials and exchange rate differentials only), vs. derivatives measured at their fair value.

(3) The known CPI in the fourth quarter of 2012 was lower by 0.7%. The total effect included under financing revenues from current operations in the fourth quarter with respect to the CPI-linked position amounted to financing expenses of NIS 45 million, compared to financing expenses of NIS 8 million in the corresponding period last year. Excluding the effect of the lower CPI, financing profit from current operations increased by 7.2%.

Below is total financing revenues by operating segment (NIS in millions) [1]:

	For the year ended December 31,			
Operating segment	2012	2011 [3]	Change amount	Change rate
Retail banking:				
Mortgages	633	556	77	13.8%
Household	1,096	1,055	41	3.9%
Small business	450	442	8	1.8%
Total Retail banking	**2,179**	**2,053**	**126**	**6.1%**
Private banking	74	90	(16)	(17.8%)
Commercial banking	172	175	(3)	(1.7%)
Business banking	731	564	167	29.6%
Financial management[2]	153	235	(82)	(34.9%)
Total	**3,309**	**3,117**	**192**	**6.2%**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.

(2) Excluding the effect of accounting treatment of derivatives at fair value, financing revenues increased by NIS 15 million, or 6.9%.

(3) Reclassified.

For definition of operating segments, see below in chapter "Description of Businesses of the Bank Group by Operating Segment".

The average balances of financial assets in the different linkage segments (including impact of derivatives) are as follows (NIS in millions):

Linkage segment - financial assets	2012	2011	Change rate
Israeli currency - non-linked	140,511	138,425	1.5%
Israeli currency - linked to the CPI	52,612	48,116	9.3%
Foreign currency (1)	76,360	74,702	2.2%
Total	**269,483**	**261,243**	**3.2%**

(1) Local activity and overseas affiliates (includes foreign currency-linked Israeli currency).

The increase in deposits with the Bank of Israel and derivatives operations contributed to the increase in average balances of non-linked NIS-denominated financial assets. The increase in mortgage volume resulted in higher average balances of NIS-denominated financial assets - both CPI-linked and non-linked. The increase in average balance of foreign currency denominated financial assets is primarily due to an increase in volume of derivative operations.
Interest margins (difference between the rate of income on assets and the rate of expenses on liabilities) based on average balances[1] in the various linkage segments (including the effect of derivatives, in percent) are as follows:

	For the year ended December 31,		For the quarter ended December 31,	
Linkage segment	2012	2011	2012	2011
Israeli currency - non-linked	1.28	1.41	1.20	1.25
Israeli currency - linked to the CPI	0.59	0.41	1.18	0.48
Foreign currency (including Israeli currency linked to foreign currency) (2)	0.47	0.44	0.66	1.51
Total including impact of derivatives	**1.00**	**0.95**	**1.13**	**1.11**

(1) Average balances before expenses with respect to credit loss.
(2) Local operations and overseas affiliates.

Data with regard to revenue and expense rates of group operations as well as the financial margin represented by the interest differentials are presented under Addendum C of Management Discussion.

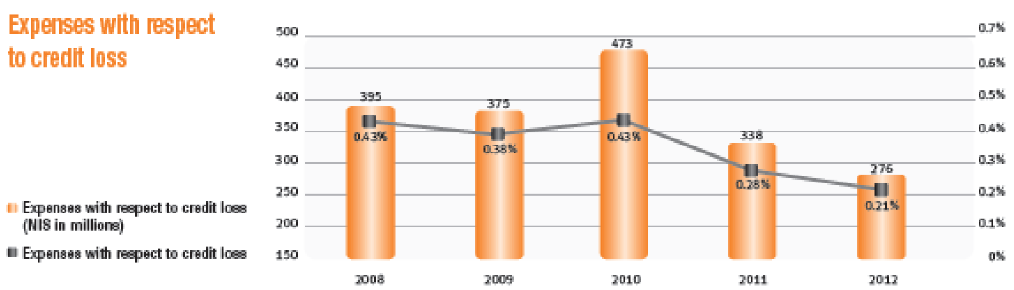
Expenses with respect to credit loss for the Group in 2012 amounted to NIS 276 million, or 0.21% of total loans to the public, net compared to NIS 338 million in 2011, or 0.28% of total loans to the public, net.
Expenses with respect to credit loss amounted to NIS 48 million in the fourth quarter of 2012, or an annualized rate of 0.15% of total loans to the public, net, compared with NIS 62 million, or an annualized rate of 0.21% of total loans to the public, net in the corresponding period last year - a decrease of 22.6%.
Expenses with respect to credit loss in 2011 include expenses with respect to linkage differentials and exchange rate differentials, against corresponding revenues under financing revenues, amounting to NIS 52 million and NIS 4 million for the twelve-month and three-month periods ended December 31, 2011, respectively.

As part of the change in the format of profit and loss, as from January 1, 2012, the definition of "interest" was modified to include CPI linkage differences for principal and interest; therefore, expenses with respect to credit loss only include exchange rate differences against the corresponding revenues under financing expenses.

Total exchange rate differences recognized in 2012 and in the fourth quarter of 2012 amounted to expense of NIS 1 million and revenues of NIS 13 million, respectively.

Development of expenses with respect to credit loss (NIS in millions) is as follows:

	For the year ended December 31,		For the quarter ended December 31,	
	2012	2011	2012	2011
Provision for credit loss on individual basis (including accounting write-offs)	275	283	(12)	63
Provision for credit loss on Group basis:				
By extent of arrears	3	(12)	-	1
Other	(2)	67	60	(2)
Total	**276**	**338**	**48**	**62**
Expense with respect to credit loss as percentage of total loans to the public (annualized)				
Total	**0.21%**	**0.28%**	**0.15%**	**0.21%**
With respect to commercial loans other than housing loans	**0.54%**	**0.70%**	**0.34%**	**0.61%**
With respect to housing loans	**0.01%**	**0.00%**	**0.03%**	**(0.06%)**



Below are details of expenses with respect to credit loss by major operating segments of the Group (NIS in millions):

	For the year ended December 31,		
Operating segment	2012	2011	Change rate
Retail banking:			
Mortgages	10	6	66.7%
Household	55	62	(11.3%)
Small business	36	84	(57.1%)
Total	**101**	**152**	**(33.6%)**
Private banking	(12)	(5)	140.0%
Commercial banking	8	6	33.3%
Business banking	178	164	8.5%
Financial management	1	21	(95.2%)
Total	**276**	**338**	**(18.3%)**

Net interest revenues after expenses with respect to credit loss in 2012 amounted to NIS 2,938 million, compared to NIS 2,761 million in the corresponding period last year - an increase of 6.4%. Including non-interest financing revenues – an increase of 9.1%.

Net interest revenues after expenses with respect to credit loss in the fourth quarter of 2012 amounted to NIS 595 million, compared to NIS 672 million in the corresponding period last year - a decrease of 11.5%. Including non-interest financing revenues – an increase of 13.8%. See also analysis of financing revenues from current operations above.

Non-interest revenues for the Group amounted to NIS 1,573 million in 2012, compared with NIS 1,509 million in 2011, an increase of 4.2%.

Non-interest revenues for the Group in the fourth quarter of 2012 amounted to NIS 602 million, compared to NIS 418 million in the corresponding period last year, an increase of 44.0%. See remarks below.

Non-interest financing revenues for the Group in 2012 amounted to NIS 95 million, compared to NIS 18 million in the corresponding period last year.

Non-interest financing revenues in the fourth quarter of 2012 amounted to NIS 229 million, compared to NIS 52 million in the corresponding period last year. This item includes, inter alia, the effect of fair value, realized gain on debentures and expenses with respect to linkage differentials on CPI derivatives, where the corresponding revenue is recognized as interest revenues, in conformity with accounting rules. See analysis of financing revenues from current operations above.

Commission revenues for the Group in 2012 amounted to NIS 1,452 million, compared to NIS 1,474 million in the corresponding period last year - a decrease of 1.5%. Commission revenues for the Group in the fourth quarter of 2012 amounted to NIS 367 million, compared to NIS 359 million in the corresponding period last year - an increase of 2.2%. The decrease in 2012 is due to lower revenues from client activity in the capital market: The average daily trading volume of shares and convertible securities on the Tel Aviv Stock Exchange was down 35%. In the fourth quarter, the effect of lower trading volumes was offset by higher commission revenues other than from clients' capital market activity.

Other revenues for the Group amounted to NIS 26 million in 2012, compared with NIS 17 million in the corresponding period last year.

Other revenues for the Group amounted to NIS 6 million in the fourth quarter of 2012, compared with NIS 7 million in the corresponding period last year.

Operating and other expenses for the Group amounted to NIS 2,786 million in 2012, compared with NIS 2,667 million in 2011, an increase of 4.5%.

Operating and other expenses amounted to NIS 740 million in the fourth quarter of 2012, compared with NIS 689 million in the corresponding period last year - an increase of 7.4%. See remarks below.

Payroll and associated expenses for the Group amounted to NIS 1,701 million in 2012, compared with NIS 1,615 million in 2011, an increase of 5.3%.

Payroll and associated expenses in the fourth quarter of 2012 amounted to NIS 454 million, compared to NIS 411 million in the corresponding period last year - an ad-hoc increase of 10.5%, due to timing differences in the accounting recording of provisions for payroll-associated expenses, compared to the corresponding period last year.

Below is analysis of the development in current annual payroll expenses (NIS in millions):

	For the year ended December 31,		
	2012	2011	Change rate
Total payroll and associated expenses	1,701	1,615	5.3%
Less:			
Effect of increase in payroll tax rate (1)	13	-	
Expenses arising from share-based payment transactions	28	22	
Current payroll(2)	**1,660**	**1,593**	**4.2%**

(1) Primarily non-recurring increase with respect to updated payroll tax rates on reserve for severance, retirement and pension pay.

(2) The increase in payroll derives primarily from salaries update.As described in chapter "Human resource management below.

Maintenance and depreciation expenses for buildings and equipment for the Group amounted to NIS 652 million in 2012, compared with NIS 608 million in the corresponding period last year – an increase of 7.2% – primarily due to increase in maintenance and depreciation expenses at Bank Yahav, amounting to NIS 14 million, due to opening of new branches, as well as a non-recurring increase due to operation of the new Bank building in Lod, amounting to NIS 16 million.

Maintenance and depreciation expenses for buildings and equipment for the Group amounted to NIS 171 million in the fourth quarter of 2012, compared with NIS 153 million in the corresponding period last year – an increase of 11.8% (includes: NIS 5 million, increase in maintenance and depreciation expenses at Bank Yahav and NIS 4 million with respect to the new Bank building in Lod, as described above).

Other expenses for the Group in 2012 amounted to NIS 433 million, compared with NIS 444 million in 2011, a decrease of 2.5%.

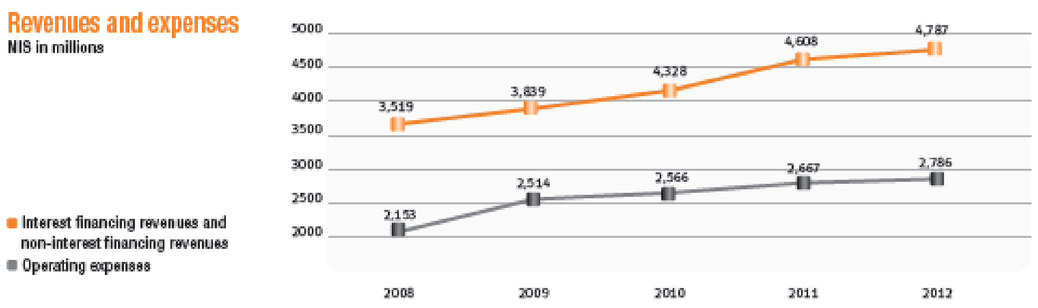
Other expenses for the Group amounted to NIS 115 million in the fourth quarter of 2012, compared with NIS 125 million in the corresponding period last year - a decrease of 8.0%. which derives primarily from decrease in the bank's capital market activity costs.

Cost-Income ratio information is as follows[1]:

	For the year ended December 31,	
	2012	2011
Cost-income ratio	58.2%	57.9%

				2012				2011
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Cost-income ratio	59.4%	57.0%	56.1%	60.3%	59.8%	53.6%	57.7%	60.6%

(1) Total operating and other expenses to total operating and financing income before expenses with respect to credit loss.



Pre-tax profit for the Group amounted to NIS 1,725 million in 2012, compared with NIS 1,603 million in 2011, an increase of 7.6%.

Pre-tax profit for the Group amounted to NIS 457 million in the fourth quarter of 2012, compared with NIS 401 million in the corresponding period last year - an increase of 14.0%.

Provision for taxes for the Group in 2012 amounted to NIS 599 million, compared with NIS 522 million in 2011, an increase of 14.8%.

In the fourth quarter of 2012, the provision for taxes amounted to NIS 176 million, compared to NIS 93 million in the corresponding period last year.

The rate of provision for taxes on profit in 2012 was 34.7%, compared to 32.6% in 2011.

In the fourth quarter of 2011, this includes a NIS 45 million reduction in expenses with respect to deferred taxes, following recommendations of the Trachtenberg Commission.

Return [1] on Group profit and its evolution relative to shareholders' equity [2] and Ratio of tier I capital to risk elements (in %):

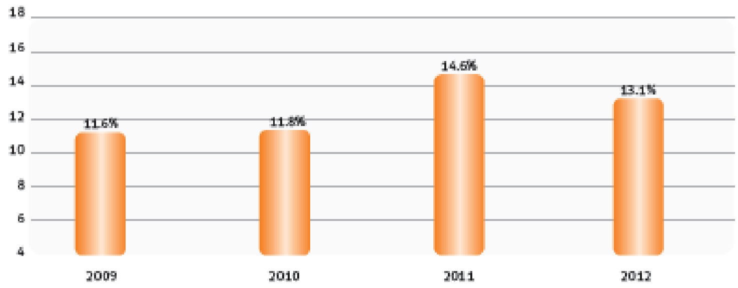
	For the year ended December 31,		
	2012	2011	2010
Net profit return on share holder's equity	13.1	14.6	11.8
Ratio of Tier I capital to risk elements for year end	8.55	7.77	7.91

				201				2011
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Net profit	13.1	13.0	15.4	13.6	16.9	14.9	15.2	14.5
Ratio of Tier I capital to risk elements (in %) for the quarter end	8.55	8.23	8.03	7.94	7.77	7.70	7.71	7.61

(1) Annualized return.

(2) Return on average shareholders' equity, including "total capital resources", as presented in reporting of revenue and expense rates, less average balance of minority interest and less/plus the average balance of unrealized gain/loss from adjustment to fair value of debentures held for trading as well as gain/loss from debentures available for sale.

Return on Equity



Earnings per share

Earnings per ordinary, NIS 0.1 par value share are as follows (in NIS):

	2012	2011	2010
Basic earnings per share:			
Net profit attributable to equity holders of the banking corporation	4.77	4.65	3.63
Diluted earnings per share:			
Net profit attributable to equity holders of the banking corporation	4.74	4.57	3.58

Development of balance sheet items

Development of key balance sheet items for the Bank Group (NIS in millions) is as follows:

	December 31,		
	2012	2011	Change in %
Balance sheet total	162,242	150,246	8.0%
Loans to the public, net	128,651	119,293	7.8%
Deposits from the public	128,499	119,236	7.8%
Securities	9,041	8,432	7.2%
Shareholders' equity	8,811	7,666	14.9%

Loans to the public, net – loans to the public, net on the consolidated balance sheet as of December 31, 2012 accounted for 79% of total assets, similar to the end of 2011. Loans to the public, net for the Group increased in 2012 by NIS 9.4 billion, an increase of 7.8%.

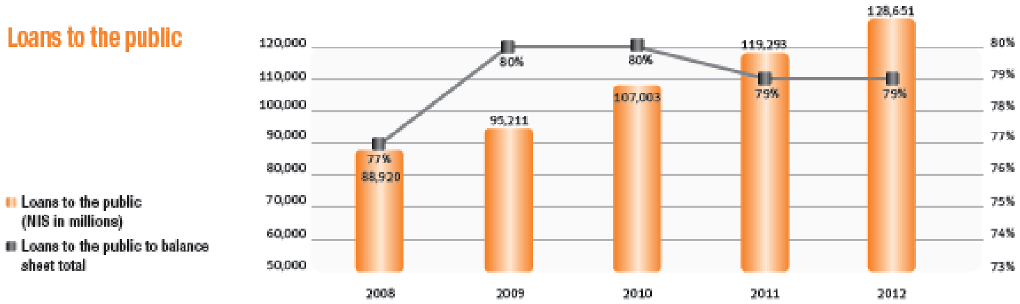
Loans to the public, net by linkage basis (NIS in millions) are as follows:

	Balance as of December 31			Share of total loans to the public as of December 31	
	2012	2011	Change in %	2012	2011
Israeli currency					
Non-linked	66,160	60,559	9.2%	51.4%	50.8%
CPI- linked	49,221	44,651	10.2%	38.3%	37.4%
Foreign currency and foreign currency linked	13,270	14,083	(5.8%)	10.3%	11.8%
Total	**128,651**	**119,293**	**7.8%**	**100.0%**	**100.0%**

Loans to the public, net by operating segments (NIS in millions) are as follows:

Operating segment	2012	2011[1]	Change rate
Retail banking:			
Mortgages	75,011	67,303	11.5%
Household	18,002	16,465	9.3%
Small business	6,860	6,428	6.7%
Total – Retail banking	**99,873**	**90,196**	**10.7%**
Private banking	1,178	1,191	(1.1%)
Commercial banking	4,679	4,778	(2.1%)
Business banking	22,921	23,128	(0.9%)
Total – business and others	**28,778**	**29,097**	**(1.1%)**
Total	**128,651**	**119,293**	**7.8%**

(1) Reclassified.



Below are details of troubled credit risk and non-performing assets before provision for credit loss, in accordance with provisions for measurement and disclosure of impaired debt, credit risk and provision for credit loss:

Reported amounts (NIS in millions)	As of December 31, 2012			As of December 31, 2011		
	Credit risk (1)			Credit risk (1)		
	On balance sheet	Off balance sheet	Total	On balance sheet	Off balance sheet	Total
1. Troubled credit risk:						
Impaired credit risk	1,664	423	2,087	1,587	297	1,884
Inferior credit risk	161	2	163	110	1	111
Credit risk under special supervision (2)	1,927	181	2,108	2,078	95	2,173
Total troubled credit risk	**3,752**	**606**	**4,358**	**3,775**	**393**	**4,168**
Includes: Non-impaired debt in arrears 90 days or longer (2)	1,659			1,814		
2.Total non-performing assets(3)	**1,609**	**-**	**-**	**1,485**	**-**	**-**

Note: On- and off-balance sheet credit risk is stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(1) On- and off-balance sheet credit is stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.
(2) Including with respect to housing loans for which a provision was made by extent of arrears, and with respect to housing loans for which no provision was made by extent of arrears and which are in arrears 90 days or longer. NIS. 1,599 miilion (2011 – NIS. 1,729 million)
(3) Non-accruing interest assets.

For more details of troubled credit risk, see Note 4 to the financial statements

Below are key risk benchmarks with respect to loans to the public:

	December 31, 2012	December 31, 2011
Ratio of impaired loans to the public to total loans to the public, net	1.28%	1.31%
Ratio of impaired loans to the public to total non-housing loans to the public, net	3.37%	3.26%
Ratio of housing loans in arrears 90 days or more to total loans to the public, net (1)(2)	1.23%	1.43%
Ratio of provision for credit loss to total loans to the public, net	1.30%	1.45%
Ratio of provision for credit loss to total credit risk with respect to the public	0.95%	1.04%
Ratio of troubled credit risk to total credit risk with respect to the public	2.44%	2.47%
Ratio of expenses with respect to credit loss to average balance of loans to the public, net	0.22%	0.30%
Ratio of net write-offs to average balance of loans to the public, net	0.27%	0.47%
Ratio of net write-offs to provision for credit loss	19.9%	30.7%

(1) Ratio of non-impaired non-housing loans to the public in arrears 90 days or more to total loans to the public, net is negligible.
(2) Balance of loans in arrears before provision by extent of arrears.

Below is the sector composition of the top 6 borrowers for the group as of December 31, 2012:

Borrower no.	Sector	Balance sheet credit risk	Off-balance sheet credit risk	Total credit risk
1.	Construction and real estate	254	648	902
2.	Construction and real estate	17	800	817
3.	Construction and real estate	166	539	705
4.	Power and water	485	216	701
5.	Communications and computer services	633	39	672
6.	Construction and real estate	122	405	527

On- and off-balance sheet credit risk is stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

Development of Group credit risk distribution by size of borrower is as follows:

	2012		2011	
Credit risk per borrower (NIS in thousands)	Share of total Group credit risk	Share of total Group number of borrowers	Share of total Group credit risk	Share of total Group number of borrowers
Up to 150	12.8%	76.2%	13.3%	76.9%
150-600	23.6%	16.9%	24.2%	17.1%
600-2,000	25.8%	6.2%	23.0%	5.4%
Above 2,000	37.8%	0.7%	39.5%	0.6%

Credit risk by major industrial sectors with respect to borrower operations in Israel (1) (in NIS millions)

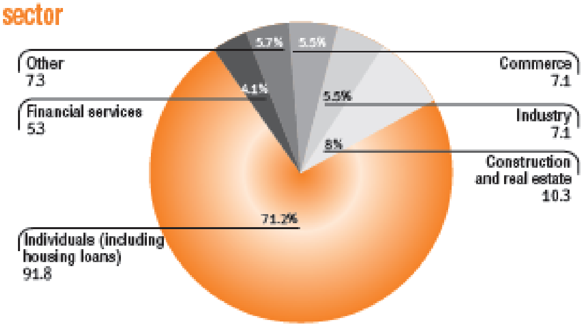
	2012		2011		
Sector	Balance sheet credit risk	% of total balance sheet credit risk	On-balance sheet credit risk (2)	% of total balance sheet credit risk	% change
Private individuals (includes mortgages)	91,766	71.3%	82,757	69.2%	10.9%
Construction and real estate	10,219	7.9%	10,081	8.4%	1.4%
Financial services	5,339	4.1%	6,019	5.0%	(11.3%)
Industry	7,057	5.5%	6,650	5.6%	6.1%
Commerce	7,136	5.5%	6,976	5.8%	2.3%
Other	7,169	5.6%	7,117	6.0%	0.7%
Total	**128,686**	**100.0%**	**119,600**	**100.0%**	**7.6%**

(1) Includes credit and investments in debentures by the public, and other assets with respect to derivatives of the public.

(2) Reclassified.

Credit risk for loans to the public is composed of on-balance-sheet risk and off-balance-sheet credit risk, which are weighted by nature of the borrower and credit type, as per Bank of Israel instructions. On-balance-sheet risk includes balances of loans to the public, derivative instruments purchased by the public and Group investment in public debentures. Off-balance-sheet credit risk includes guarantees and transactions in off-balance-sheet instruments, obligations to provide credit and unutilized credit facilities.

On Balance sheet credit risk by sector as of December 31, 2012
NIS in billions



Total Group credit risk as of December 31, 2011 amounted to NIS 178 billion, compared to NIS 168 billion in 2011 - an increase of 5.9% primarily due to housing loans.

Securities - investment in securities increased in 2012 by NIS 0.6 billion, or 7.2%. The increase in total investment in securities is within asset and liability management.

Distribution of Group security portfolio by linkage segment (NIS in millions) is as follows:

	Carrying amount as of		
Linkage segment	December 31, 2012	December 31, 2011	Change in %
Israeli currency			
CPI- linked	251	302	(16.9%)
Non-linked	5,487	5,128	7.0%
Foreign currency and foreign currency linked	3,184	2,917	9.2%
Non-monetary items	119	85	40.0%
Total	**9,041**	**8,432**	**7.2%**

Bank investments in securities in the held-to-maturity portfolio, the available-for-sale portfolio and the held-for-trade portfolio

Below are further details of Bank Group investments in securities (NIS in millions):

	Carrying amount as of	
	December 31, 2012	December 31, 2011
Government debentures:		
Government of Israel	8,114	7,410
US Government	95	86
Total government debentures	**8,209**	**7,496**
Debentures of banks in developed nations:		
UK	137	135
Israel	123	159
Germany	109	104
South Korea	26	26
Holland	38	-
Other	5	5
	438	429
Debentures of financial institutions (other than banks) in developed nations [(1)]:		
USA	51	115
UK	20	19
Luxembourg	11	11
	82	145
Total debentures of banks and financial institutions in developed nations	**520**	**574**
Corporate debentures (composition by sector):		
Industry	75	108
Construction	31	37
Power and water	57	48
Communications and computer services	1	23
Financial services	29	-
Total corporate debentures	**193**	**216**
Asset-backed debentures (CLO)	**-**	**61**
Shares	**119**	**85**
Total securities	**9,041**	**8,432**

(1) Exposure primarily consists of exposure to banks, investments and holding companies in bank groups.

Below is additional information with regard to impairment of a temporary nature of securities available for sale, listing the duration of impairment and its share out of the amortized cost (NIS in millions):

					As of December 31, 2012
	Duration in which fair value is lower than the amortized cost				
Share of impairment out of amortized cost	Up to 6 months	6-9 months	9-12 months	Over 12 months	Total
Asset-backed debentures available for sale	**-**	**-**	**-**	**-**	**-**
Other debentures available for sale					
20%	1	-	-	32	33
20%-40%	-	-	-	20	20
Over 40%	-	-	-	-	-
Total	**1**	**-**	**-**	**52**	**53**
Securities					
20%	1	-	-	-	1
20%-40%	-	-	-	-	-
Over 40%	-	-	-	-	-
Total	**1**	**-**	**-**	**-**	**1**
Total securities available for sale	**2**	**-**	**-**	**52**	**54**

					As of December 31, 2011
	Duration in which fair value is lower than the amortized cost				
Share of impairment out of amortized cost	Up to 6 months	6-9 months	9-12 months	Over 12 months	Total
Asset-backed debentures available for sale					
20%	-	-	-	3	3
20%-40%	-	-	-	9	9
Over 40%	-	-	-	-	-
Total	**-**	**-**	**-**	**12**	**12**
Other debentures available for sale					
20%	22	11	-	36	69
20%-40%	-	-	-	18	18
Over 40%	-	-	-	4	4
Total	**22**	**11**	**-**	**58**	**91**
Total securities available for sale	**22**	**11**	**-**	**70**	**103**

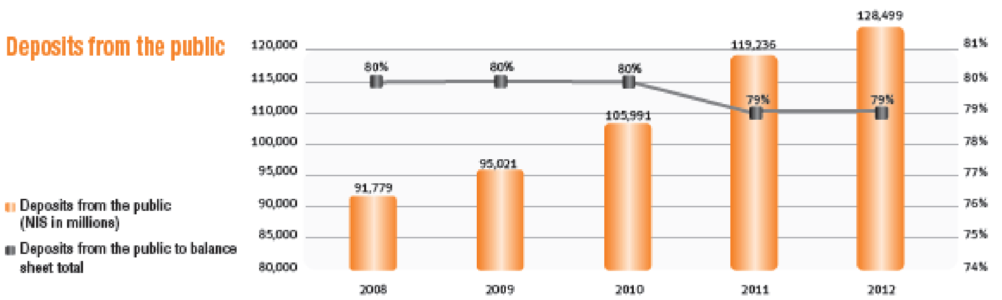
For further defails see note 3 to the financial statements

In 2012, expenses with respect to provision for other-than-temporary impairment of asset-backed debentures amounted to NIS 8 million (in 2011 - NIS 10 million with respect to bank debentures).
See Notes 3 and 23 to the financial statements for further information.

Deposits from the public - these account for 79% of total consolidated balance sheet as of December 31, 2012, similar to their weight at the end of 2011. In 2012, deposits from the public for the Bank Group increased by NIS 9.3 billion, an increase of 7.8%.

Distribution of deposits from the public by linkage basis (NIS in millions) is as follows:

	Balance as of December 31		Rate	Share of total deposits from the public as of December 31	
Linkage segment	2012	2011	of change (%)	2012	2011
Israeli currency					
Non-linked	83,411	72,554	15.0%	64.9%	60.9%
CPI- linked	21,823	23,046	(5.3%)	17.0%	19.3%
Foreign currency and foreign currency linked	23,265	23,636	(1.6%)	18.1%	19.8%
Total	**128,499**	**119,236**	**7.8%**	**100.0%**	**100.0%**



Composition of deposits from the public by operating segments (NIS in millions) is as follows:

Operating segment	2012	2011(1)	Change rate
Retail banking:			
Household	58,645	54,091	8.4%
Small business	8,159	7,773	5.0%
Total	**66,804**	**61,864**	**8.0%**
Private banking	7,077	5,831	21.4%
Commercial banking	3,358	3,471	(3.3%)
Business banking	33,934	32,524	4.3%
Financial management	17,326	15,546	11.4%
Total	**128,499**	**119,236**	**7.8%**

(1) Reclassified.

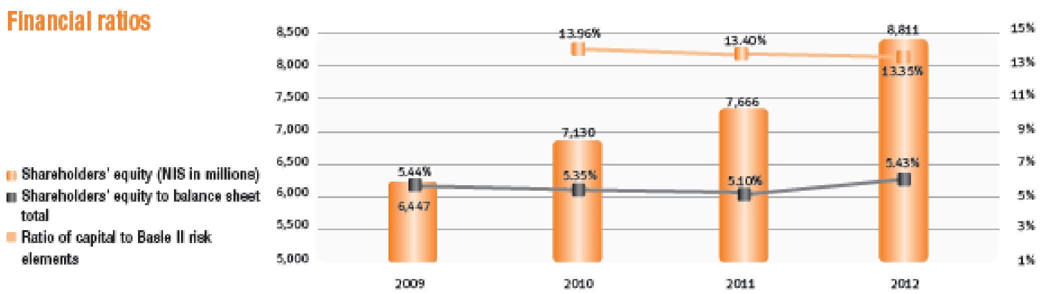
For further details on deposits from the public and deposits from banks, see Notes 9 and 10 to the financial statements.

The ratio of shareholders' equity to balance sheet total for the Group as of December 31, 2012 was 5.43%, compared to 5.10% as of the end of 2011.

Ratio of capital to risk elements

As per instructions of the Supervisor of Banks, every banking corporation is required to maintain a total minimum capital ratio of no less than 9% of weighted total of risk elements of its balance sheet assets and off-balance-sheet items, and these instructions determine the manner of calculation of total capital and total risk elements. For information about resolutions by the Board of Directors with regard to the Bank's capital targets, see Note 14 to the financial statements.
Starting on December 31, 2009, the ratio of capital to risk elements is calculated in accordance with Basel II rules. On December 31, 2012, the Advisory Committee on Banking Business received draft amendments to Proper Conduct of Banking Business Regulations 201-211 concerning adoption of Basel III directives with regard to supervisory capital and with regard to risk assets.
The Bank is reviewing the effect of anticipated changes on its capital, pursuant to the new draft directives on application of Basel III directives, as described above.
For details of these draft directives and the anticipated effect on the Bank's capital adequacy, see chapter "Legislation and Supervision of Bank Group Operations".
Development of Group ratio of capital to risk elements is as follows:

	December 31, 2012	December 31, 2011
Ratio of Tier I capital to risk elements	8.55	7.77
Ratio of total capital to risk elements	13.35	13.40
Minimum capital ratio required by the directives of the Supervisor of Banks	9.00	9.00



Major Investees

The contribution of investees to net operating profit million in 2012 amounted to NIS 142 million, compared with NIS 151 million last year. The decrease is primarily due to effect of exchange rates on investment in an overseas subsidiary, which resulted in a NIS 28 million decrease in this item, against non interest financing expenses.

Bank Yahav for Government Employees Ltd. (hereinafter: "Bank Yahav")

Bank Yahav is a banking corporation operating in accordance with a "Bank" license as per provisions of the Banking Act (Licensing), 1981. On January 28, 2009, the replacement license for the Bank's previous license dated January 11, 2005, was received which allows the Bank to do business with government and public sector employees. In accordance with the new license, Bank Yahav may engage in new operations and may expand its client base, subject to advance permission by the Supervisor of Banks.

Concurrently with receiving the new license, Bank Yahav received approval from the Supervisor of Banks to provide services to individual clients (such as salaried employees, self employed and households) and to corporations, provided that credit granted to corporations shall not exceed the specified limit. Bank Yahav operates in accordance with the new license, subject to policy of the Bank Yahav Board of Directors on this matter.

Bank Yahav's contribution to Group net profit in 2012 amounted to NIS 50 million, compared with NIS 38 million in 2011. The increase in the net profit derives from a significant increase in the activity volume. Net profit return on equity for Bank Yahav (average equity, as defined in the Supervisor of Banks' Public Reporting Regulations) amounted in 2012 to 12.2%, compared to 10.4% in 2011. Bank Yahav's balance sheet total as of December 31, 2012 amounted to NIS 18,367 million, compared to NIS 16,755 million as of December 31, 2011. The balance of loans to the public as of December 31, 2012 amounted to NIS 6,124 million, compared to NIS 5,793 million at end of 2011.

Tefahot Insurance Agency (1989) Ltd. ("Tefahot Insurance")

Tefahot Insurance is an insurance agency wholly owned by the Bank, which manages life insurance policies and property insurance policies of clients obtaining mortgages from the Bank.
Tefahot Insurance's contribution to Group net profit in 2012 amounted to NIS 69 million, compared with NIS 71 million in 2011. Net return on equity amounted to 11.5% in 2012, compared to 13.4% in 2011.

Other investees operating in Israel

In 2012, other investees operating in Israel, wholly controlled by the Bank and supported by Bank infrastructure, contributed to Bank profit NIS 21 million, net, compared with NIS 11 million, net, in 2011.

United Mizrahi Bank (Switzerland) Ltd.

United Mizrahi Bank (Switzerland) Ltd. "Mizrahi Bank Switzerland") is focused on international private banking services. The Swiss bank is held by a wholly-owned Bank subsidiary, UMOHC B.V. incorporated in Holland.
Net profit of Mizrahi Bank Switzerland in 2012 amounted to CHF 0.7 million, compared to CHF 1.6 million in 2011.
Mizrahi Bank Switzerland's balance sheet total as of December 31, 2012 amounted to CHF 167 million, compared to CHF 150 million at the end of 2011.

The net balance of loans to the public as of December 31, 2012 amounted to CHF 53 million, compared to CHF 44 million at end of 2011. The deposits with banks as of December 31, 2012 amounted to CHF 103 million, compared to CHF 74 million at end of 2011. Deposits from the public as of December 31, 2012 amounted to CHF 110 million, compared to CHF 80 million at end of 2011. Deposits from banks as of December 31, 2012 amounted to CHF 0.5 million, compared to CHF 12 million at end of 2011.

These data exclude off-balance-sheet items, such as fiduciary deposits and client security portfolios which are major components of the Bank's business operations in Switzerland.

The contribution of Mizrahi International Holdings Ltd. (B.V. Holland), which owns United Mizrahi Bank Switzerland, to Group net profit in 2012, amounted to a profit of NIS 2 million, compared with profit of NIS 30 million in 2011. These data include impact of changes in exchange rates on the investment balance, covered by the Bank's own sources. Therefore, the impact of exchange rates on the consolidated statement is not meaningful.

Excluding the impact of changes in exchange rates, the company's contribution to Group net profit in 2012 amounted to a profit of NIS 3 million, compared to NIS 8 million in 2011.

In recent months, authorities in the USA and Switzerland are in negotiations with regard to an investigation by US authorities into Swiss banks, concerning abuse of the double tax avoidance treaty between the USA and Switzerland.

As requested by Swiss authorities, several Swiss banks, including Mizrahi Bank Switzerland, have provided statistical information about their business with US clients, to be provided to US authorities. No personally identifiable information, such as client names, has been provided. Mizrahi Bank Switzerland cooperates with Swiss authorities and acts in adherence to applicable statutory provisions.

As of this date, based on information available to the Bank and the status of on-going negotiations, there is no material impact on the current business and financial standing of Mizrahi Bank Switzerland. Currently, based on existing information, the Bank is unable to estimate the expected impact on the business and financial standing of Mizrahi Bank Switzerland.

Investment in non-banking corporations

The Bank manages nostro investments in non-banking corporations. Shares of non-banking corporations in which the Bank thus invested were acquired for the purpose of earning capital gains, and are listed at fair value on the available-for-sale security portfolio and under investment in associates as it have significant influence on the corporation. About 3% of these investments are negotiable and presented at their market value. The remainder of these investments is presented at cost or at their carrying amount. In case of impairment of a non-temporary nature, in accordance with management assessment, a provision for impairment is made by the Bank.

Bank investments in non-banking corporations as of December 31, 2012 amounted to NIS 146 million, compared to NIS 135 million at end of 2011, as described below.

Under the available-for-sale securities portfolio:

A. NIS 4 million (NIS 6 million as of the end of 2011) is with respect to negotiable investments.

B. NIS 74 million is with respect to participation units in various equity funds (NIS 68 million as of end of 2011).

C. Investments in several different other corporations, which are stated at cost, the balance of the investment in which amounted to NIS 8 million as of December 31, 2012, (NIS 9 million as of the end of 2011).

Under investment in associates:

A. NIS 41 million (NIS 35 million as of end of 2011) constituting the balance of Bank investment in mezzanine funds. A mezzanine fund is a fund for interim financing, providing companies in various sectors with financing complementary to bank credit. This financing is typically extended in return for interest, stock options and other equity instruments.

B. NIS 17 million (NIS 15 million as of the end of 2011) constitutes the balance of the Bank's investment in Psagot Jerusalem Ltd., a private company that had purchased land in Jerusalem for development for residential construction, including an investment in capital notes that amounted to NIS 33 million as of December 31, 2012 (NIS 31 million as of the end of 2011). In addition, the Bank provided credit to Psagot Jerusalem Ltd., which as of December 31, 2012 amounted to NIS 16 million (as of the end of 2011 – NIS 14 million).

C. NIS 2 million (identical amount as of end of 2011) is the balance of Bank investment in Rosario Capital Ltd., a private company engaged in underwriting, assistance and consulting on private and public issuance, mergers & acquisitions, investment in securities and distribution of securities.

Bank net revenues from dividends and realized gains from investments in non-banking corporations, after provision for impairment, in 2012 amounted to NIS 29 million, compared with NIS 6 million in 2011.

Branch deployment and Direct channels

Branch deployment

Group branches are primarily aimed at providing professional, high-quality service to clients of all banking segments, close to the location where the service is required (residence, place of business). To this end, branches manage day-to-day client activities and offer to clients and the public at large advanced financial products and services, including advisory services for capital market activity and pension advisory service.

Group branches are deployed throughout Israel. The merger of Bank Mizrahi and Bank Tefahot in early 2005, the merger of Bank Adanim in 2009 and acquisition of Bank Yahav, completed in 2008, created a combined nation-wide branch network which includes, as of the date of these financial statements, 175 business centers, branches and affiliates, including 44 Yahav branches.

The Bank operates a unique service – the LIVE branches – which are branches providing full personalized service during extended business hours using a range of communication channels between clients and bankers (via telephone, fax, internet, email, SMS, video conferencing). In 2012, the Bank opened two more branches as part of this service - one of which is dedicated to students. In total, six LIVE branches are in operation, and a seventh branch is due to open in 2013.

In 2012, efforts continued to make optimal use of the branch network, adapting the branches, their nature and location to the Bank's business plan, based on a comprehensive review of branch deployment conducted by the Bank - following which it inaugurated a nation-wide framework for launching new points of sale, relocation, merging and closing branches. This plan is updated in accordance with market conditions and needs in the different regions. In 2013, the Bank plans to open 4 new commercial locations, as well as 2 mortgage sales locations, including establishing mortgage sales locations as Bank representation in Bank Yahav branches.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic development in Israel and internationally, especially the state of the economy, including macro-economic and geo-political conditions, economic policy, currency markets and capital markets, clients' financial robustness, public preferences, legislation, directives of regulatory entities, the behavior of competitors, aspects related to the Bank's image, technological development, developments in availability, purchase and rental prices of properties and staffing issues.

Direct channels

In 2012, there was continued transition of some client banking activities to direct banking channels (telephone, Internet, cell phone and self-service stations). The enlistment and usage rates of the direct banking systems continue to grow.

The banking system as a whole has gradually adopted a multi-channel strategy, at the center of which stands the branch, and direct banking services constitute an integral part thereof.

- **Hybrid Banking** - in 2012, the Hybrid Banking service was expanded and deployed to all Bank branches and to the direct banking sector.
- **Online service** - In 2012, the range of client services on the website was expanded and IT improvements were made in order to continue improving the user interface of the system and to enhance client use of the website.
  Late in the year, an extensive plan was prepared for upgrading the online systems, in cooperation with all HQ functions related to investments (especially trading securities), mortgages and international operations - in order to promote business and marketing activity concerning these and other topics.
  This plan supports the Bank's objectives for intensifying activity with existing clients, preserving clients and improving the Bank's capacity to recruit clients with securities and deposits. The plan would be carried out in 2013-2014.
- **Cell phone application** - in early 2012, a cell phone application service using smartphones was launched, initially consisting of only information about management of checking and investment accounts. In 2012, the service was expanded to include execution of basic transactions.
- **Service stations at branches** - in 2012, the Bank invested considerable effort in a project to replace service stations at the Bank with new service stations.
  The new service stations are among the newest available, with check deposit service available on all of them. In 2012 the Bank deployed 11 new stations to branches, and deployment would continue in 2013 and 2014.
  The service provided through the Internet, as well as the Hybrid Banking service, constitute the leading channels in the process of improving and strengthening customer access to the Bank's services and to improved service in general, while diverting in-person activity from the branch. Additionally, these services enable the Bank's employees to specialize in service and sales.

The Bank's operating policies in the direct banking sector are:

- To expand and upgrade the services provided through the main direct channels (telephone, Internet, cell phones, self-service stations).
- Expand use of direct channels by Bank clients, designed to improve service.
- Develop Hybrid Banking as a key channel for telephone, email and SMS contact for the commercial and mortgage areas.
- Use direct channels as a tool for building an advantage for the Bank and for attracting new preferred clients.

Direct channels offered to Bank clients include:

Telephone services

- **Mortgage Center** - allowing clients to transact a range of mortgage-related transactions. These include: filing an application and obtaining advice on housing loans, obtaining information about existing loans and making arrangements and payments for delinquent loans.
- **Sales center** - intended to enhance selling capabilities of Bank branches, as part of marketing campaigns to recruit clients, who are referred directly to the sales center, or by means of sales calls. In addition, the sales center handles sales of Tefahot credit cards, refinancing mortgages from other banks for Bank clients, sale of car loans and preventing churn.
- **Investment center** - provide skilled, professional rapid response to capital market clients for conducting transactions and investment advice, from 7am till midnight, new clients with deposits, maximize investment

campaigns (Pomegranate, Cherry, Lychee etc.), provide foreign currency services within a foreign currency extension of the trading room, launched in early 2012, and training investment advisors to be assigned to branches.

- **IVR service - telephone**-based system for hearing computer-based information about frequently asked questions and conducting transactions, including free check ordering and receiving a fax at reduced cost. This service is available 24 hours a day.

Online, cell phone, email and fax services:

- **Online service** – obtain banking information and execute transactions in your account for a range of banking products available to Bank clients at a reduced cost. This service is available 24 hours a day.
- **Cell phone application** – obtain banking information and conduct transactions by means of cellular browsing using smartphones.

  Notification Box service – a system for receiving Bank notifications of account activity in a personal notification box via the Bank's online service.
- **Cell phone service** – a system for disseminating banking and financial information through cell phones.
- PC service – a system parallel to “Mizrahi online”, enabling direct connection to the Bank’s computer, not through the Internet, and consequently – faster execution of transactions;
- **E-mail service** – a system to distribute details on transactions executed in an account through e-mail, direct to the customer's e-mail address;
- **Fax service** – makes it possible to receive current banking information about the client account on a range of subjects, at the frequency specified by the customer.

Self-service at branches:

- **Service stations** - Mizrahi-Tefahot provides clients with service stations which allow them to conduct transactions and obtain information about accounts in the commercial sector and in the mortgage sector - using self-service, 24 hours a day - even when the branch is closed. Currently there are 147 service stations deployed in branches; 64 branches allow clients to deposit checks using the service stations; and 41 branches allow you to immediately produce checks.
- **ATMs** – the Bank has 128 cash-withdrawal machines (105 at Bank branches and 23 remote); 15 ATMs include optional foreign currency withdrawal; 20 ATMs have an optional check deposit feature.

Fixed assets and installations

Information on the Bank's fixed assets is presented in Note 7 – "Buildings and equipment" in the financial statements. See the section on IT systems and computers below for additional details.

Real property

The total area of the land owned by the Bank or leased by the Bank for its use, as of December 31, 2012, is 131.3 thousand m2, as provided in the table below:

Type of property[1]	Gross area, thousand m2, as of December 31, 2012		
	Owned	Leased	Total area
Branches throughout Israel	33.4	31.8	65.2
Offices and warehouses [2]	33.8	10.3	44.1
Unused property with potential future use [3]	19.9	0.5	20.4
Properties not in use and designated for sale or to be vacated [4]	0.4	1.2	1.6
Total	87.5	43.8	131.3

(1) The Bank owns a total area of 17.2 thousand m^2 used as covered parking space (including parking space in Lod), which is not included in the table above.

(2) On February 8, 2011, the Bank acquired land with an area of 3.7 thousand m^2 adjacent to the existing Bank-owned building in Lod, for construction of an underground facility with an area of 1 thousand m^2. As of December 31, 2012, this facility is under construction and is expected to be completed in 2013.

(3) Of the assets not in use and serving for potential future use, 15.8 thousand m^2 is undergoing refurbishment and adaptation for Bank needs (13 thousand m^2 in a building in Lod), 0.5 thousand m^2 leased to others, and 0.4 thousand m^2 unoccupied. In addition, land acquired in Lod in 2011 with an area of 3.7 thousand m^2 (see note 1 above).

(4) Some 1.2 thousand m2 of the properties designated for sale or to be vacated, are leased to others.

It is Bank policy to hold only hold real estate actually needed or expected to be needed in the future. The Bank regularly reviews the extent, attributes and location of required area, based on its business plan and nation-wide branch deployment plan, and makes the required adjustments.

This information constitutes forward-looking information, based inter alia on various assumptions and forecasts with regard to the state of the economy, legislation, directives of supervisory entities, technological developments, developments in the real estate and construction market and human resource issues. This information may not materialize, or materialize in part, to the extent and on dates to be determined by Bank management or due to changes that could occur in various influencing factors that are not under sole control of the Bank.

The amortized cost of buildings and real estate for the Bank Group (including installations and leasehold improvements), net of provision for impairment, as of December 31, 2012 amounts to NIS 930 million, compared to NIS 902 million at the end of 2011. The increase is almost entirely due to the investment in the facility in the city of Lod, in computers, and in softwares as stated above.

Intangible assets

The Bank Group has data base entries of clients and employees.
The Bank owns the rights to the trademarks "Mizrahi-Tefahot", including with the infinity symbol and the words "Team", "Live", "Tefahot", "Tefahot - No. 1 in Mortgages", "Retirement portfolio Based on a Nobel Prize Winning Model", "Mizrahi Bank" with the image of the sun, "Market Leader in Mortgages Tefahot", "Israel No.1 Du Credit Hypothecaire En Tefahot" and variations of these marks. The Bank owns the rights to trademarks associated with the Bank's name in the USA, Canada, Switzerland and in the European Union as well.

IT and computers

IT services for Bank Mizrahi-Tefahot are provided by a wholly-owned subsidiary of the Bank - Mizrahi Tefahot Technology Division Ltd. (formerly: Mehish Computer Services Ltd.) (hereinafter: "the Technology Division"). The Technology Division works to develop sophisticated IT systems and to continuously improve the level of the Bank's technology equipment.
The main site serving the Bank Group IT systems includes mainframe computers, servers, data storage systems, communications equipment, printers and terminal equipment, all serving as development and operational infrastructure of the Technology Division (see below under section - "Infrastructure and operation").
The Disaster Recovery Site (DRP), located separately, includes a mainframe computer, servers, storage, communications and terminal equipment (see section "Backup and Disaster Recovery" below).
Located in the Bank's branches spread throughout the country is equipment serving as the operational infrastructure of the branches: branch server, end user stations, communications equipment, printers and other special equipment such as: counters providing information for clients, scanners and check readers.

Computer services for Bank Yahav

In 2008, Bank Mizrahi-Tefahot acquired a controlling stake in Bank Yahav (50% of shares) from Bank HaPoalim. Pursuant to a permit from the Bank of Israel, the period in which Bank Yahav would continue to receive IT services from Bank HaPoalim was extended beyond the period specified in the acquisition agreement - through December 31, 2015.
Bank Yahav's Board of Directors and a dedicated Board Committee which handles this issue on behalf of Bank Yahav, are reviewing several outlines for discontinuing IT services received from Bank HaPoalim.
The results of the review of these outlines are expected in 2013.

Infrastructure and operations

The core banking systems are based on a mainframe platform manufactured by IBM. Most of the new projects are now being developed in the open environment of Windows and Linux platforms. In the open environment around the mainframes are close interfaces designed to transfer data between the two environments. The system operates on three mainframe computers and 1800 servers. Most of the updating of the core systems is done nightly, updating the data base for the current activity that occurred during that day and the main books of the Bank, in order to provide the Bank with updated data in preparation for the next day's opening.

Backup and disaster recovery

The Bank's disaster recovery policy is based on operating the main systems at a backup site within no more than 8 hours. To this end, a disaster recovery plan (DRP) was established, based on an agreement with IBM Corp., to obtain backup facility services at the IBM site, combined with equipment owned by the Bank installed at the backup site. The solution includes a mainframe computer, data storage means, servers and 150 work stations. Data at the DRP site is updated in real time by the "hot backup" method. There are open systems, defined by the Bank as having a low criticality level, which are not included in the backup site. Data for these systems is fully backed up. In case of emergency, the required equipment would be installed and the software would be loaded from the central disk facility. In 2013, site expansion will continue and systems will be added, according to priorities to be set by the Bank.

In order to ensure reliability of the DRP system and the disaster recovery capability, exercises are conducted twice annually, together with the different divisions, in order to test the systems.

Concurrently with update of the information at the backup site, critical information for core systems on the central computer are updated at a third site, located on Heleni HaMalka Street, Jerusalem - in order to provide information survivability in case of an extreme scenario where both the main site and the backup site are impacted simultaneously.

In addition to the backup system, other means provide physical equipment and infrastructure security, in both the main site and the backup site: identification of leaks, identification of flooding, preventing electrical surges, etc.

Relocation of data center to Lod

Bank Mizrahi-Tefahot has decided to consolidate the data center services of the Technology Division at a new site in the city of Lod. This data center would include the IT and telephony infrastructure currently located at the central site in Tel Aviv. Upon relocation to Lod, the Tel Aviv site would serve as a stand-alone DRP site for the Bank.

In 2010, construction of the site to hold the data center was completed. In 2011, the communication core, was installed and some Bank employees were relocated to offices in Lod. Concurrently, relocation of the servers to the Lod site has started; to date some 320 servers of the development environment have been relocated.

Information security

The Bank Group has a function for managing the security of applications and the network, which is responsible for information security technology, in accordance with Proper Banking Conduct Regulation 357, as follows:

- Realization of the Bank's policy on data security issued from a technology standpoint, including in overseas branches.
- Implementation of regulatory requirements related to data security.
- Immediate response to information security events (in particular - cyber events).
- Approval of the transfer and removal of information, in accordance with the Bank's policy.
- Involvement in design and implementation of projects and project approval from information security standpoint.
- Developing infrastructures and management of data security projects.
- Information security policy for overseas Bank affiliates.

The Bank is ISO-certified with regard to information security for direct banking. See the chapter on Risk Management for Bank policy on information security.

Implications of information security risk and cyber incidents at the Bank

In line with technology development around the world, especially in cyber space, the Bank uses multiple channels, such as internet, telephone and cellular networks, which expose the Bank to cyber risk. The risk factors to which the Bank is exposed include impact to service availability, to obligations of confidentiality and business confidentiality and to information integrity. According to estimates, there are concerns that these risk factors would be exacerbated in future. The Bank regards the risk of cyber incidents as a key component of information security risk. Therefore, and in line with Bank of Israel requirements, in 2012 the Bank conducted a comprehensive assessment of information security risk. This assessment included a survey for cyber incident assessment, which has been applied by banks in Israel and around the world. This model evaluates the Bank's risk level compared to what is common at similar institutions in Israel and world wide. It also reviewed the likelihood of success of any attack on the different environments at the Bank. Based on the outcome, a current, dynamic, comprehensive protection plan was put in place. In addition, the Bank takes specific measures to identify risk in those operations exposed to cyber incidents, in order to prevent and mitigate information security risk for Bank employees, subcontractors and outsourcers.

In 2012, the Bank took several cyber-focused measures, including:

- Real time prevention and monitoring
- Identification of anomalies and attacks within the network
- External scans to identify weaknesses
- Log file collection and analysis from systems and infrastructure
- Deploying a quick-response expert team
- Specification and implementation of on-going process for cyber risk management
- Central administration and alerts for information security events
- Physical security of all IT facilities
- Tests applied with regard to human resource reliability

Outsourcing – the Bank takes multiple measures to prevent, monitor and identify failures due to use of outsourcing, while providing a response in line with the aforementioned guidelines.

In conjunction with preparations for handling cyber threat and its variations, over the past year the Bank also acted with regard to recruitment and training of professional staff, purchased and deployed advanced tools for implementing a dynamic protective envelope, improved its capability to gather, analyze and monitor unusual activity on the Bank's information networks.

In 2012, there were no significant cyber attack events at the Bank.

Vendors

The Bank Group, through the Technology Division, has several significant suppliers of hardware and software infrastructure, some of which have unique expertise and knowledge of their field, or a limited number of suppliers operate in the relevant field:

- IBM – hardware and software for mainframes in a server environment and for storage infrastructure, including maintenance services. IBM provides the main infrastructure in hardware and software for the core banking systems. IBM is a major international corporation, providing similar services, on an almost exclusive basis, to all major banks in Israel, and to most of the world's major banks.
- Microsoft – operating systems and infrastructure for servers, computerized office and end stations.
- CA – mainframe software.
- Cisco - communications equipment.

Projects

The Bank Group, through the Technology Division, is pursuing multiple projects requiring major IT investments, which are in various development and deployment stages. These projects may be grouped as follows:

- Projects under development.
- Projects put into operation in recent years, which are handled in conjunction with the regular work plan.
- Development of IT infrastructure.

A. Projects under development:

- Trading room operation system - replacement of the current system used for operating the trading room, so as to adapt the computer system to the range of transactions and scope of operations.
- Continued development of the Hybrid Banking project, which was launched in 2011, including installation of an IP telephony system to replace the old call center systems and to link business systems at the call center and branches. Project development for the commercial side was completed in 2012.
- Advanced modeling system for capital allocation.

B. Projects put into operation in recent years, which are handled in conjunction with the regular work plan:

- New mortgage system - completed conversion of mortgages to the new Shoham mortgage system.
- Impaired debt management system - a system intended as response to directives of the Bank of Israel with regard to this issue. The system was partially launched in 2010 to produce reports for Bank of Israel, and was fully operational in early 2011.
- CRM system at the Bank branches - customization of the CRM system for work at mortgage branches, with emphasis on maximizing client opportunities.
- Dedicated system for management of audit reports. The system enables improved computer-based monitoring of findings and recommendations in audit reports.
- New system for General Ledger management and for compiling the Bank's financial statements. The system started operation in preparing the financial statements for the first quarter of 2012.
- Bank website – the existing website was replaced by a new one, based on advanced infrastructure.

C. Development of IT infrastructure:

Investment in infrastructure development forms an important basis, allowing the Bank to support expansion of its business through development of new, state-of-the-art banking systems. This includes, inter alia, mainframe computer upgrade, server farm expansion and upgrade, storage system customization, communication system expansion and workstation replacement at branches.

Investments and expenses with respect to IT

Below is information about investments and expenses for the Bank with respect to IT:

IT-related expenses, as listed on the 2012 statement of profit and loss (NIS in millions):

	For the year ended December 31, 2012 (Reported amounts, NIS in millions				2011
	Software	Hardware	Other	Total	Total
Payroll and associated expenses [(1)]	150	24	53	227	
Usage license expenses not capitalized into assets [(2)]	84	10	-	94	
Outsourcing expenses [(3)]	17	3	1	21	
Depreciation expenses [(4)]	144	30	4	178	
Other expenses [(5)]	12	1	90	103	
Total expenses	**407**	**68**	**148**	**623**	**601**

Additional IT-related assets not expensed in 2012 (NIS in millions):

	For the year ended December 31, 2012 (Reported amounts, NIS in millions				2011
	Software	Hardware	Other	Total	Total
Payroll and associated expenses [(1)]	8	-	-	8	
Acquisition of usage license expenses [(1)]	41	30	4	75	
Outsourcing expenses [(2)]	71	7	-	78	
Total	**120**	**37**	**4**	**161**	**182**

Balance of IT-related assets as of 2012 (NIS in millions):

	For the year ended December 31, 2012 (Reported amounts, NIS in millions				2011
	Software	Hardware	Other	Total	Total
Total depreciated balance as of December 31, 2012	**468**	**74**	**10**	**552**	**539**
Includes: Payroll and associated expenses	35	-	-	35	41

(1) Includes payroll of hardware and software professionals as well as payroll of other IT staff, such as: administrative staff, maintenance staff, operations staff. Payroll costs added to assets include labor costs for development of software for the Bank's own use, capitalized into assets in accordance with generally accepted accounting practices.

(2) These expenses primarily consist of current software maintenance. These expenses are included on the financial statements under "Maintenance and depreciation expenses for buildings and equipment". Additions to assets with respect to usage licenses are with respect to software acquisition. These expenses are included on the financial statements under "Maintenance and depreciation expenses for buildings and equipment".

(3) These expenses are with respect to hardware and software maintenance by external employees. These expenses are included on the financial statements under "Maintenance and depreciation expenses for buildings and equipment". Additions to assets with respect to outsourcing include cost of external employees employed by the Bank to develop software for the Bank's own use.

(4) For details of accounting policy with regard to depreciation expenses, see Note 1. L. to the financial statements.

(5) Includes NIS 44 million which constitutes payments to banks providing IT services to Bank Yahav. Also includes expenses with respect to rent and taxes, communication and general & administrative expenses.

Off balance sheet activity

Provident funds – the Group provides operating services to provident funds. The value of assets in funds to which the Group provides operating services, amounted as of December 31, 2012 to NIS 62.5 billion, compared to NIS 58.1 billion as of December 31, 2011.

Client activity in securities – The value of the securities portfolios in the custody of the Bank, held by clients, amounted to NIS 165 billion as of December 31, 2011, compared with NIS 153 billion at the end of 2011. Revenues from client activity in securities for the Group amounted to NIS 215 million in 2012, compared with NIS 265 million in 2011, a decrease of 21.9%.

Operations based on extent of collection – the Bank has credit and deposits from deposits whose repayment to the depositor is contingent on collection of credit (or deposits) for which the Bank receives margin- or collection-fee based revenue. The balance of credit from deposits based on extent of collection as of December 31, 2012 amounted to NIS 15.2 billion, compared to NIS 16.8 billion at end of 2011. These amounts exclude standing loans and government deposits extended for them. For additional details, see Note 19.B. to the financial statements.

Description of Businesses of the Bank Group by Operating Segment

Bank Group operating segments

The Bank manages its operations in six major operating segments, which are distinguished by client characteristics and type of banking services required, as well as by the organizational unit responsible for servicing each segment. Operating segment definition is based on the Bank's organizational structure, as described below. The operations in the six operating segments include all areas of banking operations including classic banking activity (loans and deposits), securities activity for clients and activity in derivative instruments. Operations of the various segments are conducted via Bank branches, trading room, Business Centers, Bank HQ departments and subsidiaries in Israel and overseas.

The Bank's operating segments are:

Household segment - under responsibility of the Retail Division, This segment includes household clients with relatively minor financial activity, as well as the mortgage sector. The division provides appropriate banking services and financial products to segment clients, including in the field of mortgages.

Small business segment - under responsibility of the Retail Division, The segment serves small companies and small business clients, having an indebtedness level of less than NIS 6 million, sales of less than NIS 30 million and liquid asset balance of less than NIS 10 million. Banking services and financial products, including commercial banking services as required, are provided to segment clients.

Private banking – private banking is under responsibility of the Private Banking and International Operations sector of the Financial Division. Private banking sector clients are individual clients with liquid assets (primarily short-term deposits and security investments) over NIS 1 million. Clients of this segment have high financial wealth, to which the Bank offers access to unique products and services in capital management activity, advisory service and investment management.

Commercial banking – clients of this segment are private and public companies of medium size (middle market) and medium level of indebtedness, and are served by the Business Banking Division, primarily by the Business sector, which operates via six business centers located throughout Israel. Business customers are assigned to the Business sector primarily using the following criteria: total indebtedness of NIS 6 - 25 million, sales of NIS 30-120 million or liquid assets of NIS 10-40 million. Segment clients operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

Business banking - this segment is under responsibility of the Major Corporations Sector of the Business Division. This segment serves the largest business clients. Criteria by which clients are assigned to the Corporate sector include: total indebtedness over NIS 25 million, sales over NIS 120 million or liquid assets over NIS 40 million. This segment provides a range of banking and financial services to the largest companies in the economy, in an array of industries, at relatively high levels of indebtedness. Segment clients operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

Financial management - operations in this segment include, inter alia, management of assets and liabilities, management of exposure to market risk, management of the nostro portfolio and liquidity management as well as trading room operations in the financial and capital markets. The segment is under responsibility of the Finance Division, except for investments in non-banking corporations, which are under the responsibility of the business division.

The main products offered by the Bank's different operating segments are:

- **Banking and finance** - an array of banking services offered to private and corporate clients, including management of checking account, provision of a current loan account, different kinds of credit and guarantees, receiving deposits, foreign trade activities (imports, exports, documentary credit, etc.), trading in derivative instruments, including trading in currencies and interest rates, etc.
- **Capital market** - security transactions for clients on stock exchanges in Israel and overseas, provident fund operating services and mutual fund distribution, which are among investment tracks available to Bank clients.
- **Credit cards** – A set of financial products and banking services given in conjunction with credit cards issued to Bank clients by credit card companies in Israel.
- **Mortgages** – Housing loans secured by charges on a residence, out of the Bank's funds and within the framework of government aid programs.
- **Construction and real estate** - banking operations vis-à-vis companies in the real estate sector, as well as unique banking services for the real estate sector, including the financing of real estate products by the closed financing method.

The principles used in assigning balances, income and expenses to clients in the system are as follows:

- Credit interest revenues and deposit interest expenses are directly attributed to the client. For credit, an expense set at cost of capital raised is attributed to clients, against an inter-segment credit to the Financial Management segment. For deposits, revenue set at cost of capital raised is attributed to clients, against an inter-segment debit to the Financial Management segment. Each of the segments is credited for capital attributed to operations there of, against a debit to the Financial Management segment. Capital consumption is measured by the average risk-free assets managed by the segment.
- For derivative instrument operations, profits are attributed to the client at the spread incorporated in the price of the derivative instrument quoted to the client. Profit arising from changes to fair value of derivatives is attributed to the Financial Management segment.
- Profit and loss from Bank investment in securities and from strategic positions are attributed to the Financial Management segment.
- Expenses with respect to credit loss are directly attributed to clients on behalf of whom they were made.
- Commission and other revenues are specifically attributed to clients.
- Payroll, building maintenance and other expenses attributed specifically to branches, are loaded on branch clients.
- Payroll expenses of headquarters staff, maintenance and other expenses not specifically related to branches, are loaded on clients based on appropriate load bases.
- Expenses attributed directly to Bank branches, including salary and benefits, rent and maintenance are attributed to different segments as inter-segment expenses, based on segment affiliation of client services by the branches.
- Provision for tax on operating profit is attributed to clients, pro-rated in accordance with the effective tax rate and accounting for tax impact referring to specific segments and not to all Bank operations.

- Return on equity is calculated as the ratio of net profit to attributed equity. Equity is attributed based on the average risk assets of the customers.
- Balance sheet and assets-under-management balances are specifically attributed to clients.
- Fixed assets are attributed based on appropriate ratios.

In order to analyze results of Bank operations by relevant criteria, clients have been assigned to the organizational units in charge of servicing them. Information presented below by operating segment is based on the Bank's organizational structure on client assignment to various departments and then to operating segments, and on attribution of results and balances to clients and segments in the profitability measurement system.

Financial Information on Operating Segments

Since uniform rules have not been prescribed to allocate the clients to the segments, it is not possible to compare information regarding the Bank's pro rata share of the Banking system in the different operating segments, in profit and return on capital.

Summary of financial results of operating sectors, as defined by the Bank, (reported amounts, NIS in millions) are as follows. See Note 30 to the financial statements for details.

Profitability

	Net profit		Share of total net profit (in %)		Return on equity (in %)	
	For the year ended December 31,					
	2012	(1) 2011	2012	2011	2012	(1) 2011
Household:						
Mortgages	381	366	35	35	13.0	14.6
Other	119	157	11	15	12.1	17.6
Private banking	38	46	4	4	39.9	41.0
Small business	160	137	15	13	38.8	34.9
Commercial banking	59	69	5	7	14.3	17.2
Business banking	305	198	29	19	10.5	7.7
Financial management	14	71	1	7	3.0	24.9
Total	**1,076**	**1,044**	**100**	**100**	**13.1**	**14.6**

(1) Reclassified.

Household segment

General information on the operating segment

The household segment mainly consists of individual clients, with low levels of indebtedness and relatively small-scale financial activity. Segment clients include those with individual accounts, joint accounts for two spouses etc. as well as mortgage borrowers. The segment is highly diversified, and is handled by the Bank's Retail Division.

In 2012, the Bank continued to deploy Hybrid Banking, which was launched in late 2011. Hybrid Banking – an optimal combination of personal and digital banking, allowing all clients direct access to their personal banker at the branch by using a range of communication channels. This unique, innovative service concept puts to use technological advances in the banking world, to create an immediate, direct link between the client and their personal banker at the branch. Unlike other banking concepts, technology is not intended as replacement of personal bankers at the branch, but rather to bond and solidify their ties with clients. Moreover, staff at the Bank's call center was divided into Branch Teams, each assigned to a specific branch and serving as an integral part of the branch. Accordingly, Bank clients can reach their banker at the branch, or one of the branch team members, by telephone, cell phone, SMS and email messages from anywhere during 12 hours of operation, from 8am to 8pm.

Products

Below is a description of the notable products in the household segment and the primary services offered within the scope of these products.

Banking and finance

Most of the services are provided within this framework

- Credit and debitory accounts – The credit limits for debitory account activity are determined according to the client's needs, the level of his income and the judgment of the Bank based on factors including economic models. In accordance with Proper Conduct of Banking Business Regulation 325, clients are not allowed to exceed their determined credit limit.
- Investments – providing investment-related services to customers, such as: Various deposits for different terms.
- Loans – general-purpose loans which include, inter alia, loans not intended for home purchase secured by pledging a lien on a residential property, and other loans for various terms and under different conditions.
- Assistance in financing car purchase - activity related to loans for new car purchase from importers, whereby the Bank and several car importers work jointly to offer joint promotions for financing car purchasing by clients.

Mortgages

The main services in the mortgage sector are loans from the Bank's funds; additionally, the Bank is engaged in the mortgage sector in providing execution and clearinghouse services for loans provided by the State, including loans in conjunction with the Ministry of Housing and Construction Assistance Program. Mortgage operations also include the offering of life and property insurance to borrowers (insurance incidental to the mortgage) via the Bank-owned insurance agency.

Volume of mortgages granted by the Household segment is as follows:

	Loans granted (NIS in millions)			Rate of change	
	2012	2011	2010	2011-2012	2011 over 2010
Mortgages issued (for housing and any purpose)					
From Bank funds	17,333	16,437	16,413	5.5%	0.1%
From Treasury funds:					
Directed loans	184	85	166	116.5%	(48.8%)
Standing loans and grants	215	101	194	112.9%	(47.9%)
Total new loans	**17,732**	**16,623**	**16,773**	**6.7%**	**(0.9%)**
Refinanced loans	1,755	1,422	1,308	23.4%	8.7%
Total loans issued	**19,487**	**18,045**	**18,081**	**8.0%**	**(0.2%)**
Number of borrowers (includes re-financed loans)	48,261	47,413	50,721	1.8%	(6.5%)

A description of the main mortgage services is provided below:

Loans out of Bank funds - loans out of Bank funds and at its risk, granted as free loans (which are not within the scope of the Ministry of Housing's aid program) for the purchase of real estate, for construction, generally for the borrower's residence. The loans are issued for a long term of up to 30 years (and in some tracks - up to 35 years), considering the kind of loan and repayment ability of the borrower.

The Bank issues credit in different linkage segments and offers a "combined mortgage" – a loan composition that combines the following elements or a part of them: CPI-linked component at fixed or variable interest, non-linked NIS component bearing fixed or adjustable interest and a foreign-currency linked component bearing adjustable interest. The combined mortgage enables the Bank to maintain profitability and allows clients to diversify risk.

In view of the low Bank of Israel interest rates, and its decrease in 2012 (similar to 2011 and 2010) in the past year, too, borrowers preferred to take out adjustable-rate loans in the non-linked NIS-denominated sector as well as in the CPI-linked sector, where the interest rate is more attractive, compared to fixed-rate loans. However, the share of loans bearing adjustable interest was slightly lower, compared to an increase in the share of loans bearing fixed interest, partially reflected in a gradual increase in the non-linked fixed interest track (a relatively new track, added in 2010 to the range of tracks offered by the Bank to borrowers).

For information about restrictions on the LTV ratio for housing loans, see below under legislation in this segment.

Services in conjunction with the Ministry of Housing Assistance Program – Beyond the banking activity of granting credit, the Bank acts as an extension of the State in servicing eligible Ministry of Housing recipients.

These services include loans within the Ministry of Construction and Housing's assistance program, including location-based loans, contingent grants and rental subsidies (until 2006), as provided below:

A. **Loans** - as from July 1, 2004, a new two-year agreement went into effect between Bank Tefahot, at that time, and the Government, whereby the collection commission rate determined by the tender held by the Ministry of Finance, with the participation of the mortgage banks will apply to loans to eligible borrowers issued on or after July 1, 2004, which are significantly lower than the commission rate on loans issued until June 30, 2004.

The agreement is between the entire banking sector, including the Bank, and the Government - with the decision as to which bank to use to realize the entitlement is up to the client obtaining the mortgage.

This agreement has been continuously extended each year, most recently through June 30, 2013.

Bank revenues from all loans to eligible borrowers under State responsibility in 2012 amounted to NIS 75 million, compared to NIS 85 million in 2011.

For details of the agreement between the Ministry of Finance and banks, for provision of loans to eligible borrowers with low point rating out of Bank funds and under Bank responsibility, see Note 19.D.18).

In addition to ordinary loans in conjunction with the Assistance Program, there is a special arrangement for providing subsidized loans, issued by the Ministry of Housing and Construction under conditions that are updated from time to time, the objective of which is to encourage the purchase of new homes in certain communities that the State has an interest in populating ("location-based loans").

In the loans area, the Bank is involved, in addition to the ordinary banking services, in the array of administrative aspects required for services to Ministry of Housing and Construction eligible participants, such as issuance of eligibility certificates.

B. Contingent grant – A loan given as part of housing assistance from State funds that gradually is converted to a grant, subject to the conditions stipulated by the Ministry of Housing and Construction.

Life insurance and property insurance of borrowers (incidental to mortgages) – The vast majority of borrowers are insured in life insurance policies related to the loan, and most of the properties serving as collateral are insured by property insurance.

Through November 30, 2005, some borrowers would obtain insurance coverage under insurance arrangements which were customary at the Bank at the time. As from December 2005, a call center is operated at an insurance company, which is a wholly-owned and wholly-controlled subsidiary of the Bank, and some borrowers choose to obtain insurance coverage through the Bank's insurance agency while others make other insurance arrangements.

Marketing of insurance

In accordance with directives of the Supervisor of Insurance and of the Supervisor of Banks, life insurance and home insurance incidental to housing loans are marketed by an insurance agency wholly-owned by the Bank (Tefahot Insurance Agency (1989) Ltd.), whose operations are separate from those of the Bank, and is restricted to exclusively engage in home insurance, including water damage, and in life insurance incidental to loans granted by the Bank.

In order to maintain the required separation between the mortgage activities and insurance activities, special stations linked directly to the Bank-owned insurance agency were set up in the Bank branches that issue mortgages. At these stations, the client purchases life insurance and property insurance independently and produces the insurance forms necessary for taking out the loan.

The Bank's income from insurance incidental to mortgages (in NIS millions):

	2012	2011	2010
Life insurance	101	92	86
Property insurance	26	33	33
Total revenues from sale of insurance	**127**	**125**	**119**

The increase in life insurance revenues in 2012 is due to larger business volume in the insurance portfolio.

In 2012, a Ministry of Finance regulation came into effect, whereby commission paid by an insurer to an insurance agent with respect to comprehensive property insurance required as collateral for a housing loan may not increase a certain rate.

Capital market

This product includes client activities in the capital market, including buying, selling and custody of various securities and services provided for such securities (receiving interest, dividends, bonuses etc.) This also includes mutual fund distribution services and provident fund operating services.

Credit cards

Credit cards are one of the key means of payment in the economy. As part of the activities with clients in the household segment, the clients a range of credit cards are offered. In this area, the segment works vis-à-vis credit card companies Isracard and CAL. The Bank offers its clients credit cards that are issued by these companies when opening a private account in the Bank, according to the client's request. Credit card companies, on their part, use the Bank as a conduit for distributing their cards to the Bank's clients. The Bank offers its clients almost all kinds of credit cards existing in the Israeli economy. The Bank also has several products in the credit card sector:

"The Card" - a branded credit card unique to the Bank. The Card provides unique promotions and activity focused on consumer and banking benefits. The objective of The Card is to reinforce relationships and extend activity with existing clients, as well as another means of recruiting new clients by the Bank.

For details of the agreement with the CAL group, inter alia, with regard to issuance of the branded credit card, see Note 19.D.13) to the financial statements.

"Tefahot Credit Card" – the product is aimed at assisting mortgage sales as well as opening of current accounts. The product enables the allocation of a credit facility, based on the client's repayment ability and the asset already pledged to the Bank, through which the client can finance additional expenses involved in purchasing a home (furniture, renovations, etc.), or for any other reason. To this end, the client will be issued a unique credit card. The credit card charges will accumulate in the current account and be transferred periodically to the mortgage account.

"Current" credit card for Tefahot clients - in conjunction with the Bank's synergy activity, it offers a credit card based on "The Card" platform, intended for clients who took out a mortgage at the Bank and do not have an active current account at the Bank. These clients enjoy the various benefits of "The Card" club, and monthly charges are paid to the Bank by debit order to the client's active account at another bank.

"Free Student credit card" – this card provides students with general-purpose credit. Credit with this card may be used over 3 years and bears a special, attractive interest rate for the actual credit utilized. Credit payments are flexible, with initial repayment of principal and interest starting on the third anniversary of the card issue date (a 1-year extension may be applied for). Clients may repay early, in full or partial payment, with no fees or charges.

Unique Bank services

The key unique service offered by the Bank is Hybrid Banking, which allows clients easy, direct access to a personal banker using a range of readily available technologies, as described above. Moreover, under the household segment, the Bank offers its clients services which express the advantages of the combination of products offered by the Bank to its clients as described above. Within this structure, the Bank offers various benefits in current accounts and credit of clients who take out mortgages, in order to encourage the mortgage clients to maintain their current account in the Bank. The Bank also offers mortgage-related benefits to clients with current accounts in the Bank, in order to encourage these clients to take out mortgages through the Bank. The applicable benefits have also been applied to Bank Yahav clients, based on their activity and attributes.

The unique services that the Bank offers its clients in the household segment include retail banking products and mortgage products, as provided below:

Executive Account – the unique brand, "Executive Account", launched in 2007 allows a preferred segment of individuals to make the most of managing their current account with the Bank. The brand emphasizes service, account management, bank value propositions, financial benefits and non-banking services provided to Executive Account clients. Clients may use professional advisors for financial, pension and mortgage advisory services.

"Interest-free Overdraft" – Set-off of debit and credit balances of a customer during the month; this service is provided to select customers.

Benefits to mortgage holders – unique benefits offered to specific groups of clients who have a mortgage account with the Bank. The benefits included an interest-free facility in the current account, as well as interest on the credit balance up to the level of the monthly mortgage payment. The benefit is given every month, subject to the client's meeting other prescribed conditions during that month.

Retirement advisory service - the Bank offers a retirement advisory service to Bank clients and to clients of other banks, both salaried and self-employed, based on an advisory model supported by a computer system developed by the Bank. This advisory service is provided by qualified pension advisors, providing an objective advisory service.

See the description of competition in the segment below for alternatives to these products.

Legislation

In November 2012, the Supervisor of Banks issued a letter instructing all banks not to approve housing loans with an LTV ratio in excess of 75% for purchase of a real estate interest constituting a single apartment, 70% - for an alternative apartment and 50% - for any other apartment, including for investment purposes.

In November 2012, the Governor of the Bank of Israel issued an amendment to the Banking Rules (Customer Service) (Commissions), 2008 and also issued the Banking Ordinance (Customer Service) (Elimination of Supervision of Certain Banking Service and Modification in Another Case), 2012. The new directives apply to banking corporations as from January 1, 2013. According to the new amendment and ordinance, the Bank is required to provide public transparency with regard to commissions charged, and to take several actions to reduce commissions charged to individual and small business accounts.

In November 2012, the Supervisor of Banks directed banking corporations to take measures, starting on March 1, 2013, including re-specify the rate of commissions on securities, aligning these in as much as possible with commissions actually charged, and change the nature of client contracting to be based on the commission rate or amount, rather than on a discount off the list price.

In February 2013, the Advisory Committee on Banking Business received a draft directive by the Supervisor of Banks, which specifies an update to risk weighting of housing loans with respect to capital allocation by the Bank, reducing the credit conversion factor for guarantees to secure investments of apartment buyers and an update to group provision with respect to housing loans.

For further details and description of the normative framework applicable to the Bank, and recently-published legislative arrangements, some of which have effect on operations of the household segment, see below in chapter on Legislation and Supervision of Bank Group Operations.

Technological changes

For technology changes, see chapter "IT and Computer Systems".

Critical success factors in the Household Segment

The Bank is exposed to hundreds of thousands of mortgage-holding clients which constitute a natural target population for marketing additional products of the Bank. Expansion of the client base and broadening the array of services to clients in the Household segment, while exploiting the reservoir of the mortgage clients represents a critical factor for the success of this segment.

Furthermore, upon acquisition of 50% of Bank Yahav's issued share capital by the Bank. in 2009, clients of Yahav strengthen operations of the retail segment when exposed to potential additional activity within the Group; for example, in the mortgage sector.

Clients

The activities of the household segment are characterized by broad diversification of loans and deposits in the retail banking sector and of the loans portfolio among the hundreds of thousands of households that took out mortgages from the Bank over the years. Therefore, the loss of one client or another does not have a material effect on the overall activity of the segment.

Marketing and distribution

Generally, marketing and distribution of the products and services of this segment are carried out through the network of Bank branches and through direct channels, serving Hybrid Banking.

Bank branches – the Group operates 175 business centers, branches, affiliates and representative offices across the country, including 44 Yahav branches. The Bank continues to improve branch deployment and to expand its points of sale, through measures including the addition of commercial activity to the mortgage branches and mortgage activity in the commercial branches. For details, see chapter on Branches.

Direct channels - after launching Hybrid Banking as described above, the nature of direct channel operation changed, and they were redefined to be tools serving the branch. Currently, the stand-alone direct channels (i.e. not assigned to bank branches) are: sales center, investment center, backup center, Bank website, self-service devices and information provided via cell phone.

- Sales and backup centers - the sales center is intended to enhance selling capabilities of Bank branches, as part of marketing campaigns to recruit clients, who are referred directly to the sales center, or by means of outgoing sales calls. The backup center was created to extend business hours, improve service and responsiveness through the call center. The Bank operates call centers at two sites, in Tel Aviv and in Jerusalem. The center located in Jerusalem covers mortgage operations, while the Tel Aviv center provides backup for commercial operations.
- Website – in 2012 the Bank expanded the range of services available to clients in order to continue its policy of reducing client dependence on the actual branch. In 2009, IT improvements to the website were specified in order to continue improving the user interface of the system and to enhance client use of the website.
- The Bank’s automatic teller machines constitute an additional marketing and service arm.

See the chapter on Marketing Operations below for additional information.
The Bank has no dependence on outside marketing and distribution parties in this segment.

Competition

Banking and Finance, credit cards and the capital market

The number of competitors in the household segment is the number of banks operating in the economy, with the focus on the five commercial bank groups. In recent years, the retail banking market sees strong competition among banks. Generally, one can state that the retail banking products offered by the different banks are similar, and therefore, competition focuses on the quality of service, the rates of the margins and commissions paid by the clients.
In addition to the inter-bank competition, intensified efforts are discerned by non-banking entities (mainly insurance companies, credit card companies) that also approach this population segment with offers to provide credit. The credit card companies, together with retail chains and other entities, are also taking measures to issue credit cards directly to clients, not through a bank. See below regarding entry and exit barriers.
In the capital market sector, the competitors also include private investment houses, in addition to insurance companies.
The Bank deals with the existing competition by aspiring to provide quality service and launching unique products. As aforesaid, the Bank believes that the Tefahot and Adanim mergers and the Yahav acquisition hold potential for expanding activities in the household segment, based on on-going activities vis-à-vis clients.

Mortgages

Most of the mortgage activity in Israel is conducted through 10 banks operating in this field. For dozens of years, the Bank has been the leader in the mortgage sector, in terms of the volume of loans issued and the balance of the loans portfolio. Based on Bank of Israel data, the Group's share of provision of housing credit, out of Bank funds and out of State funds in the mortgage sector, reached 35% in 2012. Group market share, in terms of housing loan portfolio, is 34% at the end of 2012. The Bank's major competitors are Bank Leumi, Bank Hapoalim and Discount Bank. Insurance companies also compete in the mortgage sector. See below with respect to entry and exit barriers.

The Bank has adopted different means to deal with the competitive environment in which the mortgages sector operates, including extensive advertising, use of marketers in the field, development and institution of new products, maintaining a presence in the new-homes market, by financing residential construction projects, etc. Another facet of the Bank's dealing with the competition in the mortgage sector is investing resources in constant improvement of its professional standard and the service it provides to clients.

The main entry barriers in this segment are:

- Client habits
- Regulatory limitations
- Minimum capital requirements
- Training professional personnel
- Construction and maintenance of physical infrastructures (such as branches) and technological infrastructures (IT systems).

Cooperation agreements

- Several years ago, the Bank contracted an agreement with EMI – Ezer Mortgage Insurance Company Ltd. ("EMI") – a company holding a license for mortgage credit risk insurance. Credit risk of some Bank clients, who obtain new loans in which the loan to value ratio is high, is insured by EMI. This insurance is intended to cover damage that the Bank could sustain in the event of a credit failure, if the proceeds from foreclosing the collateral are insufficient to cover the balance of the borrower's debt. The insurance is for the upper layer of the loan, so that EMI is meant to cover the first loss and then reduce (or absolutely prevent) a loss to the Bank in the event of realization at a loss.
  Due to the Bank of Israel restricted origination of housing loans with LTV over 75%, as of this date the Bank no longer approves new loans with credit insurance and LTV over 75% (except for loans exempted from this directive, such as: re-financing loans).

  For details, see the chapter on Legislation and Supervision of Bank Group Operations.

- The Bank entered into a series of agreements with several companies that issue credit cards, principally Isracard Ltd. (since 1979) and Israel Credit Cards Ltd. (since 1995), that arrange the relations between the parties. Pursuant to the agreements, the Bank will take action to distribute the credit cards issued by the said companies to their clients. The agreements prescribe mechanisms for calculating the amounts to which the Bank is entitled for the activities of its clients in the cards issued, including based on the volume of usage by the Bank's clients of the credit cards of these companies. The agreements specify the manner in which the credit cards are to be used, the division of liability between the credit card companies and the Bank. Pursuant to the agreements, the Bank is entitled to appoint an overseer on its behalf, who will participate in meetings of the Board of Directors (including meetings of the Board of Directors' subcommittees, except for the audit committee) of Isracard.

For details of the agreement signed with CAL Group, including a new arrangement whereby Bank-branded credit cards have been issued - see Note 19.D.13) to the financial statements.

Business goals and strategy

The Bank sees importance in continuing to develop the household segment as part of the Bank's future activities. The key goals in the household segment and the resultant business strategy are presented below:

- Increasing household market share by broadening the client base, mainly among the clients of the former Bank Tefahot, of Adanim and of Bank Yahav, as a platform for achieving growth in market share and income.
- Retaining Bank share of the mortgages market and expanding it, while focusing on areas with high profitability, by providing valuable proposals to clients, based on the synergy between the mortgage, commercial and financial activities.
- Expanding activity in the branch network and converting all the branches into sales units in the household segment, for traditional banking activity and mortgage activity, and for cross-selling to clients.
- Continued development of products aimed at focused population groups, in order to increase volumes of activity.
- Leveraging the ties between the business banking segment in the construction and real estate industry and between the mortgages segment. In this area, emphasis is placed on maximizing the marketing of mortgages to the buyers of homes in projects built by the real estate segment's clients.

Material systems on which the segment relies for developing its operations are:

- The CRM (Client Relations Management) system, aimed at presenting all relevant information to the Banker in order to offer appropriate products to the client and improve client relations.
- Computer system to support the mortgage origination and administration process, which allows for online operations and processing, as well as daily updates of balances. The system allows for flexible specification and on-going operation of various mortgage products, as well as for development of new, flexible products - allowing the Bank to be competitive and to rapidly react to changes in the business environment.
- In recent years, the Bank has upgraded its branch computer system, initiating use of ".NET" technology. This system positions the Bank in the top tier in terms of operations and service to clients and employees.

The results of the segment are exposed to a threat, due to reasons including the strong competition deriving from its attractiveness, since it is a segment in which the risk is low (due to the relatively high dispersal of clients). Additionally, the segment's results are affected by the entry of credit card companies into retail financing (see details below).

The population of mortgage clients at the Bank (following the merger of Tefahot and Adanim) and acquisition of the holding stake in Bank Yahav, offer an opportunity to expand the Group's client base and to expand operations in the household segment.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic development in Israel and internationally, especially the state of the economy, demand for housing and mortgages, legislation, directives of regulatory entities, the behavior of competitors (including non-banking entities), aspects related to the Bank's image, technological development, developments in availability and price of properties and staffing issues.

Results of Household Segment

	For the year ended December 31, 2012					For the year ended December 31, 2011 [1]				
	Banking and finance	Credit cards	Capital market	Mortgages	Total	Banking and finance	Credit cards	Capital market[2]	Mortgages	Total
										NIS in millions
Interest revenues, net:										
From outside operating segments	214	28	-	3,023	3,265	126	26	-	3,448	3,600
Inter-segment	867	(20)	-	(2,390)	(1,543)	911	(19)	-	(2,892)	(2,000)
Total interest revenues, net	**1,081**	**8**	**-**	**633**	**1,722**	**1,037**	**7**	**-**	**556**	**1,600**
Non-interest financing revenues	-	-	7	-	7	-	-	11	-	11
Commissions and other revenues	244	130	165	239	778	237	124	206	241	808
Total revenues	**1,325**	**138**	**172**	**872**	**2,507**	**1,274**	**131**	**217**	**797**	**2,419**
Expenses with respect to credit losses	55	-	-	10	65	62	-	-	6	68
Operating and other expenses										
From outside operating segments	1,355	28	55	279	1,717	1,300	27	60	248	1,635
Inter-segment	(116)	(3)	-	-	(119)	(113)	(3)	-	-	(116)
Total operating and other expenses	**1,239**	**25**	**55**	**279**	**1,598**	**1,187**	**24**	**60**	**248**	**1,519**
Pre-tax profit	31	113	117	583	844	25	107	157	543	832
Provision for taxes on profit	11	40	41	202	294	7	36	51	177	271
After-tax profit	**20**	**73**	**76**	**381**	**550**	**18**	**71**	**106**	**366**	**561**
Net profit (loss):										
Before attribution to non-controlling interest	20	73	76	381	550	18	71	106	366	561
Attributable to non-controlling interest	(50)	-	-	-	(50)	(38)	-	-	-	(38)
Attributable to equity holders of the banking corporation	**(30)**	**73**	**76**	**381**	**500**	**(20)**	**71**	**106**	**366**	**523**
Return on capital (net profit as % of average capital)					**12.8%**					**15.4%**
Average balance of assets	14,840	2,560	-	68,457	85,857	13,750	2,419	-	61,359	77,528
Average balance of liabilities	55,799	2,560	-	87	58,446	48,953	2,419	-	88	51,460
Average balance of risk assets	15,038	-	-	36,725	51,763	14,080	-	-	32,180	46,260
Average balance of securities	-	-	26,895	-	26,895	-	-	23,927	-	23,927
Loans to the public, net (end balance)	15,219	2,783	-	75,011	93,013	13,813	2,652	-	67,303	83,768
Deposits from the public (end balance)	58,645	-	-	-	58,645	54,091	-	-	-	54,091
Average balance of other assets managed	8,675	-	-	11,531	20,206	8,275	-	-	12,875	21,150
Profit from interest revenues before expenses with respect to credit loss:										
Margin from credit granting operations	522	8	-	601	1,131	470	7	-	524	1,001
Margin from receiving deposits	524	-	-	-	524	527	-	-	-	527
Other	35	-	-	32	67	40	-	-	32	72
Total interest revenues, net	**1,081**	**8**	**-**	**633**	**1,722**	**1,037**	**7**	**-**	**556**	**1,600**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.

(2) Reclassified.

Contribution of the household segment to Group profit in 2012 amounted to NIS 500 million, compared to NIS 523 million in the corresponding period last year – a decrease of 4.4%. Below are key factors affecting the change in segment contribution:

Contribution of mortgages in 2012 amounted to NIS 381 million, compared to NIS 366 million in the corresponding period last year - an increase of 4.1%. The increase is due to an increase of 13.8% in net interest revenues before expenses with respect to credit loss, which is due to expanded operations, reflected in an increase of 11.6% in average assets. Conversely, operating expenses attributed to this sub-segment increased by NIS 31 million and the expenses with respects to credit loss attributed to this sub-segment increased by NIS 4 million.

Contribution of households (excluding mortgages) in 2012 amounted to NIS 129 million, compared to profit amounting to NIS 157 million in the corresponding period last year, a decrease of 24.2%. Net interest revenues before expenses with respect to credit loss increased by 4.6% due to higher volume. Conversely, commissions and other revenues decreased by 4.9%, due to a decrease in revenues from commissions on securities, while operating expenses increased by 3.8%.

Private Banking Segment

General information on the operating segment

Private banking is the concept of banking services geared to clients with high financial wealth, with a considerable part of their activity executed in the management of financial assets. Private banking clients at the Bank are primarily individual clients with liquid assets and security investments over NIS 1 million, and corporations with liquid assets in excess of NIS 8 million.

Financial consulting, which constitutes a significant part of the service offered to this operating segment, is provided to the clients of the segments who have signed consulting agreements. A response is also provided for other financial needs of these clients, while providing high-quality personal service and offering a range of advanced products.

The banks in Israel have invested substantial resources in recent years in the development and upgrading of the private banking services and in increasing their market share in this segment. This is due to the following factors:

- The potential in expanding business relationships with clients of a high socio-economic position assigned to this segment.
- Growing demand by clients of this segment for a high standard of professional and personal service, as prevails worldwide.
- Accelerated development of advanced investment products, such as: structured products, hedge funds, ETFs and others, which are alternatives to traditional products (savings accounts, securities etc.)

Products

The products and services offered to clients of this segment are as follows:

- Banking and finance – A wide range of banking and finance products are offered to this segment's clients, while formulating an investment strategy suitable for each client, tailored to his character and special needs, as well as an array of advanced investment products including deposits and structured products.
- Credit cards - the Bank offers a range of credit cards issued by Israeli credit card companies to segment clients.
- Capital market - this product includes client operations in the capital market, including buying, selling and custodial services of various securities, and provision of services with respect to securities (receipt of interest, dividends, bonus etc.) This also includes mutual fund distribution services and provident fund operating services.

Legislation

A description of the normative framework applicable to the Bank, including to the Private Banking segment, is provided below under the chapter Restrictions on and Regulation of Bank Group Operations.

Technological changes

For technology changes, see chapter "IT and Computer Systems".

Critical success factors

The critical success factors in the Private Banking Segment include development of marketing and business activities that rest on the understanding of the clients' needs and on providing professional, fast and effective service that offers a comprehensive solution to the client's needs in all banking areas.

Clients

This segment serves clients with high financial wealth, mainly individual clients with liquid deposits and security investments exceeding NIS 2.5 million and business clients with such liquid balances in excess of NIS 8 million.
The client group served by this segment is heterogeneous, there are no material dependencies or relations between clients and the Bank, so that the private banking segment is not dependent on any specific group of clients whose loss may materially impact its operations.

Marketing and distribution

In addition to the marketing and distribution activities through the Bank's private banking department and through direct channels, conferences are conducted for clients in this segment, according to select population segments and inquiries through direct mail. The Bank has no dependence on outside marketing and distribution parties in this segment.

Competition

The concept of the unique services defined by the Bank as "private banking" prevails throughout the global and international banking system, and also in Israel. However, it should be noted that the criteria that determine whether one belongs to this segment, the service approach and its specific nature change, and do not rest on identical principles in all the banks. Also, accordingly, the volume of the Bank's activities in this segment relative to its competitors is not known, and public information is not available about the proportionate share in the private banking system of the different banks.
In addition to local banks, there is competition in this segment from foreign banks and non-banking entities, such as investment houses, types of funds (from Israel and overseas) and insurance companies.
In order to deal with current competition in this segment, the Bank invests substantial resources in the professional training of its employees, in providing high quality service and in maintaining strong ties with the client, in the organization of professional conferences for the segment's select clients, in introduction of specialized and unique products to the segment's clients, and in efforts to identify and attract new clients on a regular basis.

The main entry barriers in this segment are:

- Regulatory limitations
- Minimum capital requirements
- Training professional personnel
- Building and maintaining physical and technological infrastructure (IT systems, with emphasis on consulting systems and CRM).
- A supply of unique financial products.

Business goals and strategy

The Bank plans to continue to develop its global private banking network, based on centralized management, centers of professional support and cooperation between Bank affiliates and units in Israel and throughout the world.

Continuing to provide professional, reliable service and to maintain close relationships with clients would allow the Bank to expand its business with segment clients.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including macroeconomic and geopolitical conditions, economic policy, the currency market and capital market in Israel and world-wide, other factors that impact the exposure to financial risk, clients' financial robustness, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, aspects related to the Bank's image, technological developments and manpower matters.

Results of Private Banking Segment

	For the year ended December 31, 2012			For the year ended December 31, 2011 [2]		
	Banking and finance	Capital market	Total	Banking and finance [1]	Capital market	Total
						NIS in millions
Interest revenues, net:						
From outside operating segments	(12)	-	(12)	10	-	10
Inter-segment	85	-	85	79	-	79
Total interest revenues, net	**73**	**-**	**73**	**89**	**-**	**89**
Non-interest financing revenues	1	-	1	-	1	1
Commissions and other revenues	26	29	55	23	33	56
Total revenues	**100**	**29**	**129**	**112**	**34**	**146**
Expenses with respect to credit loss	(12)	-	(12)	(5)	-	(5)
Operating and other expenses						
From outside operating segments	78	-	78	74	-	74
Inter-segment	5	-	5	5	-	5
Total operating and other expenses	**83**	**-**	**83**	**79**	**-**	**79**
Pre-tax profit	29	29	58	38	34	72
Provision for taxes on profit	10	10	20	15	11	26
Net profit attributable to equity holders of the banking corporation	**19**	**19**	**38**	**23**	**23**	**46**
Return on capital (net profit as % of average capital)			**39.9%**			**41.0%**
Average balance of assets	2,274	-	2,274	2,533	-	2,533
Average balance of liabilities	6,958	-	6,958	6,352	-	6,352
Average balance of risk assets	1,191	-	1,191	1,201	-	1,201
Average balance of securities	-	7,767	7,767	-	9,672	9,672
Loans to the public, net (end balance)	1,178	-	1,178	1,191	-	1,191
Deposits from the public (end balance)	7,077	-	7,077	5,831	-	5,831
Average balance of other assets managed	2	-	2	-	-	-
Profit from interest revenues before expenses with respect to credit loss:						
Margin from credit granting operations	31	-	31	35	-	35
Margin from receiving deposits	41	-	41	52	-	52
Other	1	-	1	2	-	2
Total interest revenues, net	**73**	**-**	**73**	**89**	**-**	**89**

(1) Reclassified.

(2) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.

Below are key factors affecting the change in segment contribution:

Contribution of the private banking segment to Group profit in 2012 amounted to NIS 38 million, compared to NIS 46 million in the corresponding period last year.

Net interest revenues before expenses with respect to credit loss decreased by NIS 16 million mainly due to decrease in the spread of deposits, which arise from the low interest. Operating expenses increased by 5.1%. Furthermore, in 2012 there were 12 million revenues with respect to credit loss attributed to the segment, compared to revenues of NIS 5 million in the corresponding period last year.

Small Business Segment

General information on the operating segment

The small business segment operates within the retail division, and mainly serves small companies and small business clients with relatively low turnover and total indebtedness of up to NIS 6 million. This segment is characterized by large client diversification. In view of the fact that the availability of data and their quality regarding the clients of this segment is relatively lower than for major business clients, there is a need for professional service and appropriate means of control, in order to assess the quality of the client for the purpose of issuing credit. Additionally, this segment is characterized by a high percentage of collateral required from the clients to ensure credit repayment.

Products

Banking and finance

Within the scope of this product, the Bank provides the following services:

- Loans for various purposes – business loans, loans against the discounting of checking, credit cards etc.
- Import/export activities – foreign currency operations, adaptation of credit facilities to the nature of the client's activities using technological means, such as: EDI online.
- Investments – an array of investment activities, such as: Various deposits for different terms.
- Management of checking account facilities – The facilities are determined according to the client's needs, turnover and judgment of the Bank.

Credit cards - the Bank offers a range of credit cards issued by Israeli credit card companies to segment clients.

Capital market - this product includes customer activities in the capital market, including buying, selling and custody of various securities and services provided for such securities (receiving interest, dividends, bonuses etc.) This also includes mutual fund distribution services and provident fund operating services.

Legislation

A description of the normative framework applicable to the Bank is provided under the chapter Legislation and Regulation of Bank Group Operations.

Technological changes

See the chapter on IT Systems above for the technological changes, including with respect to provident funds and pension consultancy.

Critical success factors

The critical success factors in this operating segment are personal service and providing banking solutions for the range of the client’s financial needs.

Clients

Operations of the small business segment are typically highly diversified in terms of retail credit and deposits. Therefore loss of any client does not materially impact segment operations, so that the segment is not dependent on any individual client nor on any small number of clients.

Marketing and distribution

The main marketing and distribution factors in the segment are the Bank's branches and direct channels. There is no dependence on outside marketing channels. For details of these marketing and distribution factors, see description of the household segment.

Competition

Competition in this operating segment is primarily within the banking system, as well as activity by non-bank credit providers, such as insurance companies, non-bank credit cards and various financing companies. The Bank's principal methods for dealing with the competition are active marketing, personal ties with the client, providing personal service and comprehensive professional solutions for the full range of client financial needs.
Due to differences among banks in segment definitions, the Bank is unable to estimate its market share of this segment.

The main entry barriers in this segment are:

- Regulatory limitations
- Minimum capital requirements
- Training professional personnel
- Construction and maintenance of physical infrastructures (such as branches) and technological infrastructures (IT systems).
- Customer habits – with emphasis on maintaining current relationships and reputation of banking institutions

Business goals and strategy

The Bank's business strategy consists of expansion of its operations in the small business segment, while constantly evaluating risk at the individual client level and for the entire sector and industry.

Below are the key goals in the small business segment and the business strategy deriving from these goals:

- Increasing marketing activity vis-à-vis clients, while segmenting the clients by occupation, size of operation and individual needs.
- Maximize potential profitability for each client by adopting a comprehensive view of client activity, creating a comprehensive relationship based on credit products and marketing of other products – depending on client attributes.
- Expanded activity in State fund for small and medium businesses.
- Expand geographic deployment of services provided to segment clients.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including GDP growth and impact of macroeconomic and geopolitical conditions, borrowers' financial robustness, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, technological developments and issues of human resources.

Results of the Small Business Segment

	For the year ended December 31, 2012				For the year ended December 31, 2011 [1]			
	Banking and finance	Credit cards	Capital market	Total	Banking and finance [2]	Credit cards	Capital market	Total
								NIS in millions
Interest revenues, net:								
From outside operating segments	309	7	-	316	407	6	-	413
Inter-segment	138	(5)	-	133	30	(4)	-	26
Total interest revenues, net	**447**	**2**	**-**	**449**	**437**	**2**	**-**	**439**
Non-interest financing revenues	1	-	-	1	-	-	3	3
Commissions and other revenues	206	14	18	238	199	14	23	236
Total revenues	**654**	**16**	**18**	**688**	**636**	**16**	**26**	**678**
Expenses with respect to credit loss	36	-	-	36	84	-	-	84
Operating and other expenses								
From outside operating segments	450	4	5	459	434	3	4	441
Inter-segment	(53)	-	-	(53)	(50)	-	-	(50)
Total operating and other expenses	**397**	**4**	**5**	**406**	**384**	**3**	**4**	**391**
Pre-tax profit	221	12	13	246	168	13	22	203
Provision for taxes on profit	77	4	5	86	55	4	7	66
Net profit attributable to equity holders of the banking corporation	**144**	**8**	**8**	**160**	**113**	**9**	**15**	**137**
Return on capital (net profit as % of average capital)				**38.8%**				**34.9%**
Average balance of assets	6,873	306	-	7,179	6,312	233	-	6,545
Average balance of liabilities	8,280	-	-	8,280	7,164	-	-	7,164
Average balance of risk assets	5,160	-	-	5,160	5,046	-	-	5,046
Average balance of securities	-	-	5,606	5,606	-	-	6,980	6,980
Loans to the public, net (end balance)	6,538	322	-	6,860	6,136	292	-	6,428
Deposits from the public (end balance)	8,159	-	-	8,159	7,773	-	-	7,773
Average balance of other assets managed	191	-	-	191	223	-	-	223
Profit from interest revenues before expenses with respect to credit loss:								
Margin from credit granting operations	344	-	-	344	323	-	-	323
Margin from receiving deposits	80	-	-	80	83	-	-	83
Other	23	2	-	25	31	2	-	33
Total interest revenues, net	**447**	**2**	**-**	**449**	**437**	**2**	**-**	**439**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new layout adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.
(2) Reclassified.

Contribution of the small business segment to Group profit in 2012 amounted to NIS 160 million, compared to NIS 137 million in the corresponding period last year - an increase of 16.8%.

Below are key factors affecting the change in segment contribution:

Net interest revenues before expenses with respect to credit loss increased by Nis 10 million. As result of an increase in the credit balances attributed to this segment. Expenses with respect to credit loss decreased by NIS 48 million. In the corresponding period, several significant provisions for individual clients were included. while operating expenses attributed to this segment increased by 3.8%.

Commercial Banking Segment

General information on the operating segment

The Commercial Banking segment primarily includes medium-sized private and public companies (Middle Market), having medium turnover, ranging from NIS 30 to 120 million, and total indebtedness ranging from NIS 6 to 25 million. This is highly diversified over different economic sectors. Segment clients are served under responsibility of the Bank's Business Division.
Clients in this segment use a range of banking services, associated with a relatively high ratio of collateral compared to Business Banking segment clients.

Products

Segment clients are primarily offered services in the banking and finance sector. Within this framework, the Bank issues different kinds of credit, including for working capital purposes: foreign trade services – importing, exporting, documentary credit; short and intermediate-term loans, bank guarantees, etc.; transactions in foreign currency, including trading in derivatives, factoring services and investment in deposits and in securities.

Legislation

A description of the normative framework applicable to the Bank, including to this segment, is provided below under the chapter Restrictions on and Regulation of Bank Group Operations.

Technological changes

For details of technology changes and projects undertaken by the Bank's IT department, see below under Information Systems and Computing.

Critical success factors

The critical success factors in the Commercial Banking Segment include development of marketing and business activity resting on understanding the needs of clients, and providing fast and effective professional services that offers a comprehensive solution adapted for all of the client's banking needs. This is done by offering diverse and innovative products while controlling the risk deriving from the segment's activities.

Clients

Segment clients are mainly medium-sized private and public companies (Middle Market) with medium turnover of NIS 30-120 million and total indebtedness from NIS 6-25 million. In this segment, there is no dependence on a major individual client.

Marketing and distribution

The segment primarily engages in marketing and distribution using seven business hubs for which the Business Division is responsible, including a business hub specialized in settlement, as well as business centers and Bank branches throughout Israel. There is no dependence on outside marketing channels.

Competition

The existing competition in this operating segment is mainly within the banking system. Activities of non-banking financing entities are small, and are mainly evident in factoring activities.

The Bank's main methods for dealing with the competition are to provide comprehensive professional solutions for the client's needs, to maintain personal ties with the client, and tailor a professional solution for the client's needs quickly and effectively.

Due to differences among banks in segment definitions, the Bank is unable to estimate its market share of this segment.

The major barriers facing a customer in moving to and from the Bank, derive mainly from the difficulty in transferring collateral from one bank to another; a factor that is significant in this sector, which is characterized by a relatively large volume of collateral. In order to increase the Bank's market share of this segment, despite the aforementioned challenges, the Bank primarily strives to improve service, professional attitude and responsiveness to client needs.

The main entry barriers in this segment are:

- Regulatory limitations on banking corporations – including per-borrower and per-group of borrower limitations, These limitations are primarily effective for smaller banks in Israel.
- Minimum capital requirements – requirements due to total segment volume of activity.
- Training and retaining professional manpower – the activity in the Commercial Banking segment requires professional knowledge, experience and familiarity with the different industry and with the typical clients and their needs. The service provider must provide high quality, rapid service, while providing optimal solutions.
- Construction and maintenance of physical infrastructures (such as branches) and technological infrastructures (IT systems).
- Client habits – based on maintaining current relationships and reputation of banking institutions

Business goals and strategy

The Bank's business strategy emphasizes the significant expansion of the client base and growth in the activities of the commercial banking segment.

The Bank intends to continue expanding operations in this segment, primarily by recruiting new clients and expanding banking services to current and secondary clients. This is based on the range of products offered to segment clients, as described above.

The Bank will continue to operate, under the Business Banking Division, dedicated departments for serving clients of the various segments, assisted by regional business hubs.

For details regarding risk management, see chapter on Risk Management.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including macroeconomic and geopolitical conditions impacting, inter alia, GDP growth, the currency market and capital market in Israel and world-wide, other factors that impact the exposure to financial risk, borrowers' financial robustness, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, including non-banking entities, aspects related to the Bank's image, technological developments and manpower matters.

Results of the Commercial Banking Segment

	For the year ended December 31, 2012				For the year ended December 31, 2011 [1]			
	Banking and finance	Credit cards	Capital market	Total	Banking and finance	Credit cards	Capital market	Total
								NIS in millions
Interest revenues, net:								
From outside operating segments	198	-	-	198	240	-	-	240
Inter-segment	(27)	-	-	(27)	(67)	-	-	(67)
Total interest revenues, net	**171**	**-**	**-**	**171**	**173**	**-**	**-**	**173**
Non-interest financing revenues	-	-	1	1	-	-	2	2
Commissions and other revenues	48	3	9	60	50	3	12	65
Total revenues	**219**	**3**	**10**	**232**	**223**	**3**	**14**	**240**
Expenses with respect to credit loss	8	-	-	8	6	-	-	6
Operating and other expenses								
From outside operating segments	65	-	1	66	65	-	-	65
Inter-segment	68	-	-	68	66	-	-	66
Total operating and other expenses	**133**	**-**	**1**	**134**	**131**	**-**	**-**	**131**
Pre-tax profit	78	3	9	90	86	3	14	103
Provision for taxes on profit	27	1	3	31	28	1	5	34
Net profit attributable to equity holders of the banking corporation	**51**	**2**	**6**	**59**	**58**	**2**	**9**	**69**
Return on capital (net profit as % of average capital)				**14.3%**				**17.2%**
Average balance of assets	4,655	49	-	4,704	4,846	42	-	4,888
Average balance of liabilities	3,545	-	-	3,545	3,189	-	-	3,189
Average balance of risk assets	5,172	-	-	5,172	5,176	-	-	5,176
Average balance of securities	-	-	3,633	3,633	-	-	3,212	3,212
Loans to the public, net (end balance)	4,625	54	-	4,679	4,720	58	-	4,778
Deposits from the public (end balance)	3,358	-	-	3,358	3,471	-	-	3,471
Average balance of other assets managed	224	-	-	224	154	-	-	154
Profit from interest revenues before expenses with respect to credit loss:								
Margin from credit granting operations	144	-	-	144	144	-	-	144
Margin from receiving deposits	24	-	-	24	22	-	-	22
Other	3	-	-	3	7	-	-	7
Total interest revenues, net	**171**	**-**	**-**	**171**	**173**	**-**	**-**	**173**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.

Contribution of the commercial banking segment to Group profit in 2012 amounted to NIS 59 million, compared to NIS 69 million in the corresponding period last year - a decrease of 14.5%. Below are key factors affecting the change in segment contribution:

Interest revenues, net of expenses with respect to credit loss decreased by NIS 2 million; in addition, commissions and other revenues decreased by NIS 5 million due to lower commission revenues on securities. Expenses with respect to credit loss increased by NIS 2 million, while operating and other expenses decreased by NIS 3 million year over year.

Business Banking Segment

General information on the operating segment

The segment specializes in providing complete banking and financing services to the largest companies, in a range of sectors, with total indebtedness exceeding NIS 25 million per client and turnover in excess of NIS 120 million. This segment also includes the banking service group for companies in the construction and real estate sector. This is in accordance with the approach of the Bank's Executive Management regarding the segment allocation of the real estate activities and corresponds with the manner in which these customers are serviced and the organizational structure of the Bank. The Bank’s business division is in charge of serving clients of this segment.
In its activities in this segment, the Bank emphasizes improved profitability through expansion of activity in innovative financing areas with very high profitability relative to capital, mainly trading in derivative instruments.

Products

Segment clients are offered a range of banking and finance products, including: Different types of credit – on call, short-term, intermediate-term and long-term loans, different types of guarantees; foreign trade activity – importing, exporting, documentary credit; financing of infrastructure products, mergers and acquisitions; and trading in derivatives.

Real estate

In this sector, the Bank offers credit to finance the purchase and construction of real estate, mainly residential construction products in areas of high demand, while insisting on the applications of tests prescribed in order to maintain the quality of the loan portfolio, and these include ties with customers having financial strength and stability, transactions characterized by favorable safety cushions for the Bank, and management using methods that reduce the risk.
The main services provided to clients of the real estate sector are:
Credit for construction - in this sector, the Bank provides credit, in particular short- and medium-term loans, used to finance land acquisition and investment in construction, as well as various types of bank guarantees.

Financing for construction projects - construction project financing is a unique service, provided by the Bank exclusively to clients in this sector. Within this framework, the client is allocated a package of financial and banking services, suited to the specific needs of each project and based on its characteristics. This includes allotment of credit facilities for land acquisition, construction loans, financial guarantees, performance guarantees and guarantees to home buyers in projects. The Bank issues construction financing mainly by the financial support method, in which the Bank channels the financing sources, including the buyers’ monies deposited with it, in a manner that advances completion of the project.

Purchase groups - a purchase group is a collection of individuals, gathered for the purpose of jointly acquiring land and buying construction services on said land. Alternatively, existing land owners join forces to jointly construct, by ordering construction services.
The Bank provides dedicated financing for projects of this type, and assists them from preliminary stages of forming the group, through completion of construction.

Legislation

A description of the normative framework applicable to the Bank is provided below under the chapter Restrictions on and Regulation of Bank Group Operations. Below we describe some of this legislation and other arrangements, which impact operations of the Business Banking segment.

Transactions with related parties - pursuant to Proper Conduct of Banking Business Regulation No. 312 ("Banking Corporation's Business with Related Parties"), the Bank is subject to a restriction, whereby the indebtedness of any Group component may not exceed the product of its share of the controlling block and 10% of the banking corporation's capital, i.e. 5% for each of the controlling shareholders' borrower groups.
For details of criteria for transactions with controlling shareholders, stipulated by the Audit Committee and its reconfirmationi, see below under Transactions with Controlling Shareholders.

Financing acquisition of means of control – The provisions of Proper Banking Conduct Regulation No. 323 ("Financing an Acquisition of Means of Control in Corporations") limit the balance of loans given to acquire the means of control in corporations, where the percentage of the financing for this acquisition exceeds 50% of the acquisition cost, at a percentage not to exceed 70% of the Bank's capital. Additionally, the regulation limits the balance of credit given by a banking corporation for an acquisition of the means of control of another banking corporation or a banking holding company, when the percentage of the financing of such an acquisition exceeds 30% of their acquisition cost, to the lower of 5% of the lending bank's capital or 5% of the capital of the acquired bank, or another rate that the Supervisor prescribes for a bank corporation with capital below NIS 500 million. This limitation is not effective with respect to the Bank's activity as of the date of the financial statements.

Industry limit – The provisions of Proper Banking Conduct Regulation No. 315 ("Supplementary Provision for Doubtful Debts") stipulate that when all the debts ("debt" –as defined in the regulation, after all the deductions permitted by the regulation are deducted from it) of a certain industry to the bank corporation (on an unconsolidated basis) exceeds 20% of the total debts of the public to the bank corporation, this excess will be considered as debt in deviation, for which the bank must make a supplementary provision for doubtful debts. This limit is evaluated on unconsolidated basis. The amendment to a directive issued by the Supervisor of Banks in September 2009 stipulated that, with regard to the real estate sector, the Bank may choose to reach exposure of up to 22%, provided that exposure to infrastructure projects in the real estate sector shall not exceed 18%. This limitation is not effective with respect to the Bank's activity as of the date of the financial statements.

Limits on indebtedness of a borrower and a group of borrowers – In accordance with Proper Banking Conduct Regulation No. 313 ("Limitations on Debts of a Borrower and a Group of Borrowers"), a limitation has been imposed on the Bank, whereby the Bank is permitted to grant credit to a "borrower" or a "group of borrowers", as defined in the regulation, after certain amounts provided in the regulation were deducted from the debts, not to exceed 15% or 25% of the Bank's capital, respectively. The Regulation further stipulates that total indebtedness of borrowers and groups of borrowers at the Bank, whose net indebtedness to the Bank exceeds 10% of the Bank's equity, may not exceed 120% of said equity.

Securing home buyers – the Sale Law (Apartments) (Securing Investments of Home Buyers), 1974 ("the Sale Act" or "the Act") prohibits the apartment seller ("seller" and "apartment" as defined in the Act) to receive proceeds exceeding 7% of the price, unless the buyer is secured through one of the alternatives provided in the Act. One of the alternatives provided in the Act to secure apartment buyers is the furnishing of a bank guarantee under the Sale Act.

The use of this alternative is very prevalent and accepted by companies engaged in the construction industry and contributes to the growth in the Bank's off-balance sheet credit risk.

Financial assistance - Proper Banking Conduct Directive no. 326 on Financial Assistance stipulates that a banking corporation shall not finance a construction project using the financial assistance method, unless a book of payment vouchers is produced and provided to the construction contractor for each apartment to be sold in the project. This is designed to secure funds of apartment buyers in project financed using the financial assistance method, and to ensure concentration of resources designated for project construction, and in particular proceeds from sale of apartments, in the project account designated for this purpose. These payment vouchers will be used for all payments to be made by the apartment buyer to the developer for the cost of the apartment. The regulation specifies the details to be included on each payment voucher. The regulation required the banking corporation to issue a guarantee to the apartment buyer for any amount paid by a payment voucher, or to ensure provision of other collateral pursuant to the Apartment Sale Act within 14 days from the payment date. Furthermore, the regulation specifies arrangements for providing information to buyers with regard to matching of the project account to a specific project, and determines the details to be included in the assistance agreement with the developer in order to allow for implementation of the voucher system.
This regulation applies to financial assistance agreements signed on June 1, 2008 or later.

Credit risk management – in December 2012, the Bank of Israel issued Proper Conduct of Banking Regulation 301 concerning credit risk management, which includes, inter alia, a definition of the credit risk management structure required of banking corporations and the allocation of authority at the bank with regard to credit risk management. The effective start date of this regulation is January 1, 2014. The Bank is preparing to implement this regulation.

Proper Conduct of Banking Business Regulation re: capital adequacy (Basel II) - the Business Division, which is in charge of the Business Banking segment, implements the implications of provisions of Basel II, in conjunction with the Bank's overall activity concerning this issue. The Business Division deals mainly with the credit aspects deriving from the provisions of Basel II and the related provisions. For details of the Basel II guidelines and its implementation preparation, see below the chapter on Legislation and Supervision of Bank Group Operations.

Technological changes

See the Chapter on IT systems and computerization for information on technological changes and the computerization projects being carried out in the Bank.

Critical success factors

Critical factors for success in the Business Banking segment include a strong ability to analyze the client's needs and their financial condition. Identification of risk arising from activity vis-à-vis clients, including as a result of expected changes in the economy and the industry in which it is engaged, and provision of professional, fast and effective service that offers a comprehensive and appropriate solution to the client's needs in all banking areas. This is done while by a variety of innovative products. The Bank also sees the continuous, high-quality monitoring of risk and handling of troubled debt as a key tool for managing the credit portfolio in this sector, allowing the Bank to minimize exposure to credit loss.

Clients

Segment clients include large business clients with sales in excess of NIS 120 million or total indebtedness in excess of NIS 25 million. Furthermore, according to Bank management approach with regard to segment assignment of real estate operations, and in line with serving of these clients and with the Bank's organizational structure, the Business Banking segment includes all clients who receive banking services in the construction and real estate sector, even though they may have medium indebtedness levels. In this segment, there is no dependence on a major individual client.

Marketing and distribution

The main marketing and distribution parties in this segment are the managers and liaisons in the Business Banking Division, concurrent with the Bank's branches and business centers. The Bank has no dependence on outside marketing channels.

In order to provide an optimal response to segment client needs, the servicing of the business banking clients in this segment was placed under the Major Corporation Sector of the Bank's Business Division, divided into departments and teams having specific industry specialization. The teams are assisted, as needed, by consulting provided by professional Bank departments involved in factoring, foreign trade, capital market, derivatives operations etc. - in order to provide a comprehensive solution for client needs. Real estate clients are served by the construction and real estate segment, which is also part of the Business Division, and which operates, inter alia, via three regional business departments located at major activity hubs, the Purchase Group Department and 12 branches specialized in providing financial assistance.

Competition

Most of the competition in the Business Banking Segment is with large and mid-sized banks in Israel, and for some services – the entire capital market. Entry by foreign banks and non-banking entities, mostly insurance companies, is focused on long-term credit. Note that in the years prior to the financial crisis, the share of banks out of financing for Israel's business sector decreased, and the share of other competitors in this sector increased. As a result of the financial crisis in Israel and overseas, this trend has been reversed - and the share of the banking system out of total balances has grown, based on data published by the Bank of Israel.

Alternatives for the products and services offered by the Bank to clients of the Business Banking segment include raising capital and debt through public and private offerings, and through the services provided by insurance companies. The Bank's key asset for dealing with the competition is the existing human infrastructure and the experience gained in providing professional service and adapting banking solutions to the client's needs.

The Bank's main methods for dealing with the competition are to provide professional service that is fast and effective, while offering optimal solutions for the customer's needs in a diverse array of its financial activities. As part of its operations in this segment, the Bank places emphasis on the best possible personal service to the business client and adapting it to the client's needs according to his unique characteristics, while focusing on industry expertise and providing specific professional advice in specialty areas.

Similar to the competition within the banking and financial products, most of the competition in providing unique services to real estate and construction comes from the banking system. In recent years, non-banking entities have launched operations for financing projects in this sector. However, these entities are limited by the scope of activity and the services they are capable and permitted to provide. Thus for example, insurance companies often participate in project financing by issuing insurance policies to buyers in lieu of guarantees under the Sale Law, but they do so in cooperation with the banking system.

The Bank's primary methods for dealing with the competition in the area of construction and real estate services are based on providing comprehensive professional solutions for the clients' needs, readily available and fast service, and maintaining close and personal ties with clients. This is achieved mainly via dedicated business departments specializing in the construction and real estate sector.

Due to differences among banks in segment definitions, the Bank is unable to estimate its market share of this segment.

The main entry barriers in this segment are:

- Regulatory limitations on banking corporations – including per-borrower and per-group of borrower limitations, This is due to large credit volume required for operations in this segment.
- Other regulatory limitations – These limitations are related, inter alia, to certain activities. For example: non-banking entities are limited in their entry to independent activity in the real estate industry, as a result of the Sale Law, which requires, under certain conditions, the issuance of bank guarantees to the buyers of units in construction projects. Insurance companies are permitted to issue insurance policies to buyers, but they are not permitted to provide other services required for clients in this industry.
- Minimum capital requirements – requirements due to business activity volume.
- Training and retaining professional manpower – the activity in the Commercial Banking segment requires professional knowledge, experience and familiarity with the different industry and with the typical customers and their needs. The service provider must provide high quality, rapid service, while providing optimal solutions. These factors form a significant barrier to entry for financing providers wishing to launch operations in this segment.
- Construction and maintenance of physical infrastructures (such as branches) and technological infrastructures (IT systems).

Business goals and strategy

The Bank's business strategy in the Business Banking segment is directed toward maximizing the economic potential of the capital, based on the existing customers, by focusing on activities having high profitability relative to the capital needed for them, through, inter alia, the following activities:

- Implement an approach based on total outlook on the business client, leveraging credit products and offering other products to establish a comprehensive client relationship.
- Segment business clients by size, sector of operation and other attributes in order to optimally specify their business needs and to provide an appropriate, professional solution.
- Emphasis on profitability and return on uses, and transition to measuring return and risk pursuant to rules specified in Basel II recommendations on management of credit risk and operating risk.

The risk in realizing the strategy described above is mainly a reduction in the volume of activity with certain clients, from which the Bank's profit is relatively low, or a relatively high risk associated with doing business with these clients.. In contrast, the overall profitability of the Bank could rise, as it focuses on profitable clients and expansion of activity with them, while utilizing the Bank's capital resources.

Note that macro-economic change poses significant challenges to credit management, at the Bank in general and in the Business Banking segment in particular, with some segment clients exposed, directly or indirectly, to extensive financial and economic operations in Israel and overseas, as well as to capital raising capacity on financial markets. Therefore, the Bank allocates significant resources to enhancing means for testing and control of exposure, aimed at tightening supervision of the credit portfolio. Credit applications are reviewed most diligently, including analysis of exposure under different scenarios.

For details regarding risk management, see chapter on Risk Management.
This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including macroeconomic and geopolitical conditions impacting, inter alia, GDP growth, the capacity to raise funds in the capital market and demand for real estate, economic policy, the currency market and capital market in Israel and world-wide, other factors that impact the exposure to financial risk, clients' financial robustness, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, including non-banking entities, aspects related to the Bank's image, technological developments and manpower matters.

Results of the Business Banking Segment

	For the year ended December 31, 2012				For the year ended December 31, 2011 [3]			
	Banking and finance[1]	Capital market	Construction and real estate	Total	Banking and finance[1][2]	Capital market	Construction and real estate	Total
								NIS in millions
Interest revenues, net:								
From outside operating segments	(2)	-	333	331	(78)	-	294	216
Inter-segment	439	-	(115)	324	430	-	(126)	304
Total interest revenues, net	**437**	**-**	**218**	**655**	**352**	**-**	**168**	**520**
Non-interest financing revenues	68	8	-	76	33	11		44
Commissions and other revenues	81	26	109	216	86	23	87	196
Total revenues	**586**	**34**	**327**	**947**	**471**	**34**	**255**	**760**
Expenses with respect to credit loss	169	-	9	178	140	-	24	164
Operating and other expenses								
From outside operating segments	176	7	34	217	184	2	37	223
Inter-segment	71	-	15	86	71	-	13	84
Total operating and other expenses	**247**	**7**	**49**	**303**	**255**	**2**	**50**	**307**
Pre-tax profit	170	27	269	466	76	32	181	289
Provision for taxes on profit	59	9	93	161	22	10	59	91
Net profit (loss) attributable to equity holders of the banking corporation	**111**	**18**	**176**	**305**	**54**	**22**	**122**	**198**
Return on capital (net profit as % of average capital)				**10.5%**				**7.7%**
Average balance of assets	19,707	-	7,212	26,919	19,220	-	6,002	25,222
Average balance of liabilities	29,370	-	2,332	31,702	27,958	-	2,255	30,213
Average balance of risk assets	20,490	-	15,833	36,323	19,387	-	13,975	33,362
Average balance of securities	-	59,957	-	59,957	-	60,730	-	60,730
Loans to the public, net (end balance)	15,788	-	7,133	22,921	16,940	-	6,188	23,128
Deposits from the public (end balance)	31,285	-	2,649	33,934	30,521	-	2,003	32,524
Average balance of other assets managed	171	-	90	261	15	-	71	86
Profit from interest revenues before expenses with respect to credit loss:								
Margin from credit granting operations	370	-	182	552	278	-	124	402
Margin from receiving deposits	53	-	17	70	54	-	17	71
Other	14	-	19	33	20	-	27	47
Total interest revenues, net	**437**	**-**	**218**	**655**	**352**	**-**	**168**	**520**

(1) Includes operating results with respect to credit cards, whose amount is not material.

(2) Reclassified.

(3) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new formatt adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.

Contribution of the business banking segment to Group profit in 2012 amounted to NIS 305 million, compared to NIS 198 million in the corresponding period last year. An increase of 54.0% Below are key factors affecting the change in segment contribution: Contribution of the construction and real estate sector increased by NIS 54 million, 44.3%, compared to the corresponding period last year - primarily due to an increase of 28.2% in total revenues along with unchanged expenses. Moreover, in 2012 expenses with respect to credit loss attributed to the sub-segment amounted to NIS 9 million, compared to expenses of NIS 24 million in the corresponding period last year.

Contribution of business banking excluding construction and real estate increased by NIS 53 million, primarily due to a NIS 117 million increase in financing revenues (interest revenues, net and non-interest financing revenues), due to higher credit spreads. Expenses with respect to credit loss increased by NIS 29 million. Commissions and other revenues as well as operating expenses were essentially unchanged.

Financial Management Segment

Operations in the Financial Management segment cover several key areas: Management of Bank assets and liabilities, management of the debenture portfolio, management of exposure to market risk and liquidity management as well as trading room operations in the financial and capital markets. Additionally, the segment includes investment in shares in non-banking corporations. This is in line with management view of how these operations should be managed.

Operations of this segment are managed by the Financial Division, except for investments in non-banking corporations which is managed by the Business Banking Division.

The sources of the activity in the debenture portfolio are the surplus Israeli currency and foreign currency liquidity. The surplus liquidity is surplus of the sources beyond the holding of liquid means against financing needs, as required in the liquidity model prescribed Proper Banking Conduct Regulation No. 342, the management of liquidity risks (see the chapter on Risk Management for details on the liquidity model and limitations of management and the Board of Directors). Segment operations are intended to maximize returns on investment of said surplus, through highly-liquid assets with low credit risk, subject to the market risk management policy, and within limitations imposed by the Board of Directors and by management with regard to exposure to market risk. Threshold criteria were also prescribed for nostro debenture activity, based on the credit risk inherent in the portfolio's activity, to diversify investments and to increase the liquidity. The nostro debenture activity is subject to compliance with credit limits specified by its Bank for countries, banks and companies - with the bulk of activity involving risk is with the State of Israel. The Financial Management segment operates in Israel and overseas.

As for management of market risk exposure, the Bank actively manages the negotiable portfolio in order to generate gain at the specified risk level. The bank portfolio is regularly managed and monitored in order to improve interest revenues, subject to the risk appetite. The volume of activity and risk must meet the market risk exposure limits prescribed by the Board of Directors and management. See the chapter on risk management for details on the risk limitations and the manner in which the exposure to market risks are managed.

The Bank's activities in the financial management segment require that the Bank allot capital. Capital requirements with regard to market risk, is in accordance with Proper Conduct of Banking Business Regulation no. 208 (Basel II, Pillar 1), which refers, inter alia, to interest risk in the negotiable portfolio, which is monitored using the standard model. Capital allocation with regard to interest risk in the Bank portfolio is required in conjunction with Basel II, Pillar 2. The Bank manages this risk in terms of erosion of economic capital, under different scenarios of changes to interest rates.

The financial management segment functions as an activity that "clears" all of the Bank's trading activity, and leaves for those executing transactions a fixed margin, known in advance, that is calculated assuming full coverage of the transaction. The exposure to market risk remains in financial management. The prices at which the segment "buys" and "sells" sources and uses vis-à-vis the Bank's other units, for the purpose of their carrying out regular business activities, are the transfer prices (“shadow prices”) of the Bank that are determined regularly by the financial management segment.

One of the tools used by the segment in managing liquidity and exposure to market risk is the issuance of subordinated notes, inter alia, through the subsidiary, Mizrahi-Tefahot Issuance Company Ltd., as provided below in the chapter on Sources and Financing.

The segment includes the Bank's trading room operations in financial and capital markets. These operations include market making in all standard derivative instruments trading over-the-counter in Israel and back-to-back trading in complex derivative instruments. The trading room also serves major clients trading in securities in Israel and overseas.

Business goals and strategy

The segment includes management of the debenture portfolio, management of exposure to market risk and liquidity management. Segment objectives in these areas are: active management of exposure and of the debenture portfolio, aimed at maximizing gain, while maintaining appropriate, controlled exposure to market- and liquidity risk, which reflects the Bank's risk appetite, subject to limits specified by decisions of the Board of Directors and management.

The segment also acts to raise financial sources as needed for Bank operations, while complying with liquidity limitations and minimum capital ratio objectives, as per decision of the Board of Directors. This would be achieved by raising deposits in different linkage segments and for different terms, and by issuing various obligatory notes.

This segment also includes Bank operations in the trading room on financial and capital markets. The Bank constantly strives to expand its operations in this area by expanding the client base and intensifying business activity and client relationships, inter alia, by improving cooperation between Bank departments operating within the trading room, development of new transaction types and investing in acquiring professional knowledge.

A critical success factor in this operating segment is the Bank's ability to understand the macro and micro factors affecting the market trends and conditions, for correctly identifying the market conditions and the ability to act quickly in opening and closing positions. In addition, professionalism of staff in this area and technology systems in support of the various activities identityingother units needs, as well as co-operation on needs identification between different Bank units.

Management of the financial segment and its various components requires highly professional skills, supported by appropriate IT systems and by advanced models for management of transactions and risk. These are all guided by the policy which includes clear restrictions and rules, and are controlled using advanced means of control. In particular, with regard to Bank exposure to other financial institutions in Israel and overseas, in exposure to different financial products and in exposure to clients whose financial robustness may be particularly sensitive. For details of Bank exposure to foreign financial institutions, see the chapter on Risk Management.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including macroeconomic and geopolitical conditions impacting, inter alia, GDP growth, the capacity to raise funds in the capital market, economic policy, the currency market and capital market in Israel and world-wide, other factors that impact the exposure to financial risk, clients' financial robustness, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, including non-banking entities, aspects related to the Bank's image, technological developments and manpower matters.

Financial Management Segment results

	For the year ended December 31, 2012			For the year ended December 31, 2011 [1]		
	Banking and finance	Capital market	Total	Banking and finance[2]	Capital market	Total
						NIS in millions
Interest revenues, net:						
From outside operating segments	(884)	-	(884)	(1,380)	-	(1,380)
Inter-segment	1,028	-	1,028	1,658	-	1,658
Total interest revenues, net	**144**	**-**	**144**	**278**	**-**	**278**
Non-interest financing revenues	(5)	14	9	(53)	10	(43)
Commissions and other revenues	82	49	131	70	60	130
Total revenues	**221**	**63**	**284**	**295**	**70**	**365**
Expenses with respect to credit loss	1	-	1	21	-	21
Operating and other expenses						
From outside operating segments	244	5	249	218	11	229
Inter-segment	13	-	13	11	-	11
Total operating and other expenses	**257**	**5**	**262**	**229**	**11**	**240**
Pre-tax profit (loss)	(37)	58	21	45	59	104
Provision for taxes on profit (loss)	(13)	20	7	16	18	34
After-tax profit (loss)	**(24)**	**38**	**14**	**29**	**41**	**70**
Share in net profits of affiliates, after tax	-	-	-	1	-	1
Net profit (loss):						
Before attribution to non-controlling interest	(24)	38	14	30	41	71
Attributable to non-controlling interest	-	-	-	-	-	-
Attributable to equity holders of the banking corporation	**(24)**	**38**	**14**	**30**	**41**	**71**
Return on capital (net profit as % of average capital)			**3.0%**			**24.9%**
Average balance of assets	28,110	-	28,110	24,802	-	24,802
Includes: Investments in associates	60	-	60	52	-	52
Average balance of liabilities	35,811	-	35,811	35,562	-	35,562
Average balance of risk assets	5,476	-	5,476	4,960	-	4,960
Average balance of provident and mutual fund assets	73,821	-	73,821	77,626	-	77,626
Average balance of securities	-	42,271	42,271	-	32,886	32,886
Loans to the public, net (end balance)	-	-	-	-	-	-
Deposits from the public (end balance)	17,326	-	17,326	15,546	-	15,546
Profit from interest revenues before expenses with respect to credit loss:						
Margin from credit granting operations	-	-	-	-	-	-
Margin from receiving deposits	-	-	-	-	-	-
Other	144	-	144	278	-	278
Total interest revenues, net	**144**	**-**	**144**	**278**	**-**	**278**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. See Note 1.D.1 to the financial statements for further information.

(2) Reclassified.

Contribution of the financial management segment to Group profit in 2012 amounted to a profit of NIS 14 million, compared to a profit of NIS 71 million in the corresponding period last year. Below are key factors affecting the change in segment contribution:

Total financing revenues (net interest revenues and non-interest financing revenues) decreased by NIS 82 million, primarily due to fair value and other effects - an expense amounting to NIS 79 million, compared to revenues amounting to NIS 18 million in the corresponding period last year. Operating and other expenses increased by NIS 22 million, or 9.2%, while expenses with respect to credit loss, attributed to this segment, decreased by NIS 20 million.

Product operations

The following is composition of contribution of credit card operations by major operating segments in the Bank Group (NIS in millions):

	For the year ended December 31, 2012			
	Household	Small business	Commercial banking	Total consolidated
Interest revenues, net	8	2	-	10
Non-interest financing revenues	-	-	-	-
Commissions and other revenues	130	14	3	147
Total revenues	**138**	**16**	**3**	**157**
Operating and other expenses	25	4	-	29
Pre-tax profit	**113**	**12**	**3**	**128**
Provision for taxes on profit	40	4	1	45
Net profit	**73**	**8**	**2**	**83**

	For the year ended December 31, 2011 (1)			
	Household	Small business	Commercial banking	Total consolidated
Interest revenues, net	7	2	-	9
Non-interest financing revenues	-	-	-	-
Commissions and other revenues	124	14	3	141
Total revenues	**131**	**16**	**3**	**150**
Operating and other expenses	24	3	-	27
Pre-tax profit	**107**	**13**	**3**	**123**
Provision for taxes on profit	36	4	1	41
Net profit	**71**	**9**	**2**	**82**

(1) Reclassified.

The following is composition of contribution of capital market operations by major operating segments in the Bank Group (NIS in millions):

	For the year ended December 31, 2012						
	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net	-	-	-	-	-	-	-
Non-interest financing revenues	7	-	-	1	8	14	30
Commissions and other revenues	165	29	18	9	26	49	296
Total revenues	**172**	**29**	**18**	**10**	**34**	**63**	**326**
Operating and other expenses	**55**	**-**	**5**	**1**	**7**	**5**	**73**
Pre-tax profit	117	29	13	9	27	58	253
Provision for taxes on profit	**41**	**10**	**5**	**3**	**9**	**20**	**88**
Net profit	**76**	**19**	**8**	**6**	**18**	**38**	**165**

	For the year ended December 31, 2011 (1)						
	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net	-	-	-	-	-	-	-
Non-interest financing revenues	11	1	3	2	11	10	38
Commissions and other revenues	206	33	23	12	23	60	357
Total revenues	**217**	**34**	**26**	**14**	**34**	**70**	**395**
Operating and other expenses	60	-	4	-	2	11	77
Pre-tax profit	**157**	**34**	**22**	**14**	**32**	**59**	**318**
Provision for taxes on profit	**51**	**11**	**7**	**5**	**10**	**18**	**102**
Net profit	**106**	**23**	**15**	**9**	**22**	**41**	**216**

(1) Reclassified.

International operations

General information regarding international operations

The international operations segment of the Bank Group includes business operations and private banking services via subsidiaries and branches in Israel and overseas. Bank Group international operations are primarily focused on private banking, providing financial services to Israeli customers who have activities outside of Israel, foreign trade finance, local credit and participation in syndicated loans. The Bank has affiliates in several countries, as described below.

International operations, in Israel and overseas, report to the Private Banking and International Operations sector in the Bank's Financial Division. In addition, control of affiliate operations is conducted by the Risk Control Department in the Risk Control Division.

International presence – affiliates, products and clients

These are the different affiliates, with business and specific issues of legislation and regulation for each affiliate:

Swiss subsidiary - UMB (Switzerland) Ltd. – specializes in private banking services, has one branch, owned by a wholly-owned subsidiary of the Bank registered in Holland – UMOHC B.V. **("the holding company").** The Swiss subsidiary is subject to the regulatory laws in Switzerland.

Overseas branches offer their clients full banking services, in accordance with the local laws and regulations. The branches are subject to the local and Israeli regulation.

- **Los Angeles Branch:** The branch is primarily engaged in commercial banking, syndicated loans and receiving deposits. Deposits with this branch are insured by the Federal Deposit Insurance Corporation(FDIC). The branch's clients are local, Israeli and international clients.
- **London Branch:** The branch is engaged mainly in business banking, including participation in loan syndicates, foreign trade, credit, receiving deposits, foreign currency trade and providing private banking services. The branch's clients are local, Israeli and international clients.
- **Cayman Islands Branch:** The Cayman Islands branch provides private banking services and is operated through the representation of the Bank by the Butterfield Bank in the Cayman Islands, pursuant to the management agreement between it and the Bank.

I**nternational private banking branches in Israel:** The Bank operates four special branches, located in Jerusalem, Tel Aviv, Netanya and Ashdod, serving foreign resident clients. These branches provide full banking services to their clients, primarily private banking. The branches are under Israeli supervision and report to the Private Banking and International Operations sector.

Mortgage center for foreign residents -The Bank operates this center in Jerusalem, specializing in marketing, approval and operation of foreign-currency denominated mortgages for foreign residents.

Representative offices: The major activities of representative offices are marketing of Bank services and its representation overseas. The Bank operates representative offices in Mexico, Uruguay, Panama and Germany.

Legislation and regulation

The overseas affiliates are subject, inter alia, to the laws of the country in which they operate, and to the regulation of the relevant authorities in that country, as set forth below:

Subsidiary in Switzerland - Federal Supervisory Authority of Switzerland FINMA.

Los Angeles branch - The State of California Financial Institution Department, the Federal Deposit Insurance Corporation (FDICFDIC) and the Federal Reserve Bank. In accordance with regulations of the Federal Deposit Insurance Corporation (FDIC), the Los Angeles Branch must hold "eligible assets", as defined in the regulations, at a ratio of 106% to its total liabilities. According to these regulations, a deposit in a bank that did not waive the set off agreement vis-à-vis the depositor does not meet the definition of "eligible assets". Therefore, the Los Angeles Branch has limited possibilities for depositing in the Bank in Israel. Furthermore, branch operations are subject to limitations of the US Bank Holding Company Act of 1956.

As for arrest and plea bargain of bank employee in the USA, see section "Legal proceedings".

London branch - the Financial Services Authority (FSA).
Cayman Islands branch - the Cayman Islands Monetary Authority (CIMA).
Mexico affiliate - Comision Nacional Bancaria y de Valores (banking regulators).
Uruguay affiliate - Banking regulation - Banco Central Del Uruguay.
Panama affiliate – banking supervision - Superintendencia de Bancos.
Germany affiliate - Financial Supervisory Authority - Financial Supervisory Authority (BaFin)

Bank Group international operations are primarily focused on private banking, foreign trade financing and credit. Following the crisis in global financial markets in recent years, the Bank's overseas affiliates have tightened the means of control and reporting of exposures to the head office, including a comprehensive sweep of all accounts and clients, in order to better supervise and control the credit portfolio. Specifically, Bank exposure to entities directly and indirectly exposed to the global financial crisis have been mapped and evaluated. Furthermore, the Bank regularly monitors its exposure to foreign financial institutions, in accordance with directives of the Supervisor of Banks.

International operations involve several unique risk factors:

- Operation under specific statutory and regulatory regimes of each country.
- Risk associated with challenges to controlling remote affiliates from the head office.
- Business risk (credit and market risk) are impacted by local factors, which may differ from the environment and factors in Israel.

Each overseas affiliate operates subject to local laws and regulations, and is regularly assisted by local legal counsel who specialize in banking operations applicable for each affiliate.
In order to handle geographic distance, which increases control risk, professional representatives of the Bank and management conduct regular visits to these affiliates.. The Internal Audit Division conducts regular audits at Bank affiliates, conducted by Division staff and by external professional entities. Risk management and internal control at affiliates are conducted jointly by the International Operations sector, the Legal Division, the Risk Control Division and the Audit Division. Credit risk is managed by specific limits set for the affiliates. Credit applications are discussed by the relevant

credit committees of Bank management. The Bank's Risk Control Division monitors and controls credit at affiliates, based on the annual work plan approved by the Bank and using local controllers who report directly to the Division. Market risk at affiliates is regularly managed by the affiliates and by the Financial Management Sector, by imposing PV and VAR limits on each affiliate and by monitoring these limits by the Risk Control Division. Operating risk at affiliates is monitored by the Compliance and Business Risk Control Division, and all affiliates report using a uniform format of any materialized operating event. The Compliance and Business Risk Control Division conducts external surveys, including operating risk and SOX surveys at affiliates, and monitors the resolution of any control gaps identified. In order to handle money laundering and terror financing issues, operating procedures for this matter have been determined by affiliates, workshops have been delivered to relevant affiliate staff, a person responsible for such issues has been appointed under International Operations, a forum has been established for prevention of money laundering and global terror financing, and technology systems for monitoring money laundering risk have been acquired.

For details regarding risk management at the Bank, arising from international operations as well, see chapter on Risk Management.

Affiliate operations in a competitive market

Bank affiliates overseas compete with local banks in their countries, with international banks and with affiliates of Israeli banks overseas. Competition is focused on the level of service and range of services provided to clients. Each international operations affiliate has a unique target audience. Critical success factors are based on providing global service at an international level. Service provided to clients is based on understanding their personal needs and providing individual solutions based on intensive knowledge of local markets in order to find the appropriate range of products.

In order to compete with current competition in this segment, extensive resources are dedicated to recruiting high-quality staff with extensive global market experience, in professional training of staff, and in offering a high-quality range of products compared to global competition. The Bank is also focused on providing high-quality service and maintaining strong client relationships, organizing professional events for select clients, launching of custom products for clients and efforts to locate and recruit new clients on a day-to-day basis.

Business goals and strategy

The Bank develops its business world-wide, including expanded operations in existing affiliates and review of acquisition of financial institutions in designated target countries.

The Bank strives to create strategic alliances with leading financial institutions in international banking and jointly work with them. The Bank also reviews options for launching unique products appropriate for each affiliate, which respond to varying needs in each market along with technology, business and regulatory changes.

This information constitutes forward-looking information, and is based on various assumptions and forecasts presented to Bank management, as described below. The information may not be realized, if Bank management finds that it is not expedient to carry out the plan, or due to changes that could occur in various influencing factors that are not under the sole control of the Bank. The influencing factors include future forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including macroeconomic and geopolitical conditions, and the currency market and capital market world-wide, other factors that impact the exposure to financial risk, clients' financial robustness, the public's preferences, legislation, directives of regulatory entities in Israel and overseas, the behavior of competitors, aspects related to the Bank's image, technological developments and manpower matters.

Results of international operations are divided among the different segments. Analysis of segment results below makes reference, inter alia, to the impact of assignment of international operations to the various segments, wherever such impact has been material.

Below are details of the impact of international operations on results of the different operating segments of the Bank Group (NIS in millions):

					All of 2012
	Household	Private banking	Business banking	Financial management	Total
					Reported amounts (NIS in millions)
Interest revenues, net	3	53	40	28	124
Non-interest financing revenues	-	1	14	3	18
Commissions and other revenues	-	40	4	2	46
Total revenues	**3**	**94**	**58**	**33**	**188**
Expenses with respect to credit loss	-	(13)	-	-	(13)
Operating and other expenses	3	64	46	7	120
Pre-tax profit	**-**	**43**	**12**	**26**	**81**
Provision for taxes on profit	-	15	4	9	28
Net profit	**-**	**28**	**8**	**17**	**53**

					2011 (1)
	Household	Private banking	Business banking	Financial management	Total
					Reported amounts (NIS in millions)
Interest revenues, net	3	66	30	19	118
Non-interest financing revenues	-	-	4	23	27
Commissions and other revenues	-	40	6	2	48
Total revenues	**3**	**106**	**40**	**44**	**193**
Expenses with respect to credit loss	-	(4)	5	-	1
Operating and other expenses	2	59	42	6	109
Pre-tax profit	**1**	**51**	**(7)**	**38**	**83**
Provision for taxes on profit	-	17	(3)	13	27
Net profit	**1**	**34**	**(4)**	**25**	**56**

(1) Reclassified.

Human Resources

Staff – general information

Provided below is information on the number of employees, in terms of full-time positions (including impact of overtime) in the Bank and in subsidiaries. The number of Bank employees provided below also includes employees who are not employed by the Bank but by companies associated with the Bank, including employees of Technology Division Ltd. and Mizrahi-Tefahot Security Services Ltd. – service companies that provide computerization, security and protection services to the Bank:

						2012
	At the Bank	Overseas branches	Total for the Bank	Subsidiaries in Israel	Overseas subsidiaries	Group total
Number of full-time equivalent positions as of December 31, 2012	4,699	56	4,755	887	28	5,670
Number of full-time employees based on monthly average	4,648	57	4,705	881	27	5,613

						2011
	At the Bank	Overseas branches	Total for the Bank	Subsidiaries in Israel	Overseas subsidiaries	Group total
Number of full-time equivalent positions as of December 31, 2011	4,578	58	4,636	855	27	5,518
Number of full-time employees based on monthly average	4,472	57	4,529	850	26	5,405

Below is the distribution of number of positions in the Group by operating segment[(1)]:

		As of December 31,
Operating segment	2012	2011
Household	3,484	3,394
Private banking	152	147
Small business	902	859
Commercial banking	290	288
Business banking	525	526
Financial management	317	304
Total	**5,670**	**5,518**

(1) Including Head Office employees that are allocated pro-rata to the various segments.

Human resource management

Bank management regards all Bank employees and managers as a key component for achieving its business strategy and growth objectives for operations and profitability. Human resources at the Bank are managed on two levels: One is services to individual employees, from recruiting through ongoing services and up to retirement. The second level is in the organizational development and training department, in conjunction with development of the Bank's human resources in all aspects.

Organizational development and training - the Bank invests in development of its staff and constant improvement of the professional and personal skills of Bank employees and managers. This is achieved through training events throughout employee tenure at the organization, from mentoring and certification upon entering the employee position, through promotion and development tracks and a range of training programs for banking, personal and managerial skills.

The Organizational Development Department is in charge of the comprehensive process of employee evaluation and feedback at the Bank. All Bank employees and managers are evaluated based on their performance over the past year; the process is concluded by a feedback interview between the employee and their supervisor, at which they discuss issues to be improved and preserved, targets for the coming year and potential professional development for the employee.

The Department is also responsible for development of intra-organizational communication, by expanding and intensifying channels for relaying messages and exposing the Bank to employees, by presenting the detailed organizational chart on the Intranet (with detailed roles and responsibilities of the various Bank departments and their managers) and through "Among us Online", a monthly newsletter, launched in 2012, which highlights professional issues, Bank departments and employees through various articles.

The Bank Training Center is responsible for professional and managerial training of Bank employees, as well as for refresher courses - as required for each position. To this end, the Training Center creates a schedule of courses, seminars and workshops in response to knowledge gaps in the various banking disciplines, in management skills and in knowledge and learning of Bank systems.

As part of this mission, in 2012 the deployment of the Hybrid Banking concept among managers and employees continued, as did the implementation of the management development concept. The Training Center continued to implement the concept of Learning Organization / Bank, through which it provides learning kits to branches in the commercial and mortgage discliplines, and once a week sends out a knowledge nugget – titled "Did you know that?" – which serves to disseminate focused knowledge in various professional disciplines. In addition, the Bank encourages achievement and expansion of academic education of its employees, as well as broadening their horizons via external workshops.

In order to improve professional skills and to streamline learning processes, the Training Center regularly evaluates its effectiveness. In 2012, the Training Center developed 7 new courses and seminars, and improved 13 existing courses, using a mix of learning methods.

Training expenses in 2012 amounted to NIS 8 million compared to Nis 9 million in 2011. In 2012, 15,812 training days were delivered, attended by 3,241 Bank employees. Compared to 3,550 employs in 15,700 training days in 2011.

Collective labor relations

The labor relations in the Bank are collective (except for a limited group of senior employees, as described below), which are expressed in two employee organizations:

A. **The Association of Bank Mizrahi-Tefahot Employees Ltd.** is a long-standing organization, which has been authorized, by virtue of an inter-organization agreement signed by the Association and the HaPoel HaMizrahi Union, by the Union to act as the representative organization of Bank employees for the purpose of signing collective bargaining agreements and of representing Bank employees (hereinafter: ("Employees' Association").

B. **The Association of Managers and Authorized Signatories at Bank Mizrahi-**Tefahot Ltd. was founded by branch- and department managers in 2005 (hereinafter: ("Manager Council"). This organization has been recognized by the Bank and by the Employee's Association as a "bargaining unit" for negotiation and signing agreements.

C. **Technology Division Employee Committee –** the organization authorized to sign, together with the MAOF trade union, on behalf of Technology Division employees, any collective bargaining agreements applicable to company employees (except for Technology Division employees employed pursuant to individual employment contracts)

D. **Bank Yahav Employees Committee –** The representative organization authorized by Yahav employees to sign collective agreements applicable to Yahav employees.

Employment terms of employees represented by the Bank's Employee Association

General

The employment terms are anchored in a series of collective agreements, together called "labor constitution". The labor constitution presents the general framework of the undertaking between the employees and the Bank, and arranges the basic employment terms. In addition, wage agreements are signed from time to time, within the framework of the constitution.

Salary agreements

In December 2003, a salary agreement was signed for the period 2002-2004, which was effective through December 31, 2004. This agreement applies to all Bank employees, except for those employees who, on December 31, 2004, were employees of the former Bank Tefahot, which was merged with the Bank on January 1, 2005.

On January 18, 2006, a salary agreement was signed for the period April 1, 2004 through March 31, 2005, for those who on December 31, 2004 were employees of Bank Tefahot, and then became employees of the Bank.

On December 21, 2005 and on January 23, 2006, agreements were signed with regard to conversion of salaries of former managers and employees of Bank Tefahot, respectively, to the salary regime used at Bank Mizrahi, and the labor constitution was applied to these employees (hereinafter: ("salary conversion agreements").

No salary agreement has been signed yet for the period 2005-2012 (except with former Tefahot employees, for whom a salary agreement was signed for the period through March 31, 2005). The Bank records, as necessary, appropriate provisions for years for which no salary agreements have been signed.

Salary update method

Salaries of most Bank employees (except for a small number of employees employed under individual contracts signed by them and by the Bank - see below under Individual Employment Contracts) are updated, in addition to cost of living adjustments in Israel, based on three key components:

A. Components which are updated regularly at rates and in the manner prescribed from time to time, in negotiations of labor agreements The key component in this group is the base salary, and other components derived from the base salary, including the key Seniority Bonus - which is updated at the start of each year at a higher rate with increasing employee seniority, are also updated with these components and reach a 4% annual increment (to base salary) for Bank employees with over 26 years' seniority.
B. Components updated in accordance with changes in the Consumer Price Index.
C. Components linked to changes in external tariffs.

All of the above components apply uniformly to all the employees, the employment terms of whom are subject to the labor constitution and to the labor agreements signed between the Bank and the Employee Association. Updates to part of the salary based on criteria not linked to the CPI, as well as payment of automatic Seniority Bonus as stated above, result in a situation where the real rate of salary increase at the Bank is higher the lower the inflation rate. In a reality of low single-digit inflation, these factors lead to an increase in real salaries, despite the absence of an update to the wage agreement.

Special payments

In addition to the regular salary elements, the Bank pays to its employees, as stipulated in the labor constitution, a one-time grant upon reaching seniority of thirteen years and eighteen years. The Bank's financial statements include a provision for these obligations, according to an actuarial calculation that is based on past experience and the probability that on the date of record, the employee will still be employed by the Bank.
The Bank also provides individual compensation tools, through which the personal compensation of each and every employee is carried out. These compensation tools are selective and are based on specific assessments of the direct managers of the Bank's employees in the different segments regarding the performance of every employee. Personal promotion is achieved primarily via promotion in rank, about which Bank management decides each year, as well as via the bonus component. Decisions relating to the extent of personal promotion and bonus or grant are not derived from provisions of labor agreements, but are influenced by the individual assessment of the employee performance, the Bank's situation and profitability in the relevant period.

Pension and benefit arrangements

A. Bank liabilities for payment of pensions and severance pay to those employed by the Bank prior to the merger with Tefahot are covered by current contributions in the employees' names to pension, provident and severance pay funds. These contributions, as well as future amounts and a one-time amount deposited in the past, release the Bank from its statutory obligation to pay severance pay to those employees. See Note 16 to the financial statements for additional information.
B. Pursuant to the labor agreement signed between the Bank and its employees on December 30, 1993, the Bank

made available long-term loans to its employees, to finance the retroactive purchase of pension rights from certain pension funds with which the Bank had undertakings in this connection. See Note 19.D.16) to the financial statements for further information.

C. Those who were employees of Bank Tefahot on the eve of the merger are covered by the Bank's obligations to pay pension and severance pay by regular deposits in the employees' names to pension, benefit and severance pay funds as well as one-time deposits. These deposits release the Bank from the obligation make severance and pension payments for the period commencing February 1, 2006, for those employees who were included in the salary conversion agreement. With respect to its liability through February 1, 2006, the Bank paid all the amounts required to cover the liability, by a deposit in pension and provident funds See Note 16 to the financial statements for information on the special liability for retirement of employees in the Bank or the former Bank Tefahot.

Special collective bargaining agreement

On April 11, 2006, the Employee Association and the Bank signed an agreement to end the labor dispute, declared with regard to the merger with Bank Tefahot ("special collective bargaining agreement"). Provisions of the special collective bargaining agreement are effective through December 31, 2010 ("term of the special collective bargaining agreement"). It stipulates, inter alia, that during the term of the special collective bargaining agreement, all of the disputes will be resolved by the mechanisms prescribed, the objective of which is to prevent the striking of the Banks' activities and applying to the relevant bodies, in order to reduce the deviations prescribed in the agreement (such as in the event of a strike of the entire economy). Therefore, throughout the term of the special collective bargaining agreement, labor unrest will be avoided, whereby the Association has undertaken that it will not go on strike. Due to the signing of the agreement, the parties to the agreement withdrew the legal proceedings between them that were outstanding and pending.

The agreement stipulates that Bank employees may choose whether or not to be members of the Employee Association. Note that the collective bargaining agreements that the Bank signs with the Employee Association also apply to those employees who are not members of the organization. The collective agreement also increased the quota of employees that may be employed under personal agreements. Furthermore, under the terms of the special collective bargaining agreement, the parties agreed to establish a collective bargaining unit for managers, as defined therein, alongside the collective bargaining unit for all Bank employees (regarding the agreement between the Manager Council and the Bank, see below).

On September 16, 2009, a special collective bargaining agreement was signed with the employee union, whereby the special collective bargaining agreement signed in 2006 was extended by a further 5 years, from January 1, 2011 through December 31, 2015. This agreement was approved by the Bank Board of Directors on October 19, 2009.

Highlights of the agreement, as for the old agreement, are as follows:

- Extension of the "employment constitution" through December 31, 2015.
- Maintaining absolute calm labor relations during the agreement period. The obligation to maintain calm labor relations shall not apply in case of a labor dispute involving all bank sector employees in Israel.
- Specification of dispute resolution mechanisms: negotiation, facilitation, arbitration.

- The Bank committed not to terminate for economic reasons any permanent employees during the term of the agreement. This commitment does not apply to individual termination for cause, incompatibility or regulatory changes.
- Enactment of a voluntary retirement program by up to 200 employees during the term of the agreement, starting in 2011. Management has the right to veto any specific voluntary retirement application without being required to provide any justification.
- Management has the option of terminating up to 50 permanent employees during the term of the agreement period, for incompatibility reasons, starting in 2011.

  The financial statements include an actuarial provision in accordance with directives of the Supervisor of Banks, to cover the expected cost of early retirement of all Bank employees. See Note 16 to the financial statements for details.

Employment terms for employees represented by the Council of Managers and Authorized Signatories

Overview – Wage Agreements

A. On April 10, 2006, the Manager Council and the Bank signed a special collective bargaining agreement in which the Bank and the Manager Council ratified the pact (hereinafter, together with previous agreements between the parties: "manager constitution"), in which the Bank recognized the Manager Council as a collective bargaining unit, within the scope of which principles were prescribed according to which the Bank would act to promote Bank managers' ranks. The manager constitution prescribed, inter alia, mechanisms for resolving disputes through arbitration, limitations on the number of managers to be employed under individual contracts and financing of the Manager Council (the Bank has undertaken to transfer an annual sum of NIS 250 thousand or 30% of the amount to be paid to the Employee Association, whichever is higher). The Bank has undertaken that the salary agreements and employment terms of members of the Manager Council will be determined in negotiations with the organization (although the organization has the right reserved to it, as long as a salary is not signed between it and the Bank, to adopt a salary agreement entered into with the Employee Association, instead of negotiating with the Bank or continue it).

   The parties also stipulated that the manager constitution will be in effect until September 19, 2008. If the organization does not cancel it until one month of days previously, the effective period of the constitution will be extended until September 19, 2011, and thereafter, for a two-year period each time, unless one of the parties gives written notice of its cancellation, all in accordance with the mechanism prescribed in the manager constitution. For details of extension of validity of the manager constitution through December 31, 2015, see section D. below.

B. By virtue of the pact and the collective agreement to ratify the pact signed between the Bank and the Manager Council (see below), the collective agreements signed between the Bank and the Employee Council signed until September 19, 2005 apply to the managers, as well as all the agreements that were and will be signed between the Bank and the Manager Council from September 19, 2005 and thereafter.

C. On March 22, 2007, the Manager Council and the Bank signed a salary agreement for 2005-2007, wherein the parties agreed on the annual salary raise for managers, payment of seniority bonus, management fee and a non-recurring bonus granted to all managers. The agreement further stipulates that the Manager Constitution shall be effective through September 19, 2011, and while it is in effect, no permanent manager with the Bank shall be terminated for economic reasons (as defined in the Manager Constitution), except for individual termination (for cause and/or incompatibility) not to exceed 8 managers for incompatibility, or termination due to regulatory changes unknown to the parties as of the date of signing the agreement. Upon expiration of the labor constitution, the commitment for non-termination for economic reasons shall expire, as mentioned above.

Furthermore, the agreement stipulates that the Bank shall establish a voluntary retirement program for managers. In each year during the term of the agreement, management would declare a period in which voluntary retirement would be possible, based on the overall framework stipulated in the employee retirement program.

D. On August 19, 2008, a special collective bargaining agreement was signed with the Manager Council whereby managers may choose to receive a seniority bonus under the new format, which is updated based on success benchmarks and on the Bank's return on equity. Furthermore, this agreement contains an extension of validity of the Manager Employment Constitution through December 31, 2015, as well as a commitment by the Council not to engage in labor unrest through this date, except in case of Bank operations being merged with another bank during the term of this agreement.

E. On March 5, 2009, a wage agreement was concluded with the Manager Council for the period 2008-2010. This agreement primarily consists of gradual expansion through July 2014 of the base used for making deposits to study funds, as well as payment of certain annual amounts by monthly installments.

F. On February 29, 2012, a wage agreement was concluded with the Manager Council for the period 2011-2012.

Pension and benefit arrangements

A. Managers who were employees of Mizrahi Bank on the eve of the merger with Bank Tefahot are covered by the Bank's obligations for the payment of pension and severance pay, by current contributions in the employees' names to pension, provident and severance pay funds, and all the aforesaid in the previous paragraph regarding the Employee Council applies to them.

B. Managers who were employees of Bank Tefahot on the eve of the Tefahot merger are covered by the Bank's obligation for the payment of pension and severance pay, by regular deposits on behalf of employees to pension funds, provident funds and severance pay funds, and non-recurring deposits. These deposits release the Bank from its obligations for the payment of severance and pension for the period as from January 1, 2006, for whoever was a manager on that date. With respect to its liability through January 1, 2006, the Bank paid all the amounts required to cover the liability, by a deposit in pension and provident funds

Employment terms of employees of Mizrahi-Tefahot Technology Division Ltd.

Employment terms of employees of the Technology Division are arranged in the labor constitution that was signed in 1989 and in a series of agreements signed by the Technology Division Employee Council, the Labor Union and the Technology Division over the years, the key points of which are provided below:

A. Salary updates for Technology Division employees are determined according to a linkage model for salary increments and for changes in the provisions given to employees of the Bank (the parent company). If in a certain year, a salary agreement is not signed by the Bank by the end of March in the subsequent year, Technology Division employees would be entitled to an advance that will be calculated according to the agreed mechanism, which would be reviewed by independent experts. The balance of the salary increase would also be calculated by an agreed mechanism soon after signing the Bank's salary agreement. It was also stipulated that if the terms of the salary agreement include a new salary increment and/or salary element that was not included in the linkage model, negotiations will be conducted with representatives of the employees regarding the increments to be given to Technology Division employees.

B. The labor constitution prescribes the maximum quota for contracted employees, pursuant to the undertaking between the Technology Division and outside vendors, which make workers available to the Technology Division , and under the professional management of the Technology Division. In this context, it should be noted that disputes have arisen in the past between Technology Division management and the Employee Council regarding the quota of contracted employees and the outsourcing of projects. On December 29, 2003, a labor dispute was announced at the Technology Division. On March 31, 2004, the parties signed an agreement to end the labor dispute, in which certain conditions were stipulated with regard to the Technology Division's undertakings with outside vendors and in outsourcing contracts. However, the parties agreed that the said agreement does not exhaust the dispute regarding outsourcing and that each party reserves for itself all the rights and claims in this matter.

C. Similar to employees of the Bank, the obligations of the Technology Division to pay pension and severance payments to its employees, except for a limited group of employees for which a provision was made, are covered by regular deposits on behalf of the employees to pension funds, provident funds and severance pay funds, in accordance to the provisions of the collective agreement applicable to these employees.

D. On January 11, 2007, a collective agreement was signed between the management of the Technology Division and the Employee Council which contains a voluntary retirement program. The plan provides for retirement in an early retirement track, for employees, who on their retirement date will be at least 55 years old and are insured in managers' insurance or an aggregating pension fund, or an increased severance pay track for other employees. The final decision on acceptance or rejection of the request for early retirement rests with the General Manager of the Technology Division. This agreement was extended by a further 12 months on February 19, 2008.

E. On March 8, 2007, the Employee Association, Manager Council, Technology Division Employee Council and the Bank signed a special collective bargaining agreement which sets terms for integrating the computer employees of Tefahot (except for a small group of employees) into the Technology Division. The agreement prescribes the format in which the terms of the computer employees of the former Tefahot will be converted and adapted to the terms prevailing in the Technology Division. Pursuant to this agreement, the collective bargaining agreements applicable to Technology Division employees, including the Labor Constitution infrastructure at the Technology Division from 1989, as well as any new collective bargaining agreement to be signed, will apply to the Tefahot employees who have been integrated.

F. On October 21, 2010, a labor dispute was declared between the MAOF trade union and the Technology Division, the Bank's IT arm. The main causes of this dispute are the demand by employees to sign wage agreements for 2005-2009, their demand to update the wage linkage mechanism, as well as re-structuring by management which, the employees claim, infringes on their rights.

Based on guidance from the MAOF trade union, since no agreement has been signed by November 7, 2010, Technology Division employees may go on strike effective immediately.

G. On January 2, 2012, the Bank President announced that Technology Division employees would not be relocated to the Technology-Logistics Center in Lod, and that this facility would be rapidly set up as the Bank's primary computer site, featuring standards appropriate for emergencies. This notification was delivered to employee representatives and to the MAOF trade union.

As of the publication date of these financial statements, Technology Division management and staff representatives continue to negotiate, but the parties have yet to reach an agreement.

Individual employment contracts

The labor agreements signed in the Bank in the years 1995, 1998, 2003 and 2006, stipulated that the Bank will be permitted to enter into individual employment contracts with senior employees, as defined in the agreements, as well as several individual employment contracts with certain officers. Some of the senior employees employed under individual employment contracts are eligible, in the event of termination by the Bank, to severance bonuses based on their period of service with the Bank, in addition to other amounts and benefits accrued to their credit in various funds. The financial statements include a provision for the severance bonuses accrued through the balance sheet date. See Note 16 to the financial statements for additional information.

For further information about employment terms of the Bank President – see Note 16.D. to the financial statements.

Employees of Bank Yahav

Overview - Labor Agreements

The employment terms and conditions of Yahav employees are specified in collective bargaining agreements and in individual employment contracts. A special collective bargaining agreement was signed in March 2004.

In December 2007, Bank Yahav management and the employee union signed an agreement aimed at specifying the compensation system at the bank for the period 2008-2012. Pursuant to this agreement, the employees are eligible to receive an annual bonus and ranking at variable rates based on the ratio of net profit return on bank capital. This agreement places stronger emphasis on the variable component of compensation, depending on bank performance, which reflects the importance associated by bank management and employees with a stronger link between employee performance and compensation.

On July 14, 2008, an agreement was signed by Yahav management and employee union, concerning safeguarding of the bank's independence. This agreement is for a 5-year term, and it stipulates that the collective bargaining agreements currently in place at Yahav would also be extended by an additional 5 years.

The payroll agreement in effect at the Bank during the reported period expired on December 31, 2012. In February 2013, Bank management and employee representatives signed an MOU with regard to a collective bargaining agreement for 2013-2016. The parties agrees to negotiate, based on this MOU, the signing of such a collective bargaining agreement. The MOU would become effective after it is approved by both parties' organs, and the issues contained there in would become effective after signing the collective bargaining agreement.

Severance pay and pension

Yahav's obligation to pay severance or retirement pay is primarily covered by current deposits based on the salary for pension purposes to official provident funds in the name of the employees. The Bank customarily makes up the difference, for employees eligible to receive severance pay, between the employee's most recent salary multiplied by their number of years in service and the amount accrued in their name in the aforementioned provident funds.

With regard to fraction of its employees, Yahav committed to deliver, upon termination of their employment for any reason, the severance pay component of recognized provident funds (pursuant to Section 14 of the Severance Pay Act). The Bank is not required to make up the difference for these employees between the employee's most recent salary multiplied by their number of years in service and the amount accrued in their name in the aforementioned provident funds.

As for senior executives, the Bank has committed to release to them the severance pay component accrued in the pension fund, in addition to their final salary multiplied by their number of years in service. In addition, Yahav has committed to pay senior executives' salary during an adjustment period, should their employment be terminated by the Bank. An appropriate provision with respect to these obligations has been made on the financial statements.

Yahav committed to make monthly payments through the official retirement age to two senior executives who retired from Yahav, with this payment linked to changes in the CEO salary. The financial statements include an appropriate provision based on actuarial estimate.

Redemption of unutilized sick leave

Retiring employees are entitled, under the labor agreement, to partial cashing of unused sick days. Bank Yahav has included a proper provision in its accounts, based on an actuarial assessment.

Jubilee bonus

Yahav employees are eligible to receive a Jubilee bonus upon completion of 25 years of service, and bank retirees are eligible to receive holiday gifts. Bank Yahav has made a provision for the Jubilee bonus and for holiday gifts to retirees based on an actuarial assessment.

Stock Options

For details of the stock option plan for Bank President, for Bank officers and for other employees, see Note 16.A to the financial statements.

Bank remuneration policy

On April 5, 2009, a letter was received from the Supervisor of Banks, instructing banks to adopt an appropriate remuneration policy by December 31, 2009. In accordance with the letter, the Board of Directors is required to set remuneration policy, based on a set of principles determined by the Supervisor. After setting policy, the Bank is required to review existing agreements, and to act in as much as possible to align them with the policy which has been set. In accordance with the Supervisor's directive, the Board of Directors approved the Bank's remuneration policy in October 2009.

Remuneration at the Bank consists of current base remuneration (salary and benefits), short-term incentives (bonuses etc.) and long-term incentives based on achievement of long-term objectives (stock option plans).

The remuneration system is intended to reinforce behavior which the Bank seeks to encourage, Bank values and success in achieving objectives set by the Board of Directors. The remuneration policy reflects, in the Bank's opinion, a proper balance between increasing motivation and striving for achievement, on the one hand, and the enterprise-wide strategy and the risk management policy set by the Bank, on the other hand.

The remuneration policy differentiates between employees, thereby encouraging strong motivation and individual contribution by employees, while incorporating quantitative parameters (profitability) and qualitative ones (service level).

On November 25, 2012, the Board of Directors appointed Board members Gideon Sitterman (Chairman), Avi Ziegelman and Sabina Biran to the Remuneration Committee, pursuant to Section 118a of the Corporate Act, 1999.

The remuneration policy has yet to be approved pursuant to Amendment 20 of the Corporate Act, and the Bank is preparing to implement this amendment (see below in chapter "Legislation and Supervision of Bank Group Operations").

Bank organizational structure

The Bank organizational structure is intended to support achievement of Bank objectives and realization of its business plan. The organizational structure is based on divisions, sectors and other units that report to the President, as follows:

Retail Division – This division consolidates most of the banking activity of private customers and small business customers. Division operations include: The retail sector, primarily responsible for operations of the Household segment and of the Small Business segment; and the mortgage sector, responsible for mortgage operations. Bank branches and business centers operate under this division in six geographic regions and the LIVE sector, which is operates by personal bankers via a range of communication channels (internet, telephone, SMS, fax and video chat).

Business Banking Division – this division consolidates most of the banking activity of the large corporations and of business customers. This division includes the corporate sector, in charge of operations of the business banking segment, and the business sector, in charge of operations of the commercial banking segment, operating 6 geographically-distributed business centers, as well as a business center for customers in the rural sector. The division also includes other units providing specialized services for clients in specific sectors: the construction and real estate sector, the international finance and trade sector and the diamonds business center. The division also operates the special client sector, in charge of arrangement and collection of troubled debt in all divisions.

Finance Division – The division includes the financial management sector - which is responsible for management of the Bank's financial assets and liabilities - and the capital market trading sector, which operates an integrated trading room active in all financial markets, in trading currencies, interest rates and Israeli and overseas securities, and the Information & Client Service Sector which supports all financial market operations, providing back-room services. The division is also in charge of international operations of the Group and of its private banking operations. This is achieved via the private banking and international operations sector, which is responsible for these operations via the private banking units in Israel and via affiliates and subsidiaries overseas.

Client Assets and Consultancy Division - this division includes the departments which provide pension consulting and financial consulting services offered to clients. The division is also responsible for the subsidiaries operating in the capital market: Etgar Investment Portfolio Management Company of the Mizrahi Tefahot Group Ltd., Mizrahi-Tefahot Trust Company Ltd. and the provident fund sector.

Information Technology Division - in charge of information technology, including pursuant to requirements of Proper Banking Conduct Regulation 357, through the Mizrahi-Tefahot Technology Division Ltd., a wholly-owned subsidiary of the Bank.
Planning and Operations Division- this division includes: the Process Engineering Division, responsible, inter alia, for back-office banking operations and the Planning & Economics Division, responsible for supervision and control of subsidiaries. This division is also responsible for: Bank insurance (including: banking insurance as well as officer and director insurance), insurance incidental to mortgages and the clearinghouse.

Risk Control Division - this division includes risk control at the Bank, including management of the Bank's operating risk. This division is also in charge of information security issues. In June 2012, as part of re-organization of the Risk Control Division, a Chief Compliance Officer for the Bank Group was appointed in the Risk Control Division. The Compliance Department, headed by the Bank Compliance Officer, is no longer part of the Legal Division, and now reports to the Chief Compliance Officer in the Risk Control Division.

Human Resources and Administration Division – this division includes management of human resources, training, logistics, administration and improved efficiency (including properties and construction) as well as security.

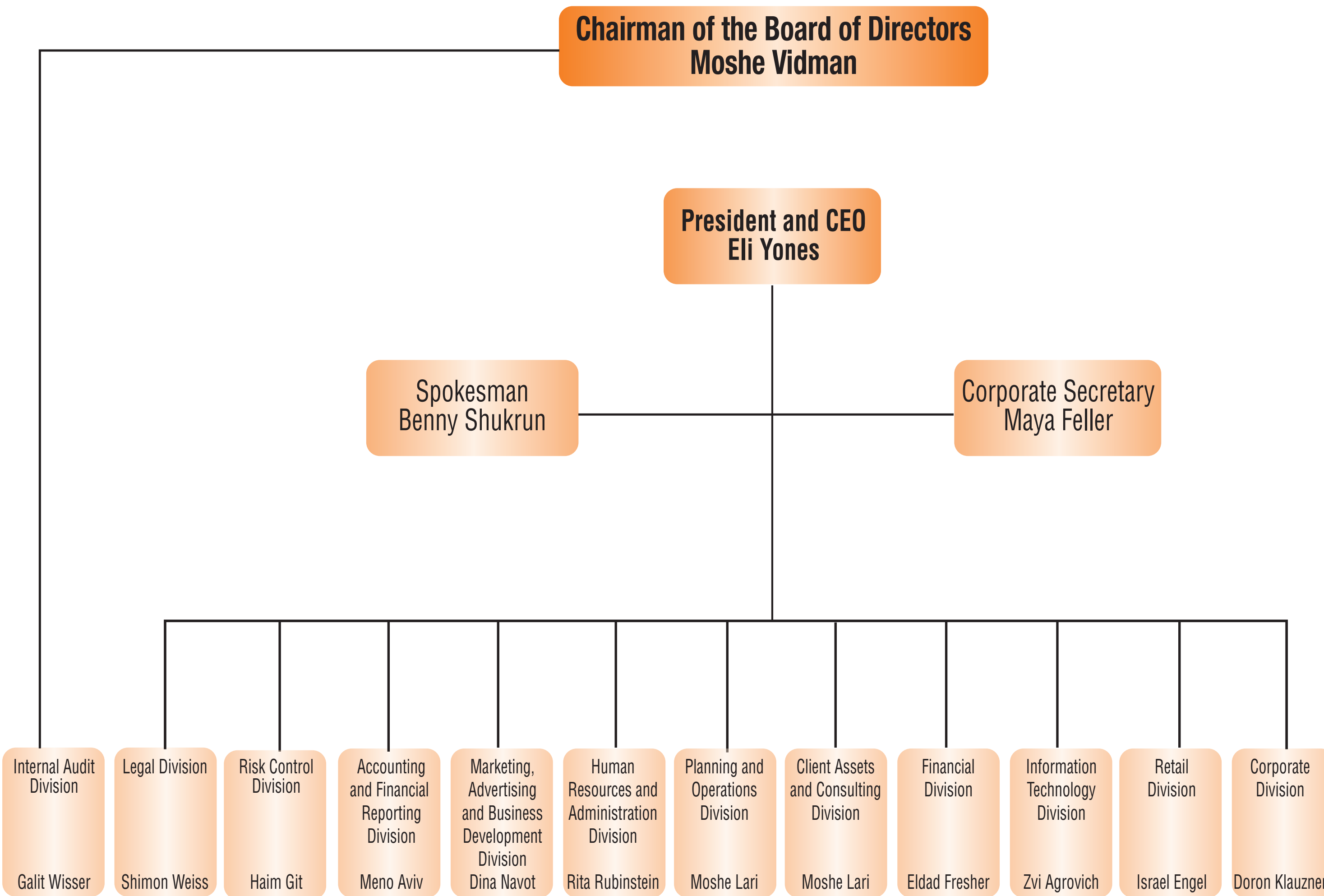
Marketing, Advertising and Business Development Division – This division consolidates activities relating to advertising, marketing, and development of financial products that the Bank markets to customers.

Accounting & Financial Reporting Division - in charge of preparing the Bank's public financial statements, reporting to statutory authorities and to management, taxation, main ledger, mortgage ledger, accounting, treasury and payroll department. The division also in charge of classifications and provisions of troubled debts.

Legal Department – the Legal Department is responsible for providing legal services for all of the Bank's units, for creating the legal infrastructure for the Bank's activities, for management of exposure to legal risk and to handle claims against the Bank.

Internal Audit Division – the division is responsible for conducting internal audits of Bank business and operating units. The division is also responsible for handling the public inquiries and complaints against the Bank.

Organizational Chart of the Bank



Tax Laws Applicable to the Bank Group

The Bank is classified as a "financial institution" under the VAT Act, 1975 and is therefore liable for payment of taxes on salary and profit, as well as for corporate tax as per the Income Tax Ordinance (New Version), 1961.

Corporate tax and profit tax

The overall tax rate for corporate tax and profit tax applicable to Bank revenues in 2012 was 35.53%.
The payroll tax is at 17% of payroll expenses for the Bank, and is not expected to change in coming years. Payroll tax is considered an expense for calculation of the corporate tax.
For details of the increase in the VAT rate, see below the chapter "Legislation and Supervision of Bank Group Operations".

Tax assessments

The Bank has finalized tax assessments through 2007. The former Bank Adanim has finalized, or deemed final, tax assessments through 2008. Bank Yahav has finalized tax assessments through 2002.

Arrangements and approvals from tax authorities

The Bank has made arrangements and obtained approvals from tax authorities for the following merger transactions executed by the Group:

In conjunction with the merger of the Mizrahi Bank Investment Company Ltd. into the Bank, the former's assets and liabilities were transferred to the Bank. Accumulated tax losses and accounting losses generated as of the merger date may be offset by the Bank in accordance with a formula stipulated in the tax authority approval over a 10 year term, starting in 2004.

See Note 28 to the financial statements for additional information.

The Bank has arrangements with the tax authorities, as follows:

- Overseas Affiliates Arrangement – According to this arrangement, certain wholly-owned subsidiaries of the Bank that operate overseas pay taxes in Israel on their income, based on the financial statements of these companies. Taxes paid overseas may be set off from the tax liability in Israel, and dividend distributions to the Bank are exempt from tax in Israel.
- On December 31, 2007, the Supervisor of Banks published a circular regarding “Measurement and Disclosure of Impaired Debt, Credit Risk and Provision for Credit Loss”, effective as from January 1, 2011.
  According to an agreement signed by the banks and the Tax Authority in 2012, provisions for credit lossfor individually-handled debt would be allowed as a tax deductible expense in the year in which it was recorded. In any tax year in which the provision balance is decreased, the Bank would be taxed at the tax rate applicable on the date of recording the provision, plus interest and linkage differences. As for accounting write-offs with respect to debt treated on group basis, one half of the net write-offs in each tax year would be allowed as a deduction in the year following the write-off, and the other half would be allowed in the following year. No deductible expense would be allowed with respect to provisions recorded on group basis. Provisions with respect to housing loans are

excluded from this agreement, and would be treated as previously.

Certain differences deducted from the Bank's shareholders equity as of December 31, 2010 due to initial application of the new directive would be allowed as a tax deduction in five equal annual installments starting in the 2011 tax year.

The aforementioned principles would apply to debt provided for during 5 years from the effective start date of the new directive. After this date, mechanisms have been specified for extensions.

Overseas operations

The Bank has branches in Los Angeles, London and the Cayman Islands. Profit or loss of these branches is included in the profit or loss reported by the Bank to the tax authorities in Israel.

The State of Israel has signed treaties for avoidance of double taxation with the U.S. and England. Pursuant to the provisions of the treaty with these countries, taxes paid in these countries for the activities of the branches there may be offset against the Bank's tax liability in Israel. The limit for offsetting foreign taxes in Israel is the amount of the tax liability in Israel deriving from the profits of these branches.

The branch in the Cayman Islands is not subject to tax in its country of incorporation.

The Bank has a subsidiary in Holland operating as a holding company, which owns a Swiss company that operates a bank in Switzerland. These companies are covered by the Overseas Affiliates Arrangement as described above.

Legislation and Supervision of Bank Group Operations

The Bank Group operates subject to a legislative framework consisting of primary legislation, regulations and directives of the Supervisor of Banks. The same framework applies to all banking corporations in Israel. Below are key changes in legislation enacted in 2012, as well as earlier changes with a future impact on Bank operations.

Anti-Trust Act (Amendment 12), 2011

The amendment to the Act, passed by the Knesset on July 18, 2011, stipulates that the Anti-Trust Supervisor (hereinafter: "the Supervisor") may determine that a small group of individuals doing business and holding a concentration of more than 50% of the total supply of assets or the total provision of services, or of their acquisition, constitutes a concentration group with regard to the amendment to the Act, and each of these persons constitutes a member of a concentration group, should the Supervisor consider that certain conditions stated in the amendment to the Act have been fulfilled.

The amendment to the Act stipulates special provisions with regard to concentration groups in the banking sector and in the insurance sector, where the Supervisor shall consult with the Governor of the Bank of Israel and with the Supervisor of Banks with regard to the Supervisor's intention to determine that a small group of individuals constitutes a concentration group, and the Supervisor shall inform the latter of the Supervisor's intention to issue a directive pursuant to section 31c(a) intended to prevent actual or foreseen significant impact to the public or to business competition among group members or in their sector, if such determination or directive concerns any person acting in a sector which falls under the responsibility of the Bank of Israel pursuant to provisions of the Bank of Israel Act; should the Governor of the Bank of Israel or the Supervisor of Banks, after receiving notice pursuant to this section, consider that issuing such a directive would jeopardize the stability of any banking corporation of the stability of the banking system, they shall inform the Supervisor, who shall avoid issuing such a directive.

Provisions of section 31d of the body of the Act, with regard to the Supervisor avoiding issuing a directive due to notice from the Governor of the Bank of Israel, the Supervisor of Banks or the Supervisor of the Capital Market, as the case may be, because issuing such directive may impact the stability of entities or systems specified in sub-sections (a) or (b) of that section, shall apply through January 1, 2014; the Minister of Finance, with approval of the Knesset Economics Committee, may extend the aforementioned period for additional two-year terms.
In the estimation of the Bank's management, it is not possible at this stage to estimate the effect of the implementation of the law on the operating results of the Bank.

Court Order Execution Act (Amendment 36), 2012

The Act, enacted in January 2012, replaces a previous arrangement with regard to court order execution with regard to evacuation of a leasehold not subject to the Tenant Protection Act. The Act stipulates that a court order execution file may be opened, in order to execute a court order for evacuation of a leasehold, only 15 days after the verdict has been handed down or delivered to the debtor.
Moreover, in lieu of separate warning and evacuation notices, these will be merged into a single notice, requiring only 21 days' wait before the date which the Registrar may specify as the evacuation date.

It was further stipulated that evacuation may be carried out within 14 days from the date specified as the evacuation date, rather than on a single, specific date; the Court Order Execution Service Registrar was also authorized to extend this deadline by 14 days at a time, and the notice of this new date is to be delivered in a more effortless manner than required for delivery of the original evacuation notice.

The Act comes into effect 30 days after its publication. The amendment has no impact on the bank's financial statements.

Banking Act (Legislation amendments), 2012

The Act, enacted by the Knesset in March 2012, includes legislative amendments designed to extend supervision of and control over banking corporations, inter alia, by supervision of those holding means of control or who have control over such corporations.

The key change in the legislative amendment stipulates that a shareholder holding 2.5% or more of Bank shares, may nominate 1.75 Board members to the Board Member Election Committee.

The legislative amendment also includes changes to composition of the Board Member Appointment Committee in banking corporations, which is authorized to appoint Board members in certain cases, so that the stipulation that the Committee shall also include members capable of presenting the needs of the banking corporation to the Committee.

Section 36 of the Act, requiring the banking corporation to report ownership of means of control, was also amended so that the reporting requirement would apply to those holding 1% or more of any type of means of control, compared to 2.5% prior to this amendment. In addition to these amendments, the Act includes other amendments to the Banking Ordinance and to the Banking Act (Licensing), 1981 - arising from the Bank of Israel Act, 2010, which replaced the Bank of Israel Act, 1954. The amendment has no impact on the bank's financial statements.

Banking Act (Customer Service) (Amendment no. 18), 2012

The Act, enacted in May 2012, amends Section 5a of the Banking Act (Customer Service), 1981 which concerns the obligation of banking corporations to provide written notice to clients of the amount or rate of commissions charged for their services; in order to make it easier for the senior population to read the information in such notice, the Act authorizes the Governor of the Bank of Israel to specify rules with regard to the form of the notice sent to clients who are senior citizens, including with regard to the minimum letter size in such notice. The amendment has no impact on the bank's financial statements.

Dishonored Check Act (Amendment no. 9), 2012

The Dishonored Check Act stipulates various provisions with respect to restricting bank accounts and clients, including provisions with regard to alerts and notices to be delivered to the account holder, to anyone holding power-of-attorney or who is an authorized signatory in the account, of such restriction and of the number of checks not honored or the bank account.

Pursuant to the amendment of the Act, enacted in May 2012, banks would be explicitly required to inform any person wishing to join an existing account, upon joining, - as account owner or by holding a power of attorney - of the number of checks refused in this account over the year prior to their joining date, of any restrictions imposed on the account, or of its ownership over the three years prior to their joining date, as well as of the account owner being classified as "special restricted client"; the banks' obligation to inform of any restrictions imposed in the three years prior to the joining date would be gradually implemented.

The amendment to the Act became effective on September 15, 2012.

The amendment has no impact on the bank's financial statements.

Uniform Contract Act (Amendment no. 4) (Setting minimum rate for linkage as an unfair term), 2012

Section 3 of the Uniform Contract Act, 1982 authorizes the Court or the Court of Law for Uniform Contracts to rescind any unfair terms in a uniform contract. Subject to provisions of the Act, an unfair term is any term included in a uniform contract which is unfair towards customers or provides an unfair advantage to suppliers, and which may result in unfair treatment of customers. Section 4 of the Act stipulates a presumption as to terms in a uniform contract which are presumed to be unfair.

According to the amendment to the Act, enacted in July 2012, the list of presumptions was expanded to include a presumption whereby any term in a uniform contract which stipulates that linkage of price or other payment pursuant to the contract to any index, such that a decrease or increase in the index would not be credited to the customer, would be presumed to be an unfair condition.

The amendment further stipulates that the Minister of Justice, with approval by the Knesset Finance Committee, may specify regulations with regard to circumstances or types of contracts to which the aforementioned presumption would not apply. The amendment to the Act became effective on November 9, 2012. Application of the amendment has no material impact on the Bank's financial statements.

The Court Order Enforcement Act (Amendment no. 41), 2012

In this amendment, enacted on July 25, 2012, the interim directive with respect to the fast collection track at the Enforcement and Collection Authority was extended for a further 4 years, with changes made arising from lessons learned from operation of the fast track over the past 3 years.

Thus it was decided to also exclude from the fast track any debtors with total debt in excess of NIS 100,000, and to specify that the 8 month duration for a fast track case would start upon delivery of notice to the debtor - rather than from the case creation date.

. In the fast track there is no entitlement to legal fees, except for an application to enforce a claim for a specified amount, provided that the awarded party is represented by an attorney.

Deficit Reduction and Tax Burden Modification Act (Legislative amendments), 2012

The amendment to the Act, dated August 2012, stipulates that the rate of National Insurance payable by employers would gradually increase from 2013 to 2015, by the stipulated steps, for the portion of salary in excess of 60% of the average salary nationwide.

The amendment to the act will become effective on January 1, 2013. Application of the amendment is not expected to have any material impact on the Bank's financial statements.

The Corporate Act (Amendment no. 20), 2013 (Terms of employment and office in public companies and debenture companies)

Amendment no. 20 of the Corporate Act ("the Act"), enacted on November 5, 2012, is designed to regulate officer remuneration at public companies and at debenture companies, by specifying a special procedure for their approval.

According to the Act, public companies and private companies that have issued debentures to the public, must adopt a remuneration policy with regard to officers' terms of employment and office, to be specified by the company's Board of Directors, as recommended by the Remuneration Committee and subject to approval by the General Meeting of shareholders. The Act requires a Remuneration Committee to be created as a dedicated committee tasked with officers' terms of employment and office, to be composed of external Board members and Board members independent of the controlling shareholder.

The remuneration policy would be set based on considerations and provisions listed in the Act, including: Contribution to promotion of company objectives and profitability based on a long-term viewpoint, creating appropriate incentives in view of the company's risk management policy, ratio of the officer's pay to that of other company employees including sub-contractors, ratio of fixed to variable pay components, based on measurable criteria. With respect to retirement bonus - also including the circumstances of the officer's retirement. The remuneration policy is to include maximums for variable components and retirement bonuses.

Officers' terms of employment and office at the company would generally be based on the remuneration policy, with exceptions allowed in special cases for recruiting and preserving outstanding officers.

The Act increases the involvement of shareholders, in particular, minority shareholders, in setting remuneration policy, in specifying terms of employment and office which deviate from such policy and in approving the CEO's employment terms. Therefore, the remuneration policy is to be approved by the General Meeting of shareholders, in addition to a simple majority, by a majority of those shareholders who have no personal interest resulting from relations with the controlling shareholder. For a company that has issued debentures to the public, only a simple majority would be required. The Act allows the Board of Directors and the Remuneration Committee to approve a policy opposed by the General Meeting of shareholders, by giving the reasons for their decision after reconsidering the matter – should they believe this would be in the best interest of the company.

The Act includes changes to approval processes of terms of employment and office, including: The Remuneration Committee would replace the Audit Committee; approval of company CEO's pay would also require approval by the General Meeting of company shareholders (unless exempted by the Remuneration Committee in the case where such approval would thwart the contract and provided that the pay is in line with the remuneration policy); terms of employment and office of VPs are subject to approval by the General Meeting of shareholders if in exception to the remuneration policy; terms of employment and office of Board members, which already require approval by the General Meeting of shareholders, would now require approval by a majority of non-controlling interest if in exception to the remuneration policy.

The Act further stipulates that for a public subsidiary of a subsidiary, the position of the General Meeting of shareholders where minority shareholders are allowed to vote, would be binding - with respect to both the remuneration policy and approval of specific terms of employment and office which are subject to approval by the General Meeting.

The amendment is effective as from December 12, 2012.

Provisions of this amendment shall apply to terms in office and employment terms of officers to be approved as from the effective start date, and to any extension of terms in office and employment terms of officers set prior to the effective start date and approved there after. Each company should set its remuneration policy within nine months from the effective start date.

The Bank is acting to implement provisions of this amendment. Application of the amendment is not expected to have any material impact on the Bank's financial statements.

Banking Rules (Customer Service) (Commissions) (Amendment), 2012

On November 28, 2012, the Bank of Israel published the amendment which abolishes securities management fee with respect to MAKAM (short-term Government debentures) and with respect to money market funds; imposes restrictions on bank commissions with respect to securities transactions; and abolishes other commissions applicable to households and small businesses.

The amendment became effective on January 1, 2013. The implementation of the amendment and the commissions update according to the amendment is expected to decrease the volume of commissions which are collected from households and small business. Overall material impact on the financial statements is not expected.

Regulations Governing Investment Advice, Investment Marketing and Investment Portfolio Management (Reports), 2011

These regulations were officially published on June 14, 2012. The regulations expand the current reporting obligation with regard to investment advisory service, marketing and portfolio management - to clients and to the Israeli Securities Authority (ISA).

- Reporting obligations by portfolio managers – the regulations stipulate the obligation by portfolio management corporations to provide their clients with a quarterly statement, to include various details and information listed in the regulations, including information about returns, expenses, management fees etc. In addition, portfolio managers are required to publish an annual report to the public at large, including: information about the portfolio management methodology, incentive structure, management fees charged, commission rebates, client churn rate etc.

- Reporting obligations to ISA with regard to investment advisor activity – in conjunction with this reporting, the Bank is required to file a monthly report with ISA, including information about all transactions made by investment advisors in assets in advised accounts over the month prior to filing the report. In addition to the aforementioned monthly report, ISA may require additional, more specific and detailed reports from the Bank.

  Application of these regulations has no material impact on the Bank's financial statements.

ISA directive with regard to disclosure of re-statement of financial statements upon uncovering a material error

On March 11, 2012, ISA issued the aforementioned directive in order to provide uniformity in disclosure details which companies are required to provide when reporting error correction. The existence of a material error on the financial statements requiring correction constitutes an "event or matter" to be reported in an Immediate Report pursuant to Regulation 36(a) of the Securities Regulations (Periodic and Immediate Reports). The Immediate Report should include, inter alia, any details significant for investors' understanding of the material error, its implications on the financial statements and the effects of its correction, description of the error correction, including corrected amounts and amendments to the financial statements. According to this directive, the amended financial statements should be published no later than 10 business days after the date on which an Immediate Report of the existence of material error was required to be published. Moreover, the Board of Directors' Report enclosed with the periodic or quarterly financial statements in which the material error was corrected, should include commentary by the Board of Directors with regard to re-statement of the financial statements, including conclusions by the Board of Directors and management of the corporation with regard to effectiveness of internal control over financial reporting and disclosure, details of measures which the Board of Directors has resolved to apply and tools which the Board of Directors has resolved to use in order to prevent recurrence of errors in financial reporting.

Letter from the Supervisor of Banks with regard to adoption of recommendations by the ministerial committee on regulation of custodian services

On January 16, 2013, the Supervisor of Banks announced the adoption of recommendations by the ministerial committee on regulation of custodian services (hereinafter "the custodian services report"), published in January 2012, in order to establish basic norms in this field (most of which are already currently applied by the Bank). The committee's recommendations would gradually come into effect as from October 2013. These recommendations govern the issue of custody of client assets and stipulate, inter alia, that:

The Bank, being custodian or intermediary, has a duty of diligence and a fiduciary duty to its clients, and should take all reasonable measures in order to ensure the safeguarding of ownership rights in client assets and cash, and safeguarding of rights arising from asset ownership. A custodian or intermediary shall not mix, including on their records and accounts, the assets of one client with those of another client, nor client assets with those of the custodian / intermediary. Moreover, a custodian or intermediary shall not create any right lien right, offset, lien or any other right with respect to client assets without consent of the client. The recommendations further stipulate that an independent auditor shall conduct, at least once annually, an audit of the custodian or intermediary with regard to compliance with various provisions of the custodian services report.

The report further regulates reporting which the Bank should provide to its clients with regard to being custodian of their assets. The custodian or intermediary should specify and apply standards and internal procedures for selection, appointment and periodic review of any financial institution used to deposit assets and cash, and should review the financial robustness of such financial institutions. An intermediary should act diligently, in good faith and with due card in selecting and contracting with a third-party custodian.

Mutual Investment Regulations (Distribution commission) (Amendment), 2013

On March 11, 2013, the Knesset Finance Committee approved the amendment to Mutual Investment Regulations, so as to reduce the distribution commissions paid by investment houses to banks for distributing their mutual funds. Pursuant to this amendment, commissions for money market funds would be reduced from 0.125% to 0.1%; for debenture and equity funds they would be reduced to 0.35% from 0.4% and 0.8%, respectively; and for NIS funds they would be reduced to 0.2% from 0.25%.

The amendment would become effective 30 days after the regulations are officially published. The expected effect on the Bank's financial statements is not material.

Increase in VAT rate

On May 15, 2012, the Knesset Finance Committee decided that the VAT rate, which was to decrease to 15.5% as from 2013, would remain unchanged at 16%.
On August 2, 2012, an ordinance was issued which raised the VAT rate to 17% as from September 1, 2012. The tax rates applicable to the Bank in 2012 and 2013 are 35.53% and 35.90%, respectively.
The effect of this change on the financial statements is not material.

Corporate governance aspects

In an Immediate Report dated February 4, 2013, reference no. 2013-01-029781, the Bank made public the Supervisor of Banks' complete review report with regard to corporate governance aspects. In an ImmediateRreport dated February 6, 2013, reference no. 2013-01-031425, the Bank made public the actions it was required to take pursuant to findings of this report.
These references constitute inclusion by way of reference of all information included in the aforementioned Immediate Reports published by the Bank on February 4, 2013 and February 6, 2013.

FATCA (Foreign Account Tax Compliance Act)

In accordance with the Act, which became effective in the USA in March 2010, foreign financial institutions, including banks around the world, are required to provide to the IRS (US Tax Authority) information about US tax payers.
According to the Act, foreign financial institutions are required to identify all accounts of individual and entities directly or indirectly owned by Americans, and to report some of them (based on criteria specified in the Act) to the IRS.
Any foreign financial institution which would not sign an agreement with the IRS, will be subject to the requirement for withholding tax at 30% on relevant payments from a US Source. The withholding tax shall apply to financial assets of the foreign financial institution as well as to assets of its clients.

The Act is designed to:

- Reduce tax avoidance by US persons using accounts outside the USA.
- Increase tax revenues paid by US persons to the USA, and increase transparency and reporting of assets and balances of clients identified as American to the IRS.

In January 2013 The IRS published rules for implementation of the Act, and the Bank is preparing to implement these, as part of preparations for implementation of the Act, which will become effective in January 2014.
The Bank avoids providing consulting or any assistance with regard to how accounts are to be identified as American or with respect to US taxation, including any advice with regard to FATCA.
In addition, the Bank records a group provision for housing loans as well, except for provision by extent of arrears.
The Bank has put in place a methodology for calculating the group provision with respect to housing loans, whereby the provision amount is derived from the increase in current credit grant volume compared to past periods. The calculation method has been approved by the Supervisor of Banks.
For details of the Supervisor of Banks' draft concerning group provision for credit loss with respect to housing loans, see chapter "Legislation and Supervision of Bank Group Operations".

The Dodd Frank Wall Street Reform and Consumer Protection Act

In 2012, rules were published governing application of the Dodd Frank Wall Street Reform and Consumer Protection Act, enacted in the USA in 2010 (hereinafter: "the reform").
The reform is designed, inter alia, to mitigate credit risk in trading on the OTC derivatives market, systemic risk arising there from and increase transparency of this market.
The reform stipulates, inter alia, that transactions are to be settled by a central clearing house to consist of large, major banks which would guarantee each party's compliance with their obligations.
Binding procedures concerning collateral are to be specified, and all swap transactions made are to be reported to central information repositories, which would store this information and make it accessible to all market players.
The reform classified financial entities by scope of trading and imposes obligations based on this classification (swap dealer, MSP etc.)
The rules set forth in the reform apply to US entities and to non-US entities which conduct transactions of significant volume (as defined in the reform) with US entities.
The Bank is preparing to apply the relevant rules of the reform, which would come into effect during 2013, as they apply to the Bank with regard to its relations with foreign financial institutions.

Proposed legislation

From time to time, proposals for legislative amendments are brought before the Knesset on various matters, some of which could have an impact on the businesses of banking corporations, including the Bank. However, as of the date of the financial statements, these bills are in different stages of legislation, they may be modified and there is no certainty as to when they will be completed or if they will eventually become provisions of binding legislation.

Proper Conduct of Banking Business Regulation 205 concerning "Securitization"

On May 15, 2012, the Supervisor of Banks issued an update to Proper Conduct of Banking Business Regulation 205 concerning securitization. This update includes an amendment of the Regulation based on a publication by the Basel Committee dated July 2009. The effective start date of this regulation is December 31, 2012. Application of the amendment is not expected to have any material impact on the bank's financial statements.

Proper Conduct of Banking Business Regulation 208 concerning "Market risk"

On May 15, 2012, the Supervisor of Banks issued an update to Proper Conduct of Banking Business Regulation 208 concerning market risk. The update includes an amendment of the regulation based on a publication by the Basel Committee dated February 2011, which includes amendments of guidance with regard to capital allocation for market risk within the scope of Basel II. Most of these amendments of the regulation concern treatment of exposures included in a "portfolio for trading correlations", increased capital requirements with respect to securitization exposures in the portfolio held for trade, treatment of credit derivatives and elimination of the easement for a liquid, highly diversified stock portfolio. The effective start date of this regulation is December 31, 2012. Application of the amendment is not expected to have any material impact on the Bank's financial statements.

Proper Conduct of Banking Business Regulation 209 concerning "Treatment of non-liquid positions"

On May 15, 2012, the Supervisor of Banks issued an update to Proper Conduct of Banking Business Regulation 209 concerning treatment of non liquid positions.. The provisions in this regulation are part of the amendments stipulated by a Basel Committee publication dated February 2011. The regulation primarily consists of directives with regard to prudent, conservative estimation of all positions measured at fair value in accordance with GAAP, for positions in both the portfolio held for trade and in the banking portfolio. The Supervisor does not expect banking corporations to modify the existing estimation procedures used for financial reporting, and some of these changes are already included in Public Reporting Regulation 661. The effective start date of this regulation is December 31, 2012. Application of the amendment is not expected to have any material impact on the bank's financial statements.

Proper Conduct of Banking Business Regulation 301 concerning "Board of Directors"

On December 29, 2010, the Supervisor of Banks issued an amendment to regulation 301 concerning the Board of Directors, in conjunction with updating of Proper Conduct of Banking Business Regulations and its adaptation to the Basel II framework. The regulation specified rules for Board operation, roles and authority, structure and composition, including its committees, processes for confirmation of Board member qualifications for their position etc. - all this in addition to provisions of the Corporate Act, 1999.

The Regulation emphasizes the Board's place and role in proper corporate governance of a banking corporation, specified the Board's responsibility for business and financial robustness of the banking corporation and specifies the Board's roles in exercising this responsibility. Thus, for example, the Board must set corporate strategy and approve corporate policies, supervise management activities and their compliance with Board policy, ensure existence of clear responsibilities and reporting channels within the banking corporation, specify the organizational culture with regard to professional conduct and integrity etc.

The regulation further stipulates that the Board must discuss and set overall strategy objectives for the banking corporation group, and that the Board of a controlled entity must take into consideration the overall strategy objectives of the Group, in as much as they are in line with the best interest of the controlled entity.
As for credit, the Board is expected to focus on creating appropriate control and supervision structures over management activity, and to limit its involvement in credit approval.
Most of the amendments to the regulation became effective on January 1, 2012.
The Bank has implemented the directive and is acting in accordance with it.

On December 31, 2012, the Supervisor of Banks issued another amendment of Regulation 301 with regard to the Board of Directors, due to updates made to the Banking Act. The regulation was adapted to changes made upon publication of Proper Conduct of Banking Business Regulation 310 with regard to risk management, and Regulation 311 with regard to credit risk management, as described below, as well as Public Reporting Regulations with regard to making provisions for credit loss. These amendments come into effect on January 1, 2014. The Bank is preparing to apply this regulation.

Proper Conduct of Banking Business Regulation 307 concerning "The Internal Audit Function"

As part of adapting Proper Conduct of Banking Business regulations to the work framework of the Basel Committee on Banking Supervision and reinforcing the principles of corporate governance, in December 2011 the Bank of Israel issued Proper Conduct of Banking Business Regulation 307 concerning the Internal Audit function. The regulation became effective on July 1, 2012.

The regulation covers, inter alia, the attributes of the Internal Audit function, its roles, position, independence and qualifications of its staff. The regulation also refers to the scope and operation of the Internal Audit in Israel and overseas, its work methods, the need to base it on a detailed, risk-focused work plan and also to reporting by this function.

The regulation had no material effect on the Bank.

Proper Conduct of Banking Business Regulation 310 concerning "Risk Management"

On December 23, 2012, the Supervisor of Banks issued Proper Conduct of Banking Business Regulation 310 concerning risk management. The regulation is primarily based on Basel guidelines for risk management, as reflected in recommendations made by the Basel Committee. The regulation includes a corporate-wide risk management concept, listing five principles for risk management. The regulation also clarifies the processes required of the Board of Directors in order to duly discharge its duties pursuant to Proper Conduct of Banking Business Regulation 310, including a requirement to appoint a Risk Management Committee of the Board of Directors. According to the regulation, senior management is responsible for regular risk management, and is required to create a Risk Management function, and to appoint a Chief Risk Officer to head this function. The regulation lists the responsibilities and position of the Risk Management function. The effective start date of this regulation is January 1, 2014.

The Bank is preparing to implement this regulation.

Application of the regulation is not expected to have any material impact on the bank's financial statements.

Proper Conduct of Banking Business Regulation 311 concerning "Management of credit risk"

On December 23, 2012, The Supervisor of Banks issued Proper Conduct of Banking Business Regulation 311 concerning management of credit risk. The regulation is primarily based on Basel principles dated September 2000. This regulation specifies the credit risk management structure required of a banking corporation, and the authority of different bodies of the banking corporation with regard to credit risk management. These requirements adopt the approach whereby, in order to support appropriate decision making with regard to credit and to minimize the effect of any conflict of interest, strong involvement is required of an entity independent of the business units. Such involvement is particularly required in forming credit policy, classifying debt and determining provisions for credit loss. The regulation further stipulates that decisions with regard to approval of material credit exposure would be made with reference to the opinion of the Risk Management function. The effective start date of this regulation is January 1, 2014. The Bank is required to present to the Supervisor a plan for implementation of the regulation, by July 1, 2013.

The Bank is preparing to implement this regulation.

Proper Conduct of Banking Business Regulation 350 concerning "Management of operating risk"

On December 23, 2012, the Supervisor of Banks issued an update to Regulation 350 concerning management of operating risk, based on Basel Committee guidelines dated June 2011. This Regulation is an update to the previous Regulation 350 (dated February 14, 2012), with regard to application of Regulation 310. The regulation stipulates 10 basic principles for management of operating risk, in reference to the framework for management of operating risk and the listed principles mostly relate to issues of corporate governance and to the operating risk management environment.

The regulation comes into effect on January 1, 2014 and the Bank is preparing to implement this regulation. Application of the regulation is not expected to have any material impact on the bank's financial statements.

Proper Conduct of Banking Business Regulation 355 concerning "Management of business continuity"

On December 25, 2011, the Supervisor of Banks issued regulation 355 concerning management of business continuity, in conjunction with updating of Proper Conduct of Banking Business Regulations and its adaptation to the Basel II framework. This regulation is designed to ensure adoption and implementation of appropriate standards for management of business continuity by banking corporations, and is part of action by the Supervisor of Banks to fortify the management of operating risk and emergency readiness at banking corporations.

The effective start date of the regulation is July 1, 2012, except for issues of business continuity of suppliers and service providers for critical processes, and to directives with regard to alternate site - which became effective on December 31, 2012. Implementation of this regulation had no effect on Bank business.

Restriction on loan-to-value ratio for housing loans

On November 1, 2012, the Supervisor of Banks issued a letter instructing all banking corporations not to approve housing loans with an LTV ratio in excess of 75% for purchase of a real estate interest constituting a single apartment, 70% - for an alternative apartment and 50% - for any other apartment, including for investment purposes.

The Supervisor of Banks further instructed the banks to obtain, inter alia, an affidavit from the loan applicant, certified by an attorney, with regard to the borrower's compliance with the required conditions for the apartment to qualify as a sole apartment or alternate apartment, and to make the loan contingent on, inter alia, obtaining a copy of the statement provided by the applicant to the Tax Authority pursuant to Section 73(c) of the Real Estate Taxation Act, and to store any such documentation.

The Supervisor of Banks directed the banks not to approve any housing loan such that the total LTV ratio for such loan, together with the balance of previous loans provided and secured by the same apartment, would exceed the aforementioned maximum LTV ratios.

The Supervisor of Banks excluded from the scope of this directive any housing loans granted for repayment of an existing housing loan, including refinancing, whose amount does not exceed the balance of the repaid loan, as well as any housing loans where 50% or more of the loan is granted out of State funds and guaranteed by the State.
The aforementioned directive shall apply to housing loans approved in principle as from November 1, 2012.
According to data available at the Bank about the composition of the LTV ratio for buyers of new apartments and buyers of a second apartment, this new restriction approximately reflects the upper limit of LTV ratios for mortgages actually granted to this population. As for investment properties, there may be some effect on the scope of business.

Supervisor of Banks' directives with regard to residential real estate

On February 18, 2013, the Advisory Committee on Banking Business received a draft directive by the Supervisor of Banks, which specifies an update to risk weighting of housing loans with respect to capital allocation by the Bank, as follows:

For loans with LTV ratio of up to 45%	– risk weighting of 35%
For loans with LTV ratio over 45% and up to 60%	– risk weighting of 50%
For loans with LTV ratio over 60%	– risk weighting of 75%
and for leveraged loans bearing adjustable interest	– risk weighting of 75%

This compares with current risk weightings as follows:

For loans with LTV ratio up to 75%	– risk weighting of 35%
For loans with LTV ratio over 75%	– risk weighting of 75%
and for leveraged loans bearing adjustable interest	– risk weighting of 100%

In addition, the credit conversion factor for guarantees to secure investments by apartment buyers was reduced from 20% to 10% if the apartment has been delivered to the tenant; the directive further stipulates that the balance of group provision for credit loss maintained with respect to housing loans shall be no less than 0.35% of the balance of housing loans excluding any loans for which a provision by extent of arrears is maintained. The draft directive stipulates that its effective start date would be January 1, 2013, and for guarantees under the Sale Law - it would apply retroactively. The Bank is preparing to apply the directive when finalized, in accordance with changes to be made by the Bank of Israel following comments received from banking corporations.

Bank management believes, based on the balance of housing loans as of December 31, 2012, that the expected effect of applying the new directive is an increase of NIS 179 million in group provision with respect to housing loans; after the related tax effect, Bank capital would be reduced by NIS 116 million.

Repricing of commissions with respect to securities transactions

On November 28, 2012, the Supervisor of Banks issued a circular concerning repricing of commissions with respect to securities transactions.

Further to findings and recommendations included on the interim report by the team created to review increasing competition in the banking sector, with regard to commissions and benefits with respect to securities transactions, and further to the Amendment to Addendum I to Banking Rules (Customer Service) (Commissions), 2008 - as described above - the Bank is required to set the new rate of commissions charged for buying, selling and redeeming securities with respect to shares and debentures, taking into consideration the changes made to the commission structure in the aforementioned Amendment to Addendum I (setting a differential rate by transaction channel and setting a maximum commission), as well as the need to align these, in as much as possible, with the price actually charged. The Bank is also required to inform the Supervisor of Banks of its new commission rates, as described above, by March 1, 2013 concurrently with issuing a public notice of this change, as mandated by Banking Rules (Customer Service) (Due Disclosure and Document Delivery), 1992. In addition, the Bank is required to change its contracting with clients with regard to discounts allowed on commissions with respect to securities transactions, to be based on the commission rate or amount - rather than on a discount percentage off the price list commission rate or amount – for new or renewed agreements as from March 1, 2013.

The re-pricing is expected to decrease the volume of commissions which are collected from households and small business. Overall it is not expected to have material no impact on the bank's financial statements.

Report on corporate accountability

On October 3, 2011, the Supervisor of Banks issued a circular re Report on Corporate Accountability. According to this circular, banking corporations should make public a report for a period of up to two years about their corporate accountability, as stipulated in the directive. The report would be published for the period starting on or after January 1, 2012. The Bank is preparing to implement the regulation.

Other regulations

In addition, banking corporations are required to file Immediate Reports with the Supervisor of Banks (inter alia, with regard to embezzlement, fraud and acquisition of means of control), as well as monthly reports (inter alia, reporting of financial data, of the banking corporation's board of directors, senior staff and auditor, ratio of capital to elements of risk, etc.).

Recommendations of Basel Committee on Banking Supervision ("Basel Committee")

The Basel Committee is an international body established in 1974 by the central banks of different countries. The Committee's decisions and recommendations, although they have no binding legal validity, prescribe the supervisory regulations acceptable to the supervisory bodies of the banking systems in a majority of countries throughout the world. On June 26, 2004, the Basel Committee published new recommendations intended to assure proper regulation for arranging the rules of capital adequacy of banks in different countries ("Basel II"). A final, updated version of these regulations was published in June 2006. Basel II recommendations supersede the previous regulation dated 1988, known as Basel I, which included capital requirements due to credit risk, and was expanded in 1996 to include capital requirements for market risk as well.

Application of Basel II directives improves measuring and management of different risk factors facing the financial institution, and ensures better alignment of capital requirements to the risk level to which the financial institution is exposed.

Key recommendations of the Basel Committee

Whereas the Basel I regulation was mainly aimed at capital allocation for credit risk and market risk to which the financial institution is involved, Basel II expanded these regulations to afford better stability to financial institutions, by also implementing a culture concerning risk management and control. Therefore, Basel II regulations include, in addition to a material change in how capital is calculated (the first layer of the regulations), also two other layers, as described below.

Basel II, Pillar 1 includes minimum capital allocation with respect to market risk, credit risk and operating risk. The guidelines stipulate how capital is allocated for credit risk by enabling calculation of the minimum capital using a standard model relying on external debt rating by rating agencies recognized by the regulatory authority (in Israel: the Supervisor of Banks) , uses a large number of exposure groups while adapting risk coefficients to the various groups, and recognizes financial collateral which may be offset against the exposure. The regulations allow banks to calculate the minimum capital requirement using internal models. These models are based on bank assessment of its borrowers' quality, the probability of borrowers entering a state of credit default, and the expected loss to the bank in case of credit default. Use of internal models requires approval by the regulatory authority, which is only granted after extensive validation of the model.

In the field of credit risk the capital allocation is chosen by standard model, which estimate the Bank's exposure for, basis risks, interest risks, and stock in the Bank's negotiable portfolio.

In the area of operational risk, the guidelines propose three alternative approaches for calculating the required capital: The basic indicator approach, according to which the bank will allocate capital for operational risk as a fixed percentage of the average annual gross revenue; the standard approach, in which the capital requirements are calculated by multiplying gross revenues from each line of business by a specific coefficient specific to that line of business; the advanced measurement approach, whereby the bank will allocate capital based on an internal model to be developed within the organization.

Basel II recommendations specify multiple principles for operating risk management, relating to aspects such as: degree of supervision by bank management and Board of Directors, existence of suitable organizational structure and culture, including a system of internal reporting and an efficient and effective flow of information, and the existence of appropriate support systems. The department charged with handling operating risk is required to act in order to map and identify operating risk, collect actual failure data and take action to reduce potential damage arising from an operating failure at the bank. Basel II principles further stipulate the responsibility of the Internal Auditor as an additional layer in handling operating risk.

The second layer of Basel II involves the Supervisory Review Process (SREP) and the Internal Capital Adequacy Assessment Process (ICAAP) aimed at ensuring that bank capital is in line with its risk profile. This is over and above the minimum capital the bank is required to maintain pursuant to the first layer. This includes, inter alia, a review of the required capital due to other risk not included in the minimum capital requirement of the first layer, such as: Interest risk in the bank portfolio, concentration risk, liquidity risk, reputation risk etc. Furthermore, the directives for this layer review the bank’s risk management processes, risk control processes, level of the bank’s corporate governance, existence of supporting procedures, reporting and process management closely linked to risk management and the corporation’s profit, such as credit pricing processes, rating processes, specification of authority etc.

In addition, Layer 2 mandates checking if the bank has enough capital to meet its strategic plan, and if it has enough capital to protect against down-turns and economic crises which may occur and which may impact the bank. Therefore, stress tests are an important tool in estimating the capital required of banks, and these feature prominently in the Layer 2 of the directive.

Layer 3 of the Basel II directive involves reporting and disclosure to the regulating authority and to the public. This requires the bank to provide detailed, extensive disclose of its risk level and its risk management processes. In October 2009, the Bank received detailed directives concerning implementation of disclosure requirements for implementation of Pillar 3 of Basel II, and the Bank applies these requirements in these financial statements.

Application of the Basel Committee recommendations by the Israeli banking system

In Israel, Basel Committee recommendations have been implemented in Proper Conduct of Banking Business Regulations as follows:

- Proper Conduct of Banking Business regulation 201 - Introduction, scope and requirement calculation;
- Proper Conduct of Banking Business regulation 202 - Capital elements;
- Proper Conduct of Banking Business regulation 203 - Calculation of capital required with respect to credit risk using the standard approach;
- Proper Conduct of Banking Business regulation 204 - Calculation of capital required with respect to credit risk using the internal rating approach;
- Proper Conduct of Banking Business regulation 205 - Handling of securitization transactions;
- Proper Conduct of Banking Business regulation 206 - Calculation of capital required with respect to operating risk;
- Proper Conduct of Banking Business regulation 208 - Calculation of capital required with respect to market risk;
- Proper Conduct of Banking Business regulation 211 - Directives for assessment process of appropriateness of capital adequacy at banking corporations (Pillar 2);

Pillar 3, which stipulates directives and expectations with regard to market discipline (disclosure requirements), was incorporated into the collection of public reporting directives. On February 14, 2011, the Supervisor of Banks issued a circular which stipulates that as from January 1, 2011, the capital requirements included in Proper Conduct of Banking Business regulation 311 (Basel I) were cancelled.
The disclosure stipulated by the Supervisor of Banks, in accordance with Pillar 3 requirements, is included below. The Bank's capital adequacy as of the report date, in the disclosure format set by the Supervisor of Banks, is presented in Note 14 to the financial statements.

Under Basel II, Pillar 2 (Proper Conduct of Banking Business Regulation 211 - ICAAP Process), all risk types material to Bank operations have been mapped. ICAAP is a comprehensive process in which senior Bank executives are involved. The Bank has specified its risk appetite for all material risk types to its operations, authored policy documents for risk types added during mapping and extended existing policy documents, in conjunction with the ICAAP process. The risk appetite, risk mapping and determination of the materiality there of are submitted for approval by the Board of Directors' Risk Management Committee and the Board of Directors plenum, on annual basis.

In April 2012, the Bank submitted to the Bank of Israel its ICAAP document (as of December 31, 2011), which reflects the Bank's assessment of the capital required to cover all risk to which the Bank is exposed in conjunction with its business operations, as per guidance from the Bank of Israel, and in coordination with Bank of Israel comments on the SREP process conducted at the Bank.

Results of the capital assessments conducted within this document, indicate that the Bank has sufficient capital to cover all risk factors to which it is exposed, both under normal and stress conditions.

In conjunction with application of Pillar 2, the Bank continues in accordance with the work plan to regularly eliminate gaps identified vis-à-vis requirements of the Basel Committee in various risk areas, to deliver appropriate training to senior staff at the Bank and to improve its risk management and capital management policy documents in line with Pillar 2 directives.

On October 28, 2012, the Bank received comments from the Supervisor of Banks on the Bank's ICAAP document and comments in conjunction with the Supervisory REview Process. The Bank is currently preparing to compile the next ICAAP document, as of December 31, 2012, in which reference would be made to different aspects arising from the Supervisory REview Process.
On February 14, 2012, the Bank of Israel issued a new directive for handling operating risk (update to Proper Conduct of Banking Business regulation 350), based on the new Basel directive for handling this risk, dated June 2011. The Bank is in final stages of implementing this directive.

Basel III

In late 2010, the Basel Committee adopted a new directive, known as Basel III. This directive, originated by the recent crisis in global markets, consists of a multiple amendments to the Basel II directive, including: Strengthening of capital base, increase in minimum capital ratios, specification of new benchmarks and methodologies for handling liquidity risk, reinforced methodology for handling counter-party risk, specification of the leverage ratio as a new ratio etc. According to the Committee-specified schedule, this directive would be gradually applied world-wide starting in 2013.

On March 28, 2012, the Supervisor of Banks issued a directive to all banking corporations, citing a higher minimum core capital ratio than the one currently required. According to the directive, all banking corporations would be required to achieve a minimum core capital ratio of 9% by January 1, 2015. In addition, large banking corporations, whose total consolidated balance sheet assets exceed 20% of total balance sheet assets for the Israeli banking sector, would be required to achieve a minimum core capital ratio of 10% by January 1, 2017. The directive with regard to a minimum core capital ratio of 10% does not apply to the Bank. The core capital ratio should be calculated in conformity with Basel III provisions.
On July 23, 2012, the Bank Board of Director instructed Bank management to bring forward implementation of the Supervisor of Banks' directive dated March 28, 2012 - so as to implement it, if possible, as from January 1, 2014. Moreover, the Board of Directors has resolved to instruct Bank management to maintain, in as much as possible, appropriate safety margins to this end.

On December 31, 2012, the Advisory Committee on Banking Business received draft amendments to Proper Conduct of Banking Business Regulations 201-211 (concerning adoption of Basel III directives with regard to supervisory capital and with regard to risk assets). Proper Conduct of Banking Business Regulation 202 (Capital measurement and adequacy - supervisory capital) adopts the Basel III recommendations in Israel.
The draft amendment is primarily focused on improving capital quality and size and improving the coverage for Credit Valuation Adjustment (CVA) risk. Below are the key amendments included in these drafts:

- **Capital structure**

  Supervisory capital would be composed of only two tiers: Tier I capital (including Tier I equity and Tier I additional capital) and Tier II capital.

  The requirement for Tier III capital to cover market risk was eliminated.

- **Qualified capital instruments for Tier I additional capital and Tier II capital**

  Qualification criteria were specified for capital instruments classified as Tier I additional capital and as Tier II capital. These instruments are to include a mechanism for absorbing principal loss, whereby conversion into shares or principal reduction would take place when the Tier I equity ratio drops below 7% for Tier I additional capital instruments, or below 5% for Tier II capital instruments.

- **Non-controlling interest**

  The amount of non-controlling interest recognized as capital would be limited, and excess equity at a subsidiary would not be recognized.

- **Group provision for credit loss**

  The amount of group provision would be recognized as Tier II capital up to 1.25% of weighted risk assets for credit risk.

  On the other hand, the provision amount would be added to the weighted risk assets for credit risk.

- **Adjustments to and deductions from supervisory capital**

  – Deferred taxes due to temporary differences would be accounted for as follows:

  – Up to 10% of Tier I equity - weighted at 250% risk weighting.

  – Over 10% of Tier I equity - would be deducted from capital.

  – Investments in equity components of financial institutions - banks, insurance companies and any company doing business in the capital market segment - would be accounted for as a deduction from capital or by risk weighting, subject to specified tests.

  – The accumulated gain with respect to cash flow hedging of items not listed at fair value on the balance sheet - would be deducted from capital. This means that positive amounts would be deducted from capital and negative amounts would be added to capital.

  – Accounting adjustments with respect to liabilities of derivatives arising from a change in the Bank's credit risk (Debit Valuation Adjustment - DVA) would be deducted from capital.

- **Capital allocation with respect to CVA loss**

  In addition to capital requirement with respect to default risk arising from counter-party credit risk under the standard approach, an additional capital allocation is required to cover the risk of potential loss which may arise from marking to market value of OTC derivatives.

  In order to comply with the new requirements in conjunction with application of the Basel III directives, a graduated transition period of several years was specified, until these directives are completely applied.

  – Supervisory adjustments and deductions from capital and non-controlling interest not qualified for inclusion under supervisory capital - an annual 25% deduction as from January 1, 2014.

- Capital instruments not qualified as supervisory capital - a 10% deduction from the balance of such instruments, from the effective start date through January 1, 2022.

The draft Regulation 202 stipulates that the target date for compliance with the minimum 9% Tier I capital ratio for a non-large banking corporation is January 1, 2015 - in line with the Supervisor of Banks' letter dated March 28, 2012.

The Bank is reviewing the effect of anticipated changes on its capital, pursuant to the new draft directives on application of Basel III directives, as described below.

For more information about the Bank's business strategy, see chapter "Significant events in the Bank Group's business" below.

The Bank is preparing for immediate application of the Supervisor of Banks' anticipated requirements, as listed in the draft regulations.

As directed by the Supervisor of Banks, the Bank was required to present the effect of anticipated application of Basel III directives upon the transition date; the Bank believes this would result in a 0.3% decrease in Tier I capital ratio.

The Bank's core capital ratio, calculated pursuant to Basel II directives, as of December 31, 2012 is 8.55%.

For further information about the Bank's capital adequacy ratio see reference under section "Capital adequacy" in the chapter "Risk Management" – "Basel II: Pillar 3 - Market Discipline".

Significant Agreements

A. Employment agreements signed with the Employee Council, the Manager and Authorized Signatory Association, the Yahav Employee Committee and the Technology Division Employee Committee. For details, see "Human Resources" chapter above.

B. Letters of indemnification. See Note 19.D.4) through 19.D.9) to the financial statements for details.

C. Agreement with Israel Credit Cards Ltd. (hereinafter: "CAL") and with Diners Club Israel Ltd., a company controlled by CAL, for joint issue of Visa, MasterCard and Diners Club debit cards, including Bank-branded cards, to be distributed by the Bank to its clients. The agreement, in addition to operational arrangements, also grants the Bank an option to acquire from CAL, by way of allotment, CAL ordinary shares - all subject to terms and conditions stipulated in the agreement. See Note 19.D.13) to the financial statements for further information.

Legal Proceedings

For material legal proceedings to which the Bank is party, see Notes 19.D. 10) and 19.D.11) to the financial statements.

Parliamentary investigative Committee on the Location and Restitution of Assets of Holocaust Victims ("the Investigative Committee")

In January 2005, the Parliamentary Enquiry Committee on Identification and Restitution of Assets of Holocaust Victims (hereafter: "the Enquiry Committee") published its report, after which the Knesset enacted the Holocaust Victims' Assets Act (Restitution to heirs and dedication for assistance and memorial purposes), 2006 (hereinafter: "the Act"), based on which the Holocaust Restitution Company of Israel Ltd. was founded in 2006 (hereinafter: "the Company").

The Company applied to the Bank, citing monetary claims pursuant to provisions of the Act, with regard to accounts managed by the Bank and with regard to general Bank accounts and to Bank shares - which the Bank rejected. However, due to the importance and sensitivity of this issue, and due to its sincere desire to help Holocaust survivors, the Bank has conducted, since August 2009, detailed and comprehensive discussions with the Company, designed to resolve their disagreements.

In view of the important public role of the Company and its objectives, and mutually desiring to resolve the disagreement, the Bank signed a settlement agreement on November 4, 2012 whereby the Bank, with no admission of any liability or any claim of any kind made against the Bank, paid to the Company on November 5, 2012 the final amount of NIS 9.5 million - for full and complete settlement of claims and demands made by the Company or by any other person, whether known upon signing this agreement or unknown and to become known in future - all pursuant to the agreement.

In exchange for this payment to the Company, the Bank and any Bank Group entity are no longer liable, and were replaced by the Company which assumed complete liability for this matter for all intents and purposes. The Company also committed to indemnify the Bank Group for any payment which the Group may have to make to any third party, for any reason, with respect to assets of Holocaust victims.

The Bank sees great importance in any activity involving assistance to Holocaust survivors, and is fully confident that funds paid to the Company would be used for worthwhile purposes and for providing assistance to Holocaust survivors in need, to secure their respectable livelihood in future.

Arrest and plea bargain of bank employee in the USA

On December 19, 2007, a Bank employee, since then retired, was arrested in the USA on claims that he assisted a Yeshiva, resident in the USA, to defraud the US tax and securities authorities; this employee and others were indicted before the Los Angeles Court of Law.

The Bank's Los Angeles branch has been subpoenaed to produce documents. Since this is a criminal investigation still under way by US law enforcement agencies ("law enforcement agencies"), the subpoena includes prohibition of disclosing information to others; however the Bank informed the law enforcement agencies that proper disclosure of this matter would be made in its financial statements.

Further note that the law enforcement agencies reported that the Bank is a target of this investigation, but the agencies are still considering their position with regard to the Bank. Based on a review conducted by the Bank, it has not committed any offense in Israel nor in the USA, and if any offenses have been committed by the Bank employee as the indictment alleges, he did so in violation of Bank procedures and his obligations to the Bank.

On June 27, 2008, in conjunction with a plea bargain, the bank employee (who has since retired) admitted to assisting only one bank client to avoid tax payments. All other charges against the bank employee, including money laundering offenses, will be erased. In the plea agreement, the bank employee does not implicate the bank or any of its employees in his actions. The plea agreement was filed with the Los Angeles Court. In early March 2009, the (former) Bank employee was sentenced to a prison term concurrent with the actual period since his arrest, and was released.

The Bank has expressed its consent to cooperate with law enforcement agencies, subject to legal provisions and to the US-Israel Treaty. The law enforcement agencies consented to the Bank responding to the subpoena by a document discovery process to last several months. The Bank has provided the aforementioned documents, and continues to provide documents as requested by enforcement agencies in the USA, subject to orders of the competent Court in Israel.

The Bank has been and is still negotiating a cooperation and non-prosecution settlement agreement. with enforcement agencies in the USA

The Bank has informed the Supervisor of Banks of the aforementioned events and developments.

Determination by the Restrictive Trade Practices Authority

On April 26, 2009, the Bank received a determination by the Anti-Trust Supervisor pursuant to Section 43(a)(1) of the Restrictive Trade Practices Act, 1988, whereby restrictive trade practices existed between the Bank and Bank Hapoalim Ltd., Bank Leumi Le-Israel Ltd., Bank Discount Le-Israel Ltd. and First International Bank of Israel Ltd., with regard to commission-related information sharing, since the early 1990s through commencement of the Supervisor inquiry into this matter, in November 2004. This is a civil determination which constitutes a-priori evidence of the content there of in any legal proceeding.

On March 24, 2010, the Bank appealed this ruling to the Anti-Trust Court. The Restrictive Trade Practices Authority filed its response to the appeal on February 22, 2011. In accordance with the Court's proposal, all parties have consented to transfer discussion of the appeal to arbitration. For details of a claim filed against the Bank based on the determination by the Anti-Trust Supervisor, see Note 19.D.12) to the financial statements.

Monetary sanction imposed on the Bank

On May 9, 2012, the Bank received a letter from the Supervisor of Banks, which announces the filing of a motion to impose a monetary sanction on the Bank for an alleged breach of provisions of the Prohibition on Money Laundering Act, 2000. The motion to impose a monetary sanction is based on findings in an audit report by the Supervisor of Banks with regard to AML, which refers to the period from 2007 through mid-2010.

The Bank has reviewed the findings listed in the audit report. The Bank has accepted some of these, with regard to the period under review. Moreover, in early 2010 the Bank replaced the person in charge of implementing the Bank's obligations pursuant to the Act, and since then the Bank has expanded its activity, including with regard to training and deployment of the relevant directives, and has taken extensive measures to amend the shortcomings listed in the audit report, which were mostly relevant only for the period under review.

The Bank filed its response to this motion on June 9, 2012.

On July 24, 2012, the Committee for Imposing Monetary Sanctions on Banking Corporations (hereinafter: "the committee") held a meeting at which the Bank concluded its verbal claims, in conformity with the committee's operating procedure.

On September 19, 2012, the Bank received a letter from the Supervisor of Banks, informing the Bank of a monetary sanction imposed on the Bank, amounting to NIS 3.8 million - paid on October 9, 2012.

Monetary sanction imposed on subsidiary

On March 29, 2012, the Bank subsidiary "Etgar Investment Portfolio Management Company of the Mizrahi Tefahot Group Ltd." (hereinafter: "Etgar") received demand for payment of a civil law fine amounting to NIS 335 thousand, pursuant to section 38e of the Arrangement of Engagement in Investment Consultancy, Investment Marketing and Management of Portfolios Act, 1995 (hereinafter: "the Act"), following an audit conducted in 2010 at Etgar, which revealed several cases where client portfolios contained securities with low trading volumes, for which no appropriate disclosure was made on the quarterly financial statements. Furthermore, the aforementioned audit revealed several cases where Etgar received commission rebates from a stock exchange member, without obtaining positive consent of the clients in advance to the exact rate of rebate. Note that ISA has reduced the original fine amount from NIS 709 thousand to NIS 335 thousand, inter alia due to the fact that these errors were corrected, and clients received management fee credit with respect to the aforementioned securities.

Events outside the Normal Course of Bank Group Business

Updates to employee stock option plan

On May 19, 2008, after approval by the Bank's Audit Committee and Board of Directors, option warrants were allotted to Bank officers, branch, department and affiliate managers as well as to other employees of the Bank and its subsidiaries.

On March 21, 2010, after approval of the Bank's 2009 financial statements, the Board of Directors decided, as recommended by the President and the Remuneration Committee, and after approval by the Audit Committee, that for calculation of the annual rate of return for 2009, for each of the stock option plans published by the Bank in 2008 and 2009 ("the stock option plans"), the provision recorded on the Bank's 2009 financial statements with respect to employee retirement, amounting to NIS 170 million (NIS 118 million after tax) should be eliminated and charged linearly over the period 2010-2015. This is because, in accordance with generally accepted accounting principles, the aforementioned provision was fully recognized in 2009, and would not be charged over time, concurrently with the economic benefit generated by the retirement plan for employees.

Accordingly, and as an outcome of the aforementioned decision by the Board of Directors, after charging the aforementioned provision linearly for 2012 (as part of the overall charging for the period 2010-2015), the annual rate of return for 2012, for each of the stock option plans, would be 12.9% instead of 13.1% - the rate published in the Bank's 2012 financial statements.

Therefore, for calculating eligibility to exercise stock options pursuant to any of the stock option plans, the reduced rate of 12.9% would be used - as resulting from the aforementioned calculation.

On April 30, 2012, the Bank's Board of Directors resolved, after approval by the Bank Audit Committee, to approve a plan for award of 238,333 option warrants to an officer who was hired by the Bank in March 2012. The option plan is based on the principles of the stock option plan for VPs at the Bank. For further information, see Note 16.A. to the financial statements.

Business Strategy

On July 23, 2012 the Bank's Board of Directors approved a new strategic plan for 2013-2017, based on the following principles:

- The target set in the plan is to present, in 2017, an average net operating profit return on equity of 17%, based on the target core capital ratio of 7.5%.
- The Bank Board of Directors instructed the Bank to bring forward implementation of the Supervisor of Banks' directive dated March 28, 2012, whereby the Bank should adopt by December 31, 2014 a target core capital ratio of no less than 9%, to be applied, if possible, as from January 1, 2014. Moreover, the Board of Directors has resolved to instruct Bank management to maintain, in as much as possible, appropriate safety margins to this end. The core capital ratio will be calculated based on Basel III directives with adjustments to be specified by the Supervisor of Banks. Consequently, the average equity basis used for Bank operations would be increased, therefore, arithmetically, any given profit would result in a lower return figure. Accordingly, the target average net operating profit return on equity, adjusted for the regulatory requirement for core capital ratio of 9% or higher, would be 14.5% in 2017. In comparison, this return on equity is equivalent to 17% based on regulatory capital requirements during the term of the current strategic plan.
- During this strategic plan, the dividend distribution policy adopted by the Bank would be maintained, whereby, subject to the Bank’s core capital ratio being no less than the target set by the Board of Directors, the Bank would distribute annually dividends equal to 40% of net operating profit and 80% of profit from extraordinary items.

Forecasts and Assessments with Regard to Bank Group Business

The Bank bases its new five-year plan on several major goals and efforts in the following areas:
- Maintain the Bank's position as a leader in the mortgage market.
- Further increase in the Bank's market share of the household segment, reinforcing the service concept derived from Hybrid Banking and operation of the Bank's LIVE branches.
- Position the Bank as a key service provider to small and medium businesses.
- Expand the business client base and form unique value propositions, in line with needs of such clients.
- Increase the Bank's market share of deposits from the public.
- Continue establishing the Bank's leadership position in currency markets and expand Bank market share in this segment.

Growth engines for achieving the goals of the new multi-annual strategic plans are:
- Maintain the operating efficiency ratio (total expenses to total revenues), and take steps to improve it to less than 55%.
- Reinforce capital management capacity and prepare for issuing complex, innovative capital instruments.
- Reinforcing risk management capacity, by applying advanced risk pricing models (application of these advanced models was not taken into consideration for compliance with objectives of the new strategic plan).

- Foster a service-oriented organizational culture.
- Take further steps to continue organizational growth of the Bank's core operations, at a higher rate than for all of the banking system, similar to the Bank's achievements over the past 8 years.

The growth engines are aimed to have Bank revenues grow at an average annual rate of over 8% (though not in linear fashion), while maintaining expenses at a moderate annual growth rate of 4.5% (also not in linear fashion).
The Bank bases its new multi-annual strategic plan, inter alia, on the following efforts: reinforcing the Bank's position as an efficient, service-oriented bank which controls expenses, constantly improves as part of the organizational culture, a new performance-based remuneration plan which is being prepared by the Bank, continued expansion of activity of the Back-office Operations Division, transferring additional logistics and operations activities from the branches to this Division, improved efficiency of the IT Department and continued activity by Bank Yahav on development of price-focused banking service, offering an appropriate service alternative.

The aforementioned plan is a strategic plan which specifies Bank objectives for the next five years, and does not constitute a forecast or assessment with regard to achievement of these objectives; as such, by its nature, the strategic plan may not materialize. Moreover and without derogating from the generality of the aforesaid, in as much as this plan includes forward-looking information, as defined in the Securities Act, 1968, this information is based on assumptions, facts and data (hereinafter jointly: "assumptions") brought before the Bank Board of Directors, including: Absence of change in legislation and regulatory provisions which would impact the business environment, absence of geo-political developments and changes which would change or impact the business environment, stabilization of the global economy in coming years at negligent growth rates in per-capita GDP (following the global economic slow-down in recent years), growth of Israeli economy in coming years by an average 3.5% or higher, higher prices in Israeli economy in coming years at a rate not to exceed the known Government-set target, and an interest environment which reflect such target. These assumptions may fail to materialize due to factors other than under the Bank's control, which may affect the aforementioned issues and cause the strategic plan not to materialize. The influencing factors include forecasts on various matters related to economic developments in Israel and internationally, especially the state of the economy, including macroeconomic and geopolitical conditions, and the currency market and capital market, other factors that impact the exposure to financial risk, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, aspects related to the Bank's image, technological developments and manpower matters.
The Board of Directors will monitor execution of the strategic plan, and may make changes to this plan from time to time, as required, including due to changes in factors which may affect the plan, as described above.

Marketing Operations

The Bank's marketing activities and its marketing strategy are derived from the Bank's strategic plan. Marketing channels used by the Bank to base the strategic plan there upon, include: the nation-wide branch network, business center branches, business centers, professional headquarters units and LIVE branches.

Marketing strategy

The marketing strategy derives from growth and profitability targets that were prescribed within the scope of the Bank’s business plan, which is based on achieving the goals provided below:

- Increase the Bank's share of the retail market, by expansion of the customer base, in particular growth in the total number of customers in the Bank's household segment, while focusing on profitable target groups.
- Increase the Bank's share of small to medium business clients.
- Expansion of client activities with the Bank, along with increase in average revenue per client, focusing on mortgage clients, household clients, clients of significant financial means and clients with potential future profitability, such as military staff and students, and turning secondary clients into primary clients.
- The increase in average revenue per client would be achieved, inter alia, by better aligning financial products with client needs, increasing the number of products per client, enhancing use of existing products and by using advanced marketing tools to prevent a decrease in volume of activity, increasing loyalty of existing clients, preserving and increasing the volume of their financial activity and preventing churn.
- Maintain the Group's market share in mortgages, and maintain the Group's positioning as leader in this area and continue to reinforce expertise of the Bank's staff in this field.
- Leverage the extensive client base for mortgages to promote further growth of retail banking.

In order to further establish the Bank as a differentiated component of the banking system, to improve the client experience at the Bank and to achieve business targets as described, in 2012 the Bank deployed Hybrid Banking - a unique way to provide high-quality and highly available service to Bank clients.

In order to achieve these objectives of the marketing plan, the Bank operates based on the following principles and means:

- Focus the Bank on quality of service provided to its client base through Hybrid Banking, making the service component into a comprehensive client experience - a key component of Bank operations vis-a-vis clients.
- Intensive client awareness and communicating the existing benefit in the combination of retail banking and mortgage banking to clients, employees and the general public. This combination enables the Bank to offer customers a broader range of solutions under one roof, and to provide better service.
- Total financial viewpoint, placing the customer and his current account in the center, with the Bank offering other value propositions, which provide real added value to the customer in various areas, including: Investment management, retail credit products, credit cards, mortgage and pension advisory service.

- Offer innovative products and services based on client needs, by applying professional analysis of needs and price-performance considerations with regard to the client.
- Use a distinctive and differentiating media language to base the Bank's position as a desired, preferred brand.

  In 2012, the Bank took further action to establish Hybrid Banking as a differentiating tool. To this end, the Bank undertook marketing and media steps to highlight Hybrid Banking as Mizrahi-Tefahot's way to provide the highest standard of service in the banking system.

In 2012 the Bank also reinforced its activity in the student segment, with the understanding that this is a high-quality segment representing potential future profit for the Bank. In order to do so, the Bank opened a new Mizrahi-Tefahot LIVE branch, branded "Students LIVE", which specializes in providing personal banking service to appropriate for the student segment.

As for deposits, the Bank continued to establish its unique marketing media "fruit language" to promote further growth in this area.

As for small businesses, the Bank conducted activity focused on credit - in view of the Bank being awarded the Government-guaranteed credit tender.

As for mortgages, the Bank further reinforced its expertise perception through marketing and media activity in the "experts" domain and by providing attractive value propositions to clients.

Based on market research conducted by the Bank, one may deduce that these Bank activities have impacted banking in Israel as follows:

- Mizrahi-Tefahot now has an image perception advantage over its competitors in the public's mind, and is perceived by the public at large as the most different bank in the Israeli banking system.
- Mizrahi-Tefahot's potential market share is significantly higher than its reported market share - which means there are many potential clients interested in joining the Mizrahi-Tefahot family.
- The Tefahot brand is the leading mortgage-related brand.

Over many years, the Mizrahi-Tefahot brand has been grown from the bottom up, making sure that each product supports the basic tenets which guide the Bank - a professional, personal, human, innovative bank - in order to create clear differentiation.

Marketing products and tools

- To strengthen and set apart the Mizrahi-Tefahot brand and to build an outstanding, differentiating competitive positioning intended to give the Bank a leading position in the current and future competitive arena.
- The brand-related positioning activities include use of mass media, internet media and regional promotional activities intended to create an image effect, to raise the public's awareness of the Bank and to fortify the Bank's positioning and values.
- Create a marketing strategy for major Group brands, such as Mizrahi-Tefahot using the concept "Handling peoples' money", the Tefahot brand using "the mortgage experts", the investment world using "the professionals", "executive account", "the Card" - the first ever credit card in Israel which is a bank customer club, and Mizrahi-Tefahot Live, a unique banking service based on a back-office branch.

- Develop the client experience for all Bank clients in all branches and sectors, and contact potential clients for recruitment.
- Nurture and preserve current customers in the strategic target audience, and intensify activities with them. Activity among existing customers is based mainly on retaining and intensifying activities of the share of retail and business clients, formulating unique offers with value and developing a service policy that supports the positioning and needs of the customer and aids in improving customer satisfaction over time, thereby helping to achieve the growth, profitability and preservation objectives which the Bank had set for itself.
- Further position Tefahot as the mortgage experts and foster synergy between Mizrahi-Tefahot and Tefahot while intensifying the link.
- Establish "The Card" - Mizrahi-Tefahot's credit card - as a unique loyalty club with added value reflected by attractive value propositions in both banking and non-banking fields.
- Develop digital capabilities by upgrading the Bank's cellular application for various platforms, and continued improvement of marketing communications capabilities in this area.
- Development of appropriate infrastructure, in order to enable the required marketing activity, centered on approaching each client with the suitable value proposition, at the right time, using the right channel and message for the client. Infrastructure development primarily includes constant improvement of getting to know the clients using the enterprise data warehouse (DWH) and continued development and improvement of Client Relationship Management (CRM) systems. These activities help the Bank to provide better service and to offer more focused value propositions through the Bank's improved value proposition system.

Sources and financing

Group financing sources include: deposits from the public and from banking institutions, including by means of credit obtained from the Bank of Israel; issuance of obligatory notes; various debentures; and shareholders' equity. The Group selects the mix of financing sources based on its business objectives, including objectives for profitability, return on equity and capital adequacy – subject to statutory limitations applicable to banking corporations and in accordance with the state of the capital market and management forecasts regarding development therein.

Deposits

The Bank distinguishes between different source types by type of clients. The Bank examines the degree of concentration of the depositors, and within this framework, management has specified guidelines with regard to holding of liquid resources against large depositors. Furthermore, guidelines have been specified with regard to the ratio of volatile deposits to total deposits. These guidelines are part of the liquidity risk management system.

Total deposits from the public for the Group as of December 31, 2012 amounted to NIS 128.5 billion, compared to NIS 119.2 billion at end of 2011. Deposits from the public in the NIS-denominated, non-CPI linked segment increased in 2012 by 15.0%; deposits in the CPI-linked segment decreased by 5.3%; and deposits denominated in or linked to foreign currency decreased by 1.6% - for details see chapter "Development of balance sheet items" above.

Bank of Israel

The Bank of Israel serves as a key party for the short-term financing and absorbing money for the entire banking system, and for Mizrahi Bank in particular. It should be noted that a bank that borrows money from the Bank of Israel must provide collateral, and the Bank takes this parameter into account in its day-to-day management of liquidity.

Another source for raising short-term funds is the inter-bank money market.

Among the factors influencing the scope and types of deposits in the banking system is the monetary policy of the Bank of Israel. Below is a survey of the monetary tools used by the Bank of Israel for the purpose of implementing its monetary policy:

Bank of Israel interest rate - The Bank of Israel publishes monthly the interest rate for the following month. This interest constitutes the base interest rate for tenders on loans and deposits made available to the banking system, as will be provided below.

Liquidity requirement - The directives of the Bank of Israel require banks to hold liquid balances for deposits from the public, at varying percentages, according to the period of the deposit. The required liquidity percentages are presently 6% on demand deposits and 3% on time deposits of one week to one year. In deposits for periods of one year or more, there is no liquidity requirement. As from late January 2011, the Bank of Israel imposed a new liquidity requirement with respect to currency swap transactions and FOREX futures transactions with foreign residents, including foreign banks. See the chapter on risk management for information on the management of liquidity risk by the Bank.

Deposits with Bank of Israel to absorb excess liquidity - When there is excess liquidity in the system, the Bank of Israel absorbs it through tenders on deposits that it makes available to the banking system. The deposit tenders are for a short term of 1,7 or 30 days. The maximum interest rate for these tenders is the stated interest rate of the Bank of Israel. Moreover, there is a window for depositing daily deposits in the Bank of Israel, unlimited in amount, at interest that is 0.50% lower than the Bank of Israel interest rate. In 2012, the banking system - including the Bank - had excess liquidity, and throughout the year, the Bank of Israel offered deposit tenders for terms of one day / week . month in order to absorb this excess.

Short-term Government debentures (MAKAM) - Another financial instrument used to absorb surplus shekel liquidity is the short-term Government debenture (MAKAM), through regular issuances to the public and the activity of the Bank of Israel in the secondary market.

Tools for injecting liquidity into the system:

Loan tenders - For the purpose of injecting liquidity into the banking system, the Bank of Israel makes available short-term credit tenders for 1-7 days, in which the minimum interest is the Bank of Israel interest. Moreover, the Bank of Israel provides a daily credit window at interest that is 0.5% higher than the Bank of Israel interest. Receipt of credit from the Bank of Israel, whether through the credit tender or the credit window, is limited to the collateral amount that each bank has in the Bank of Israel.

Real Time Gross Settlement (RTGS) system - the RTGS system allows clients to transfer in real time NIS-denominated amounts from an account at one bank to an account at another bank. Settlement is immediate and final.

Obligatory notes and debentures issued to the public

Obligatory notes

The Bank is acting to raise long-term sources via issuances, inter alia via Mizrahi Tefahot Issuance Company Ltd. ("Tefahot Issue"), a wholly-owned subsidiary of the Bank. Over the years, Tefahot Issue Company issued subordinated notes to the public under published prospectuses.

As of the date of the financial statements, total obligatory notes (Series 26-35), including subordinated notes, issued to the public by Tefahot Issuance amounted to NIS 8,928 million par value (as of December 31, 2011 - NIS 6,871 million), of which NIS 2,131 million in subordinated notes (as of December 31, 2011 - NIS 2,131 million).

On February 25, 2011, Tefahot Issuance issued a shelf prospectus for issuance of up to 10 series of subordinated notes, 10 series of debentures, extension of subordinate notes (Series 31), extension of debentures (Series 29 and Series 32) as well as issuance of two series of commercial paper.

In 2012, Tefahot Issuance issued obligatory notes amounting to NIS 2,057 million par value for consideration amounting to NIS 2,161 million, pursuant to a shelf prospectus dated February 25, 2011.

On January 21, 2013, Tefahot Issuance issued debentures (Series 29 and Series 35), with total par value of NIS 1,305 million for consideration of NIS 1,509 million.

Complex capital instruments

In November 2006, the Bank raised, in a private placement to institutional investors, the sum of NIS 451 million (NIS 460 million par value) via issuance of subordinated notes (Series A), that will be deemed Upper Tier II capital for maintaining a minimum capital ratio. On May 21, 2007 the Bank published a prospectus under which the complex capital instruments were listed for trading in early June 2007. Starting in June 2007 and through publication of these financial statements, the Bank issued and listed for trading additional complex capital instruments amounting to NIS 1,242 million par value in exchange for NIS 1,193 million in proceeds.

All of the Bank's complex capital instruments (Series A) as of December 31, 2012, issued and listed for trading amounted to NIS 1,702 million par value, issued for consideration amounting to NIS 1,644 million.
The revalued balance of the complex capital instruments as of December 31, 2012 was NIS 1.9 billion, similar to 2011. See Note 14 to the financial statements for details.

Rating of Bank obligations

In accordance with rating provided by Maalot Standard & Poor's (hereinafter: "Maalot"), the Bank's issuer rating, including deposits deposited with the Bank, is AA+, unchanged since the Bank was first rated in 2003.
On January 13, 2013, Maalot confirmed the Bank's issuer rating and its Stable rating outlook. According to Maalot: "The Bank's rating reflects its strong business position in the Israeli banking system, which accounts for its system-wide importance, as reflected in the support reflected by the final rating, good credit quality and a diverse, stable base of retail sources... The stable rating outlook reflects our assessment that Mizrahi-Tefahot would maintain its business position and appropriate risk profile, even should the Israeli economy come under certain pressures over the short to medium term. We believe that these pressures would not significantly impact the Bank's profitability or capital base..."
The rating of subordinated notes issued by Tefahot Issuance remained one rank below the issuer rating, i.e. rated ilAA.
The complex capital instruments, which constitute upper Tier II capital, are rated ilA+.
On January 3, 2013, Moody's rating agency maintained the Bank's long-term deposit rating at A2 with negative rating outlook.

Adjustable rate credit

A significant part of the credit loans issued by the Bank are at adjustable interest rates. In the non-linked shekel sector, the variable-interest loans are issued based on the changes in the prime interest rate. The prime interest rate is based on the Bank of Israel interest plus 1.5%, and if this ratio changes, the Bank is permitted to change the method for determining the variable interest accordingly. The prime interest rate could change every month, according to a decision by the Governor of the Bank of Israel on a change in the monetary interest.
This year, the Bank also started granting NIS-denominated mortgages bearing variable interest varying at 5 year intervals, with the interest rate update mechanism ("anchor") based on NIS-denominated Government debentures bearing fixed interest.
In the CPI-linked sector, most variable-interest loans are mortgages, with various frequencies for interest rate updates: 1 year, 2.5 years, 5 years, 7 years and 10 years. The interest rate update mechanism ("anchor") is based on CPI-linked Government debentures.
In the foreign currency (and/or foreign currency linked) segment, most of the loans are at adjustable rates, varying with changes in the LIBOR interest rates. The commonly used periods are 1-month LIBOR and 3-month LIBOR.

Risk Management

Basel II: Pillar 3 - Market Discipline

Below is qualitative information and quantitative data related to all risk factors to which the Bank is exposed, which are managed in line with the policy set by the Board of Directors. The information has been compiled in accordance with disclosure requirements of Basel II recommendations, Pillar 3, as applied to banks by Public Reporting Directives, and in accordance with the directive on qualitative reporting with regard to exposure to and management of market risk.

Below are references to information required pursuant to reporting directives of the Bank of Israel, included below and elsewhere in these financial statements:

Subject	Disclosure	Chapter in Board of Directors' Report / Note to financial statements
Application scope	Group entities, consolidation basis, limits on supervisory capital	Risk Management chapter
Capital structure	Key attributes of equity instruments	Note 14 – Capital Adequacy
	Details of capital components	Note 14 – Capital Adequacy
Capital adequacy	Qualitative and quantitative disclosure	Risk Management chapter
	Capital adequacy ratios for the Group	Note 14 – Capital Adequacy
Credit risk	Qualitative and quantitative disclosure	Risk Management chapter
	Credit risk exposure by economic sector	Management Discussion, Addendum E - Credit Risk by Economic Sector
	Credit risk exposure by contractual term to maturity	Risk Management chapter
	Credit risk exposure by major geographic regions	Management Discussion, Addendum F - Exposure to Foreign Countries
	Information about troubled debt	Note 4 - Loans to the Public
	Provision for credit loss by economic sector	Management Discussion, Addendum E - Credit Risk by Economic Sector
	Credit loss with respect to housing loans	Risk Management chapter
Credit risk mitigation	Qualitative and quantitative disclosure	Risk Management chapter
Counter-party credit risk	Qualitative and quantitative disclosure	Risk Management chapter
Securitization		Risk Management chapter
Market risk, liquidity risk, interest risk in bank portfolio	Qualitative and quantitative disclosure	Risk Management chapter
Operating risk	Qualitative disclosure	Risk Management chapter
Equity positions in bank portfolio	Qualitative and quantitative disclosure	Risk Management chapter
	Accounting policy	Note 1 - Reporting Principles and Accounting Policies
Legal risk	Qualitative and quantitative disclosure	Risk Management chapter
Risk factors	Qualitative and quantitative disclosure	Risk Management chapter

Application scope

Provisions of Proper Conduct of Banking Business Regulations nos. 201-211 "Measurement and Capital Adequacy" apply to the Bank Group and in particular to the Bank - Bank Mizrahi-Tefahot Ltd. - the parent company of the Group. Group companies to which the framework applies, in accordance with the supervisory consolidation basis, are the companies consolidated with the Bank's consolidated financial statements. For details of Bank Group companies, see Note 6 to the financial statements.

To the best knowledge of Bank management, and relying on legal counsel, there are no prohibitions or significant restrictions on transfer of funds or supervisory capital between Bank Group companies.

Capital adequacy

The Bank assesses its capital adequacy in accordance with Basel I rules, as set forth in Proper Conduct of Banking Business Directive Nos. 201-211. Key rules and approaches applied by the Bank are described above, under Description of Basel II Guidelines in the chapter on Legislation and Supervision of Bank Group Operations. The Bank applies the standard approach to assess exposure to credit risk, the basic indicator approach to assess exposure to operating risk, and the standard approach to assess exposure to market risk. The Supervisor of Banks has stipulated that within 3 years from the start date of applying the basic indicator approach to assessment of exposure to operating risk, banks must transition to using the standard approach. Consequently, as from January 1, 2013, the Bank would evaluate its initial risk exposure using the standard approach. The Bank started in 2012 to develop a use test process for advanced credit risk management models (IRB). In 2013 the bank decided to stop development of advanced models and to transit the project to maintain status which will reserve the development. Especially in the mortage sector, a primary component in the bank's loan portfolio.

The Bank regularly monitors its capital adequacy ratio, in order to ensure compliance with requirements of the Supervisor of Banks and with limitations set by the Board of Directors, as well as to prepare in advance to respond to evolution of risk assets and capital requirements at the Bank. For this purpose, the Board of Directors has created an internal procedure which specifies the measurement frequency of capital adequacy, the required reporting and actions to be taken if the capital ratio drops below the minimum levels specified; a capital planning and management forum has been created, attended by the Manager, Finance Division - CFO (chair), Risk Control Division - CRO, and the Manager, Accounting and Financial Reporting Division - the Chief Accountant and the Manager, Planning and Operations Division.

For further details of the Bank's capital adequacy ratio, see reference in chapter "Legislation and Supervision of Bank Group Operations".

For details of the risk adjusted capital ratio, see Note 14 to the financial statements.

Composition of risk assets and capital requirements with respect to credit risk by exposure group are as follows:

	As of December 31, 2012		As of December 31, 2011	
Exposure group	Weighted risk asset balances	Capital requirement(1)	Weighted risk asset balances	Capital requirement(1)
Sovereign debt	565	51	924	83
Public sector entity debt	374	34	350	32
Banking corporation debt	927	83	1,824	164
Corporate debt	39,572	3,561	39,107	3,520
Debt secured by commercial real estate	2,194	197	1,718	155
Retail exposure to individuals	11,585	1,043	11,265	1,014
Loans to small businesses	2,213	199	2,172	195
Residential mortgages	37,396	3,366	32,865	2,958
Securitization	-	-	88	8
Other assets	3,910	352	2,660	239
Total	**98,736**	**8,886**	**92,973**	**8,368**

(1) Capital requirement calculated at 9% of risk asset balance, in accordance with interim directive on application of Basel II, Pillar 3.

Risk assets and capital requirements with respect to market risk and operating risk are as follows:

	As of December 31, 2012		As of December 31, 2011	
	Weighted risk asset balances	Capital requirement(1)	Weighted risk asset balances	Capital requirement(1)
Market risk	1,119	101	947	85
Operating Risk(2)	7,093	638	7,851	707
Total	**8,212**	**739**	**8,798**	**792**

(1) Capital requirement calculated at 9% of risk asset balance, in accordance with interim directive on application of Basel II, Pillar 3.
(2) Pursuant to proper conduct of banking business Regulation 206, calculated based the standard approach (as of December 31, 2011 based on the basic indicator approach)

Development in percentages of Group ratio of capital to risk elements is as follows:

		Ratio of capital to risk elements
		As of December 31
	2011	2012
	Reported	
Ratio of Tier I capital to risk elements	8.55	7.77
Ratio of total capital to risk elements	13.35	13.40
Total minimum capital ratio required by the Supervisor of Banks	9.00	9.00

Risk exposure and assessment there of

Day-to-day activities in a variety of balance sheet and off-balance-sheet financial instruments expose the Group to risk, mainly – market and liquidity risk, credit risk, and operating risk. The risk management policy, in various aspects, is designed to support achievement of the Group's business goals while limiting exposure to such risk.

Risk management at the Group is conducted regularly in accordance with Proper Conduct of Banking Business Regulation 339 of the Bank of Israel, and in accordance with the framework specified in Basel II, Pillar 2. In December 2012 The bank of Israel issued proper conduct of Banking Business Regulations 350, 310 and 311 about Risk management. Also conduct 313 was updated.For additional details see chapter "legislation and supervision of bank group Operations". To this end, the Group appointed risk managers, as well as the CRO - who is the Risk Control Division Manager. Bank management regards the Bank's risk control and management system as one of its core competencies, so that it is the Bank's policy to constantly strive to improve the risk control and management system,

The Bank's management believes that risk control and management must be an integrative process. The management of risk from a total viewpoint, for all of the Bank's financial activity, on and off-balance sheet, enables the Bank to maximize the utilization of the correlation between the different risk factors (basis and interest) in the various linkage segments, and the best possible diversification of the risk. In addition to measuring the total risk value, the Bank measures and manages the mix of risk elements.

The Bank has put in place an organization in which risk management and control for the group is composed of 5 major layers:

Board of Directors - Sets Bank policy on risk and capital management, including approval of risk appetite and limitations, approval of business objectives and setting the strategic plan, as well as the risk profile derived there from. The Board of Directors approves the risk and capital management policy and monitors its implementation.

Management - committed to identification and management of material risk to which the Bank is exposed (each Risk Owner in its own area). Management is tasked with setting policy for management of each risk factor, determination of the Bank's position with regard to capital requirements for each risk factor, and development of strategies and tools for risk mitigation and for reducing potential damage.

Business units - these risk-taking units are at the forefront of risk management, and use tools and procedures for on-going risk management.

CRO - in 2011, the Bank established a dedicated division for risk control. The Risk Control Division Manager is the Bank's Chief Risk Officer (CRO). The Risk Control Division is the central line for risk control operations, using dedicated systems (sometimes different than those used by the business units) and procedures. The Division uses monitoring tools as close as possible to operations of the business units and to the risk-taking events. These include intraday monitoring tools, as described below.

Internal Audit - forms another layer for tracking and monitoring risk level. Internal Audit operations usually take place after risk has been taken. Internal Audit, using the tools in its use, acts independently to map and assess the risk level at the various units.

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The list of material risk factors identified by the Bank, and executives appointed as Risk Owner for each one, are as follows:

Risk type	Risk owner
Credit (including CRM and environmental risk)	Manager, Business Division
Counter-party, derivatives and counter-party, sovereigns and banks	Manager, Financial Division
Credit concentration	Manager, Business Division
Securitization(1)	Manager, Financial Division
Market (including concentration)	Manager, Financial Division
Interest in bank portfolio	Manager, Financial Division
Liquidity (including concentration)	Manager, Financial Division
Operating (including concentration)	Manager, Risk Control Division
Model	Manager, Risk Control Division
Clearance	Manager, Financial Division
Goodwill	Manager, Marketing and Advertising Division
Regulatory	Management, each in their own domain
Legal	Chief Legal Counsel
Compliance	Manager, Risk Control Division
Prohibition of money laundering	Manager, Risk Control Division
Information Technology	Manager, Information Technology Division
Human Resources	Manager, Human Resources and Administration Division
Business and Strategy	President

(1) The bank has no securitization operations; therefore securitization risk has been defined by the Bank as a non-material risk.

Credit risk

Credit risk is the risk of the Bank incurring a loss due to the counter party to a transaction potentially failing to meet their commitments. This risk may arise from multiple factors which may impact the entire loan portfolio, a specific sector or an individual client. These risk factors include, inter alia, macro-economic changes, business risk arising from client operations, credit concentration risk etc.

The Bank's Board of Directors has defined the credit policy, including the Bank's risk appetite for sectors, borrower groups, mortgages etc. The limitations specified under risk appetite are monitored at the frequency specified under the credit policy, and compliance with these limitations is reported to the Bank's Board of Directors and management. Monitoring is performed by the business units and by the Risk Control Division.

The Bank has approved a dedicated policy on credit concentration risk, in which it has specified the risk appetite in this area and specified methodology for measurement, control and reporting. Bank policy with regard to credit is based upon the Bank's objectives and business strategy, emphasizing macro-economic changes in Israel and overseas and the implications there of on credit risk.

The Bank’s credit policies prescribe principles and rules for making credit available and for the management and control over the loan portfolio, in order to preserve its quality and reduce the inherent risk. These principles and rules enable controlled management of the risk involved in granting loans to borrowers, at the level of the individual borrower, group of borrowers and the level of economic and business sectors. The credit policy is reviewed during the year, in view of developments in the business environment in which the Bank and the Bank's clients operate.

In December 2012 The bank of Israel issued proposed conduct of banking business 311 about credit risk management. For additional details see chapter "Legislation and Supervision of bank group Operations"

Quantitative components of Basel II, and to an even greater extent, its qualitative components, significantly affect how credit risk is managed at the Bank, in particular the ICAAP process conducted in conjunction with Basel II, Pillar 2. The ICAAP process reviews credit risk management processes, including setting of credit policy and specification of risk appetite, in view of the Bank's risk profile.

Group operations with regard to credit to the public are managed by several key segments, which differ in client attributes and types of banking services these clients require, as well as in the organizational unit responsible for handling each client type:

- The Household segment, Small Business segment and mortgage operations are under the responsibility of the Retail Division.
- The Commercial Banking segment and Business Banking segment are under the responsibility of the Business Division.
- Clients of international operations are under the responsibility of the International Operations sector of the Financial Division.

For details of client attributes in each segment, see chapter on Description of Bank Group Business by Operating Segment and chapter on International Operations.

As part of the credit granting process, transaction data is reviewed in accordance with criteria stipulated by the Bank. The decision making process for granting credit is hierarchical, from branch level to Board of Directors level. Each unit which provides credit monitors on a regular basis credit repayment in accordance with terms agreed as well as the financial status of the client, based on their level of indebtedness. Any findings requiring action are reported to the entity in charge of the relevant credit.

The Bank operates on multiple levels to monitor and mitigate credit risk in as much as possible, from the credit approval stage, required collateral and financial covenants specified in accordance with procedures, authorization and diversification policy specified by the Bank, through to regular control by business units and dedicated control units. This is done with constant effort invested in improving the professional expertise of those involved with credit, by means of baking courses and training, as well as professional seminars at all levels. Concurrently, the Bank invests extensive resources in improving its control mechanisms and IT systems available to decision makers in the credit sector.

Considerations in extending credit – The considerations involved in granting credit are based mainly on the quality of the client, his reliability, financial strength, liquidity, repayment ability, seniority in the industry, length of time with the Bank, behavior in the account and on the quality of the collateral, as described below. Likewise, the Bank works to match credit type and terms to client needs. In cases in which loans are issued based solely on the quality of the borrower, without a collateral requirement, certain contingencies are set at times, including compliance with financial covenants.

Procedures - Procedures for granting credit and for processing credit and collateral, as well as the relevant IT systems there for, are regularly reviewed and updated to adapt them to the changing business environment, while learning lessons from different events.

Risk diversification - The Bank's credit policies are based on diversification and controlled management of risk. Risk diversification is characterized by several aspects: Diversification of the loan portfolio across economic sectors, including increased exposure to specific sectors, diversification across client size groups, diversification across different linkage bases, geographic diversification if applicable (construction sector, mortgages). For details on concentration risk management, see below.

Authority to grant credit – In order to streamline the decision-making process as it relates to granting credit while minimizing risk, a ranking of authority was determined for officers and credit committees at different levels, up to the level of the Board of Directors and its Credit Committee.
Credit-granting decisions, beginning from the district level, are made by credit committees in order to minimize the risk in relying on the judgment of a single individual. The credit authorizations include limitations on credit limit as well as on the percentage of unsecured credit that each authorized official is permitted to approve, and other guidelines were prescribed relating to the prerogative to exercise authority in certain situations.

Currency exposure in credit - Borrowers with currency exposure are offered means of safety and protection (hedging transactions) in order to reduce their exposure, in addition to other measures that the Bank adopts to minimize the risk of the Bank's exposure from the activities of these customers. Guidelines were prescribed to intensify the monitoring, control, and supervision of the activities of borrowers whose debts to the Bank are sensitive to exchange rate fluctuations, including the creation of simulations and future scenarios of changes in exchange rates. Special controls are also used for clients, when securities form a significant element of their collateral.

Credit in the construction and real estate sectors - In financing the construction and real estate industry, specific analysis and monitoring tools are used to assist the Bank in reaching decisions on the granting of financial support to the various projects. Construction financing in this industry is focused mainly on residential construction in areas with strong demand and mid-level prices. In addition, the financing is allocated between geographic regions, based inter alia on relevant demand.
In providing credit for construction, the Bank focuses on the financial support method (closed assistance). The application of this method is designed to reduce the exposure to risk in the granting of the loans, because it incorporates current and close monitoring of the progress of the financed project, both before the loans are provided, and as the project receives the financial support, while maintaining a distinction between the financed projects and the business risk inherent in the other activities of the developer-borrower. The Bank is assisted by outside construction supervisors, and also relies on liens on the land in the project, to secure the loans. Loans are issued for financed projects only by branches with professional knowledge of the subject, and under the supervision of the regional affiliates of the construction and real estate sector.

Borrower rating - The Bank has developed a system for rating business borrowers, based on a computerized testing model that combines quantitative and qualitative assessments of borrower, which has been adapted for a range of business borrowers according to various economic sectors. The Bank regularly maintains the different existing models and develops new models, and acts to adapt, update and improve them in line with changes in the business environment.
This system is used for most of the Bank’s business loans. The objective of the system is to provide for credit risk management and to support decision making processes. The system determines the rating of a borrower as a function of the quality of the client, the collateral furnished and the amount of credit received.

Monitoring and control - Control over credit operations is a key component in maintaining quality of credit extended by the Bank to clients, including maintaining the quality and position of collateral required to secure credit. The Bank continuously acts to identify and locate, as soon as possible, any indications of impairment of borrowers' repayment capacity or any deterioration in the state of their collateral, in order to avoid potential credit failure. The Bank applies different control mechanisms, some of which are internal controls within the credit management chain, which are regularly conducted by branches, regions, headquarters and specific units involved there with, and some - controls by entities external to the credit process.
The control mechanisms at branches, regions and headquarters are based on Bank procedures as well as internal procedures of these units, and are regularly followed as part of the normal business routine of the various levels. Each credit level controls the relevant credit decisions of those levels reporting to it, as well as the current credit behavior of these clients.
Additional controls are implemented by headquarter units of the Business Division, at different frequencies, by different entities which report to the supervisors there of. There are lateral identification and control processes in place, along with specific processes adapted to each sector's unique operations.
Furthermore, the Mortgage sector conducts an internal review process aimed at identifying faults and weaknesses soon after they actually occur. The process is designed to draw attention of the relevant entities to quality of work at the branch, quality of underwriting and adherence to procedures and regulations.

Concurrently, control is exercised by dedicated Bank units. The Business Credit Control Department, of the Business Division, uses computer systems to discover and alert to unusual accounts and clients, including based on information external to the Bank. Control is applied to banking operations in accounts flagged due to risk indications, based on criteria specified by the Bank for the population under control, as well as for all Bank clients by means of IT systems which provide alerts and report notifications and unusual occurrences. In the Real Estate sector, a dedicated control unit operates to control and review various aspects with regard to handling of real estate transactions by the Bank. In the Mortgage sector, a nation-wide underwriting center operates to enhance control of complex loan approval or of special populations, where loan approvals are provided by a professional, specialized team working at the Mortgage headquarters. In addition, both the Business Division and the Retail Division include division controllers, who perform various controls at division level, including responsibility for watch lists.
In June 2012, as part of reorganization of the Risk Control Division, the Division assumed responsibility for the Analysis Department, which provides independent review of major credit applications, presenting its recommendations as part of the credit approval process to senior forums at the Bank.

The Risk Control Division is a control entity for credit risk within the second defensive line. The Analysis Department participates in approval of credit applications - as an independent entity. The Department reviews all credit applications discussed by the Business Division's credit committee, by the Supreme Credit Committee and by the Board of Directors' Credit Committee - providing its independent opinion with regard to such applications. The analysis recommendations include a recommendation as to actual approval of the application, and as to any further conditions or restrictions to be considered as a condition for approval of the credit application. The department representative regularly attends meetings of the aforementioned credit committees.

In addition, the Risk Control Department of the Risk Control Division controls credit risk in accordance with the Bank of Israel’s Proper Conduct of Banking Business Directive no. 319, by rating borrowers and quality of the Bank's loan portfolio, based on an annual work plan approved by the Board of Directors' Credit Committee and by the Board of Directors. This work plan regularly includes the following:

- Monitoring low-rated borrowers on criteria model or on independent rating by the Risk Control Department.
- Credit control at London and Los Angeles branches via external entities which report to and are professionally guided by the Risk Control Department in Israel.
- Credit control at the Cayman Islands branch by the Risk Control Department, in conjunction with the aforementioned work plan.
- Testing of reliability and quality of rating provided by the credit departments, with reference to quality of the model and rating results generated there by, and their implications for the Bank's loan portfolio.
- Analysis of the mortgage portfolio, including developments in extending residential credit, as well as credit breakdown by different criteria.
- Review of the Bank's loan portfolio in view of the credit policy and risk appetite limitations adopted by the Bank.

Monitoring and control systems - the Bank Group regularly uses computer systems for management and control of credit risk. These computer systems provide control tools for personnel, including the specific unit assigned with identifying and controlling credit risk, to identify loans that exceed credit limits or are under-collateralized, as well as tools for identifying credit-risk developments resulting from the existence of various parameters in client-account development and management. There are several significant systems which play an important role in processes of credit management, risk management and control, including risk management systems, systems for identifying and alerting credit risk, for providing alert information, monitoring of financial covenants, automatic debt classification system and computer system for control and management of all accounts under legal proceedings.

Handling of non-performing loans and collection of debts – The handling of problem loans requires special focus and professionalism, other than the level that approved or processed the credit extended and collateral received. Initial identification is typically computer-based by designated departments for identification and control. Identified clients are handled by the Special Client Sector of the Business Division.

In order to identify credit risk materializing, or which may materialize, at the Bank, the Bank regularly conducts a process to review and identify debt, based on specified criteria. Some of these criteria require debt to be classified as troubled debt, while others provide a warning and allow the professional entity to exercise discretion. Debt is reviewed by a ranking of authorizations specified in Bank procedures. This authorization ranking includes individual authorizations, from branch and headquarters staff, to authorizations at higher levels, granted to committees in the Accounting and Financial Reporting Division management, and senior Bank management. Concurrently with the identification and classification process, a built-in, independent control process is conducted by regional management and by designated units at headquarters.

A computer system which supports application of directive for measurement and disclosure of impaired debt, credit risk and provision of credit loss including in identification and control processes, carries out logical, criteria-based testing and determines defaults for debt classification as debt under special supervision, inferior debt, impaired debt or debt in restructuring, as required.

Identification of housing loans (mortgages) with risk attributes is automated by identifying criteria for arrears and other qualitative criteria. In early stages of arrears, the Bank mostly applies automated collection processes. Later on, the Bank applies proactive processes, both internal and external, including legal proceedings.

As a lesson learned from the most recent crisis in global financial markets, in 2008-2009, the Bank enhanced testing and control of exposure, including with regard to exposure of Bank clients to entities and countries undergoing a financial crisis, or any other specific risk. Furthermore, the Bank regularly monitors its exposure to foreign financial institutions, inter alia in accordance with directives of the Supervisor of Banks.

Provision for credit loss - upon application of the new directive for measurement and disclosure of impaired debt, credit risk and provision for credit loss on January 1, 2011, the Bank implemented a computer system for identification and classification of debt where risk of credit loss exists or may emerge. The system is connected to various infrastructure systems at the Bank, combining data to allow for debt review designed to assess their robustness and their expected cash flows. The new system applies automated processes for identification, review, classification and determination of provisions, including process documentation and hierarchical approvals based on authorities set forth in Bank procedures. The system also allows for handling troubled debt not identified by the automated identification processes, but rather using qualitative tests of the Bank's loan portfolio.

The decision about the amount of provision for credit loss is derived from the quality of credit and collateral, the financial and legal standing of the borrower and guarantors, as well as environmental and sector conditions in the client environment.

For further details of the new directives and their effect on financial statements, see Note 1.J. to the financial statements.

Environmental risk - In recent years, global awareness of the potential financial exposure arising from regulations related to environmental protection has grown. Environmental risk to the Bank is the risk of loss which may be incurred due to the Bank being directly liable for an environmental hazard caused by a project financed by the Bank, to impairment of collateral exposed to environmental risk or to deterioration in the financial standing of a borrower due to high expenses arising from environmental protection regulation. Environmental risk also includes other risk factors derived from this risk (goodwill, third party liability etc.)

Therefore, it is of prime importance that the Bank set its policy for management of environmental risk, including the capacity to identify, assess and monitor the risk over time.

On June 11, 2009, the Bank received a letter from the Supervisor of Banks, demanding that banks act to incorporate management of exposure to environmental risk within all risk factors at the Bank, including specification of procedures for identification of significant risk when granting credit and inclusion of risk assessment within periodic assessment of quality of credit extended. The Bank is forming a dedicated environmental risk policy, including a methodology for identification, assessment and handling of environmental risk. The environmental risk policy is approved annually by the Bank Board of Directors.

Below is the composition of credit exposure by exposure group and by balance sheet item, after provision for credit loss:

	As of December 31, 2012										
	Sovereigns	Public sector	Banking corporations	Corporations	Secured by commercial real estate	Retail for individuals	Small business	Housing loans	Securitization	Others	Total (2)
Loans(3)	14,589	250	1,788	29,322	2,360	15,058	3,836	79,587	-	-	146,790
Securities(4)	6,726	13	756	240	-	-	-	-	-	-	7,735
Derivatives(5)	-	385	915	1,669	-	26	4	-	-	-	2,999
Other off-balance-sheet exposures	84	284	35	35,767	374	10,324	1,602	4,267	-	-	52,737
Other assets(6)	-	-	-	-	-	-	-	-	-	4,900	4,900
Total	**21,399**	**932**	**3,494**	**66,998**	**2,734**	**25,408**	**5,442**	**83,854**	**-**	**4,900**	**215,161**

Below is the composition of credit exposure by exposure group and by balance sheet item, before provision for credit loss(1):

	As of December 31, 2011										
	Sovereigns	Public sector	Banking corporations	Corporations	Secured by commercial real estate	Retail for individuals	Small business	Housing loans	Securitization	Others	Total (2)
Loans(3)	12,895	290	2,804	29,416	1,771	14,462	3,569	71,207	-	-	136,414
Securities(4)	6,585	17	644	386	-	-	-	-	25	-	7,657
Derivatives(5)	-	264	2,352	1,719	-	27	7	-	-	-	4,369
Other off-balance-sheet exposures	-	401	160	34,810	317	10,037	1,492	3,611	-	-	50,828
Other assets(6)	-	-	-	-	-	-	-	-	-	3,561	3,561
Total	**19,480**	**972**	**5,960**	**66,331**	**2,088**	**24,526**	**5,068**	**74,818**	**25**	**3,561**	**202,829**

(1) After deduction of accounting write-offs and before provision for credit loss on individual and group basis.
(2) Balance of on- and off-balance sheet balances, after on- and off-balance-sheet offsets, excluding impact of credit risk mitigation, conversion factors and risk weighting factors, as defined under Basel II rules.
(3) Includes credit to the public, credit to the Government, deposits with banks and borrowed securities, and excluding general provision for doubtful debts, which is part of the equity basis.
(4) Excludes balances deducted from the equity basis and investment in securities in the negotiable portfolio.
(5) Includes face value of derivatives (including credit derivatives), after effect of add-on factors and positive fair value of derivatives.
(6) Excludes derivatives and balances deducted from the equity basis, including cash, investment in shares, fixed assets and investment in investees.

Composition of credit exposure before provision for credit loss, by contractual term to maturity, by major gross credit exposure type, is as follows [(1)]:

					As of December 31, 2012
	Up to 1 year	1-5 years	Over 5 years	Without maturity	Total [(2)]
Loans [(3)]	44,052	23,536	79,097	105	146,790
Securities[(4)]	504	4,601	2,630	-	7,735
Derivatives [(5)]	1,533	549	917	-	2,999
Other off-balance-sheet exposures	43,520	8,177	1,040	-	52,737
Other assets [(6)]	3,096	-	86	1,718	4,900
Total	**92,705**	**36,863**	**83,770**	**1,823**	**215,161**

					As of December 31, 2011
	Up to 1 year	1-5 years	Over 5 years	Without maturity	Total [(2)]
Loans [(3)]	42,013	22,523	71,807	71	136,414
Securities[(4)]	1,488	4,903	1,266	-	7,657
Derivatives [(5)]	1,935	1,011	1,423	-	4,369
Other off-balance-sheet exposures	41,128	8,644	1,056	-	50,828
Other assets [(6)]	1,818	62	48	1,633	3,561
Total	**88,382**	**37,143**	**75,600**	**1,704**	**202,829**

(1) After deduction of accounting write-offs and before provision for credit loss on individual and group basis.

(2) Balance of on- and off-balance sheet balances, after on- and off-balance-sheet offsets, excluding impact of credit risk mitigation, conversion factors and risk weighting factors, as defined under Basel II rules.

(3) Includes credit to the public, credit to the Government, deposits with banks and borrowed securities,

(4) Excludes balances deducted from the equity basis and investment in securities in the negotiable portfolio.

(5) Includes face value of derivatives (including credit derivatives), after effect of add-on factors and positive fair value of derivatives.

(6) Excludes derivatives and balances deducted from the equity basis, including cash, investment in shares, fixed assets and investment in investees.

Credit risk - standard approach

Below is composition of credit exposure amounts[1] by exposure group and weighting, before and after credit risk mitigation[2]:

Before credit risk mitigation

											As of December 31, 2012
	0%	20%	35%	50%	75%	100%	150%	350%	Gross credit exposure	Deducted from equity	Total
Rated exposures:											
Sovereign debt	18,926	2,355	-	-	-	118	-	-	21,399	-	21,399
Public sector entity debt	-	-	-	920	-	-	-	-	920	-	920
Banking corporation debt	-	2,994	-	364	-	84	-	-	3,442	-	3,442
Corporate debt	-	51	-	231	-	-	-	-	282	-	282
Securitization	-	-	-	-	-	-	-	-	-	-	-
Other assets	-	-	-	-	-	-	-	-	-	33	33
Total	**18,926**	**5,400**	**-**	**1,515**	**-**	**202**	**-**	**-**	**26,043**	**33**	**26,076**
Non-rated exposures:											
Public sector entity debt	-	-	-	13	-	-	-	-	13	-	13
Banking corporation debt	-	19	-	23	-	-	-	-	42	-	42
Corporate debt	-	-	-	-	-	65,904	262	-	66,166	-	66,166
Debt secured by commercial real estate	-	-	-	-	-	2,709	-	-	2,709	-	2,709
Retail exposure to individuals	-	-	-	-	25,104	60	105	-	25,269	-	25,269
Loans to small businesses	-	-	-	-	5,357	13	17	-	5,387	-	5,387
Residential mortgages	-	-	62,621	-	13,962	6,253	211	-	83,047	-	83,047
Other assets	999	-	-	-	-	3,796	105	-	4,900	87	4,987
Total	**999**	**19**	**62,621**	**36**	**44,423**	**78,735**	**700**	**-**	**187,533**	**87**	**187,620**
Total exposure	**19,925**	**5,419**	**62,621**	**1,551**	**44,423**	**78,937**	**700**	**-**	**213,576**	**120**	**213,696**

(1) Balance of on- and off-balance sheet balances, after on- and off-balance-sheet offsets, after provision for credit loss, excluding impact of credit conversion factors and risk weighting factors, as defined under Basel II rules.

(2) Mitigation using guarantees, credit derivatives and other qualified collateral.

After credit risk mitigation

	As of December 31, 2012										
	0%	20%	35%	50%	75%	100%	150%	350%	Gross credit exposure	Deducted from equity	Total
Rated exposures:											
Sovereign debt	18,644	2,504	-	-	-	106	-	-	21,254	-	21,254
Public sector entity debt	312	-	-	868	-	-	-	-	1,180	-	1,180
Banking corporation debt	-	2,987	-	364	-	81	-	-	3,432	-	3,432
Corporate debt	-	51	-	231	-	-	-	-	282	-	282
Securitization	-	-	-	-	-	-	-	-	-	-	-
Other assets	-	-	-	-	-	-	-	-	-	33	33
Total	**18,956**	**5,542**	**-**	**1,463**	**-**	**187**	**-**	**-**	**26,148**	**33**	**26,181**
Non-rated exposures:											
Public sector entity debt	-	-	-	13	-	-	-	-	13	-	13
Banking corporation debt	-	144	-	90	-	-	-	-	234	-	234
Corporate debt	-	-	-	-	-	56,789	246	-	57,035	-	57,035
Debt secured by commercial real estate	-	-	-	-	-	2,397	-	-	2,397	-	2,397
Retail exposure to individuals	-	-	-	-	23,313	38	104	-	23,455	-	23,455
Loans to small businesses	-	-	-	-	3,822	10	16	-	3,848	-	3,848
Residential mortgages	-	-	62,620	-	13,894	6,253	188	-	82,955	-	82,955
Other assets	999	-	-	-	-	3,796	105	-	4,900	87	4,987
Total	**999**	**144**	**62,620**	**103**	**41,029**	**69,283**	**659**	**-**	**174,837**	**87**	**174,924**
Total exposure	**19,955**	**5,686**	**62,620**	**1,566**	**41,029**	**69,470**	**659**	**-**	**200,985**	**120**	**201,105**

Before credit risk mitigation

											As of December 31, 2011
	0%	20%	35%	50%	75%	100%	150%	350%	Gross credit exposure	Deducted from equity	Total
Rated exposures:											
Sovereign debt	16,255	2,880	-	-	-	345	-	-	19,480	-	19,480
Public sector entity debt	-	-	-	723	-	-	-	-	723	-	723
Banking corporation debt	-	4,112	-	1,188	-	61	-	-	5,361	1	5,362
Corporate debt	-	117	-	295	-	177	-	-	589	-	589
Securitization	-	-	-	-	-	-	-	25	25	36	61
Other assets	-	-	-	-	-	-	-	-	-	37	37
Total	**16,255**	**7,109**	**-**	**2,206**	**-**	**583**	**-**	**25**	**26,178**	**74**	**26,252**
Non-rated exposures:											
Public sector entity debt	-	-	-	249	-	-	-	-	249	-	249
Banking corporation debt	-	49	-	537	-	-	-	-	586	-	586
Corporate debt	-	-	-	-	-	64,927	245	-	65,172	-	65,172
Debt secured by commercial real estate	-	-	-	-	-	1,985	-	-	1,985	-	1,985
Retail exposure to individuals	-	-	-	-	24,179	37	157	-	24,373	-	24,373
Loans to small businesses	-	-	-	-	4,989	12	28	-	5,029	-	5,029
Residential mortgages	-	-	56,625	-	12,932	4,281	208	-	74,046	-	74,046
Other assets	926	-	-	-	-	2,600	46	-	3,572	87	3,659
Total	**926**	**49**	**56,625**	**786**	**42,100**	**73,842**	**684**	**-**	**175,012**	**87**	**175,099**
Total exposure	**17,181**	**7,158**	**56,625**	**2,992**	**42,100**	**74,425**	**684**	**25**	**201,190**	**161**	**201,351**

(1) Balance of on- and off-balance sheet balances, after on- and off-balance-sheet offsets, after provision for credit loss, excluding impact of credit conversion factors and risk weighting factors, as defined under Basel II rules.

(2) Mitigation using guarantees, credit derivatives and other qualified collateral.

After credit risk mitigation

	As of December 31, 2011										
	0%	20%	35%	50%	75%	100%	150%	350%	Net credit exposure	Deducted from equity	Total
Rated exposures:											
Sovereign debt	16,264	2,893	-	-	-	346	-	-	19,503	-	19,503
Public sector entity debt	-	-	-	718	-	-	-	-	718	-	718
Banking corporation debt	-	4,103	-	1,232	-	59	-	-	5,394	1	5,395
Corporate debt	-	117	-	295	-	-	-	-	412	-	412
Securitization	-	-	-	-	-	-	-	25	25	36	61
Other assets	-	-	-	-	-	-	-	-	-	37	37
Total	**16,264**	**7,113**	**-**	**2,245**	**-**	**405**	**-**	**25**	**26,052**	**74**	**26,126**
Non-rated exposures:											
Public sector entity debt	-	-	-	250	-	-	-	-	250	-	250
Banking corporation debt	-	55	-	712	-	-	-	-	767	-	767
Corporate debt	-	-	-	-	-	56,260	220	-	56,480	-	56,480
Debt secured by commercial real estate	-	-	-	-	-	1,823	-	-	1,823	-	1,823
Retail exposure to individuals	-	-	-	-	22,545	13	153	-	22,711	-	22,711
Loans to small businesses	-	-	-	-	3,673	7	25	-	3,705	-	3,705
Residential mortgages	-	-	56,625	-	12,886	4,279	208	-	73,998	-	73,998
Other assets	926	-	-	-	-	2,600	46	-	3,572	87	3,659
Total	**926**	**55**	**56,625**	**962**	**39,104**	**64,982**	**652**	**-**	**163,306**	**87**	**163,393**
Total exposure	**17,190**	**7,168**	**56,625**	**3,207**	**39,104**	**65,387**	**652**	**25**	**189,358**	**161**	**189,519**

Significant exposure to groups of borrowers

Below is credit risk with respect to significant exposure to borrower groups as of December 31, 2012.

Disclosure is provided with regard to each group of borrowers whose net indebtedness, on consolidated basis, after allowed deductions pursuant to Proper Conduct of Banking Business Regulation 313, exceeds 15% of the banking corporation's capital (as defined in Regulation 313).

NIS in millions:

	On-balance sheet credit risk, net (1)	Off-balance sheet credit risk				
		With respect to derivatives	Other	Deductions	Total credit risk	Share of equity
Group 1	1,153	116	1,227	33	2,463	17.3%

(1) After deduction of accounting write-offs and provision for credit loss on individual basis.

Bank business with major borrower groups is conducted subject to several guidelines designed to mitigate risk associated with such business:

- Business with borrower groups is primarily done with established, leading public companies.
- Credit it mostly provided for short- and medium term, to be used in current operations of these companies.
- Credit is diversified among Group companies operating in different segments and economic sectors.
- Credit is provided, in as much as possible, to companies which are not mutually dependent or which are subject to mutual covenants or guarantees.

The Bank takes the following steps in order to manage exposure to groups of borrowers:

- Set financial covenants as needed.
- Provide credit against collateral, in as much as possible, and closely monitor exposure not secured by collateral.
- Closely monitor company operations and financial results.
- Closely monitor compliance of borrower group companies with financial covenants, if and when specified.

Leveraged financing

The Bank conducts, in some cases, leveraged financing transactions, in which a client is extended credit for purchasing a controlling stake, characterized by a high LTV ratio compared to the value of shares, and relying exclusively on the shares being acquired as the source for credit repayment. The Bank reviews these transactions with due diligence, based inter alia on internal valuations as well as on external valuators. Terms and conditions specified for the transaction include sensitivity tests and financial covenants, which if met, require the borrower to provide additional collateral.

Details of Bank exposure to credit constituting leveraged financing are as follows:

Economic sector of acquired company	Total balance sheet credit	
	As of December 31	
	2012	2011
Commerce	115	146
Communications and computer services	235	270
Construction and real estate	304	354
Total	**654**	**770**

Below is information on the Bank's exposure to foreign financial institutions [(1)] [(2)] (NIS in millions):

	As of December 31, 2012		
External credit rating	On-balance sheet credit risk [(3)]	Off-balance sheet credit risk [(4)]	Current credit exposure
AAA to AA-	709	-	709
A+ to A-	2,183	21	2,204
BBB+ to BBB-	8	-	8
BB+ to B-	-	7	7
Lower than B-	-	-	-
Unrated	5	-	5
Total credit exposure to foreign financial institutions	**2,905**	**28**	**2,933**
Includes: Troubled commercial credit risk, net [(5)]	5	-	5

	As of December 31, 2011		
External credit rating	On-balance sheet credit risk [(3)]	Off-balance sheet credit risk [(4)]	Current credit exposure
AAA to AA-	1,929	124	2,053
A+ to A-	859	134	993
BBB+ to BBB-	5	-	5
BB+ to B-	2	6	8
Lower than B-	-	-	-
Unrated	7	-	7
Total credit exposure to foreign financial institutions	**2,802**	**264**	**3,066**
Includes: Troubled commercial credit risk, net[(5)]	4	-	4

(1) Foreign financial institutions include: banks, investment banks, brokers/dealers, insurance companies, institutional entities and entities controlled by the former. Bank exposure is almost entirely to banks and investment banks primarily incorporated in the UK, USA, Germany, Spain and Switzerland. Exposure is primarily with respect to institutions incorporated in OECD countries.

(2) After deduction of provision for credit loss.

(3) Bank deposits, credit to the public, investment in debentures, securities borrowed or acquired in conjunction with re-sale agreements and other assets with respect to derivative instruments.

(4) Primarily guarantees and commitments to grant credit, including guarantees to secure liabilities of third parties, which have been weighted at 50% of their amount – in accordance with Proper Conduct of Banking Business Regulation 313 (excluding off-balance sheet derivatives).

(5) Credit risk for impaired, inferior credit or credit under special supervision, excluding credit risk with respect to individuals.

The aforementioned credit exposure excludes exposure to financial institutions for which complete, explicit government guarantees are in place, and excludes investments in asset-backed securities. For details of investments in asset-backed securities, see Note 3 to the financial statements. For further information with regard to credit exposure composition with respect to derivative instruments vis-à-vis banks and dealers/brokers (domestic and foreign), see Note 19e to the financial statements.
Some of the exposures listed in the above table are included under Management Review - Addendum E - Credit Risk by Economic Sector, enclosed with these financial statements under the Financial Services sector. This Management Review also includes deposits with banks, credit to the public, public investment in debentures and other assets with respect to derivative instruments. Future transactions, weighted in accordance with rules set forth in Proper Conduct of Banking Business Regulation 313, are included under Management Review as part of off-balance sheet credit risk, and are excluded from the above table.
In conjunction with its policy regarding management of exposure to foreign financial institutions, the Bank Board of Directors sets, inter alia, the maximum exposure limit for states and foreign financial institutions, while adjusting the exposure limit to the risk assessment for each state and financial institution. Exposure limits are set based, inter alia, on rating of the various states and financial institutions and on Bank assessment of the risk level in a manner which diversifies exposure.
The Bank determines the exposure limit to each financial institution based on the most recent rating available for said institution, and only ratings provided by one of the leading international rating agencies are used – based on financial information for the institution under review. Exposure limits per institution include maximum exposure amount and maximum time to maturity for different types of activities and transactions. To this end, the existence (or absence) of an offset agreement for derivative operations with that financial institution is also taken into consideration. The policy also specifies a hierarchy of authority for approval of specific transactions within the exposure limits.

The Bank monitors current ratings published for financial institutions to which it has exposure, and adjusts the exposure limits and actual exposure, as required, to the current rating. The Bank also reviews on a regular basis any additional information available with regard to these institutions in order to monitor exposure even where the credit rating may not reflect the complete picture.
The Bank takes into consideration the maturity dates of its credit exposure in conjunction with the Bank's liquidity requirements. Deposits are normally deposited for short terms, while exposure with respect to derivatives and investments in securities are for longer terms.

Ratings – Bank activity with overseas entities generates exposure to sovereigns and to financial institutions. The Bank has set a policy with regard to review and routing of risk arising from this exposure. For credit risk exposure management, as described above, the Bank uses ratings by independent rating agencies, primarily: Fitch, Standard & Poor's, and Moody's. These ratings are accounted for as part of the considerations in setting limits on Bank exposure to sovereigns and banks, intended primarily for derivatives operations, financing and guarantees for foreign trade and investments in the nostro portfolio.
The Bank acquires the ratings, and analysis underlying such ratings, from Fitch and Moody's. The main rating used by the Bank for independent analysis is the rating provided by Fitch.

Credit loss with respect to housing loans

In conjunction with credit risk management, the Bank takes various actions to mitigate risk associated with provision of housing loans. The Bank estimates the risk associated with provision of housing loans as low, relative to the inherent risk in the Bank's overall loan portfolio, due to the high level of client diversification, geographic diversification of borrowers, relatively low leverage, intensive review procedures of borrower quality and their repayment capacity, and securing credit with property as collateral, and occasionally with credit insurance as well.
The Bank act regularly to control and manage the risk associated with housing loans, for which the Retail Division and other Bank entities are responsible.

Risk appetite in mortgage segment

As part of its credit policy and its credit risk policy, the Bank has set various restrictions on housing loan operations, to account for major risk factors. These factors are reviewed from time to time and restrictions are added as needed.
The key parameters used for specifying risk appetite in the mortgage segment are: results of the differential risk premium model, LTV ratio of the loan, property location (geographical risk) and credit quality benchmark (see below under Credit Control). As from 2013, restrictions were added on other parameters: repayment to income ratio, loan purpose, loan term, loan track mix, property type, credit insurance and cross restrictions on combinations of multiple parameters.

Means for risk management in housing loans

Criteria for loan approval

The Bank has specified uniform, quantitative criteria for review and approval of housing loan applications. Along with the uniform criteria, decision makers at the Bank exercise their judgment. The guiding criteria for granting housing loans have been determined, inter alia, based on the following:

A. Accumulated experience at the Bank with regard to housing loans, including lessons learned over time with regard to parameters which determine borrower quality and quality of loan collateral.

B. Results of current credit reviews which include, inter alia, review of changes to credit quality in certain sectors.

C. Assessment of credit risk arising from variable macro-economic market conditions.

D. Assessment of credit risk in different areas of the country, due to security-related and other events.

These criteria are regularly updated in line with market developments. Thus, for example, in 2009 the Bank decided, due to the low prime lending rate, to instruct bankers and loan approvers to review borrower repayment capacity, accounting for potential increase in monthly repayment due to the prime-linked component for scenarios including a 2 percentage point increase in the prime lending rate over its current rate upon loan approval.

Credit authority

The Bank has created a ranking of authority for approval of housing loans (at branch, region and headquarters level). The authorized entity to approve the loan is determined based on data in the loan application and on its inherent risk (data about borrowers, LTV ratio, risk premium and nature of the transaction). To enhance control over approval of complex, high-risk loans and loans to specific populations (such as: new immigrants, transactions between family members and individual borrowers), and to make use of specialization in such loans, such applications are sent for approval by the Underwriting and Control Department operating at the mortgage headquarters, staffed by a professional team supervised by the Deputy Manager, Mortgages at the Retail Division.

Model for determination of differential risk premium

The Bank has developed a model for calculation of differential risk premium, based on past empirical data, for rating transaction risk at the loan application stage. For each application, an individual risk premium is calculated based on all risk factors identifiable in client information and attributes of the desired transaction.

This premium reflects an estimate of overall transaction risk, allowing for assessment of client odds of being in arrears on the loan or becoming insolvent - at the outset of the application stage. This premium is used for both credit decision making and for pricing of client interest rate.

Built-in controls in loan origination system

The Bank manages its mortgage operations using a dedicated computer system developed for this purpose, which includes the following built-in controls:

- Ensure information completeness required for loan and activities required in preparation of the material, review and approval of the loan.
- Rigid, real-time control over transactions by authorization. Use of this preventive control methodology significantly reduces the need for discovery controls after loan origination.
- Workflow process with real-time control over execution of all required tasks at each stage of the loan origination process, sending the application to the authorized entity for performing the required actions at each stage of the loan approval process.

Use of this system has resulted in improved control in different stages of the loan origination process, while achieving uniformity among different Bank branches.

Mortgage-related training

The Bank Training Center delivers courses for training, development and improvement of all those involved in provision of housing loans. Training content is determined in cooperation with the Mortgage Headquarters, and staff at headquarters participates in training delivery to bankers. In 2012, the Bank continued to deliver, along with the basic course, an advanced mortgage banker's course as well as a mortgage course designed for managers of commercial branches. These courses include, inter alia, special emphasis on risk management. An additional track for training and certification of mortgage bankers was also developed. This track will be launched in 2013.

Training of staff and management has significant impact on their professional level when granting credit and making credit-related decisions, as well as during ongoing management of client credit.

Professional conferences

The Retail Division regularly holds professional conferences for managers and bankers. In these conferences, extensive reviews of developments in the mortgage market are presented, along with steps to be taken to handle the risk associated with such developments. Over the past year, as in the previous year, special emphasis was placed at conferences on Bank of Israel directives issued in 2010 and 2011, as well as the most recent directive dated November 2012 and their impact on providing housing loans (including capital and risk asset allocation, restrictions on originating adjustable interest rate loans, LTV restrictions etc.)

Credit control

Credit control is a key factor in maintaining quality of credit provided by the Bank to its clients. Control over housing loans is exercised at the individual loan level as well as for the entire mortgage portfolio.

At the individual loan level, the Bank acts to identify as early as possible any symptoms indicating a decline in borrower repayment capacity, in order to identify as soon as possible any credit failure situation. The Bank operates various controls, including regular internal controls at branches, regions and headquarters, as well as additional controls by entities external to the process and to the credit units - the Risk Control Division and Internal Audit.

The Bank maintains control over quality of new credit provided by branches, by means of a monthly Credit Quality report, which includes all loans originated by the Bank between 6-18 months prior to the reported date which are over 3 months in arrears. This report is designed to assist branches in reducing the extent of arrears, and to increase awareness of troubled loans by those originating and approving loans in order to learn lessons for future credit approval. Along with the individual report, listing loans, details of arrears etc., a statistical report is also produced, showing the extent of arrears at each branch, compared to the region and to the Bank as a whole, and compared to previous months. Management of the Retail Division regularly monitors handling of debt in arrears, using this report.

For the entire mortgage portfolio, control is maintained of restrictions imposed by the Bank's risk appetite, both at the Retail Division and at the Risk Control Department of the Risk Control Division. A credit control report is produced semi-annually, with extensive review of the risk profile of the housing loan portfolio, with regard to the following:

- Risk appetite
- Analysis of major risk attributes
- Review of state of arrears and credit quality
- Client debt collection
- Housing loan portfolio for special populations
- Stress testing
- Purchase groups.

Tools for risk mitigation in housing loans

Collateral

In accordance with Bank procedures for mortgages, loans are only provided if secured by property collateral. In some cases, the Bank demands guarantors for the debt, in addition to property collateral.
For verification of information about the property offered to the Bank as collateral and to determine its value, an assessor visit to the property is normally required, providing a report which describes the property, its location, physical condition and market value. Assessors are party to an agreement with the Bank and act in accordance with Bank guidance, including a structured procedure for conducting assessments, identifying exceptions etc.

The common practice for assessment in the mortgage sector is to use an abbreviated assessment. However, since 2006, the Bank has required assessors to conduct extended assessment for some of the loans for purchase of existing apartments, self-construction or general-purpose loans with high-risk property types, which includes additional tests subject to criteria set for this matter.

Insurance

According to Bank procedures, all properties serving as collateral must be insured under property insurance. In addition, the borrowers are insured by life insurance assigned to the Bank in case of death prior to complete repayment of the loan.
For some loans (usually loans with LTV ratio higher than 75%), the Bank contracted with EMI Corp., which provides credit insurance in case the proceeds from realization of the property collateral for the loan should fail to cover the outstanding loan amount. This credit insurance process is a key risk mitigator.
As from November 1, 2012, the Bank of Israel restricted origination of housing loans with LTV over 75%, so that as of this date the Bank no longer approves new loans with credit insurance and LTV over 75% (except for loans exempted from this directive, such as refinancing loans). However, loans approved with credit insurance, prior to the effective start date of this directive, in which the loan agreement was signed by December 31, 2012, will be originated in 2013.

LTV ratio

The maximum LTV ratio approved by the Bank is determined by the credit policy and is periodically reviewed. Generally, the Bank requires borrowers to contribute part of the financing for the acquisition. This equity payment forms a safety cushion in case the property is realized during a down-turn in the real estate market. Furthermore, borrower equity is a further indication of the borrower's financial robustness. As from November 1, 2012, the Bank restricted the LTV ratio for approval of applications for housing loans, pursuant to the Bank of Israel directive on this matter. The LTV ratio for loans to acquire rights to real estate constituting a "single apartment" (as defined in the directive) shall not exceed 75%, for an "alternative apartment" (as defined in the directive), the LTV ratio shall not exceed 70%, and for acquisition of an investment property, general-purpose loan or loan extended to foreign residents - the LTV ratio shall not exceed 50%. For details, see the chapter on Legislation and Supervision of Bank Group Operations.

Entities participating in risk management for housing loans

Mortgage Management Department of the Retail Division

This department handles different events which occur during the loan term, whether initiated by the Bank or by the borrower. One of the key tasks is monitoring of collateral provided. During loan origination, the Bank usually received interim collateral, and the final collateral is expected to be received during the loan term. The department also monitors receipt of life and property insurance policies during the loan term.

Risk Control Division

The Risk Control Division reviews the quality of the Bank's loan portfolio and the risk profile of the Bank portfolio. As for mortgages, the portfolio is analyzed semi-annually from 2012, including analysis of developments in housing loan grants and our market share, as well as credit composition by various criteria. As from this year, this analysis is performed semi-annually. This report is discussed by the Supreme Credit Committee and is presented to the Bank Board of Directors.

Credit risk and credit concentration monitoring forum

The Bank operates a forum for monitoring credit risk, headed by the Manager, Risk Control Division, which promotes issues such as: analysis of credit portfolio risk level, application of advanced modeling approaches, specification of triggers for activating stress testing; supervision of design and application process of stress testing, and monitoring of the risk profile of the Bank's loan portfolio. This forum operates another entity, composed of professionals in the business domain, control and economists who review the credit portfolio (and in particular the mortgage portfolio), inter alia, in view of the risk appetite restrictions specified.

Early in the second quarter of 2012, the Bank started monitoring its mortgage portfolio using advanced Basel models (IRB II). This monitoring is part of the Bank project for development, validation and application of advanced models for various segments of the mortgage portfolio. Analysis of the mortgage portfolio using the new models is in addition to current analysis conducted by the Bank using "traditional" tools.As described above, in early 2013 the bank stopped the project development while maintaining the capabilities which achieved regarding the portfolio level analysis. Particular in performing stress tests regularly.

Legal Division

As part of the underwriting process, collateral for non-standard loans (loans to individuals, transactions involving family members) and high-value loans are reviewed by the Mortgage Advisory Department, a specialized entity in the Legal Division. This test complements the loan approval and review conducted at the branch and the regional underwriting department.

Collection Department

The Bank operates a dedicated Collection Department, which handles debt collection from borrowers in arrears and realization of properties. Processing is automatically launched once the client fails to make a mortgage payment for the first time. If this failure is not resolved, processing continues by the Telephone Collection Center (prior to filing a law suit), designed to reach payment arrangements with clients. If such an arrangement with borrowers cannot be reached, the debt is processed by the Bank's Collection Department, which includes a dedicated department for mortgage debtors, and legal proceedings are initiated vs. the debtors.

Arrears Forum

The Arrears Forum of Bank management convenes monthly, headed by the Manager, Business Division, and reviews the current state of affairs with regard to collection in the previous month, implications on the financial statements and on the provision for credit loss. The Forum specifies targets for debt processing and for reducing arrears.

Internal Audit

The work plan for Internal Audit with regard to loans includes, inter alia, reference to review of entities involved in loan approval, origination, administration and control.

Attributes of the Bank's housing loan portfolio

The Bank's policy with regard to mortgages is based on a conservative approach, limiting specific risk for each loan by reviewing various attributes. These attributes include: LTV ratio, ratio of repayment to regular income of the borrower, and borrower capacity to make current repayments even under scenarios involving a change in interest rates. Whenever loans are granted with attributes which do not meet one or more of the standards set by the Bank for these attributes, the Bank requires additional bolstering for the loan, such as credit insurance, additional guarantors for the loan, proven repayment capacity not based on regular income of the borrower etc. In recent years, due to expansion of the housing market and a relatively low interest environment, the Bank has enhanced measures taken to mitigate risk, as reflected by a significant decrease in loan risk factors, as detailed below (all data below as of December 31, 2012).

LTV ratio

One of the key parameters used by the Bank in minimizing risk in its housing loan portfolio is the LTV ratio (ratio of loan amount to value of the property pledged as collateral). As from November 1, 2012, the Bank of Israel limited the LTV ratios for housing loans (as described above). The effect of this directive on the Bank's credit portfolio would only be manifested over the long term.

The average loan-to-value ratio for the Bank's mortgage portfolio as of December 31, 2012 was 57.8%, compared to 58.6% on December 31, 2011 and to 60.1% on December 31, 2010. Out of the total loan portfolio of the Bank, amounting to NIS 80.1 million, some 84% were granted with an original LTV ratio under 75%, which secures the loan even in case of an extreme 25% decrease in value of the property pledged as collateral.

The LTV ratio in this report is the historical LTV ratio calculated upon loan approval, and does not account for any current repayments which reduce the loan balance nor any changes in value of properties pledged as collateral. The significant increase in housing prices since late 2008, along with reduced loan balances with respect to current repayment, result in a lower current LTV ratio for loans granted through 2008, so that most all of the loans currently have LTV ratios under 75%. Total loans granted at LTV ratios over 75% in the past two years amounted to NIS 3.4 billion, or only 4.3% of the total housing loan portfolio.

Loans granted with a high LTV ratio are usually secured by credit insurance, which significantly reduced risk for the Bank, although it does not affect the LTV or repayment percentage calculation. Out of the balance of loans granted with an original LTV ratio higher than 75%, a total of NIS 5.1 billion is insured by credit insurance - 40.5%.

Over the past two years, due to measures taken by the Bank to reduce risk in the mortgage portfolio, the percentage of loans granted with a high LTV ratio out of total housing loan portfolio of the Bank decreased to 10.3% for loans granted 1-2 years ago, 11.4% for loans granted 3-12 months ago and 10.9% for loans granted in the fourth quarter of 2012.

Repayment as percentage of regular income

The LTV ratio of a housing loan is a benchmark of loan security, regardless of borrower attributes. When a mortgage is approved, the Bank requires borrowers to show their capacity to make current loan repayments on schedule, primarily by calculating the ratio of monthly repayment to regular income of the borrower.
The average repayment ratio for the Bank's housing loan portfolio is 30.7%. 69.0% of the Bank's mortgage portfolio was granted to borrowers with a repayment ratio under 35% (the average repayment ratio for these borrowers is 23.5%). Some 22% of the mortgage portfolio were granted to borrowers with a repayment ratio of 35% to 50% (the average repayment ratio for these borrowers is 40.5%), and only 9% were granted to borrowers with a repayment ratio over 50% (the average repayment ratio for these borrowers is 61.9%).
The loans with a high repayment ratio are loans granted to borrowers with significant other assets, whose repayment capacity is not necessarily based on current income, to borrowers with very high income where the repayment ratio is less significant, or where additional bolstering of the loan is in place, in addition to the pledged property and repayment capacity of the borrower, such as financially robust guarantors.

Even loans granted with a repayment ratio higher than 50% maintain the average LTV ratio, and some 88% of these are granted with a LTV ratio under 75%.

Loans bearing variable interest

The Bank allows its clients to obtain housing loans which include a portion bearing NIS-denominated interest based on the prime lending rate.

Over the past decade, the prime lending rate decreased from 10% in 2002-2003, through 5%-6% in 2004-2008 to 2%-4% in 2009-2012. Therefore, the risk associated with loans bearing interest based on the prime lending rate is primarily due to loans granted since 2009, assuming that the prime lending rate is expected to rise, reflecting a positive real interest in the economy.
The Bank provides clients with the knowledge and expertise of its staff in order for clients to understand the risk involved with a loan bearing interest linked to the prime lending rate and how this risk may be mitigated or avoided. The Bank advises clients to attribute appropriate weighting to this risk, and to be cautious when deciding upon the loan composition.
The repayment capacity of clients who obtained loans in the period when the prime lending rate was high is reviewed using the high interest rate. Over the past two years, when interest rates were low, these clients benefited significantly from lower loan costs. In this low interest environment, the Bank nevertheless took measures to reduce loans provided bearing interest linked to the prime lending rate: From 27.5% of loans granted 1-2 years ago, the Bank reduced the percentage of loans linked to the prime lending rate to 24.40% for loans granted 3-12 months ago and down to 24.9% for loans granted in the fourth quarter of 2012.
Total loans linked to the prime lending rate granted over the past two years, which constitute the major portion of risk associated with such mortgages, is NIS 8.2 billion, or only 10.2% of the housing loan portfolio.

Note however that before approving a loan linked to the prime lending rate, the Bank reviews the repayment capacity of the borrower under scenarios where the prime lending rate would increase by 2 percentage points.

The directive by the Supervisor of Banks dated May 3, 2011, which restricts the portion of loans extended bearing variable interest to 33.3% of total loan amount, has also contributed to further reduction in variable interest loans extended, and to mitigation of risk in this area.

Loan amount

Loans granted by the Bank with an original amount over NIS 2 million amounted in total to NIS 3.3 billion, or only 4.1% of the Bank's housing loan portfolio.

Below are details of various risk attributes of the housing loan portfolio (NIS in millions):

LTV ratio	Repayment as percentage of regular income	Loan age [1] (time elapsed since loan grant) Up to 3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
Up to 60%	Up to 35%	1,468	3,951	4,817	10,523	4,253	2,290	27,301
	35%-50%	567	1,620	1,864	2,856	1,014	380	8,301
	Over 50%	196	599	895	1,375	478	215	3,758
60%-75%	Up to 35%	1,174	2,943	3,877	8,807	1,842	799	19,441
	35%-50%	398	1,178	1,541	2,384	585	211	6,297
	Over 50%	122	411	562	947	285	113	2,440
Over 75%	Up to 35%	373	1,025	1,132	3,153	1,466	1,912	9,060
	35%-50%	97	303	354	796	447	639	2,636
	Over 50%	12	46	73	267	231	283	912
Total		**4,407**	**12,076**	**15,114**	**31,107**	**10,600**	**6,841**	**80,146**
Includes:								
Loans granted with original amount over NIS 2 million		170	474	758	1,565	290	50	3,307
Percentage of total housing loans		3.9%	3.9%	5.0%	5.0%	2.7%	0.7%	4.1%
Loans bearing variable interest:								
Non-linked, at prime ending rate		1,096	2,952	4,157	14,465	3,469	333	26,472
CPI-linked[2]		111	333	1,624	6,724	1,608	1,682	12,082
In foreign currency [2]		160	368	1,166	2,261	563	143	4,661
Total		**1,367**	**3,653**	**6,947**	**23,450**	**5,640**	**2,158**	**43,215**
Non-linked loans at prime lending rate, as percentage of total housing loans		24.9%	24.4%	27.5%	46.5%	32.7%	4.9%	33.0%
CPI-linked loans bearing variable interest as percentage of total housing loans		2.5%	2.8%	10.7%	21.6%	15.2%	24.6%	15.1%
Loans with LTV over 75% as percentage of total housing loans		10.9%	11.4%	10.3%	13.6%	20.2%	41.4%	15.7%

(1) The loan balances presented above are aged based on the date of loan origination, and include under the same age group any loan balances actually provided at a later date.

(2) Pursuant to directives by the Supervisor of Banks, these include loans for which the interest rate is adjusted up to once every 5 years.

Credit risk mitigation

The Bank Group takes different actions to mitigate risk associated with extending credit and with credit concentration (on this issue, see chapter on credit risk and concentration monitoring forum). Below is a description of major tools used to mitigate risk in conjunction with the Bank's credit policy.

Collateral – Bank procedures specify the asset types which may be recognized as collateral for providing credit. The commonly used collateral types at the Bank are: Deposits, securities, liens on real estate, vehicles, , credit vouchers, checks, bank guarantees and institutional, corporate or individual guarantees. As part of the collateral policy, rules and principles were prescribed as to the level of reliance on each type of collateral, with regard to its character, marketability, price volatility, promptness of realization and legal status, in addition to assessing the repayment ability of a client as a criterion for issuing the loans.

The collateral is matched, as far as possible, to the type of credit that it secures, while taking into account the period of time, types of linkage, character of loans and their purpose, as well as how quickly it can be realized. Collateral coefficients determine the extent to which the Bank is willing to rely on specific collateral to secure credit. The value of the collateral, with the use of safety factors, is, as far as possible, calculated automatically by the IT systems. The safety factors for different types of collateral are examined at least once a year and are approved by the Board of Directors' Credit Committee. There is also collateral in place which is not accounted for in calculating safety factors, but only used to reinforce existing collateral. The Bank also approves, on a limited, case-by-case basis, the granting of credit solely on the basis of the borrower's obligation.

Bank procedures specify rules for ongoing collateral management, including updates to the value of collateral: Deposits and bank guarantees are regularly updated based on their terms and conditions; collateral consisting of negotiable securities is regularly updated based on their market value; with regard to collateral consisting of real estate, the procedure determines the date for valuation by a licensed assessor in accordance with the type of credit secured by the property. Valuation is also carried out in case of concern regarding material impairment of the collateral, which may cause the Bank to face shortage of collateral.

As stated above, including in the chapter on Basel Committee Recommendations, the Bank makes extensive use of collateral not recognized under credit mitigation rules of Basel II (real estate, liens on automobiles, personal guarantees) in order to mitigate credit risk.

Hedges - Borrowers with currency exposure are offered means of safety and protection (hedging transactions) in order to reduce their exposure, in addition to other measures that the Bank adopts to minimize the risk of the Bank's exposure from the activities of these clients. Guidelines were prescribed to intensify the monitoring, control, and supervision of the activities of borrowers whose debts to the Bank are sensitive to exchange rate fluctuations, including the creation of simulations and future scenarios of changes in exchange rates. Special controls are also used for clients, when securities form a significant element of their collateral.

Credit insurance – The Bank used credit insurance for housing loans (mortgages), such that mortgages with high loan-to-value ratios are secured, for the part exceeding the loan-to-value ration determined by the Bank, by EMI insurance company. Thus the Bank reduces risk associated with the loan to a limited share of total collateral.

Concentration - The Bank has approved a current, dedicated policy on concentration risk with regard to credit. The Bank's credit policies are based on diversification and controlled management of risk.

Risk diversification is characterized by several aspects:

- Diversification of the loan portfolio among the different economic sectors, including limiting exposure in certain sectors.
- Diversification over sized groups of clients.
- Diversification over linkage segments.
- Geographic diversification where relevant (construction industry, mortgages).

Economic sectors: The Bank's Executive Management and Board of Directors hold discussions on the issue of credit to certain industrial sectors, as is necessary, mainly as it relates to industries that are sensitive to fluctuations in business cycles. Credit policy for the sensitive industries is set on the basis of an economic analysis of the developments forecast for these industries. The Bank maintains distribution of indebtedness among different sectors, so as not to create extraordinary indebtedness according to provisions of Proper Banking Conduct Regulation 315. Loans to certain sectors, such as diamonds, construction, leasing credit and start-up companies – are handled by professional units or by personnel specializing in these industries. Specific rules and procedures have been prescribed for these specific sectors, beyond those relating to the issue of credit, in order to deal with their special credit risk.

Large clients: The Bank provides credit to large clients through the Corporate sector, which operates teams with sector expertise. Occasionally the Bank limits its share of credit to a major client relative to total extent of credit to that client in the banking system, and in some cases, in order to participate in financing of certain transactions, the Bank requires a financing package to be put in place with participation of other banks (under consortium agreements). The Bank strictly complies with limits on indebtedness of a borrower and a group of borrowers, as well as on total indebtedness of major borrowers and groups of borrowers whose net indebtedness to the Bank exceeds 10%, pursuant to Proper Conduct of Banking Business Regulation 313. For further details with regard to clients served by the Corporate segment, see chapter describing the Bank's operating segments - Business Banking segment.

Linkage segments: This distribution is also reflected in providing credit in various linkage segments, such that part of the credit is more susceptible to fluctuations in the Consumer Price Index (CPI-linked credit), some is more susceptible to changes in the prime lending rate (non-linked NIS-denominated credit), and some – to foreign currency exchange rate fluctuations (foreign-currency denominated credit or linked to foreign-currency exchange rate).

Geographic diversification: The Bank maintains geographic diversification with regard to credit for construction and mortgages, in order to reduce over-concentration in extending credit.

Below is the composition of net credit exposure by risk mitigation type:

					As of December 31, 2012
		Exposure covered by guarantees		Exposure covered by	
	Gross credit exposure[1]	Amounts deducted[2]	Amounts added[2]	qualified financial collateral	Net credit exposure
Sovereign debt	21,399	(291)	157	(11)	21,254
Public sector entity debt	933	-	312	(52)	1,193
Banking corporation debt	3,484	(9)	193	(2)	3,666
Corporate debt	66,448	(251)	23	(8,903)	57,317
Debt secured by commercial real estate	2,709	(7)	-	(305)	2,397
Retail exposure to individuals	25,269	(1)	-	(1,813)	23,455
Loans to small businesses	5,387	(103)	-	(1,436)	3,848
Residential mortgages	83,047	(23)	-	(69)	82,955
Other assets	4,900	-	-	-	4,900
Total	**213,576**	**(685)**	**685**	**(12,591)**	**200,985**

					As of December 31, 2011
		Exposure covered by guarantees		Exposure covered by	
	Gross credit exposure[1]	Amounts deducted[2]	Amounts added[2]	qualified financial collateral	Net credit exposure
Sovereign debt	19,480	-	23	-	19,503
Public sector entity debt	972	-	-	(4)	968
Banking corporation debt	5,947	(9)	226	(3)	6,161
Corporate debt	65,684	(218)	-	(8,574)	56,892
Debt secured by commercial real estate	2,062	(2)	-	(237)	1,823
Retail exposure to individuals	24,373	(1)	-	(1,661)	22,711
Loans to small businesses	5,029	(19)	-	(1,305)	3,705
Residential mortgages	74,046	-	-	(48)	73,998
Securitization	25	-	-	-	25
Other assets	3,572	-	-	-	3,572
Total	**201,190**	**(249)**	**249**	**(11,832)**	**189,358**

(1) Balance of on- and off-balance sheet balances, after on- and off-balance-sheet offsets, after provision for credit losses, excluding impact of credit risk mitigation, credit conversion factors and risk weighting factors, as defined under Basel II rules.

(2) Mitigating credit risk by using guarantees results in exposures moving from their original exposure group to exposure groups with a lower risk weighting factor. Consequently, sometimes the extent of exposure in a given exposure group, after credit risk mitigation, is higher than the extent of exposure in this group before risk mitigation.

Counter-party credit risk

Counter-party credit risk (CCR) is the risk that the counter-party to a transaction will be in default before final clearance of the transaction cash flows. Economic loss would be incurred only when the transaction with the counter-party would have a positive economic value upon such default. The market value of the transaction, which may be positive or negative for either party, actually depends on volatility of market factors. Should the counter-party be in default, and the transaction have a positive fair value, this may cause the Bank to incur a loss, liquidity issues and difficulties in carrying out further transactions. Risk factors which impact counter-party credit risk are: Credit risk, market risk and liquidity risk.
The trading in financial derivatives is part of the Bank's management of assets and liabilities, and is subject to limitations prescribed by the Board of Directors. The Bank trades in these financial derivatives, both for its clients and for its own account, as part of the management of basis and interest exposure in the various linkage segments. The Bank operates in credit derivatives in its negotiable portfolio. These investments are individually reviewed by the Risk Management Committee, and are submitted for approval by the Asset and Liability Management Committee headed by the President.

Restrictions and controls - a limit restriction applies for banks and sovereigns, including reference to derivatives. Furthermore, a restriction applies to customer facilities based on certain parameters. The Risk Control Division includes a dedicated department, specialized in control of exposure arising from capital market operations, which daily reviews clients active in this field. The trading room operations are controlled, including testing of compliance with various limitations prescribed by the Board of Directors and Executive Management.
The Bank applies another mechanism for control and management of client risk, by measuring VaR (Value at Risk) of the client portfolio on a regular basis and frequently during the day. Currently this mechanism is under further developments. In order to have another line of control. In addition to those which already taken on clients who act in all trade forms.

Risk mitigation - in order to participate in capital market activity, clients are required to provide collateral in accordance with Bank procedures. In its activities vis-à-vis banks and sovereigns, the Bank signs ISDA agreements and CSA addendums. This allows for setting off transactions, such that the amount exchanged between parties to the transaction is limited to the net exposure amount, thereby reducing exposure of either party. CSA addendums regulate funds transfer between parties to a transaction whenever exposure reaches a certain pre-defined level, thereby reducing counter-party exposure.
Below is the current credit exposure with respect to derivatives, as of December 31, 2012:

Details	Interest contracts	Foreign currency contracts	Contracts for sharesy	Commodit contracts	Credit derivatives[2]	Total
Face value of derivatives (OTC) after impact of add-on factor	195	1,079	-	1	4	1,279
Positive fair value, gross, of financial derivatives [1]	410	611	689	-	11	1,721
Total exposure with respect to derivatives	**605**	**1,690**	**689**	**1**	**15**	**3,000**
Collateral with respect to derivatives (before safety factors)	(94)	(247)	(1,635)	(1)	-	(1,977)
Impact of safety factors on collateral	53	110	1,078	-	-	1,241
Total current credit exposure after credit risk mitigation	**564**	**1,553**	**132**	**-**	**15**	**2,264**

(1) Includes exposure arising from counter-party credit risk with respect to client activity on the stock exchange, calculated based on stock exchange rules.
(2) The Bank's credit derivatives operations are not classified as brokerage operations. For information about transactions to buy and sell credit protection, see Note 19e.

Below is the current credit exposure with respect to derivatives, as of December 31, 2011:

Details	Interest contracts	Foreign currency contracts	Contracts for shares	Commodity contracts	Credit derivatives[2]	Total
Face value of derivatives (OTC) after impact of add-on factor	307	1,297	22	-	49	1,675
Positive fair value, gross, of financial derivatives [1]	1,097	1,075	522	-	-	2,694
Total exposure with respect to derivatives	**1,404**	**2,372**	**544**	**-**	**49**	**4,369**
Collateral with respect to derivatives (before safety factors)	(81)	(496)	(524)	-	-	(1,101)
Impact of safety factors on collateral	59	260	201	-	-	520
Total current credit exposure after credit risk mitigation	**1,382**	**2,136**	**221**	**-**	**49**	**3,788**

(1) Includes exposure arising from counter-party credit risk with respect to client activity on the stock exchange, calculated based on stock exchange rules.

(2) The Bank's credit derivatives operations are not classified as brokerage operations. For information about transactions to buy and sell credit protection, see Note 19e.

Securitization

The Bank does not operate in the field of asset securitization. It is Bank policy to avoid, in principle, investment in complex securitization instruments.

As of December 31, 2012, the Bank had no investments with securitization exposure.

Below are details of investments in collateralization exposures and relevant capital requirements:

	As of December 31, 2011		
	Risk weighting	Exposure amount	Capital requirements [1]
BB+ to BBB-	350%	25	8
B+ or lower	Deducted from equity	36	36
Total		**61**	**44**

(1) Capital requirement (except with respect to exposures deducted from capital) calculated at 9% of risk asset balance, in accordance with interim directive on application of Basel II, Pillar 3.

For further details of exposure to asset-backed securities, see Note 3 to the financial statements.

Market risk

Market risk to which the Bank is exposed in different financial instruments arises from their susceptibility to unexpected changes in interest rates, inflation rates and exchange rates, so that changes in market conditions may lead to changes in the fair value of the different financial instruments. Market risk management is intended to maximize Bank profit at the prescribed risk level. Exposure to market risk is managed in accordance with the limitations prescribed by the Board of Directors, within the frameworks of and subject to which, the Bank’s Executive Management acts, according to the market conditions at any given time.

The Bank focuses on two major market risk factors:

- Interest risk - the risk of erosion of capital as a result of future interest rate changes. The exposure to interest risk results from a lack of correlation between the period to maturity of the Bank’s assets and liabilities, or from incomplete correlation of the effect of change in interest rates on the different financial instruments.
- Linkage-basis risk - the risk of erosion in capital due to changes in the value of the linkage basis – changes in prices, exchange rates and inflation rates. The exposure to basis risk exists when the Bank’s assets and liabilities are denominated in different currency or linkage segments.

Any new activity by the Bank (new financial product, new exposure type, market making etc.) is approved by the Board of Directors, after studying the market risk associated with this activity and setting limitations and mechanisms for management, measurement and control of such risk, in accordance with the New Product procedure. In accordance with directives of the Bank of Israel, in the course of risk management at the Bank, it also accounts for exposure to market risk by subsidiaries.
Risk management at the Bank consists of two main risk clusters: the bank portfolio and the negotiable portfolio. Basel II defines the negotiable portfolio with emphasis on marketability, with clear guidance as to negotiable instruments which the Bank intends to trade for gain. The Bank's negotiable portfolio includes the portfolios managed as market maker in the trading room, as well as portfolios of securities held for trade and transactions in derivatives conducted as part of a specific market strategy, managed by Financial Management under specific limitations on exposure and profitability. The bank portfolio, which is the Bank's primary activity, consists of all transactions not included in the negotiable portfolio, including financial derivatives used to hedge the bank portfolio.

Interest risk in Bank portfolio

Interest risk in the Bank portfolio is the risk of erosion of the Bank portfolio as a result of future interest rate changes. The exposure to interest risk results from a lack of correlation between the period to maturity of the Bank’s assets and liabilities, or from incomplete correlation of the effect of change in interest rates on the different financial instruments.

Interest risk in the Bank’s bank portfolio is monitored on a regular basis, both in managing interest risk for the overall portfolio in VaR terms, and in EVE (Economic Value of Equity) terms - a model which reviews changes in the economic value of the portfolio under different assumptions regarding changes to the interest rate curve, including corresponding 2% shifts upwards/downwards of the interest rate curve and historical change for various time horizons, including one year.

Below is the impact of a parallel shift of the curve by 2% on the economic value of the Bank's portfolio in EVE terms (NIS in millions):

						December 31, 2012
						Change in fair value
	Israeli currency		Foreign currency			
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total
2% increase	89	(267)	57	(14)	(7)	(142)
2% decrease	(92)	179	(19)	7	2	77

						December 31, 2011
						Change in fair value
	Israeli currency		Foreign currency			
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total
2% increase	115	(33)	92	(12)	(3)	159
2% decrease	(131)	(85)	(42)	12	1	(245)

In preparing the mortgage repayment forecast for the Bank, assumptions with regard to prepayment are taken into account.

Market risk in the Bank's negotiable portfolio, primarily composed of portfolios managed in the trading room, is managed by means of quantitative limitations specified for each portfolio based on activity.

The VaR model (Value at Risk)

A summary of the models used by the Bank in calculating value at risk is presented below:

The VaR model is a statistical model that estimates the loss expected for the Bank in a certain investment period and at a pre-determined statistical level of assurance.

The VaR value constitutes an estimate of the level of market risk in financial terms. The VaR value can increase as a result of an increase in volatility in those risk factors, or as a result of an increase in the risk level inherent in different positions in a bank's portfolio. The VaR estimate is to be seen as a "risk thermometer", because an analysis of the VaR results on a day-to-day basis enables management to obtain value information on the risk level inherent in the Bank's various activities, to ascertain the Bank's risk profile, and to take the measures necessary to hedge certain risk in Bank operations. The Bank has specified restrictions (risk appetite) in VaR terms on the Bank's overall portfolio and on activity in option portfolios. VaR calculations for the Bank's overall portfolio are made daily. Calculations for the option portfolios are made hourly.

The VaR model is suitable for ordinary market conditions and does not estimate possible losses beyond the absolute level that was determined in the calculation. Therefore, the Bank strengthens the methodology with stress tests.

Stress tests – This model estimates the Bank's expected loss as a result of sharp fluctuations in the prices of risk factors in the market. Essentially, this model, by its various methods, estimates the potential loss in the "left tail" of the dispersion, i.e., beyond the significance level determined in calculating the VaR. The Bank's stress test methods are two-fold: subjective methods, relying on a decision by the Stress Test Committee established in the Bank; and objective methods, relying on factors including extreme events and scenarios that occurred in the past. The Bank has specified restrictions (risk appetite) in terms of stress tests.

As required according to the directives of the Bank of Israel, the Bank calculates the VaR values and the stress-test values on a monthly basis. The VaR is calculated based on a calculation method developed by the Bank in conjunction with world renowned experts. This calculation method was designed to improve the response speed of the VaR value to the volatility level of financial markets; in fact it combines multiple commonly used calculation methods. This method allows the Bank to handle situations where market volatility increases.

The Bank has set up a managerial and technical infrastructure to calculate the VaR model and the stress tests under different alternatives. The model results, with the analysis of these results, are regularly reported to the Bank CRO, to the Market Risk Manager, to the President, to the Risk Management Committee of the Board of Directors and to the Bank Board of Directors.

VaR estimates and stress tests are used by the Bank for its daily operation and in particular for specifying its risk appetite. The Bank examines the quality of models used in the VaR calculations, including through back testing, in order to improve the forecasting ability of the models that it uses. The Bank's VaR calculation - and in particular its back testing process - have been extensively validated in 2012, pursuant to guidance by the Bank of Israel with regard to model validation.

The Bank works constantly to improve the models that it uses, from all of the necessary standpoints, viewing these innovative models as important management tools. The Bank sees these models as highly important managerial tools, which are extensively used as tools for monitoring and controlling the risk level inherent in its activities, in different areas. Over the past year, the Bank has continued to review recent methodology evolution world-wide, in calculation of risk benchmarks (some - due to the most recent crisis in global markets).

As an outcome of this process, the Bank has expanded use of other models which allow the Bank to challenge its risk profile and in particular, those events beyond the significance level (exploration of the left-hand tail of the distribution); in 2012 the Bank started calculation of Stressed VaR, which estimates the VaR value in case of return to market conditions under the 2008-2009 financial crisis, when the market was in turmoil; the Bank also calculates the Expected Shortfall VaR, which estimates the average loss beyond the specified significance level.

Market risk in both portfolios (bank and negotiable) are managed overall by using the VaR model and stress tests. The Bank operates within the Board of Directors' limitations on market risk in terms of VaR and stress tests. For application of these models, the Bank's available capital is defined as a non-linked NIS-denominated source. The Board of Directors' limitations prescribe that the VaR for all of the Bank's activities in one-month investments will not exceed 6% of shareholders' equity, and that the maximum loss in stress tests, in the highest of all calculation methods, will not exceed 15% of equity. As noted above, the Risk Control Division conducts back testing to ascertain adequacy of the VaR model on a monthly basis, using advanced models in this field.

The internal estimate of VaR of the Bank Group presents the risk of a loss during a month, with the probability of its occurrence not exceeding 1%. Below is the maximum VaR for the Bank Group (NIS in millions):

	All of 2012	All of 2011
At end of period	167	223
Maximum value during period	239 (FEB)	286 (AUG)
Minimum value during period	144 (APR)	212 (MAR)

Following consulting provided by international experts, the Bank is conducting back testing of the adequacy of the new VaR model developed by the Bank. Review of the back testing of the VaR model for a 1-day investment horizon indicates that in 2012, too, the model was in compliance with criteria specified by the Basel committee.

Organizational structure of market risk management function (interest and basis)

Management of exposure to market risk is governed by a policy document, which is submitted annually for approval by the Bank Board of Directors. This document specifies, inter alia, the ranking of authority in market risk management and the frequency of discussions and reports on exposure status at the different levels. According to this procedure, the President is authorized to make risk-management decisions, subject to the frameworks prescribed by the Board of Directors. The Bank's risk management policies are discussed, formulated, and monitored by the Management Committee for the Management of Assets and Liabilities chaired by the Bank's President. This committee generally meets once a month, or more frequently, when special developments in the various markets occur or are forecast. According to this procedure, the Bank President is required to immediately report to the Board of Directors any deviation from the Board restrictions, and any occurrence of extraordinary events, whether internal or external.

The Finance Division Manager, who also functions as Risk Manager, heads a Monetary Committee that meets weekly to deal with practical aspects of the management of assets and liabilities. The Risk Manager is empowered to reach decisions on issues relating to the management of exposure in all the linkage segments, in order to implement the policies prescribed by the President, subject to the limitations prescribed by the Board of Directors. The Manager, Financial Division specifies guidelines for current operations of market risk management, subject to limitations specified by the Board of Directors.

The Manager, Financial Division reports to the Bank President any deviation from management limitations, in excess of the deviation permitted to the market risk manager. Any use of the market risk manager's authority to deviate should be reported at the next meeting of the Management Committee on Asset and Liability Management after the date of such deviation.

Examination and control of the various market risks is carried out on a day-to-day basis by the Financial Management Sector in the Finance Division. Market risk controls are carried out by the Risk Control Department in the Risk Control Division. The mechanisms for quantifying the exposures and controlling the compliance within the approved activity frameworks are anchored in internal work procedures. The Board of Directors also holds a quarterly discussion on the "Risk Document", as defined in Proper Conduct of Banking Businesses regulation 310, due to incidence on January 1, 2014.

Upon any unusual occurrence in the capital market, such as an unexpected change in interest rates, shake-ups in the foreign currency markets, changes in fiscal and/or monetary policy, the aforementioned committees convene for a special discussion in order to reach the decisions required by these occurrences.

Nature and scope of reporting systems for market risk (interest and basis)

The Bank operates a “risk monitoring forum" which convenes quarterly or more often, with the objective of setting the Bank's extreme scenarios, to discuss and prescribe the methodology for managing and controlling risk and to handle controlling risk, market, interest and liquidity risks. The Forum is headed by the Manager of the Risk Control Division. Also members are representatives of the Finance Division, of the Risk Control Division and of the Accounting and Reporting Department. The regular activities of the forums enables the existence of day-to-day communications regarding the management of different risk among all the divisions in the Bank that are take part in the process of managing and controlling risk. In 2012, this forum expanded its activities and now also handles issues arising from the validation process at the Bank.

Hedging and risk mitigation policy

The Bank reduces exposure to market risk of on- and off-balance sheet positions by initiating hedging derivatives transactions, managing composition of the debenture portfolio, and price alignment aimed at promoting activity in desired areas. Derivatives transactions, which are identified as hedging balance sheet positions in accordance with accounting rules, are to be specified as hedge accounting transactions, in accordance with the Bank's hedging procedure. Hedge effectiveness is the degree of correlation between changes in fair value or cash flows of the hedged item and of the hedging derivative. The hedge is considered highly effective if the changes in fair value or cash flows of the hedged item are nearly fully set off by changes in fair value or cash flows of the hedging instrument. When hedging instruments and hedged items are not fully identical, hedge effectiveness is tested quarterly.

Capital increase (erosion), NIS in millions

			Scenarios		Extreme historical scenario(1)	
	10% increase	5% increase	5% decrease	10% decrease	Maximum increase	Maximum decrease
CPI	759.8	379.9	(379.9)	(759.8)	110.9	(65.3)
Dollar	26.1	4.3	(1.9)	2.8	1.7	(1.4)
Pound Sterling	(2.1)	(0.8)	1.1	2.1	(0.6)	0.8
Yen	(2.7)	1.3	(1.3)	2.9	1.3	(1.0)
Euro	7.0	2.1	2.8	8.9	1.6	1.5
Swiss Franc	0.1	0.1	0.0	0.1	0.0	0.1

(1) Extreme scenarios were calculated based on daily changes in the exchange rate and monthly changes in the CPI, in the last 10 years.

Impact of hypothetical changes in interest rates on fair value of financial instruments of the Bank and its subsidiaries (NIS in millions) is as follows:

Fair value of financial instruments before impact of hypothetical changes in interest rates:

	Israeli currency		Foreign currency [2]			
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total
December 31, 2012						
Financial assets [1]	87,361	51,348	13,960	3,707	2,304	158,680
Amounts receivable with respect to financial derivatives[3]	68,105	5,316	48,135	7,889	5,294	134,739
Financial liabilities [1]	(89,998)	(37,080)	(17,825)	(4,409)	(2,584)	(151,896)
Amounts payable with respect to financial derivatives[3]	(66,079)	(12,555)	(44,211)	(7,254)	(4,893)	(134,992)
Total	**(611)**	**7,029**	**59**	**(67)**	**121**	**6,531**
December 31, 2011						
Financial assets [1]	[5] 79,294	46,950	14,884	3,402	2,358	[5] 146,888
Amounts receivable with respect to financial derivatives[3]	[5] 71,695	4,963	44,939	9,745	7,870	[5] 139,212
Financial liabilities [1]	(78,478)	(36,180)	(17,770)	(4,490)	(2,504)	(139,422)
Amounts payable with respect to financial derivatives[3]	(70,985)	(10,742)	(41,730)	(8,698)	(7,799)	(139,954)
Total	**1,526**	**4,991**	**323**	**(41)**	**(75)**	**6,724**

Net fair value of financial instruments, after impact of changes in interest rates[4]:

	Israeli currency		Foreign currency[2]				Change in fair value	
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total	NIS in millions	In %
December 31, 2012								
Change in interest rates:								
Concurrent immediate increase of 1%	(321)	6,860	(4)	(93)	115	6,557	26	0.4%
Concurrent immediate increase of 0.1%	(581)	7,013	52	(71)	120	6,533	2	0.0%
Concurrent immediate decrease of 1%	(945)	7,453	132	(16)	129	6,753	222	3.4%
December 31, 2011								
Change in interest rates:								
Concurrent immediate increase of 1%	1,674	4,882	265	(43)	(85)	6,693	(31)	(0.5%)
Concurrent immediate increase of 0.1%	1,544	4,984	316	(42)	(76)	6,726	2	-
Concurrent immediate decrease of 1%	1,352	5,238	380	(37)	(64)	6,869	145	2.2%

(1) Includes complex financial instruments. Excludes balance sheet balances of derivatives and fair value of off-balance sheet financial instruments.
(2) Includes Israeli currency linked to foreign currency.
(3) Amounts receivable (and payable) with respect to financial derivatives, discounted using interest rates used for calculation of the fair value.
(4) Net fair value of financial instruments presented in each linkage segment is the net fair value for this segment, assuming the indicated change in all interest rates in the linkage segment. Total net fair value of financial instruments is the net fair value of all financial instruments (excluding non-monetary items), assuming the indicated change in all interest rates in all linkage segments.
(5) Reclassified.

For further details of assumptions used in calculation of the fair value of financial instruments, see Note 20 to the financial statements.

The Bank is required to allocate capital with respect to interest risk in the negotiable portfolio, for exchange rate risk for all banking activities and for option risk. The Bank uses the effective term to maturity method in measuring interest risk, and the Delta Plus method in measuring option risk. This method quantifies the risk associated with operations of the option portfolio based on the "Greek letter" values. These reflect the sensitivity of the option portfolio to moves in the underlying asset and in standard deviation.

In accordance with Basel I rules, the Bank is also required to calculate specific risk in the negotiable portfolio. Capital requirements with respect to specific risk are intended to provide protection against negative change in the price of a single security due to factors related to the individual issuer. This requirement relates to instruments in the negotiable portfolio, and replaces the capital requirement with respect to credit risk associated with these instruments, had they been held in the Bank's portfolio.

Capital allocation for basis risk is at 8% of the net open position in each currency.

Below is the capital requirement due to market risk by risk element (NIS in millions):

	As of December 31, 2012			As of December 31, 2011		
	Capital requirement			Capital requirement		
risk element(1)	Specific risk	General risk	Total	Specific risk	General risk	Total
Interest risk(2)	1	61	62	3	40	43
Equity risk	-	-	-	-	-	-
Foreign currency exchange rate risk	-	39	39	-	42	42
Total market risk	**1**	**100**	**101**	**3**	**82**	**85**

(1) Risk associated with options activity is included under the different components, and was calculated using the Delta Plus approach, as defined in the Supervisor of Banks' directive.

(2) Calculated using the Effective Duration approach, as defined in the Supervisor of Banks' directive.

Liquidity risk

Liquidity risk results from uncertainty as to the availability of sources and the ability to realize assets within a specified period of time and at a reasonable price. Liquidity risk is managed subject to the limitations of the Board of Directors and Executive Management, as described below, in an effort to minimize the losses deriving from an investment of surplus liquidity in assets that are highly liquid, but have a low yield.

The Bank has developed an internal model to estimate the liquidity needs and liquid resources, as required by Proper Conduct of Bank Businesses regulation 342 “Management of Liquidity Risk" and in accordance with Basel provisions. The Bank’s internal model is based on statistical findings on the public’s behavior. An information system was built for daily measurement, control and reporting of the liquidity status. The Bank has a Liquidity Forum, which convenes daily, under the responsibility of the Finance Division, which meets monthly to discuss the liquidity situation and to align the liquidity needs of different Bank units with the liquidity "providers" and liquidity managers. In addition, the Risk Control

Division performs back testing of model adequacy, as required by Bank of Israel directives.

Liquidity risk management is governed by a policy document submitted annually for approval by the Board of Directors. The policy document includes a ranking of authority levels, procedures, limitations and emergency plan in the event of a liquidity crisis. Bank management has set limitations and guidelines on the following:

- A ratio of liquid resources to financing requirements higher than 1, to be used as a “safety cushion”.
- Limitations on depositor concentration.
- Guidelines for scenario survivability.

Highlights of this policy are:
- A range of reports to management and to the Board of Directors, distributed regularly.
- Key risk indicators (both internal and external), which alert of potential liquidity issues for the Bank or for the banking system.
- Resource monitoring - rules for monitoring source composition, especially for volatile sources. For the purpose of liquidity risk management, sources are distinguished by client types and by their degree of volatility. Guidelines have been specified with regard to the ratio of volatile deposits to other deposits.
- Survival horizon - measurement of the duration (in days) in which the Bank can survive on its own resources, without raising any external resources. The survival outlook is reviewed in the normal course of business and under four major extreme scenarios.
- Detailed emergency plan. This plan is part of the emergency financial procedure approved by the Board of Directors.

The Bank regularly reviews global practices in this area, including Basel III directives and FSA guidance, and will complete in the first half of 2013, as required, its preparation for the updating and application of the updated the Bank of Israel's Proper Conduct of Banking Business Regulation 342 "Management of liquidity risk", which is also based on this practice.
Liquidity risk at the Bank is managed conservatively, maintaining high liquid reserves and constantly evaluating the Bank's position under liquidity scenarios of different severity and attributes - in both NIS and foreign currency. Note that the Bank's debenture portfolio, used as liquid means, has very high levels of liquidity and credit quality.
In 2012 there were no recorded deviations from the Board of Directors’ limitations.

Nature and scope of reporting systems for liquidity risk
In conjunction with application of Regulation 342, a system of periodic and immediate reports to various entities at the Bank has been implemented. The Bank Board of Directors and management receive various reports on a daily, weekly, monthly and quarterly basis. Unusual events in liquidity management, including unusual developments in liquidity sources of the Bank, are immediately reported to management and/or to the Board of Directors.

- Daily liquidity report – a summary report of compliance with limitations set by the Board and management. of forecasted excess liquidity over the coming year, of composition of sources, of compliance with stress scenarios and intraday reporting of daily liquid balances in foreign currency and the daily forecast for the near future. All of the reports are in the central Financial Management portal, which is regularly updated to present the current situation to all relevant officers, clearly and at different levels of detail.
- Weekly liquidity report - report submitted to the Management Forum.

- Monthly liquidity report - report submitted to the Management Committee and to the Board of Directors.
- Quarterly liquidity report - report submitted to the Board of Directors, in conjunction with the Exposure Document.

Surplus liquid means over financing requirements in NIS is invested mainly in deposits with the Bank of Israel and in government debentures. Surplus liquid means over financing requirements in foreign currency is invested with the Bank of Israel, with the Federal Reserve Bank and in highly rated debentures which may be quickly realized. In 2012, investments were primarily in debentures issued by the State of Israel denominated in foreign currency. The credit exposure management policy reflected in management of excess liquidity in foreign currency has been revised in line with the global economic reality. The Bank frequently reviews credit facilities to various financial entities and primarily works with banks with the highest level of financial robustness, for the shortest duration possible, while maintaining diversification among different entities. In 2012, activity in this area vis-a-vis foreign banks was negligible.

Presented below are major data reflecting market risk, as reflected in the financial statements, while relating to the difference between the accounting presentation and measurement of economic exposure:

Financial capital – As of December 31, 2012, the Group capital exceeded its non-monetary items by NIS 7,311 million. In 2012, free capital for the Group, including financial capital, primarily financed uses in the non-linked NIS segment and in the CPI-linked segment, in line with the current asset and liability management policy at all times.

Linkage status – Details on the assets and liabilities in the various linkage segments at December 31, 2012 and December 31, 2011 are presented in Note 17 to the financial statements. However, the extent of the Bank's economic exposure is not fully reflected in the positions included in this note. In investees, as explained below.

Surplus CPI-linked assets of the Group, which include balance sheet and off-balance-sheet items as of December 31, 2012 as presented in Note 17 to the financial statements, amounts to NIS 8.0 billion, representing the economic exposure. As of December 31, 2011, after attribution of the general and supplementary provisions for doubtful debts to free capital, and classification of certain troubled loans to the non-linked NIS segment, excess use in this segment amounted to NIS 5.2 million.

Excess assets in foreign currency for the Group as of December 31, 2012 amounted to NIS 115 million. After adjustment of the economic reference to deposits used to cover investments in overseas subsidiaries, which are presented as non-monetary items, and to temporary impairment of investments in securities, the position in this segment amounts to surplus uses of NIS 43 million. As of December 31, 2011, the foreign currency position for the Group, after the aforementioned adjustments and after attribution of the general and supplementary provision for doubtful debts to free capital and classification of certain troubled credit to the NIS-denominated, non-linked segment, amounted to surplus uses of NIS 309 million.

The position in the non-linked NIS segment balances the open economic positions in the CPI-linked and foreign currency segments.

In Addendum D to Management Review, the Group's exposure to interest on a consolidated basis is presented in terms of average effective duration and in terms of fair value. Cash flows used in calculating exposure are based on assumptions with regard to withdrawal rates at exit points for early mortgage repayment. The percentage of withdrawals is based on empirical data.

For further details of assumptions used in calculation of cash flows and fair value of financial instruments, see Note 20 to the financial statements.

Below is the average effective duration of assets and liabilities as of December 31, 2012:

	Including early repayment assumptions (1)					Excluding early repayment assumptions				
	Assets		Liabilities		Average effective duration difference	Assets		Liabilities		Average effective duration difference
	Average effective duration	Fair value	Average effective duration	Fair value		Average effective duration	Fair value	Average effective duration	Fair value	
Non-linked	0.84	155,465	0.92	156,077	(0.08)	0.90	155,554	0.99	156,137	(0.09)
Linked to CPI	3.18	56,664	3.50	49,635	(0.32)	3.71	56,961	3.51	49,635	0.20
Foreign currency and linked to foreign currency	1.44	80,974	1.06	80,860	0.38	1.44	80,974	1.06	80,860	0.38
Total	**1.46**	**293,103**	**1.41**	**286,572**	**0.05**	**1.61**	**293,489**	**1.44**	**286,632**	**0.17**

(1) For details about fair value calculations and early maturity assumptions, see Note 20 to the financial statements.

In the non-linked NIS segment, the effective duration of liabilities is higher than that of assets by only 0.08 years, due to the fact that most of the activity in the unlinked shekel sector is at variable interest, linked to the prime rate, and the resultant interest risk is minimal. The effective duration gap does not reflect the degree of risk in exposure to fixed interest, which, as noted, is measured in the VaR model and stress tests. Excluding these early maturity assumptions, the effective duration of liabilities exceeds that of assets by 0.09 years.

The difference between internal rate of return (IRR) of financial assets and IRR of financial liabilities is 2.17%. Excluding the early maturity assumptions, the difference is 0.46%.

In the CPI-linked segment, the effective duration of liabilities exceeds that of assets by 0.32 years. Calculation of the effective duration is based on assumptions with regard to early withdrawals of savings and loans. Excluding these assumptions, the effective duration of liabilities exceeds that of assets by 0.2 years.

The difference between IRR of financial assets and IRR of financial liabilities is 0.64%. Excluding the early maturity assumptions, the difference is 0.65%.

In the foreign currency sector, the duration to maturity of assets exceeds that of liabilities by 0.38 of a year. In this sector, most of the activity is in variable interest, linked to the Libor rate, and, therefore the duration to maturity in this sector is low. The effect of the assumption of prepayment of savings and loans on differences in the duration to maturity and IRR is negligible.
The difference between IRR of financial assets and IRR of financial liabilities is 1.73%.

Term to maturity - The Bank's cash flows by term to maturity, as detailed in Note 18 to the financial statements, differ in character between different linkage segments, according to the type of activity in each sector.

In the non-linked NIS-denominated sector, most of the activity on the sources side is concentrated in terms of up to one year. As of December 31, 2012, some 84% of all liabilities have such terms (compared to 88% as of December 31, 2011), and 50% have terms of up to one month (compared to 55% as of December 31, 2011). As of December 31, 2012, some 50% of all assets have such terms (compared to 41% as of December 31, 2011), and 39% have terms of up to one month (compared to 23% as of December 31, 2011).

In the CPI-linked sector, the main activity on the sources side was soliciting deposits. Most of the deposits are for terms of 6-15 years, with optional withdrawal after two or three years, respectively. According to the Supervisor of Banks' directives, these balances are presented upon the nearest withdrawal date. Some 65% of all liabilities have terms of 2 years or more (same of December 31, 2011). In 2012, the Bank recycled 117% of withdrawals from CPI-linked deposits with renewed deposits of various types offered by the Bank, compared to 124% recycling in 2011.

In foreign currency, there are surplus long-term uses financed from short-term sources of up to one year. Past experience has shown that the short-term deposits are recycled regularly, constituting a basis for long-term uses in foreign currency.

Soliciting sources and Bank liquidity status - During 2012, there was an increase in the Bank's balance of deposits from the public. The balance of deposits from the public rose from NIS 119.2 billion on December 31, 2011 to NIS 128.5 billion on December 31, 2011, an increase of 7.8%.

The increase was primarily in the non-linked segment, in which total deposits from the public amounted to NIS 83.4 billion, an increase of 14.8% compared to 2011. In the CPI-linked sector, deposits from the public amounted to NIS 21.8 billion, a decrease of 5.2%, and in the foreign currency sector - to NIS 23.3 billion, a decrease of 1.7% compared to 2011.
In 2011, there were no limits on the possibility of soliciting different types of deposits in the Bank.

Market risk associated with derivatives activities

The trading in financial derivatives is part of the Bank's management of assets and liabilities, and is subject to limitations prescribed by the Board of Directors. The Bank trades in these financial derivatives, both for its clients and for its own account, as part of the management of basis and interest exposure in the various linkage segments.
The Bank trades in financial derivatives in the foreign currency, non-linked Israeli currency and CPI-linked Israeli currency sectors.
The trading in financial derivatives is mainly conducted in the Bank's trading room and is classified into three categories: hedging trades, trades for the purpose of asset and liability management (ALM) and other trades, as detailed in Note 1.O to the accompanying financial statements.

The Bank operates in credit derivatives in its negotiable portfolio. In these operations, the Bank guarantees eligibility for payment in case of change in credit rating, failure to meet obligations or any other credit event related to counter-parties which are states or overseas banks. These investments are individually reviewed by the Risk Management Committee, and are submitted for approval by the Asset and Liability Management Committee. The par value of these credit derivatives as of December 31, 2012 amounted to NIS 168 million, compared to NIS 563 million at the end of 2011.

The policy for managing the options portfolio is based on the "delta-neutral" strategy. The activities in options are subject to the quantitative limits prescribed by management, which include delta exposure (sensitivity of option price to change in price of the underlying asset), maximum VaR value for an investment of one day at an absolute level of 99% calculated by the Monte Carlo method and maximum losses under different scenarios.

The Bank operates, as part of its risk management system, a module which tests the VaR, sensitivity of option prices to changes in various parameters which determine its price (such as: price of underlying asset, standard deviation and interest rate), and the value of stress tests on the Bank's option portfolio. System VaR calculations are made hourly, intraday

The volume of transactions in financial derivatives according to the different categories is detailed in Note 19.E to the financial statements.

Operating risk

Basel I directives referred to operating risk as residual risk, and in fact defined it as risk which is not market risk nor credit risk. Basel II directives explicitly defined operating risk as the risk of loss due to failure or inappropriateness of internal procedures, people, systems or external events. Furthermore, Basel II, Pillar 1 includes capital requirements for operating risk. For details of the Basel II guidelines, see the chapter on Legislation and Supervision of Bank Group Operations.

Operating failure events which occurred at financial institutions over the past 15 years have increased legislator awareness and that of financial institutions to operating failure events and their main attributes, including:

A. Operating events may occur throughout the organization and are inherent to financial institution operations.

B. These events may result from an operating failure or may also be combined with other risk types, such as market risk, credit risk, liquidity risk, reputation risk etc.

C. A significant share of operating failures has very low probability but relatively large damage potential.

D. Operating events sometimes occur which are not under control of the financial institution, and may develop as a result of external events, some of which are unforeseen, with chances of occurring which cannot be estimated in advance, such as: natural disaster, security event.

Operating risk is inherent by its nature, and exists throughout the organization. Bank management and the Board of Directors attach great importance to this risk, and take an integrative approach to handling and management of operating risk, as an integral part of the overall corporate culture, by implementing this culture by means of training, dissemination of related content and application of elevated standards of operating control at all levels. The operational risk manager for the Bank is the head of its Risk Control Division. The Bank approach is that responsibility for operating risk management lies primarily with managers and staff of the different lines of business.

On February 14, 2012, the Bank of Israel issued Proper Conduct of Banking Business Regulation 350 with regard to operational risk management (hereinafter: "Regulation 350"). This regulation will become effective on January 1, 2013. The Bank is prepared to implement this regulation.

Bank policy with regard to operating risk states that this is a process which requires creation of an appropriate, enterprise-wide corporate culture in order to handle it. The policy addressees how risk is managed and regularly reviewed at the Bank via committees and forums, such as the Management Committee on this subject, tasked with development of plans, processes and procedures for risk management in all material products, activities, processes and systems of the Bank. The Stress Scenario Forum at the Bank is tasked with specifying stress scenarios at different severity levels, in order to quickly identify events and malfunctions, and handle them so as to reduce their frequency and severity of the damage arising there from. The Bank also analyzes external events in Israel and overseas, which may provide information about potential circumstances and damage which may result in materialization of operating risk. Risk management is also achieved by means of the Internal Control Trustees forum, as well as a forum headed by Bank division managers, designed to handle such risk at division level. Concurrently, the Internal Control Forum, tasked with integrating multiple central control entities, including the Compliance, Operating Risk, Process Engineering and Internal Audit units.

At the end of 2011, the Board of Director's Risk Management Committee and Plenum approved a new policy document on internal control, including reference to Bank handling of operating risk. This document specifies the high-level principles for handling internal control aspects, and is based on the Basel Committee directive dated 1998. In late 2012, the Board of Directors' Risk Management Committee and the Board plenum approved an update to the policy document related to operating risk, as part of Bank preparations for implementation of Regulation 350.

Another layer in the area of operating risk is that of internal audit, which acts independently. The operating risk policy specifies the role of Internal Audit as the entity in charge of carrying out periodic audits of risk management processes, taking part in methodologies for capital calculation with respect to risk, involvement with fraud and embezzlement issues, data gathering, documentation, debriefing and reporting of events, participation as observer on committees and involvement with the Internal Control Forum. The policy also specifies the roles of different professional units and of branches.

In recent years, the Bank has prepared to put in place comprehensive infrastructure of processes and methods for handling operating risk. These preparations include, inter alia, the following:

- Deployment of a corporate culture, as determined by the Board of Directors and by Bank management, by means of training and instilling a supportive corporate culture throughout the organization.
- Putting in place an appropriate organizational structure for the Risk Control Division.
- Appointment of internal control trustees in branches and headquarters units.
- Assignment of a dedicated representative of the Risk Control Division in the trading room.
- Conducting risk surveys and establishing work plans to handle those risk factors identified.
- Quantitative data gathering and analysis with respect to actual monetary losses.
- Creation of an enterprise portal for management and handling of operating risk and SOX.
- Debriefing various events.

In 2007, the Bank conducted operating surveys to map these risk elements for most Bank departments. These reviews are one of the major tools used in identifying operating risk in order to mitigate it. Findings of these operating risk reviews, as well as reports of relevant events, are discussed by the Steering Committee on Operating Risk, headed by the Operating Risk Manager. The Bank is taking action to eliminate gaps as they are identified, and to improve controls in order to ensure minimized operating risk. This is based on priorities derived from the risk severity and probability, and based on decisions by the Steering Committee. The Operating Risk Department closely monitors progress made on required improvements and reports to the Steering Committee. Since then and in 2012, the Bank continued to conduct surveys which were integrated with process mapping and control review as part of application of provisions of the Sarbanes-Oxley Act (SOX). In early 2013 the bank of Israel directed the bank, that the Accounting and report, department will be responsible for SOX.

The Bank is preparing to conduct operating risk surveys, including mapping of business processes and risk & control self-assessment (RCSA) in a prolonged process over a 3-year period. The Bank is reviewing how also to include, in the risk survey process, compliance infrastructure surveys and legal risk surveys - utilizing the overall perspective and interaction between these risk factors.

In 2012, the Bank launched a process to specify a range of Key Risk Indicators (KRI), which would present in quantitative values statistical benchmarks which reflect various risk factors, and would be used to measure operating risk in various areas at any time and over a period of time. The Bank intends to use these indicators as from 2013.

As part of preparations for handling operating risk and for application of the Basel directives on this issue, the Risk Control Division gathers and identifies operating risk and loss / near loss events from all Bank units. The Risk Control Division operates the Operating Risk Management system of the Bank, used as a repository for managerial information and as a key tool for analysis and reporting of the level of operating risk at Bank business units. This system was expanded in the last year with additional internal control aspects, and additional models were developed for information security, internal audit and compliance.

The risk monitoring process at the Bank includes reporting of internal financial data, operating data, regulatory compliance data and external data with regard to events and conditions relevant to operating risk. These reports include regular reports made by the business units to the Risk Control Division, and integrated reporting routines to Bank management and to the Board of Directors.

Operating risk mitigation

Due to the significance of operating risk, the Bank takes different steps to mitigate this risk. The most important step is to instill a corporate culture which promotes strong awareness of operating risk, and of deployment of risk-mitigating processes, as well as to implement operating procedures with regard to risk control and to deliver training to Bank employees. The Bank has developed a mechanism designed to empower internal control officers with tools for conducting lesson learning processes at their units, in addition to lesson learning processes regularly conducted by the Bank.

The Bank has established a policy and operating plans for case of emergency, for backup, recovery and business continuity in case of physical damage to Bank infrastructure.

Mitigating operating risk via insurance - The Bank is insured under a banking insurance policy, against damage which may be incurred in the course of normal operations, as a result of human error, fraud, embezzlement etc. The Bank has also obtained an officers' insurance policy, which applies to all officers at the Bank and at the different Bank Group companies, which provides insurance coverage for personal claims which may be filed against officers with respect to their actions in the course of their position with Group companies.

The Bank has obtained specific insurance policies for property damage and liability, which provide insurance coverage of Bank property and liability.

Information security

In accordance with Proper Conduct of Banking Business regulation 357, the Bank appointed a Data Security Manager, who reports to the Manager, Risk Control Division. The data security unit, headed by the Data Security Director, is responsible for prescribing the Bank's data security policy, for developing data security software, and to follow-up its implementation in the Bank, examining the effectiveness of the data security system and dealing with exceptional data security events. Information security policy at the Bank is implemented, inter alia, by the Information Security Department of Mizrahi-Tefahot Technology Division Ltd., a wholly-owned subsidiary of the Bank. See also under chapter on IT above.

Equity positions in bank portfolio

For details of equity investments in the Bank portfolio, see Notes 3 and 6.A. The investment balance includes investments in negotiable and public shares amounting to NIS 4 million, and investment in non-public shares amounting to NIS 175 million.

	As of December 31, 2012	
	Fair value	Capital requirement(1)
Shares	64	6
Venture capital / private equity funds	115	10
Total equity investment in bank portfolio	179	16

	As of December 31, 2011	
	Fair value	Capital requirement(1)
Shares	68	6
Venture capital / private equity funds	35	3
Total equity investment in bank portfolio	103	9

(1) Capital requirement calculated at 9%, in accordance with interim directive on application of Basel II, Pillar 3.

Legal risk

Proper Conduct of Banking Business Regulation 350 concerning "Operating risk" defines legal risk to include, inter alia, exposure to fines or penalties arising from supervisory action, as well as from individual arrangements. This definition is wider than the definition in Proper Conduct of Banking Business Regulation 330 on "Risk management", where legal risk is defined as "risk of loss due to inability to legally enforce an agreement".

The Bank regards legal risk in its wider definition, with regard to Bank conduct in its relationships with various stake holders (clients, suppliers, other third parties etc.) Legal risk includes risk arising from legislative and regulatory provisions, rulings by judiciary or quasi-judiciary authorities as well as legal risk arising from regular Bank operations. The Chief Legal Counsel for the Bank has been appointed Chief Legal Risk Manager. The Bank constantly strives to minimize as much as possible the legal risk associated with its current operations, and acts to disseminate a practical culture leading to identification and mitigation of legal risk in all its different aspects.

The Bank's Legal Division regularly analyzes the legal risk element of its activities, the risk boundaries (arising, for example, from the counter-party identity, from creation of collateral etc.) as well as specific risk attributes while reviewing risk level and exposure there to, with attention to the different lines of business at the Bank.

The Bank's Legal Division applies internal processes to ensure regular monitoring of developments in legislation, rulings and other regulatory provisions which could have implications for the day-to-day activities of the Bank Group. In this context, the Legal Division provides guidance to relevant Bank entities with regard to implementation of the implications arising from these updates. The Legal Division provides regular counsel to different Bank units, including to some subsidiaries. This is done, inter alia, by providing opinion, editing and updating legal documents, support for updates to procedures etc.

The Bank has specified procedures to help in minimizing legal risk, including regulating the interface between the Legal Division and different Bank departments. The Legal Division is also involved in training delivered to branches, at the Bank's Training Center and in compiling professional eLearning kits for imparting the legal knowledge required for regular Bank operations.

Similar reference is made for Bank affiliates overseas (branches and subsidiaries), with these affiliates receiving assistance from local external attorneys approved by the Bank's Legal Division. The Bank's overseas subsidiaries and affiliates have adopted similar procedures with regard to management of legal risk, and provide immediate and quarterly reports to the Legal Risk Manager of the Bank with regard to any legal risk identified in these entities.

Compliance

The complexity and development of banking activity requires the Bank to adhere strictly to fulfilling the range of obligations imposed on it in its business ties with its customers, by virtue of statutory provisions applicable to a banking corporation. As stipulated by Proper Conduct of Banking Business Regulation 308 with regard to Compliance Officer, the Bank has appointed a Compliance Officer who heads the Compliance and AML Department. In June 2012, as part of reorganization of the Risk Control Division, a Chief Compliance Officer for the Bank Group was appointed in the Risk Control Division. The Compliance Department, headed by the Bank Compliance Officer, is no longer part of the Legal Division, and now reports to the Chief Compliance Officer in the Risk Control Division.

In November 2011, the Bank's Board of Directors approved an updated compliance program. The Compliance Department acts to disseminate a compliance culture across the Bank and strives to implement consumer provisions applicable to Bank relationships with its clients, so as to minimize the likelihood of any breach of laws and regulations, to discover, as early as possible, any such breach - thereby minimizing Bank exposure to claims and other damage which may ensue.

The Compliance Department conducts compliance surveys on different issues and provides training to deploy compliance systems at the Bank. The Compliance Officer is member of different forums at the Bank, in order to ensure an enterprise-wide view of various compliance aspects.

Prohibition of money laundering

In June 2012, as part of reorganization of the Risk Control Division, a Chief Compliance Officer was appointed in the Risk Control Division, who is also in charge of implementation of the Prohibition of Money Laundering Act, and of the Prohibition of Financing Terrorism Act for the Bank Group, including Bank affiliates overseas. The Compliance Officer, who is also in charge of implementation of the Prohibition of Money Laundering Act, and of the Prohibition of Financing Terrorism Act for the Bank, is no longer part of the Legal Division, and now reports to the Chief Compliance Officer in the Risk Control Division.

The Compliance and Prevention of Money Laundering Department implements statutory requirements on this issue. The Department handles subjective reports of unusual activity reported to the AML Authority, and conducts various controls over activity in different accounts based on their risk profile, providing regular advice to branches on this matter and delivers training customized for bank staff in different roles. Moreover, in line with Bank policy set by the Board of Directors in May 2010, a knowledge test is administered once every two years to all Bank employees. Such a test was conducted in 2012.

The Bank operates different computer systems for identifying unusual activity and for monitoring the handling of subjective reports.

The Bank applies on Group basis, with required changes, its policy in this area as well as statutory provisions, at its subsidiaries and branches in Israel and overseas.

On September 19, 2012, the Bank received a letter from the Supervisor of Banks, informing the Bank of a monetary sanction imposed on the Bank, amounting to NIS 3.8 million, for breach of provisions of the Prohibition on Money Laundering Act, 2000. For more information see legal proceeding chapter.

Risk factors

For a discussion of the risk factors that impact the Bank and its activities, see the discussion in the chapter on risk management above. A mapping of the risk factors and their impact on the Bank Group are presented below:

Risk factor	Risk factor impact
Overall effect of credit risk	Intermediate
Risk from quality of borrowers and collateral	Intermediate
Risk from industry concentration	Intermediate
Risk from concentration of borrowers/ borrower groups	Intermediate
Overall effect of market risk	Intermediate
Interest risk	Intermediate
Inflation risk	Intermediate
Exchange rate risk	Low
Share price risk	Low
Liquidity risk	Intermediate
Operating risk	Low
Compliance risk	Low
Money laundering	Low
Legal risk	Low
Reputation risk(1)	Low

(1) The risk of impairment of the Bank's results due to negative reports about the Bank.

Description of methodology used by the Bank to estimate impact of different risk:

Market risk

The effect of the risk was measured using VaR values for each risk, with respect to the VaR value limit determined by the Board of Directors.

The Bank's Board of Directors prescribed the VaR limit in order to prevent the creation of high market risk. Therefore, it was prescribed that risk with VaR value equal to or higher than the Board of Directors' limitation has strong effect. Risk with VaR value equal to or higher than 70% of the Board of Directors' limitation has intermediate effect and the risk with VaR value below this is considered having a low effect.

Other risk

The degree of influence of credit risk, liquidity risk, operational risk, legal risk and goodwill risk – were determined based on management's assessments, as performed from time to time, and in coordination with the ICAAP process conducted by the Bank, and outcome there of, under leadership of the Bank's risk managers. The ICAAP process accounts for both qualitative and quantitative aspects, including the Bank's risk profile, outcome of various scenarios at the Bank and the capital planning process. In the fourth quarter of 2011, in conjunction with the ICAAP process, the Bank conducted self-assessment of the quality of risk management for risk mapped by the Bank. This process was based on rating the risk level and management quality, conducted independently by teams on behalf of risk managers and teams on behalf of risk control. This process added another dimension to the Bank's ability to evaluate the impact of different risk levels and their management quality on risk profiles and on the specified risk appetite.

Social involvement and charitable donation

As a business organization whose activities and achievements depend on the community in which it operates, the Bank sees itself as obligated to show involvement and to support all facets of the community's needs.

The Bank emphasizes a focused social area "Advancing and Nurturing Disadvantaged Children and Youth in Crisis" and channeled to it most of the charitable donations and volunteer activities of the Bank and its employees. The Bank is working to realize social policy in a manner that expresses its strength, involves the Bank's employees in active volunteerism and leverages its physical, financial and human abilities and resources by means of "Mizrahi-Tefahot in the Community". This social brand is intended to differentiate the social activities of the Bank and to create identification among the Bank's employees and managers. The focused communal activities are carried out with the maximum collaboration of its employees and managers, geographic diffusion and diversification of activities, while utilizing the Bank's diversification, the existence of extensive partnerships with communal organizations throughout the country, and intensified intra-organizational and extra-organizational community involvement.

Contributions to the community became a central and important goal on the agenda of the Bank's employees, while management is providing incentives and encouragement to employees to take part in these activities, and the results are already evident in the field and in employee response.

Some 125 Bank branches have connections to different social organizations and institutions working on behalf of disadvantaged children and youth at risk, in communities in which branches are located. “Adoption” of these organizations is reflected by volunteer work by branch and headquarters staff, assistance and mentoring while providing assistance to the populations they treat, and providing financial assistance – Bank donations for purchase of products to benefit the children and youth.

In 2012, the activity in the field was expanded significantly, by branches and Head Office units that have not yet forged ties with suitable organizations in the community, and activities with organizations already adopted by the Bank were intensified.

Within the scope of the Bank's activities, an educational package "Financial" was prepared, to train youth in financial areas and is moderated by employees of the Bank who volunteer in schools and social organizations. The "Financial" package was translated into Sign Language, in order to make it accessible to the deaf and hearing-impaired community in Israel, for which the Bank was awarded first prize in the Israeli Management Center's human resources competition, for promoting social agendas.

In 2012, the Financial package was upgraded by adding other relevant lessons, designed to allow additional audiences to use the content of this package.

In order to expand the range of partners in these activities, the Bank initiates projects to add additional stakeholders -

- Employees and family members - through the Passover Walk and the popular race of the Jerusalem Marathon, conducted in cooperation with the Israel Cancer Society.
- Clients – continuation of project "Partners by Choice" to include Bank clients in the designation of charitable donations to social organizations focused on helping children and youth, to whom the Bank provides support for social ventures. Upon conclusion of the project, the Bank's charitable donation was divided among 8 organizations selected by the clients.
- In conjunction with Bank assistance to non-profits who employ people with special needs, the Bank held several events designed to help these non-profits increase their revenues by enhancing public awareness of the important social endeavors of these non-profits and to help in gaining exposure for their following products:
- The Bank upgraded a unique website, "Added Value", was issued, listing community and environmentally-friendly products produced in community organizations by people with special needs, and by organizations which promote and distribute green products in support of the environment.
- The "Heart-felt creation for the community" fair took place, with 30 non-profits participating in order to expose their products to extensive audiences and to allow the non-profits to sell their products to tens of thousands of fair visitors.
- The Bank promotes an organizational culture which encourages its employees to purchase gift items for their own needs, in addition to purchases made by the Bank from these non-profits.
- The Bank conducted the "Added Value Shield" competition for social business entrepreneurship, with outstanding NGOs that leverage social causes for social business entrepreneurship.
- The Bank held a seminar for managers of social NGOs designed to provide them with managerial tools, to improve their management skills.

In 2012, the Bank intensified links with institutions of higher education, by cooperating with the Management College in establishing a banking track, sponsored by the Bank, delivering lectures to students by volunteer employees and managers and by providing scholarships for students in need of assistance.

The Bank also sponsored various benefits for children at risk, including:

- Realizing dreams and wishes of children with severe illness, together with Heartwish foundation and Bank employees.
- Together with Zichron Menachem foundation, which cares for children with cancer, the Bank held a fun day in Eilat for 150 sick children, with financing and assistance from Bank employees.
- The Smiles Train for children with cancer, together with Larger than Life foundation and with assistance from Bank employees.

Below is a list of new ventures launched by the Bank in 2012:

- "ZAZIM" – youth movements for the community. The project goal is to encourage youngsters and members of youth movements, to act and volunteer for the society and community in which they live.
- Art summer camp for youngsters with artistic talent from families of limited means in Ramat Gan, in co-operation with Shenkar College.
- Community activity in Lod - following relocation of Bank units to Lod, the Bank started being involved in this city, with the Bank and its staff helping in financing and carrying out significant social projects in the city.
- "Me for you" - an educational program for social entrepreneurship, volunteer work and empowerment of youth, especially those of limited means, in co-operation with LATET NGO.
- Pre-military school – assistance in funding a "cross-Israel" trek held by the pre-military schools for Israel, in which students at these schools meet with communities and neighborhoods where social and cultural activities will be conducted in co-operation with Bank employees.

In 2012, the Bank Group allocated NIS 6.1 million to social involvement and charitable donation, compared to NIS 3.6 million last year. In addition, Bank employees and managers invested in 2012 over 27,000 hours in community work on different projects, similar to last year.

Disclosure concerning the Internal Auditor

The following is information about the Chief Internal Auditor of the Bank Group, who started in office on July 7, 2011:

Name	Galit Weiser
Start of term in office	July 2011
Education	CPA; undergraduate degree in Accounting and Economics (Hebrew University); graduate degree in Business Administration (Hebrew University).
Experience	Deputy Chief Internal Auditor at the Bank; previously, Chief Internal Auditor of Bank Tefahot.

Pursuant to provisions of Section 146(B) of the Corporations Act, 1999 - the Internal Auditor is not an interested party of the corporation, an officer or relative there of.

Pursuant to provisions of Section 8 of the Internal Audit Act, 1992, the Internal Auditor holds no other position in addition to her position as Chief Internal Auditor, other than as Ombudsman, Internal Auditor of Bank Yahav and Auditor of Bank Mizrahi-Tefahot subsidiaries. Furthermore, the Bank’s Internal Auditor holds no position outside of the Bank which creates or may create conflict of interest with her position as Internal Auditor.

Pursuant to banking regulations (Internal Audit), this was effective until October 14, 2012.And to Proper conduct of banking business regulation 307 concerning "internal audit function" which became effective in July 2012.Audit staff is only appointed with consent of the Internal Auditor. Audit staff acts on behalf of the Internal Auditor for the purpose of internal audit, and is only instructed on audit-related matters by the Internal Auditor. Internal audit staff does not hold other positions with the banking corporation in addition to internal audit, other than as Ombudsman. Internal Audit staff may only sign on behalf of the banking corporation documents related to audit work or to inquiries from the public. Internal audit employees are terminated with due process and consent of the Internal Auditor.

As of December 31, 2012, the Internal Auditor is eligible to receive 144,253 option warrants to buy Bank shares. For further details, see Note 16.A. to the financial statements.

The Board of Directors believes that the extent of Bank securities owned by the Internal Auditor does not impact the quality of her work.

The Internal Auditor is a full-time employee of the Bank.

Appointment

In June 2011, appointment of the Internal Auditor was confirmed by the Audit Committee and the Board of Directors, based on the Auditor's experience and educational qualifications.

Identity of the Internal Auditor's Supervisor

The Internal Auditor reports to the Chairman of the Board of Directors.

Internal Audit work plan

Internal Audit work is based on a multi-annual audit plan focused on risk for a 4-year period from which an annual work plan is derived.

Considerations in determining the multi-annual audit plan

- Mapping of activities carried out by different Bank departments according to organizational structure, assignment of potential risk to each activity and setting audit frequency in line with the risk (relating separately to audit frequency at branches, headquarter departments and subsidiaries).
- Risk surveys conducted at the Bank.
- Regulatory requirements arising from directives of the Supervisor of Banks.
- Basel II directives and the ICAAP process.
- Current audit reports of the Bank of Israel.
- Findings in audit reports of the Audit Division.
- Decisions of the Audit Committee and the Chairman of the Board of Directors, as well as requests from the Bank's President.

The multi-annual work plan is prepared by the Internal Auditor, brought up for discussion by the Board of Directors' Audit Committee and sent to the Bank President. After discussion and recommendation by the Audit Committee, the plan is submitted for approval by the Board of Directors.

Accordingly, on January 21, 2013, the Board of Directors approved the Internal Audit work plan for 2013-2016.

Considerations in determining the annual audit plan

In addition to the aforementioned considerations, used as basis for determining the multi-annual audit plan from which the annual audit plan is derived, the annual work plan includes additional special tests required of Internal Audit by request of the Audit Committee. In addition, the audit refers to issues as requested by the Bank President.

Material Changes to the work plan are made by the Internal Auditor as needed, in coordination with the Chairman of the Audit Committee and/or the Board of Directors' Audit Committee.

Similar to the multi-annual audit plan, the annual audit plan is also prepared by the Internal Auditor and brought for discussion by the Board's Audit Committee. The plan is also submitted to the President. After the Board's Audit Committee recommends approval of the plan, the plan is submitted for approval by the Board of Directors.

Accordingly, on January 21, 2013, the Board of Directors approved the Internal Audit work plan for 2013.

Overseas audits or audits of held corporations

The Bank's Internal Auditor includes in the annual and multi-annual audit program the active corporations held by the Bank, during her tenure as their internal auditor, except for Bank Mizrahi Switzerland, which had its own internal auditor during the reported period. With respect to this company, the Internal Auditor verifies on a regular basis that there is proper internal auditing.

At Bank Yahav, a separate audit plan is submitted to the Bank Yahav Board of Directors.

Scope of employment of the Internal Auditor and their staff

The Internal Auditor is a full-time employee of the Bank.

The average number of positions for employees reporting to the Internal Auditor in 2012, including internal auditors of subsidiaries and overseas branches is as follows:

In Israel		Outside of Israel
Employees engaged in internal audit	Employees engaged in role of Ombudsman	Employees engaged in internal audit
43 (1)	6	2.5(2)

(1) Includes 4 full-time positions for audit at Bank Yahav. In addition, Internal Audit at Bank Mizrahi-Tefahot used outsourced services equivalent to 1 full time position.

(2) Includes use of external service providers overseas.

Conducting audits

The Internal Auditor performs the audit based on the generally accepted professional standards.

- Various legal requirements, including provisions of the Internal Audit Act, 1992, Banking Regulations (Internal Audit), 1992 which was effective until October 14, 2012, and regulatory authorities' instructions relevant to the audited area, including guidelines and directives of the Supervisor of Banks, including Proper Conduct of Banking Business Regulation 307 concerning "Internal Audit function", which became effective in 2012.
- Standards for Professional Engagement in Internal Audit of the Global Institute of Internal Auditors.

The Board of Directors and the Audit Committee believe that audit is conducted in accordance with the aforementioned professional standards so as to achieve the objectives of the internal audit.

Access to information

The Internal Auditor received complete access to all the information he needed pursuant to regulation concerning "internal audit function", as stated in Section 9 of the Internal Audit Law, 1992. including constant and direct access to the Bank's IT systems, including financial data. Note that in conducting audits of subsidiaries and overseas operations, auditors are also given full access as stated above.

Submitting report on Auditor's findings

The Auditor regularly sends every audit report to the Chairman of the Board of Directors, the chairman of the Audit Committee, the President and head of the internal audit unit. Audit reports are submitted in writing. Once every six months, the Auditor submits to members of the Audit Committee the list of all reports submitted during the six-month period. All of the reports are discussed in a forum including the division manager and/or official in-charge of the audited unit or activity. The significant reports, at the request of the President or the Chief Internal Auditor, are discussed in a forum headed by the President or the Bank's Executive Management. The Chairman of the Audit Committee, in consultation with the Internal Auditor, determines the material audit reports to be discussed by the Audit Committee.

On July 22, 2012, a semi-annual list was distributed in conjunction with reporting the performance of the Internal Audit work plan for the first half of 2012. This report was discussed by the Audit Committee at its meeting held on August 12, 2012. The annual summary report of Internal Audit in 2012 was distributed on February 21, 2013 and is scheduled to be discussed at the Audit Committee meeting to be held on March 20, 2013. Other major reports were discussed during the year at regular meetings of the Audit Committee.

Assessment of Internal Auditor's activities

The Board of Directors and the Audit Committee believe that the scope, nature, continuity of the activity and the work plan of the Internal Auditor are meant to realize the objectives of internal auditing.

Remuneration of the Internal Auditor

For details of remuneration and payments to the Internal Auditor, see under the chapter on Remuneration of Senior Officers.

The Board of Directors believes that the size of remuneration provided to the Internal Auditor should not influence her judgment with respect to his work.

Accounting Policy on Critical Matters

The consolidated financial statements of the Group are prepared in accordance with the directives and guidelines of the Supervisor of Banks on the preparation of annual financial statements of a banking entity. The significant accounting policies are detailed in Note 1 to the financial statements.

The application of generally accepted accounting principles by management at the time that the financial statements are prepared occasionally involves various assumptions, assessments and estimates that affect the amounts and business results reported in the financial statements. Some of the assumptions, assessments and estimates are critical to the financial position or the results of operations reflected in the Group's financial statements, because of the materiality of the matter, complexity of calculations or the extent of the probability that matters shrouded in uncertainty will be realized.

Provided below are accounting policies on critical matters:

Provision for credit loss is made as from January 1, 2011 in accordance with public reporting regulations of the Supervisor of Banks, which are based on US accounting standards codification ASC 310-10 and on guidelines by US supervisory authorities, as adopted by the Supervisor of Banks. The provision for credit loss is made in one of two tracks: individual provision and group provision, which also includes the provision for the housing loan portfolio based on a formula for extent of arrears. See Note 1.J. to the financial statements for details. The individual provision for credit loss is calculated based on public reporting regulations of the Supervisor of Banks, based on estimates by Bank management, with regard to expected cash flows and their dates, with respect to debt in excess of NIS 700 thousand. The expected cash flows would be received from different repayment sources of the debtor, including their business operations, private repayment capacity of the borrower, realized collateral provided to secure the credit, or guarantees provided by the borrower or by any third party. The provision for credit loss is the difference between the carrying amount of the debt and the value of expected cash flows, discounted using the effective interest rate of the original debt. Any debt constituting "final loss" should be written off no later than as stated in regulations. In cases where collateral is the exclusive source for debt repayment, value measurement is based on the fair value of collateral and the carrying amount of the debt is in excess of the fair value of collateral is written off against Expenses with Respect to Credit Loss. The actual losses could turn out to be different than the specific provisions made.

The group-based provision is made with respect to homogeneous groups with similar risk attributes of small debt balances (under NIS 700 thousand) as well as for non-impaired large debt balances. This provision is based on past loss rates by economic sector, as well as rates of on net accounting write-offs actually recognized as from January 1, 2011. In addition to calculating the range of historic loss rates for various economic sectors, as per the above, for determining the appropriate rate of provision, the Bank also accounts for other data, including trends in credit volume for each sector as well as sector condition, macro-economic data and general quality assessment of credit to each economic sector. Since the group-based provision is determined based, inter alia, on classification of debt as troubled and on timing of such classification, when determining the group-based provision amount, the Bank relies on estimates with regard to the borrower's financial stability and estimated repayment capacity, which are the basis for such classification as troubled debt and their timing.

The minimum provision for credit losses with respect to housing loans, calculated by extent of arrears, is based on specific directives by the Supervisor of Banks as to its calculation. The Bank reviews the debt for which a provision was made by extent of arrears, and if according to the Bank's judgment, the minimum provision is insufficient, a larger provision is made.

In addition, the Bank records a group provision for housing loans as well, except for provision by extent of arrears.
The Bank has put in place a methodology for calculating the group provision with respect to housing loans, whereby the provision amount is derived from the increase in current credit grant volume compared to past periods. The calculation method has been approved by the Supervisor of Banks.
For details of the Supervisor of Banks' draft concerning group provision for credit loss with respect to housing loans, see chapter "Legislation and Supervision of Bank Group Operations".
In addition, the Bank records a group provision for housing loans as well, except for provision by extent of arrears.
The Bank has put in place a methodology for calculating the group provision with respect to housing loans, whereby the provision amount is derived from the increase in current credit grant volume compared to past periods. The calculation method has been approved by the Supervisor of Banks.
For details of the Supervisor of Banks' draft concerning group provision for credit loss with respect to housing loans, see chapter "Legislation and Supervision of Bank Group Operations".

Derivatives are treated and presented based on US accounting standards codification ASC 815 and ASC 820. According to the guidelines, all derivatives are stated in the balance sheet at fair value. FAS 157 (ASC 820) defines fair value, and stipulates a consistent work framework for fair value measurement, by defining valuation techniques and a fair value ranking. The ranking divides instruments measured at fair value into three levels:

Level 1 - fair value measured using prices quoted for identical instruments on an active market accessible by the bank upon the measurement date.

Level 2 - fair value measured using observed data, either direct or indirect, which are not quoted prices stipulated under Level 1. Level 2 data include quoted market data on active markets, or on non active markets, if they exist, or data derived from or based upon such observed market data.

Level 3 - fair value measured by using non-observed data.

The Bank evaluates whether markets on which financial instruments are traded are active, based on the following parameters: Volume and value of transactions conducted on the market, current bid/ask spread and alignment of prices for similar transactions on the same market.
According to the standard, the non-performance risk should be reflected in estimating the fair value of debt, including derivatives, measured at fair value. The Bank estimates credit risk for derivatives using a model based on indications of credit quality of the counter-party, derived from prices of debt instruments of the counter-party traded on an active market, and from prices of credit derivatives based on the counter-party's credit quality. In the absence of such indications, the Bank calculates the adjustments based on internal ratings. The Bank reviews the materiality of the credit risk element compared to fair value as a whole, in conjunction with review of instrument classification under fair value ranking levels.

In May 2011, FASB issued an update to ASC 820 - "fair value measurement and disclosure". This is part of a FASB-IASB joint project designed to achieve compatibility in this regard. For entities applying the American standard, the new disclosure does not significantly alter prior requirements, but mostly clarifies prior requirements and provides new guidance.

The Bank prospectively applies the amendments set forth in ASU 2011-04, as from January 1, 2012. There is no mandatory application of the new disclosure requirements for financial statements for periods prior to initial application.

In June 2012, the Bank of Israel directed the Bank (in conjunction with a review of the banking system), that fair value measurement of a derivative instrument, when no quoted prices, liquid collateral or offset agreements exist which adequately secure the derivative's credit quality, and when no market information exists as to the credit quality of the counter-party (such as CDS or negotiable debentures of the counter-party) – shall be classified as a Level 3 fair value measurement. According to the Supervisor of Banks' directive, the aforementioned classification requirement shall apply to financial statements as from September 30, 2012, including an update of comparison figures.
See Note 1.T. to the financial statements for additional information. For details of derivatives measured at fair value by different fair value levels - see Note 20 to the financial statements.

Securities in the portfolio held for trading and in the portfolio of available for sale securities are stated at fair value, in accordance with the public reporting guidelines of the Supervisor of Banks. Securities classified in the portfolio held to maturity are measured at depreciated cost. The fair value of the securities is determined based on quoted market prices in active markets for the securities or for securities with similar terms, i.e. stock market price, quotes from recognized data services, such as Bloomberg, or quotes from banks acceptable to the Bank. The Bank uses internal models for reviewing the fair value of financial instruments for which there is no quote on a stock exchange, and does not rely entirely on prices obtained from counter-parties or from quoting firms. The fair value calculation was validated by the Bank's Risk Control Department, which does not participate in the fair value calculation process, assisted by an external professional consultant specializing in models for calculating fair value of financial instruments. Validation is conducted by reviewing the model assumptions and parameters; reviewing the model methodology and its application; and independently reviewing the model in comparison with other models, to the extent possible.
For details of securities measured at fair value by different fair value levels - see Note 20 to the financial statements.
The financial statements as of December 31, 2012 include critical estimates with regard to other-then-temporary impairment of several investments in securities, with a total original investment cost of USD 40 million (NIS 149 million). Total impairment recognized as other-than-temporary in nature as of December 31, 2012 amounted to USD 39 million (NIS 145 million). For the purpose of estimating the aforementioned impairment, the fair value of these investments was calculated using an internal model based on a methodology for assessment of the quality of collateralized debts, as well as on objective data, if available. In accordance with directives of the Supervisor of Banks, the fair value calculation is validated by an independent professional appointed for this purpose by the Bank. It is assumed that impairment compared to deviation of the original investment is not of a temporary nature, primarily in view of the significant decrease, the duration in which the quoted value has not increased, and the erosion of investments' safety cushions. The value of these investments in financial statements for December 31, 2012 is USD 1 million (NIS 4 million).

The actual value of these investments may turn out in the future to be materially different from the aforementioned estimate. The extent of impact on future financial statements may range from recording of a further expense amounting to USD 1 million (NIS 4 million), should it emerge that the investment value continued to decline, to recording further revenue amounting to USD 39 million (NIS 145 million) should it turn out that the full impairment was temporary.

The Bank has specified a validation procedure for fair value of instruments measured at fair value on a recurring basis on the financial statements, for which the Risk Control Division is responsible. The validation process includes review of the process for determining fair value, of the assumptions included in this process and the models used for calculation. The validation process refers to both the pure fair value, calculated at relevant market conditions according to standards and to the credit risk element included in fair value.

Liabilities for employee rights are calculated according to actuarial models, based on the discount rates prescribed by the Supervisor of Banks. The actuarial models include assumptions related to the mortality tables, disability rates, departure rates and wage hike rates. A change in any of the parameters could lead to a change in the amount of the Bank's liabilities for employee rights. Pursuant to the Supervisor of Banks' directive, the discount rate used in actuarial calculation for retired employees choosing a pension is 4%. In 2012, the Bank of Israel instructed banks to update the actuarial provisions based on a draft update of mortality tables, issued by the Capital Market Division on July 11, 2012 - reasoning that this draft is the best estimate available to banking corporations. The total impact of the Bank of Israel directive included on financial statements for the second quarter of 2012 amounted to NIS 3 million.

Bank liabilities for employee rights calculated based on an actuarial model amount to NIS 636 million. (Calculation of this liability included provision with respect to employee retirement at preferential terms)

The following is a sensitivity analysis of the total provision for employee rights to changes in key assumptions used as basis for the actuarial estimate, as of the transition date (NIS in millions):

	A 0.25% increase in discount rate	A 1% change in annual payroll increase rate		A 5% change in departure rate before retirement age		A 10% change in average benefit per retiree receiving benefits	
		Increase	Decrease	Increase	Decrease	Increase	Decrease
Severance pay provision	(5)	22	(20)	9	(10)	3	(3)
Budgetary pension	(3)	-	-	-	-	-	-
Bonuses	(2)	-	-	-	-	-	-

The financial statements include the benefit value of the stock option plan for Bank managers, estimated based on the opinion of an expert external consultant, using the Black & Scholes model based on various assumptions, mainly with regard to expected exercise date of the options and standard deviation of Bank share price. Changes in the price of the Bank's shares, the standard deviation for the Bank's shares and other factors which could affect the economic value of the benefit.

The benefit value is recognized by the Bank over the vesting term of the options using accelerated amortization. See also Note 16.A to the financial statements for details.

The actual benefit value upon exercise of the options is a deductible expense by the Bank for tax purposes, and is subject to payroll tax. The total allowed expense for tax purposes, for which the Bank would record a tax benefit on the profit & loss statement shall not exceed the original benefit value upon option grant. Any tax benefit exceeding this amount would be charged directly to equity.

Some of the Bank's stock option plans include multiple lots which vest on specified dates. The number of options which the offerees may actually exercise, will be based on the net operating profit return on the Bank's average shareholders' equity, up to an annual rate of return equal to 15%, based on the exercise eligibility formula, as stated in the option plan. Bank management has estimated a trend of annual rates of return (although not linear) in each of the plan years, and using this trend, estimated the number of stock options which each offeree would be eligible to exercise out of the total number of stock options to be granted to them in accordance with the plan. As of December 31, 2012, the number of options which each offeree may exercise have been adjusted based on actual annual rates of return for each year of the plan. Consequently, the total benefit value, charged on the financial statements to payroll expenses, whose balance (not yet recognized as payroll expenses) as of December 31, 2012 amounted to NIS 23 million.

Provisions for legal claims are determined according to management's assessments, based on the opinions of legal counsel. Among the legal claims are also motions for class actions. The provision was made for claims from which, in the opinion of management, a loss is expected, and is based on estimates of the loss, using information in the hands of management of the companies in the Group. For any claims with possible risk of loss, appropriate disclosure is made on the financial statements. No provision is recorded in the financial statements for claims as to which sustaining a loss is unlikely, or the prospects of a loss are remote.
Actual outcomes of these lawsuits may differ from the aforementioned management estimates, used for making provision for loss and their impact on financial statements may be material.

Provision for impairment of non-financial assets is made in accordance with IAS 36 “Impairment of Assets”. Provision for impairment, if needed, is based on assessor valuations updated by the assessor or valuator as required.

Deferred taxes are calculated with respect to temporary difference between the carrying amount of asset and liabilities for the purpose of financial reporting, and their value for tax purposes. Deferred tax are measured so as to reflect the tax implications expected to arise from the manner in which the Bank, at the end of the reported period, anticipates recovering or discharging the carrying amount of assets and liabilities.

Deferred taxes are measured using tax rates expected to apply to temporary differences when realized, based on statutes enacted, or essentially enacted, as of the balance sheet date.

As from January 1, 2012, the Bank applies IAS 12 "Taxes on income". The standard, as adopted by the Supervisor of Banks, contains similar provisions to those of Israeli Accounting Standard 19 "Income Taxes", applied by the banking system to date. However, along with adoption of the international standard, specific provisions issued by the Supervisor of Banks have been modified. In general, deferred taxes are recognized with respect to carry-forward loss, tax credits and deductible temporary differences, when taxable revenue is expected in future which may be used to utilize them. According to the Supervisor of Bank's directive, definition of the term "probable" is "more likely than not", as in generally accepted accounting principles for US banks for handling income taxes, rather than the translation of the term "probable" in Public Reporting Regulations with regard to deferred tax assets, which is "beyond any reasonable doubt". Initial application of the standard had no material impact on the Bank's financial statements.

The consolidated balance sheet as of December 31, 2012 includes deferred taxes, net amounting to NIS 738 million (excludes deferred taxes with respect to securities, which do not affect the provision for taxes). An increase of 1% in tax rates would cause a decrease of NIS 21 million in the provision for taxes. With respect to tax uncertainties, the Bank only recognizes the effect of tax positions if it is more likely than not that those positions would be accepted by the Tax Authority or by the Court. Tax positions recognized are measured at the maximum amount whose likelihood of realization exceeds 50%. Changes in recognition or measurement are reflected in the period in which a change in circumstances resulted in a change in judgment.

Certification process of the financial statements

The organ in charge of audit supervision at the bank is its Board of Directors. Board members' names, accounting and financial skills and professional qualifications are stated in the Board of Directors' report below. The processes of preparing, auditing and approving the financial statements involve additional organs and officers as described below.

Bank financial statements are prepared by a professional department, headed by the Chief Accountant, pursuant to directives and guidance from the Supervisor of Banks and in accordance with the disclosure policy set by the Bank's Board of Directors.

Concurrently with preparing the financial statements, and based on the draft financial statements forwarded to them, all executive management members confirm by their signature that they are not aware of any detail which may indicate that data and descriptions in the Board of Directors' Report and financial statements with regard to their areas of responsibility include any false representation or lack of material facts, that they instituted effective controls in order to ensure that any material information in their area of responsibility is brought to their attention, and that any significant fault or material weakness in the internal controls over financial reporting which is likely to impact the Bank's ability to record, process, summarize and report financial information in their areas of responsibility have been brought to the attention of the appropriate parties. For details of names and positions of bank executives, see the chapter on Bank Management below. The Bank operates a Provision for Credit Loss Committee, headed by the Chief Accountant and attended by professional credit staff, as well as a Provision for Credit Loss Committee headed by the President and attended by the Manager, Business Division; Manager, Retail Division; Manager, Finance Division; Chief Accountant; Chief Legal Counsel and other professional credit staff. In conjunction with preparation of the financial statements, the committee reviews the state of troubled loans of the Bank, their classification and provisions required. In addition, the Chief Legal Counsel and the Chief Accountant review the provisions required with respect to claims filed against the bank.

Matters of principal with regard to disclosure in the financial statements are discussed by the Financial Statements Disclosure Committee ("the Disclosure Committee") headed by the President and including the Chief Accountant, Chief Legal Counsel and other members of the Executive Management. These discussions include issues with material impact on the financial statements, issues of interest to the public, developments requiring disclosure to the public, material changes to application of accounting policies, requests or demands by regulatory authorities and issues on which Bank management and the independent auditor differ. As part of presentation of these issues to the Disclosure Committee, the independent auditors' professional comments are also presented.

As from January 1, 2013, pursuant to Section 36(D) of the Proper Conduct of Banking Business Regulation 301, the Board of Directors' Audit Committee discusses and recommends the approval of the Bank's quarterly and annual financial statements. For a listing of the names and qualifications of Audit Committee members, see below in chapter "Board of Directors".

The Audit Committee discusses the appropriateness of disclosure on the financial statements and the review of the financial statements, including all of their components, prior to having these discussed and approved by the Board plenum.

The Audit Committee reviews the assessments and estimates made in conjunction with the financial statements, internal controls associated with financial reporting, completeness and appropriateness of disclosure on financial statements; accounting policy adopted and accounting treatment applied to material issues of the corporation; valuations, including underlying assumptions and estimates, on which data on the financial statements relies.

Meetings of the Audit Committee are also attended by the Chairman of Board, the President, Chief Accountant, the Chief Legal Counsel and the independent auditors. The CRO and Chief Internal Auditor are invited to attend Committee meetings.

Pursuant to directives of the Supervisor of Banks on implementation of provisions of Sections 302 and 404 of the US Sarbanes-Oxley Act, the Audit Committee receives a report on any significant fault discovered in the disclosure processes or in internal controls over financial statements. These discussions are also attended by the Internal Auditor, the CRO and the independent auditors. Any report of significant faults is also presented to the Board of Directors.

The Audit Committee convenes twice to discuss the quarterly financial statements and three times to discuss the annual financial statements, with the final meeting held at least one week prior to the Board of Directors plenary meeting to approve the financial statements.

After discussions are concluded by the Audit Committee, its recommendations along with the draft financial statements are submitted to the Board of Directors, such that Board members receive the documents at least three days prior to the discussion there of by the Board of Directors. In conjunction with discussion by the Board of Directors, the Chief Accountant presents the financial results and an analysis. . The Chair of the Audit Committee presents the Audit Committee's recommendations to the Board of Directors - with regard to issues discussed by the Committee and to approval of the financial statements. The Board of Directors' meeting to discuss approval of the financial statements is attended, other than by members of the Board, by the President, Chief Accountant, Chief Legal Counsel, Chief Internal Auditor and independent auditors, as well as other participants invited to attend on per-case basis. The independent auditors present their comments.

At the end of this discussion, a resolution is passed to approve the Bank's financial statements and to authorize the Chairman of the Board of Directors, the President and the Chief Accountant to sign the financial statements.

Independent Auditors' report

The Independent Auditor drew attention in the Auditors' Opinion to the following:
Claims filed against the Bank with motions for class action status, as described in Note 19.D.11A-E) to the financial statements.

Controls and Procedures

In accordance with the public reporting directives of the Supervisor of Banks, based on the US Sarbanes-Oxley Act, the President and the Chief Accountant of the Bank have each separately signed a Certification attached to the financial statements on "Disclosure Controls and Procedures ("Disclosure Certification"). This directive of the Supervisor of Banks has been applied to financial statements starting on June 30, 2005.

The Disclosure Certification relates to the controls and procedures that were designed to assure that the information that the Bank requires for disclosure in accordance with the public reporting directives of the Supervisor of Banks, is accumulated, processed and sent to the Bank's Executive Management in a manner that enables decisions to be reached at an appropriate time, with respect to disclosure requirements. The certification also refers to setting of internal controls over financial reporting intended to provide a reasonable degree of certainty with regard to the reliability of financial reporting and to the fact that the financial statements for external use are prepared in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks.

At the end of the period covered by this Report, the Bank's management, together with the Presidents and Chief Accountant of the Bank, evaluated the effectiveness of the Bank's disclosure controls and procedures. Based on this evaluation, the President and Chief Accountant of the Bank concluded that at the end of this period, the disclosure controls and procedures are effective for recording, processing, summarizing and reporting the information that the Bank is required to disclose in the annual report, in accordance with the Public Reporting Regulations of the Supervisor of Banks, on the date stipulated in these Regulations.

Following shortcomings indicated by an audit conducted by the Supervisor of Banks with respect to disclosure of overall risk associated with loans to the public by economic sector, several material improvements have been made to controls and procedures related to disclosures, in order to eliminate these shortcomings. These improvements include reinforcement of and creation of procedures for client classification processes into sectors by business units, as well as expansion of control processes of classification into sectors - both at business units and at the Accounting and Financial Reporting Division. Specifically, the Bank reinforced controls to ensure proper disclosure of overall risk associated with loans to the public by economic sector in the financial statements as of December 31, 2012. Correction of faults identified by the audit will continue and will be completed by 3rd quarter of 2013.

During the quarter ended December 31, 2012, no change occurred in the Bank's internal controls over financial reporting that had a material effect, or can reasonably be expected to have a material effect on the Bank's internal controls over financial reporting.

In accordance with the directive by the Supervisor of Banks with regard to adoption of provisions of Section 404 of the Sarbanes-Oxley Act, starting with financial statements as of December 31, 2008, this report includes a declaration concerning the responsibility of management and the Board of Directors for setting and maintaining proper internal controls over financial reporting and management's assessment of the effectiveness of internal controls over financial reporting as of the date of the financial statements. Concurrently, the opinion of the Bank's independent auditors with regard to appropriateness of the Bank's internal controls over financial reporting in accordance with the applicable standards of the Public Company Accounting Oversight Board (PCAOB) is also provided.

The Code of Ethics

Full transparency is a prerequisite of corporate governance, and in particular as relates to efficient risk management. A policy of proper disclosure of events, support processes and appropriate organizational structure create regular work interfaces which support the Board of Directors and allow it to discharge its duties. In order to perform the foregoing with due professional approach, the organization promotes an "internal control culture". This means that the Bank Board of Directors and management promote, throughout the organization, a high level of ethics and integrity, to be disseminated by the following means:

- Effective communication channels to ensure messages with regard to ethics, integrity and the importance of internal audit are conveyed from the Board of Directors and executive management to all Bank staff.
- Personal example set by executive management.
- A written code of ethics, with documentation of all employees having read it and confirmed it.
- Supervisory mechanisms to ensure staff compliance with requirements and rules of conduct.
- Mechanisms to promote reporting of suspected improper actions.
- Enforcement mechanisms against those in breach of the code of conduct.

The Bank's Code of Ethics was written after over one year of meetings and sessions, attended by many Bank employees and managers. There is no doubt that purchasing it from ethic experts could short the process time however, it was not consistent the purpose of the code: authentic, accurate reflection of the Bank's spirit and prevailing organizational culture - as seen by the Bank's staff.

The process of writing the Code, based on analysis of events from the field, and deploying its values, has prepared the ground for integrating the Code in day-to-day activities as a way of life, using its values to face issues and dilemmas arising from the business routine.

On November 24, 2008 the Bank's Board of Directors approved the values of the Code of Ethics which is binding on the organization as a whole and on each employee and manger individually.

To ensure that the matter of dealing with Ethics will be frequent and observe a high level of reality, the Bank established an Ethics Committee, headed by the Bank Secretary. The committee includes representatives from headquarter units and branches. The committee assisted in deployment of the Code of Ethics, in 2009, when all Bank employees and management attended workshops for deployment of the Code of Ethics, after which each staff member signed the Code of Ethics. Upon completion of the deployment process, the Code of Ethics was published on the Bank website. The Ethics Committee convenes monthly and continues to regularly deploy the code by publishing dilemmas to Bank staff, discussing dilemmas raised from the field and reviewing the deployment process of the Code of Ethics.

In 2010, a portal dedicated to the Code of Ethics was created on the intranet including, inter alia, reports from Committee meetings, dilemmas and professional articles in this field. This portal provides another channel for reporting ethical dilemmas. Moreover, in 2012, in addition to regular activities, a management conference was held on the topic of improvement and development of skills for handling complex ethical dilemmas. In his opening address to this conference, the Bank President commented on the connection between the Bank's strategic plan and its Code of Ethics values. In addition, an ethics conference was held at the Financial Division, attended by managers of overseas affiliates - further to training delivered at these affiliates.

In 2013, the Ethics Committee would continue its intensive activity, as would on-going activities at all Bank units under the current format, including monthly meetings directed by Bank management. The 2013 work plan emphasizes improvement and enhanced awareness of the Code of Ethics values among Bank units through intra-unit forums. In addition, the Bank would establish, for the first time, a framework for measuring the effectiveness of deploying the Code of Ethics among Bank employees.

Executive Management

Below is a listing of Executive Management Forum members as of December 31, 2012 with their title and position:

Eliezer Yones	President	
Menahem Aviv	Vice-President	Manager, Accounting & Financial Reporting Division and Chief Accountant
Zvi Agrovich (1)		Manager, Mizrahi-Tefahot Technology Division Ltd.
Israel Engel	Vice-President	Manager, Retail Division
Haim Git	Vice-President	Manager, Risk Control Division and Chief Risk Officer (CRO)
Moshe Lari	Vice-President	Manager, Planning and Operations Division; Manager, Customer Assets and Consultancy Division
Dina Navot (2)	Vice-President	Manager, Marketing, Promotion and Business Development Division
Eldad Fresher	Vice-President	Manager, Financial Division and Chief Financial Officer (CFO)
Doron Klauzner	Vice-President	Manager, Business Banking Division
Rita Rubinstein	Vice-President	Manager, Human Resources and Administration Division
Galit Weiser		Chief Internal Auditor; Manager, Internal Audit Division
Dr. Shimon Weiss		Chief Legal Counsel; Manager, Legal Division
Maya Feller		Corporate Secretary
Benny Shoukroun		Bank Spokesman

(1) On July 30, 2012, Mr. Sammy Keinan resigned his position as CIO for the Bank; on September 30, 2012, Mr. Zvi Agrovich assumed this position.
(2) On April 1, 2012, Ms. Dina Navot started in her position as Manager, Marketing, Promotion and Business Development Division - replacing Ms. Na'ama Gat, who resigned from the Bank.

Senior Officers

Below are details of senior officers who are not members of the Bank's Board of Directors:

Eliezer Yones	
Start of term in office	1.4.2004
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	President
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Economics and Sociology – Hebrew University, Jerusalem; MA in Business Administration - Hebrew University, Jerusalem
Business experience (in past 5 years)	President of Bank Mizrahi-Tefahot Ltd.

Menahem Aviv	
Start of term in office	13.4.2005
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Accounting & Financial Reporting Division and Chief Accountant, Board member: Mizrahi Tefahot Issue Company Ltd.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Accounting and Economics – Tel Aviv University; MBA – Tel Aviv University; CPA
Business experience (in past 5 years)	Chief Accountant, Bank Mizrahi-Tefahot Ltd.

Zvi Agrovich	
Start of term in office	30.9.2012
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Mizrahi-Tefahot Technology Division Ltd.; CIO for the Bank
Family member of another senior officer or of an interested party in the banking corporation	No
Business experience (in past 5 years)	Manager, Mizrahi-Tefahot Technology Division Ltd.

Senior officers (continued)

Israel Engel	
Start of term in office	1.1.2005
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Retail Division Board member, Bank Yahav, Tefahot Insurance Agency (1989) Ltd.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Accounting and Economics – Bar Ilan University; MBA (Finance) – Bar Ilan University; CPA
Business experience (in past 5 years)	Manager, Retail Division - Bank Mizrahi-Tefahot Ltd.

Haim Git	
Start of term in office	1.2.1999 (in current position - 7.7.2011)
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Risk Control Division, CRO.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Accounting – Tel Aviv University; Accounting Diploma – Hebrew University, Jerusalem; CPA
Business experience (in past 5 years)	Chief Internal Auditor, Bank Mizrahi-Tefahot Ltd.

Na'ama Gat (1)	
Start of term in office	10.10.2004
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Marketing, Promotion and Business Development Division
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Psychology and English Literature – Haifa University; MA in Advertising and Marketing – Marquette University, Milwaukee, USA
Business experience (in past 5 years)	Manager, Marketing, Advertising and Business Development - Bank Mizrahi-Tefahot Ltd.

(1) On April 1, 2012, Ms. Na'ama Gat ceased to be an officer of the Bank. According to the agreement with Ms. Na'ama Gat, she retired from the Bank on July 9, 2012.

Senior officers (continued)

Galit Weiser	
Start of term in office	7.7.2011
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Chief Internal Auditor; Manager, Internal Audit Division Chief Internal Auditor, Bank Yahav and companies: "Etgar", "Trust", "Issue Company", "Tefahot Insurance Agency Ltd"(1)
Family member of another senior officer or of an interested party in the banking corporation	No
Education	CPA;; undergraduate degree in Accounting and Economics (Hebrew University); graduate degree in Business Administration (Hebrew University).
Business experience (in past 5 years)	Deputy Chief Internal Auditor at the Bank; previously, Chief Internal Auditor of Bank Tefahot.

Shimon Weiss	
Start of term in office	2.10.1999
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Chief Legal Counsel Legal risk manager
Family member of another senior officer or of an interested party in the banking corporation	No
Education	LL.B. – Hebrew University, Jerusalem; LL.M. – Hebrew University, Jerusalem; DR.JUR. – Hebrew University, Jerusalem; MBA – Tel Aviv University
Business experience (in past 5 years)	Chief Legal Counsel, Bank Mizrahi-Tefahot Ltd.

(1) Etgar – "Etgar Investment Portfolio Management Company of the Mizrahi Tefahot, Group Ltd.
Trust – Mizrahi Tefahot Trust Company Ltd.
Issue Companies: Mizrahi Tefahot Issue Company Ltd.

Senior officers (continued)

Moshe Lari	
Start of term in office	8.11.2009
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Planning and Operations Division; Manager, Customer Assets and Consultancy Division, Chairman of the Board : Mizrahi Tefahot Trust Company Ltd. . Tefahot Insurance Agency (1989) Ltd. Board Member : Bank Yahav
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Economics and Accounting - Hebrew University, Jerusalem; Graduate degree in Business Administration - Tel Aviv University; CPA
Business experience (in past 5 years)	CRO; Manager, Planning, Operations and Control Division at Bank Mizrahi-Tefahot Ltd.; Manager, Planning and Economics Division at Bank Mizrahi-Tefahot Ltd.

Dina Navot [(1)]	
Start of term in office	1.4.2012
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Marketing, Promotion and Business Development Division
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undegraduate degree in Social Work, Tel Aviv University; graduate degree in Journalism and Media, Bar Ilan University; graduate degree in Social Psychology and Sociology, Bar Ilan University
Business experience (in past 5 years)	VP, Marketing with HOT Communication Systems; VP, Marketing with Careline - Prigo Israel

(1) Appointed Manager, Marketing, Advertising and Business Development Division on April 1, 2012.

Senior officers (continued)

Dov Fogel [(1)]	
Start of term in office	18.5.1997
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Logistics, Administration and Efficiency Division
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Business Administration - New England College; MBA, specialization in Strategic Management - Hebrew University, Jerusalem
Business experience (in past 5 years)	Manager, Logistics, Administration and Efficiency Division at Bank Mizrahi-Tefahot Ltd.

Maya Feller	
Start of term in office	20.4.1997
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Corporate Secretary
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Humanities – Tel Aviv University
Business experience (in past 5 years)	Secretary, Bank Mizrahi-Tefahot Ltd.

(1) On February 5, 2013, Mr. Dov Fogel concluded his term as senior officer of the Bank.

Senior officers (continued)

Eldad Fresher	
Start of term in office	3.11.2004
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Finance Division – CFO and Market Risk Manager, Chairman of the Board Mizrahi Tefahot Issue Company Ltd., UMB Switzerland Ltd. (Zurich).
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Business Administration – Hebrew University, Jerusalem; MBA – Hebrew University, Jerusalem
Business experience (in past 5 years)	Manager, Financial Division - CFO and Market Risk Manager at Bank Mizrahi-Tefahot Ltd.

Sammy Keinan (1)	
Start of term in office	1.11.2007
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	CIO
Family member of another senior officer or of an interested party in the banking corporation	No
Education	B.Sc. In Industrial Engineering and Management – Technion; Partial studies for BA in Computer Science – Bar Ilan University
Business experience (in past 5 years)	IT Manager at Partner, CEO of Mehish Computer Services Ltd., Manager, Customer Assets and Consultancy Division, IT Manager at Bank Mizrahi-Tefahot Ltd.

(1) On July 16, 2012, Mr. Sammy Keinan announced his resignation from the position of CIO for the Bank - and his resignation came into effect on July 30, 2012.

Senior officers (continued)

Doron Klauzner	
Start of term in office	8.11.2009
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Corporate Banking Division and Credit Risk Manager
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Economics and Business Administration - Bar Ilan University
Business experience (in past 5 years)	Manager, Human Resources, Logistics and Procurement Division at Bank HaPoalim Ltd.; Manager, Risk and Strategy Division, Bank HaPoalim Ltd.

Rita Rubinstein	
Start of term in office	1.1.2007
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Human Resources and Administration Division
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Humanities and Social Sciences – Hebrew University, Jerusalem; MA in Humanities and Social Sciences, Bar Ilan University
Business experience (in past 5 years)	Manager, Human Resources and Administration Division at Bank Mizrahi-Tefahot Ltd.

Details of remuneration (1) of senior officers

(NIS in thousands)

All of 2012														
Details of remunerated party		Remuneration for services rendered[2]							Other remuneration	Total	Loans granted at beneficial terms[3]		Loans granted at standard terms
Name	Position	Extent of employment	Holding stake in Bank equity	Salary	Bonuses[17]	Social benefit contributions[4]	Share-based payment[5]	Value of additional benefits[6]			Balance as of December 31, 2011	Average term to repayment (in years)	
Jacob Perry [7]	Chairman of the Board of Directors	60%	-	1,933	-	227	-	131		2,291	-	-	199
Eliezer Yones [8]	President	100%	-	2,965	-	1,162	* 3,900	154		8,181	-	-	111
Doron Klauzner [9]	Deputy President and Manager, Business Division	100%	-	1,023	-	272	1,227	82		2,604	-	-	62
Moshe Lari [10]	Deputy President; Manager, Planning, Operations and Control Division; and Manager, Customer Assets and Consultancy Division	100%	-	1,021	-	274	1,145	81		2,521	281	5	11
Dan Lubash [11]	President of subsidiary - United Mizrahi Bank (Switzerland) Ltd.	100%	-	1,193	408	744	-	111		2,456	-	-	-
Sammy Keinan [12]	Deputy President and Manager, Information Technology Division	100%	-	852	-	1,503	-	81		2,436	-	-	36
Galit Weiser [13]	Chief Internal Auditor	100%	-	1,013	365	268	754	71		2,471	-	-	118

* Includes non-linear accounting of stock option plan for the President, approved on November 30, 2008, over a term of 5 years and 4 months. The options would be granted to the President in five lots, on April 1 of each year between 2010-2014. The plan is accounted for as follows:
NIS 1.2 million in 2008, NIS 14.3 million in 2009, NIS 10.4 million in 2010, NIS 6.4 million in 2011, NIS 3.9 million in 2012, NIS 1.9 million in 2013 and NIS .5 million in 2014. See Note 16.A.1 to the financial statements for details.

Details of remuneration [1] of senior officers - continued

(NIS in thousands)

All of 2011												
Details of remunerated party				Remuneration for services rendered[2]				Other remuneration	Total	Loans granted at beneficial terms[3]		Loans granted at standard terms
Name	Position	Extent of employment	Holding stake in Bank equity	Salary	Bonuses[17]	Social benefit contributions[4]	Share-based payment[5]	Value of additional benefits[6]		Balance as of December 31, 2011	Average term to repayment (in years)	
Jacob Perry[7]	Chairman of the Board of Directors	60%	-	1,378	1,100	27	-	138	2,643	223	-	108
Eliezer Yones[8]	President	100%	0.56%	2,891	-	795	* 6,400	146	10,232	-	-	75
Haim Git[14]	Vice-president, Chief Risk Officer	100%	-	1,024	340	1,803	445	83	3,695	38	-	92
Na'ama Gat[15]	Deputy President and Manager, Marketing, Promotion and Business Development Division	100%	-	977	-	1,377	1,074	71	3,499	427	7.5	48
Doron Klauzner[11]	Deputy President and Manager, Business Division	100%	-	989	-	313	1,824	80	3,206	-	-	41
Yekutiel Mansdorf[12]	President of subsidiary - United Mizrahi Bank (Switzerland) Ltd.	100%	-	1,270	-	3,991	-	15	5,276	-	-	-
Galit Weiser[13]	Chief Internal Auditor	100%	-	810	300	772	688	96	2,666	2,489	8.5	170

* Includes non-linear accounting of stock option plan for the President, approved on November 30, 2008, over a term of 5 years and 4 months. The options would be granted to the President in five lots, on April 1 of each year between 2010-2014. The plan is accounted for as follows:
NIS 1.2 million in 2008, NIS 14.3 million in 2009, NIS 10.4 million in 2010, NIS 6.4 million in 2011, NIS 3.9 million in 2012, NIS 1.9 million in 2013 and NIS .5 million in 2014. See Note 16.A.1 to the financial statements for details.

Remarks:

(1) Remuneration is in terms of cost to the Bank and excludes payroll tax.

(2) The amounts are included under "salaries and related expenses" in the statement of profit and loss.

(3) The benefit is under the same terms and conditions granted to all Bank employees.

(4) Includes severance pay, pension, study fund, acclimation bonus, paid leave and social security.

(5) For details of share-based payment to the President and to officers, see Note 16.A to the financial statements.

(6) Interest relates to loans granted at beneficial terms compared to market terms. There is no interest benefit with respect to deposits. In other banking transactions, the benefits apply to all Bank employees and the amount there of is immaterial.

(7) Mr. Jacob Perry – Chairman of the Bank Board of Directors – is employed by the Bank under an individual employment contract at 60% of a full-time job, effective since February 24, 2003 for an unspecified term. Mr. Perry's monthly salary is linked to the Consumer Price Index. Upon termination of his employment by the Bank as Chairman of the Bank Board of Directors, including by resignation, Mr. Perry shall be entitled to have the Bank release to him all amounts accumulated on his behalf in the executive pension insurance policy, except in case of termination of his employment under circumstances where, by law, severance pay may be denied to Mr. Perry, in whole or in part, in which case Mr. Perry would only be entitled to amounts accumulated in said pension insurance from his own contributions. Each of the parties to the employment contract may terminate the contract with six months' prior notice and subject to terms and conditions stated in the employment agreement.

As for bonuses, see details in section (17) below.

Mr. Perry resigned from the Bank on October 31, 2012.

(8) For further information about employment terms of Mr. Eliezer Yones – see Note 16.E to the financial statements. As for bonuses, see details in section (17) below.

(9) Mr. Doron Klauzner – employed by the Bank under an individual employment contract effective since November 8, 2009 for an unspecified term. Mr. Klauzner's monthly salary is linked to the Consumer Price Index. Upon termination of his employment at the Bank, Mr. Klauzner is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Mr. Klauzner is eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Klauzner shall not be eligible for an acclimation bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under extraordinary circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment contract. As for bonuses, see details in section (17) below.

(10) Mr. Larry Moshe – employed by the Bank under an individual employment contract effective since November 8, 2009 for an unspecified term. Mr. Larry's monthly salary is linked to the Consumer Price Index. Upon termination of his employment at the Bank, Mr. Larry is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Mr. Larry is eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Larry shall not be eligible for an acclimation bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under extraordinary circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment contract. As for bonuses, see details in section (17) below.

(11) Mr. Dan Lubash is employed as President of the Bank's subsidiary UMB Switzerland Ltd. in Switzerland (hereinafter: "the subsidiary").

As from May 1, 2011, Mr. Lubash is employed by an individual employment contract for a fixed term of 4 years (through April 30, 2015). Either party may terminate the contract by six months' advance notice. Should the subsidiary decide to terminate Mr. Lubash's employment prior to the term stated in the contract, under other than extraordinary circumstances as listed in the contract, the subsidiary would pay the salary, bonus and other payments, as listed in the contract, for three months beyond the six months' notice as described above.

Mr. Lubash's pay is determined by the Swiss subsidiary, and is denominated in Swiss Franks. In addition, Mr. Lubash is eligible to receive rent reimbursement for his residence in Switzerland. As for bonuses, see section (17) below.

(12) Mr. Sammy Keinan – employed by the Bank under an individual employment contract since July 1, 2004 for an unspecified term. Mr. Keinan's monthly salary is linked to the Consumer Price Index. Upon termination of his employment at the Bank, Mr. Keinan is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Mr. Keinan is eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Keinan shall not be eligible for an acclimation bonus and release of amounts accumulated on his behalf in case of termination of his employment under extraordinary circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment agreement.

As for bonuses, see details in section (17) below.

Mr. Keinan concluded his work for the Bank at the end of July 2012, and as of October 31, 2012 he is no longer employed by the Bank.

On September 10, 2012, the Board of Directors decided, after approval by the Audit Committee on September 3, 2012, to approve payment of a retirement bonus to Mr. Keinan, amounting to NIS 976,360 (gross), or 150% of the product of his most recent monthly salary and the number of his years in service with the Bank. In addition, in accordance with his employment terms, Mr. Keinan would receive a letter releasing to him all deposits made on his behalf to provident funds with respect to severance pay throughout his years of service with the Bank and its subsidiary, including all accrued gain. This amount was NIS 634,297 as of August 31, 2012. It was further decided that Mr. Keinan would be entitled to use the company car provided to him as well as to payment for his cell phone up to NIS 500 per month (tax not grossed-up by the Bank for these benefits) through 2012 or until his start date in another employment, whichever is sooner.

It was further decided that Mr. Keinan is entitled to a notice period starting on August 1, 2012 and ending on October 31, 2012. It was further approved that the Bank would waive Mr. Keinan's work for the period from August 1, 2012 through August 31, 2012, during which period Mr. Keinan would receive full payment as it was paid to him during his work at the Bank.

Moreover, in the period from September 1, 2012 through October 31, 2012, Mr. Keinan would be on leave, in exchange for his accrued leave period as per his employment terms. The unused paid leave balance would be redeemed by the Bank upon conclusion of Mr. Keinan's employment.

It was further approved that in accordance with his employment contract, Mr. Keinan would receive payment of an acclimation bonus equal to six monthly salaries, amounting to NIS 468,294.

Moreover, in accordance with Mr. Keinan's employment terms, during six months after discontinuation of Mr. Keinan's employment by the Bank, Mr. Keinan would not provide his services, in salaried nor freelance capacity, nor as consultant or in any other manner whatsoever, directly nor indirectly, to any competing entity as listed on his employment contract.

For this matter, the Board of Directors approved, after approval by the Audit Committee, that Mr. Keinan's cooling period would start upon conclusion of Mr. Keinan's employment by the Bank (i.e. on November 1, 2012) and would end on May 31, 2013.

(13) Ms. Galit Weiser - employed by the Bank since July 12, 1994. On July 7, 2011, Ms. Weiser was appointed Chief Internal Auditor of the Bank. Ms. Weiser is party to a personal employment contract dated August 29, 2011 for an unspecified term (effective as from August 1, 2011). Ms. Weiser's monthly salary is linked to the Consumer Price Index. Upon termination of her employment at the Bank, Ms. Weiser is eligible to receive an acclimation bonus equal to six monthly salaries, with no additional benefits whatsoever. Furthermore, Ms. Weiser is eligible to have the Bank, upon termination of her employment, release to her all amounts accumulated on her behalf in the various funds. Notwithstanding the foregoing, Ms. Weiser shall not be eligible for an acclimation bonus and release of amounts accumulated on her behalf in the various funds in case of termination of her employment under extraordinary circumstances, as stated in the agreement. Either party may terminate the contract by three months' advance notice.

As for bonuses, see section (17) below.

(14) Mr. Haim Git is employed by the Bank since October 4, 1989 and terms of his employment as Chief Internal Auditor of the Bank were set in an individual employment contract dated February 1, 1999 and approved by the Audit Committee of the Board of Directors for an unspecified term. Mr. Git's monthly salary is linked to the Consumer Price Index. Should the Bank decide to terminate his employment, Mr. Git would be eligible for a retirement bonus equal to 10 monthly salaries with no additional benefits whatsoever. Upon termination of his employment, Mr. Git is entitled to have the Bank release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Git shall not be eligible for a retirement bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under extraordinary circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with six months' prior notice and subject to terms and conditions stated in the employment agreement. As for bonuses, see details in section (17) below.

On July 7, 2011, Mr. Haim Git was appointed the Bank's Chief Risk Manager. On October 15, 2011, the Bank's Board of Directors decided, after approval by the Audit Committee on August 7, 2011, to amend Mr. Haim Git's employment contract. As for Mr. Haim Git's rights upon termination of his employment at the Bank, the Bank would pay Mr. Git an amount equal to his last monthly salary multiplied by his number of years in service with the Bank. In addition, the Bank would pay Mr. Git an acclimation bonus equal to six monthly salaries. Mr. Git would not be eligible to receive these payments if terminated under circumstances which allow full or partial denial of severance pay. Moreover, the advance notice period would be reduced from six to three months. In conjunction with this revision, Mr. Git's entitlement to receive a retirement bonus equal to ten monthly salaries in case of termination by the Bank has been cancelled. Upon termination of his employment, Mr. Git would be eligible to receive all amounts accrued in the different funds on his behalf.

(15) Ms. Na'ama Gat – employed by the Bank under an individual employment contract effective since October 10, 2004 for an unspecified term. Ms. Gat's monthly salary is linked to the Consumer Price Index. Upon termination of her employment at the Bank, Ms. Gat is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Ms. Gat is eligible to have the Bank, upon termination of her employment, release to her all amounts accumulated on her behalf in the various funds. Notwithstanding the foregoing, Ms. Gat shall not be eligible for an acclimation bonus and release of amounts accumulated on her behalf in the various funds in case of termination of her employment under extraordinary circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment agreement. As for bonuses, see details in section (17) below. On October 25, 2011, Ms. Gat announced her intention to leave the Bank.

On March 25, 2012, the Board of Directors decided, after approval by the Audit Committee on March 19, 2012, to approve payment of a retirement bonus to Ms. Gat, amounting to NIS 900,000 (gross), or 150% of the product of her most recent monthly salary and the number of her years in service with the Bank. In addition, in accordance with her employment terms, Ms. Gat would receive a letter releasing to her all deposits made on her behalf to provident funds with respect to severance pay throughout her years of service with the Bank, including all gain accrued there to. This amount was NIS 559,000 as of December 31, 2011.

It was further decided that Ms. Gat would be entitled to use the company car provided to her as well as to payment for her cell phone up to NIS 500 per month (tax not grossed-up by the Bank for these benefits) through 2012 or until her start date in another employment, whichever is sooner.

It was further decided to approve that Ms. Gat would be entitled to a notice period starting on April 1, 2012 and ending on July 9, 2012; the Bank waived her work during this period and she would receive in full the payment as paid to her during her work at the Bank.

It was further approved that pursuant to the employment contract, Ms. Gat would be paid an acclimation bonus equal to six monthly salaries, for a total of NIS 463,878.

It was further decided to approve an amendment of Ms. Gat's employment contract, such that in the period from April 1, 2012 through September 30, 2012, Ms. Gat may not work, in salaried or freelance capacity, as consultant nor in any other manner whatsoever, directly nor indirectly, by or on behalf of any entity competing with operations of the Bank or any of its subsidiaries or other affiliated companies in Israel or overseas - unless she would obtain advance written permission for such work from the Bank President.

(16) Mr. Yekutiel Mansdorf – was employed by the Bank since July 1, 1974. His employment terms were set in a personal employment contract dated January 1, 1999, for an unspecified term. As from October 22, 2006, Mr. Mansdorf serves as General Manager of the Swiss subsidiary, UMB Switzerland Ltd., and is on unpaid leave of absence from the Bank. Should the Bank decide to terminate his employment, Mr. Mansdorf would be eligible for a retirement bonus equal to 15 monthly salaries with no additional benefits whatsoever. Furthermore, Mr. Mansdorf would be eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Mansdorf shall not be eligible for a retirement bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under extraordinary circumstances, as stated in the agreement. Mr. Mansdorf's pay as General Manager of the subsidiary is determined by the Swiss subsidiary, and is denominated in Swiss Franks. In addition, Mr. Mansdorf is eligible to receive rent reimbursement for his residence in Switzerland. As for bonuses, see details in section (17) below.

According to terms of Mr. Mansdorf's retirement agreement dated August 1, 2011, all amounts accumulated in his name in the retirement insurance policy have been released. in pension fund and in all provident funds. In addition, Mr. Mansdorf received a retirement bonus amounting to NIS 3,737 thousand as well as redemption of six months' advance notice amounting to NIS 472 thousand. Also, in his retirement agreement, Mr. Mansdorf's eligibility to receive a retirement bonus equal to 15 monthly salaries was cancelled.

Mr. Mansdorf retired from the Bank on November 30, 2011.

(17) Bonuses

1. Bonuses with respect to 2012

1.1 Bonus to the President

In the new employment agreement, effective from December 1, 2008 through April 1, 2014, the President waived the annual bonus to which he is entitled under the previous agreement, starting on the termination date of the previous agreement. See Note 16.D to the financial statements for details.

1.2. Bonuses to VPs

VPs at the Bank received option allotments pursuant to the stock option plan approved in 2009. Each VP consented by choice not to be included in the bonus payment plan for Bank officers for each year between 2009-2012, and not to be included in the bonus payment plan for Bank officers for 2013, should it be approved by the Bank. See Note 16.M to the financial statements for further information.

1.3. Bonus to General Manager of subsidiary

On March 12, 2012, the subsidiary's Board of Directors discussed the recommendation by the subsidiary's Chairman to award a bonus to the subsidiary's CEO, in line with his employment contract and based on results in the subsidiary's financial statements and achievement of the subsidiary's objectives, with due notice to developments in the regulatory environment and to challenges facing the subsidiary; the subsidiary's Board decided to award a bonus amounting to CHF 100 thousand to the subsidiary's CEO.

1.4. Bonus to Chief Internal Auditor

The Remuneration Committee (as recommended by the Audit Committee) and the Board of Directors discussed (on March 13, 2013 and March 17, 2013) the bonus to the Chief Internal Auditor, Ms. Galit Weiser, and resolved to approve it.

The Remuneration Committee and Board of Directors were presented with the following data when discussing payment of the bonus:

Details of the Chief Internal Auditor's education, qualification, expertise, professional experience, achievements and contribution; details of the Chief Internal Auditor's roles and responsibilities; details of the salary agreements signed with the Chief Internal Auditor and financial data about her monthly salary and benefits (including retirement terms), including detailed data in terms of cost to the Bank; financial data about bonuses awarded to the Chief Internal Auditor with respect to 2011 (as from her start date in office, July 7, 2011); data about options awarded to the Chief Internal Auditor, including their fair value based on the B&S model; Chapter 1 of the outline dated June 8, 2008, which lists in section 1.1.2 the bonus plan for Bank officers, as well as immediate reports issued by the Bank on March 2, 2009 and on October 26, 2010 with regard to amendment of the bonus plan for Bank officers; payroll data for Bank employees and for independent contractors hired by the Bank, including data on the average and median pay of such employees, and data on the ration of the Chief Internal Auditor's remuneration and the salary of Bank employees and of independent contractors hired by the Bank, including the ratio to the average and median pay of such employees; summary data from the Bank's financial statements for the period ended September 30, 2012, compared to those of the other four major banks; the Bank's draft 2012 financial statements; a document listing comparison data, based on public information, for senior bank employees; the Bank of Israel circular on "Remuneration policy at banking corporations"; ISA's legal opinion no. 101-16 concerning Amendment 20 of the Corporate Act - Q&A; reasons given by the Chairman of the Board of Directors for approving the bonus to the Bank's Chief Internal Auditor with respect to 2012; the recommendation by the Audit Committee to approve the bonus to the Bank's Chief Internal Auditor with respect to 2012 (the Audit Committee, which recommended to approve the bonus to the Bank's Chief Internal Auditor, has received the aforementioned information).

The Remuneration Committee and the Board of Directors decided to approve the bonus to the Bank's Chief Internal Auditor and decided to adopt the reasons given by the Chairman of the Board of Directors and the Audit Committee's recommendation for payment of the bonus to the Chief Internal Auditor with respect to 2012. Moreover, the Remuneration Committee and the Board of Directors resolved that the ratio of variable to fixed components in the Chief Internal Auditor's remuneration for 2012 was 21% to 79% (excluding share-based payment), and members of the Remuneration Committee and of the Board of Directors consider this ratio to be reasonable and appropriate under the circumstances.

Since the other four major banks have yet to publish their 2012 financial statements, and since public information with regard to salary, bonus and options primarily refers to officers who are VPs, there is a challenge in making relevant comparisons for bonus payment, in particular for officers other than VPs. However, after review of the information provided to members of the Remuneration Committee and of the Board of Directors with regard to salary and bonus payments and with regard to stock option plans for senior bank employees (considering the aforementioned challenges), members of the Remuneration Committee and of the Board of Directors considered the bonus amount to be reasonable and appropriate under the circumstances. In addition, the Remuneration Committee and the Board of Directors decided that the Chief Internal Auditor would repay to the Bank the bonus amount paid to her with respect to 2012, under conditions to be specified in the officer remuneration policy (not yet specified by the Bank pursuant to Amendment 20 to the Corporate Act, 1999) if this was paid based on information which would turn out to be erroneous and re-stated on the Bank's financial statements.

The Remuneration Committee and the Board of Directors were of the opinion that the bonus to be paid to the Chief Internal Auditor would not affect the exercise of professional judgment by the Chief Internal Auditor.

2. Bonuses with respect to 2011 (paid in 2012)

2.1. Bonus to Chairman of the Board of Directors

The Payroll and Remuneration Committee, the Audit Committee and the Board of Directors discussed (on March 12, 2012, March 19, 2012 and March 25, 2012) the bonus to Bank Chairman, Mr. Jacob Perry, and decided to approve the bonus, subject to approval by the General Meeting of Bank Shareholders.

The Payroll & Remuneration Committee, Audit Committee and Board of Directors were presented with the following data when discussing payment of the bonus:

Highlights of the Chairman's employment terms, salary and benefits paid for 2009 and 2010 as well as bonuses paid for 2009 and 2010.

data on Bank results and profitability, including operating rate of return on equity in previous years and in 2011 (based on Bank results and profitability for the nine-month period ended September 30, 2011 and expected results for the full year), as well as comparison data, inter alia, with regard to the operating rate of return on equity and the ratio of capital to risk elements for the Bank and for 4 other banks - Bank HaPoalim Ltd., Bank Leumi Le-Israel Ltd., Israel Discount Bank Ltd. and First International Bank of Israel Ltd., as well as summary public data on remuneration of chairmen of the Board of Directors at banks, insurance companies and other public companies.

The reasoning provided by the Audit Committee and the Board of Directors for the bonus grant and amount indicated that the decision to approve the bonus payable to the Chairman of the Board of Directors was made in view of the Chairman's contribution to Bank achievements in 2011, considering the improvement in business results of the Bank in 2011, compared to its business results in 2010. Reasons cited by the Audit Committee and the Board of Directors for the requested bonus and amount there of also included the Chairman's significant contribution to implementation of corporate governance principles at the Bank and the efficient operation of the Bank's Board of Directors. Moreover, the bonus amount payable to the Chairman for 2011 was determined, inter alia, with due consideration to bonus amounts paid to the Chairman in previous years. Note that the bonus amount payable to the Chairman is 10% higher than the bonus paid to the Chairman for 2010.

After reviewing data provided to Board members with regard to salary, bonuses and stock options granted to Chairmen of Boards of Directors at banks, insurance companies and other public companies in the finance sector. The Board members consider that the bonus, amounting to NIS 1,100 thousand for 2011, is appropriate and reasonable under the circumstances.

2.2 Bonus to the President

In the new employment agreement, effective from December 1, 2008 through April 1, 2014, the President waived the annual bonus to which he is entitled under the previous agreement, starting on the termination date of the previous agreement. See Note 16.D to the financial statements for details.

2.3. Bonuses to VPs

VPs at the Bank received option allotments pursuant to the stock option plan approved in 2009. Each VP consented by choice not to be included in the bonus payment plan for Bank officers for each year between 2009-2012, and not to be included in the bonus payment plan for Bank officers for 2013, should it be approved by the Bank. See Note 16.M to the financial statements for further information.

2.4. Bonus to Mr. Haim Git

The Payroll and Remuneration Committee, the Audit Committee and the Board of Directors discussed (on February 2, 2012, February 8, 2012 and February 27, 2012) the bonus for Mr. Haim Git and resolved to approve it.

The Payroll & Remuneration Committee, Audit Committee and Board of Directors were presented with the following data when discussing payment of the bonus:

Highlights of Mr. Haim Git's employment terms, as well as bonuses paid to him for 2009 and 2010; data on Bank results and profitability, including the operating rate of return on equity in previous years and in 2011 (based on Bank results for the nine-month period ended September 30, 2011 and expected results for the full year), as well as comparison data, inter alia, with regard to the operating rate of return on equity and the ratio of capital to risk elements for the Bank and for 4 other banks - Bank HaPoalim Ltd., Bank Leumi Le-Israel Ltd., Israel Discount Bank Ltd. and First International Bank of Israel Ltd., as well as data on remuneration of officers at banks, insurance companies and other public companies in the finance sector.

Reasons cited by the Audit Committee and by the Board of Directors for awarding the bonus and its amount indicated that the decision to approve the bonus payment to Mr. Haim Git for 2011 was made in view of his contribution to Bank achievements in 2011 based on the Bank's targets for this year.

Other reasons cited by the Audit Committee and the Board of Directors indicated that the bonus amount payable to Mr. Haim Git is in proper balance between fixed remuneration (salary components) and variable remuneration (bonus and stock options) awarded to him, and that the bonus amount awarded to Mr. Git is in line with principles for bonus payment to all Bank employees for 2011.

2.5. Bonus to Chief Internal Auditor

The Audit Committee and the Board of Directors discussed (on February 8, 2012 and February 23, 2012) the bonus to the Chief Internal Auditor, Ms. Galit Weiser, and resolved to approve it.

The Audit Committee and Board of Directors were presented with the following data when discussing payment of the bonus:

Highlights of employment terms of the Chief Internal Auditor. as well as bonuses paid to her for 2009 and 2010; data on Bank results and profitability, including the operating rate of return on equity in previous years and in 2011 (based on Bank results and profitability for the nine-month period ended September 30, 2011 and expected results for the full year), as well as comparison data, inter alia, with regard to the operating rate of return on equity and the ratio of capital to risk elements for the Bank and for 4 other banks - Bank HaPoalim Ltd., Bank Leumi Le-Israel Ltd., Israel Discount Bank Ltd. and First International Bank of Israel Ltd., as well as data on remuneration of officers at banks, insurance companies and other public companies in the finance sector.

Reasons cited by the Audit Committee and the Board of Directors for award of the bonus and its amount indicated that the decision to approve the bonus to be awarded to the Chief Internal Auditor was made in view of her considerable contribution to internal audit operations at the Bank. Reasons cited by the Audit Committee and the Board of Directors also indicated that the Chairman of the Board of Directors considers that internal audit, headed by the Chief Internal Auditor, serves as an efficient tool for evaluation of internal control at the Bank. Reasons provided by the Audit Committee and the Board of Directors also indicated that the Chairman of the Board of Directors considers that the Chief Internal Auditor fulfilled her duties in the best manner possible, while maintaining her personal commitment, dedication, loyalty and investing significant effort in implementation of the Bank's internal audit plan for 2011.

Transactions with controlling shareholders

On August 6, 2008, the amendment to Securities Regulations (Periodic and Immediate Reports), 1970 became effective ("the Amendment"), whereby, inter alia, a reporting corporation is required to issue an immediate report with regard to "details of a transaction with a controlling shareholder, or which the controlling shareholder has a personal interest in its confirmation, including highlights of the transaction or contract, details of the organ which confirmed the transaction and its summary reasons for said confirmation; in this paragraph, "transaction" excludes a transaction which the most recent financial statements classify transactions of its type as immaterial."

The Bank Association has applied to the Securities Authority with regard to implementation of the provision concerning "immaterial transaction" and the disclosure outline. According to agreements between the Bank Association and the Securities Authority, banks have been exempted from issuing immediate reports about banking transactions which are not unusual, provided that the banks specify criteria for unusual and immaterial transactions.

The criteria for unusual and immaterial transactions, as previously set by the Audit Committee of the Board of Directors and re-confirmed on March 11, 2013 are as follows:

Transaction other than a banking transaction

Definition of "immaterial transaction":

A transaction other than a banking transaction, conducted in the normal course of business at market terms and conditions, and which meets one or more of the following criteria, is an immaterial transaction:

In this section, "transaction" means a transaction with a controlling shareholder, or a transaction in which a controlling shareholder has a personal interest.

A. Transaction for sale of retail products in the normal course of Bank business and at market conditions, amounting up to NIS 1.5 million per transaction, or a continuous transaction as stated above (multiple, essentially identical transactions with the same company), whose aggregate amount over one calendar year is up to 0.1% of the regulatory shareholders' equity, as defined in Proper Conduct of Banking Business regulation 312 (hereinafter - "regulatory equity"). This amount would not apply to individual transactions whose amount is under NIS 25 thousand each.
B. Transaction for provision of services, including in the field of TV advertising, in the normal course of Bank business and at market conditions, amounting up to 0.1% of regulatory equity, or a continuous transaction as stated above (multiple, essentially identical transactions with the same company), whose aggregate amount over one calendar year is up to .75% of total annual operating and other expenses by the Bank's most recent annual financial statements. This amount would not apply to individual transactions whose amount is under NIS 25 thousand each.
C. Transactions involving leasing of space, in the normal course of Bank business and at market conditions, approved in a single calendar year and amounting up to 0.1% of regulatory equity.
D. Any other transaction in the normal course of Bank business and at market conditions, where the total amount for such a transaction type in a single calendar year is up to 0.1% of regulatory equity. This amount would not apply to individual transactions whose amount is under NIS 25 thousand each.

Transactions with controlling shareholders (continued)

Banking transaction

Definition of "unusual transaction" - a transaction other than at market conditions or not in the normal course of business or a material transaction.

A banking transaction which meets one of the following criteria shall be deemed to be, for this matter, a "material transaction":

A. Indebtedness transaction - an indebtedness transaction (after deductions, as stipulated in Proper Conduct of Banking Business Regulation no. 312), which results in total indebtedness of any group of controlling shareholders exceeding 5% of regulatory equity, or a transaction which results in the increase in indebtedness of an individual borrower from among the controlling shareholders exceeding 2% of regulatory equity. If multiple indebtedness transactions are approved for the same borrower in a single calendar year, these indebtedness transactions shall be measured in aggregate. Any specific provision for doubtful debts, or write-off of any amount with regard to indebtedness of a controlling shareholder or an affiliated corporation, shall be deemed to be a material transaction. Measurement of total indebtedness, for this matter, shall be separate for the Wertheim Group and for the Ofer Group.

   "Group of controlling shareholders" - a controlling shareholder, as defined in the Securities Act, together with affiliated corporations, as the term "affiliated person" is defined in Proper Conduct of Banking Businesses regulation 312, and together with relatives of controlling shareholders included in the group.

B. Deposits - receipt of deposit from a controlling shareholder shall be deemed to be a material transaction if, consequently, total deposits from the same group of controlling shareholders would exceed 2% of total deposits at the Bank. Receipt of deposit from a company which is an "affiliated person" of the controlling shareholder, and which is not a company controlled by him, shall be deemed to be a material transaction if, consequently, total deposits from said company, on consolidated basis, would exceed 2% of total deposits at the Bank. Total deposits at the Bank would be calculated based on the most recent annual financial statements published by the Bank prior to the transaction date.

C. Transaction in securities or in foreign currency (other than an indebtedness transaction or deposit transaction, as stated above) - a transaction in securities or in foreign currency where the annual commission charged does not exceed 2% of total annual operating revenues of the Bank (less revenues from investment in shares), based on the most recent annual financial statement published by the Bank prior to the transaction date.

D. Other transactions - any other transaction for provision of financial and banking services, the revenues from which to the Bank exceed 0.1% of the Bank's total regulatory equity.

Any temporary, immaterial deviation for a period of up to 30 days would not change classification of the transaction as an immaterial transaction, and disclosure of such deviation would be provided in the annual report.

"Market terms" - terms which are not preferable to those at which similar transactions are made by the Bank with individuals or corporations which are not controlling shareholders of the Bank, or where the controlling shareholder has no personal interest in these transactions. Market terms with regard to banking transactions are compared to terms of similar transactions, of similar volume, as used for review of transactions with affiliated persons in accordance with Proper Conduct of Banking Businesses regulation 312, with Bank clients who are not affiliated persons, or are not entities where the controlling shareholder has a personal interest in transactions with them; market conditions with regard to transactions other than banking transactions are compared to conditions of similar transactions made by the Bank with suppliers and/or with regard to offers from other suppliers reviewed prior to deciding to make the commitment. In cases where the Bank has no similar transactions, market conditions are to be compared with regard to similar transactions made in the market, provided that such transactions are made in the normal course of business and that such transactions have a market in which similar transactions are made.

Indebtedness transactions to which Proper Conduct of Banking Businesses regulation 312 does not apply - as for Indebtedness transactions to which Proper Conduct of Banking Businesses regulation 312 does not apply, should the Bank become aware of any such transaction, the Bank commits to bring any such transaction for approval pursuant to Proper Conduct of Banking Businesses regulation 312 and to provide disclosure there for in the Bank's annual financial statements. The definition of "immaterial transaction" and "unusual transaction" with regard to these transactions would be similar to the aforementioned definitions by the Bank.

Transactions with controlling shareholders (continued)

Below is summary data with regard to banking transactions with controlling shareholders (NIS in millions):

A. Indebtedness transactions

	December 31, 2012				
Group of controlling shareholders	Credit balance on balance sheet	Unutilized facility	Risk assets due to derivatives activity	Guarantees provided by the Bank to secure credit of controlling shareholder or affiliated party there to	Total indebtedness[(1)]
Wertheim Group and private companies controlled there by	-	-	-	-	-
Relatives of Wertheim Group	28	34	-	-	62
Total - Wertheim Group	**28**	**34**	**-**	**-**	**62**
Ofer Group and private companies controlled there by	-	-	-	-	-
Relatives of Ofer Group	262	66	6	24	358
Reporting entities controlled by relatives of Ofer Group	-	-	-	-	-
Gadot Industries Biochemicals Ltd.	22	-	-	-	22
Oil Refineries Ltd.	165	3	-	-	168
Israel Chemicals Ltd.	-	7	2	-	9
Israel Corporation Ltd.	-	19	-	-	19
Carmel Ulpinim Ltd.	-	-	-	2	2
Total - Ofer Group	**449**	**95**	**8**	**26**	**578**

	December 31, 2011				
קבוצת בעלי השליטה	Credit balance on balance sheet	Unutilized facility	Risk assets due to derivatives activity	Guarantees provided by the Bank to secure credit of controlling shareholder or affiliated party there to	Total indebtedness[(1)]
Wertheim Group and private companies controlled there by	19	164	-	4	187
Relatives of Wertheim Group	20	-	-	-	20
Total - Wertheim Group	**39**	**164**	**-**	**4**	**207**
Ofer Group and private companies controlled there by	-	-	-	-	-
Relatives of Ofer Group	235	62	12	21	330
Reporting entities controlled by relatives of Ofer Group					
Carmel Ulpinim Ltd.	-	-	-	2	2
Gadot Industries Biochemicals Ltd.	23	-	-	-	23
Oil Refineries Ltd.	96	96	-	-	192
Israel Chemicals Ltd.	-	1	13	-	14
Total - Ofer Group	**354**	**159**	**25**	**23**	**561**

(1) Indebtedness as defined in Proper Conduct of Banking Businesses regulation 312, after set off of allowed deductions.

Transactions with controlling shareholders (continued)

B. Deposits

		December 31, 2012
Group of controlling shareholders	Balance as of December 31, 2012	Highest Balance at 2012
Wertheim Group and private companies controlled there by	7	7
Relatives of Wertheim Group and private companies controlled there by	11	20
Reporting entities controlled by Wertheim Group		
Amot Investments Ltd.	2	3
Total - Wertheim Group	**20**	**30**
Ofer Group and private companies controlled there by	4	8
Relatives of Ofer Group and private companies controlled there by	110	653
Reporting entities controlled by Ofer Group		
Meliseron Ltd.	1	2
Reporting entities controlled by relatives of Ofer Group		
Oil Refineries Ltd.	2	10
Israel Chemicals Ltd.	1	963
Israel Corporation Ltd.	5	7
Carmel Ulpinim Ltd.	-	2
Total - Ofer Group	**123**	**1,645**

		December 31, 2011
Group of controlling shareholders	Balance as of December 31, 2011	Highest Balance at 2011
Wertheim Group and private companies controlled there by	9	20
Relatives of Wertheim Group and private companies controlled there by	5	11
Reporting entities controlled by Wertheim Group		
Amot Investments Ltd.	-	2
Reporting entities controlled by Wertheim Group		
Neviot Teva HaGalil Ltd.	-	4
Total - Wertheim Group	**14**	**37**
Ofer Group and private companies controlled there by	4	12
Relatives of Ofer Group and private companies controlled there by	56	292
Reporting entities controlled by Ofer Group		
Premium Holdings Ltd.	-	1
Meliseron Ltd.	-	1
Reporting entities controlled by relatives of Ofer Group		
Oil Refineries Ltd.	-	3
Israel Chemicals Ltd.	5	210
Israel Corporation Ltd.	-	1,043
Carmel Ulpinim Ltd.	1	4
Total - Ofer Group	**66**	**1,566**

To the best of the Bank's knowledge, transactions with affiliated persons were executed in the ordinary course of business, at market terms and under terms similar to those of transactions effected with unrelated entities.

Independent Auditors' Fees [1][2][3]

(NIS in thousands)

	Consolidated		The Bank	
	2012	2011	2012	2011
For audit activities: [4]				
Independent auditors [5]	6,988	7,042	6,134	6,217
Other auditors	679	690	-	-
Total	**7,667**	**7,732**	**6,134**	**6,217**
For audit-related services [6]:				
Independent auditors [5]	41	87	27	77
Other auditors	-	-	-	-
For tax services: [7]				
Independent auditors [5]	218	264	206	249
Other auditors	-	-	-	-
For other services:				
Independent auditors [5][8]	588	421	588	421
Other auditors	509	661	-	-
Total	**1,356**	**1,433**	**821**	**747**
Total fees to auditors	**9,023**	**9,165**	**6,955**	**6,964**

(1) Board of Directors' report to the annual general meeting on auditors' fees for audit activities and for other services in addition to the audit, in accordance with Sections 165 and 167 of the Companies Law, 1999.
(2) Independent auditors' fees include payments to partnerships and corporations under their control, as well as payments under the VAT Law.
(3) Includes fees paid and accrued.
(4) Audit of annual financial statements and review of interim financial statements.
(5) Includes other independent auditors in overseas branches.
(6) Primarily includes: prospectuses, special certifications, comfort letters and forms or reports to authorities requiring auditors' signature, as well as special projects not part of regular audit services.
(7) Includes payments for preparation of reports adjusted for income tax purposes and reports to tax authorities.
(8) Includes mainly payments for consulting and various services.

Board of Directors

The Bank's members of the board of directors, their principal occupation, and other directorships as of the publication date of these financial statements are presented below:

Moshe Vidman [1][2]	
Membership of Board of Directors' committees	Audit-Chairman, Risk Management-Chairman
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	2.8.2010
Education	Undergraduate degree - Economics and Political Science, Hebrew University, Jerusalem. MBA (Financing), Hebrew University, Jerusalem.
Current occupation	Chairman of board: Moshe Vidman Ltd(owner) Board member: ICL Ltd.; Dead Sea Works Ltd.; Rotem Amfert Negev Ltd.; Melisaron Ltd.; Elrov Real Estate and Hotels Ltd.; Rosebud Ltd.; Yafora Tavori Ltd.; Ofer Investments Ltd.; Dash Apex Holdings Ltd.; Ofer Development and Investments Ltd.; Ofer Sachaf Ltd.; Ofer Brothers Investments Ltd.; Ofer Brothers(Ashkelon Industries) Ltd.;Ofer Brothers(Haifa TSL"D) Ltd.;Ofer Brothers(Jerusalem) Ltd.; A.A.B.M Ltd.; C.A.B.M Ltd.; Ofer Brothers Property Holding Ltd.; Ofer Merkazim Ltd.; Offer Commercial Centers Ltd.; Hof Haalmog Eilat Ltd.; Ofer Brothers Engineering & Development Ltd.; Ofer Industrial Assets (Nazareth) Ltd.; Ofarim Buildings Ltd.; Melissa Ltd.; C.I.D. Israel Investment & Development Co.Ltd.; Miseltoe Holding B.V Ltd.; Ofer Investments Energy Enterprises (Management) Ltd.; Ofer Investments Energy Sources Ltd.; 10 Herbert Samuel (Management) Ltd.; Ofer Holiday & Recreation Ltd.; Ofer Brothers Holdings (1989) Ltd.; Melifar Shopping Centers Ltd.(in volantry dissolution); Ofer Brothers (Raanana) Ltd.; Offer Commercial Centers (Management Maof) Ltd.; Neot Coral Beach (1990) Ltd.; Residence Towers Ltd.; Carmeli-Ypliad Ltd.;
Previous occupation (in past 5 years)	Board member, Bank Leumi Le-Israel Ltd.; Partner Communications Company Ltd.; Israel Corporation Ltd
Family member of another interested party in the corporation ?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

(1) Has "banking experience", pursuant to directives of the Supervisor of Banks.
(2) Functions as the chairman of the Board from December 1, 2012.

Board of Directors (continued)

Zvi Efrat [(1)]	
Membership of Board of Directors' committees	Credit, Payroll & Remuneration, Claims against the Bank
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	No
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	24.1.1995
Education	LL.B. - Hebrew University, Jerusalem; Attorney
Current occupation and in the past 5 years	Senior Partner, J. Gurnitzki & Co. law firm, Board member: Ephrat Smith Trust Company, Ephrat Legal Services
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

Ron Gazit	
Membership of Board of Directors' committees	Risk Management, Claims against the Bank
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	No
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	14.12.2003
Education	LL.B. – Tel Aviv University; Attorney
Current occupation and in the past 5 years	Ron, Gazit, Ruthenberg & Co. - law firm; Board member, Gazit Ruthenberg Trust Company; Board member, R. Gazit Attorney (2002)
Pervious occupation	Board member, Gover Radio Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

(1) Has "banking experience", pursuant to directives of the Supervisor of Banks.

Board of Directors (continued)

Moshe (Mosie) Wertheim [1]	
Membership of Board of Directors' committees	Claims against the Bank
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	Chairman, Central Bottling Company Ltd. (Coca Cola) (Owned by Moshe Wertheim)
Start date in office as member of the Bank's Board of Directors	24.1.1995
Education	Academic - M. Jur. and attorney; holds certificate in Business Administration
Current occupation	Board member: Central Bottling Company Ltd. (Coca Cola), Alony Hetz Ltd. (public), Ilanim Development and Investments Ltd., MWZ Holding Ltd., Info-Prod (Middle Eastern Research) Ltd., F&W (Registered Partnership), T.T. Transport and Marketing Services (1978) Ltd., Mada'im Shimushim (2000) Ltd., IMPG Management Ltd., TSRON Management Ltd., W.H.M. Properties Ltd., Alcorp Ltd., Ramcon Ltd.
Previous occupation (in past 5 years)	Board member: Keshet Boardcasting Ltd.; Keshet – Broadcasting Communication Group Ltd.; Alony Hetz Ltd.; Chairman, Central bottling Co. Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	Yes

Avi Ziegelman	
Membership of Board of Directors' committees	Audit-chairman, Credit, Risk Management, Remuneration
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	Yes
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	19.9.2007
Education	BA in Accounting and Economics – Tel Aviv University; MA in Business Economy (Finance) – Tel Aviv University; CPA
Current occupation	Board member: Tafron Ltd.; Gindi Investments 1 Ltd.; Afcon Electro-Mechanics Ltd.; Orev Technologies 1977 Ltd; Cial Technolgoy Israel Ltd; Clal Biotechnolgy Industries Ltd); Ormat Industries Ltd.
Previous occupation (in past 5 years)	Financial consultant and Board member
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	Yes

(1) Has "banking experience", pursuant to directives of the Supervisor of Banks.

Board of Directors (continued)

Mordechai Meir	
Membership of Board of Directors' committees	Audit, Claims against the Bank
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	24.12.2008
Education	BA in Accounting and Economics – Tel Aviv University; CPA.
Current occupation	Board member of the following companies: Ofer Brothers Properties (1957) Ltd; Melisaron Ltd.; Ofer Commercial Centers (MAOF Management)(in voluntary dissolution) Ltd.; C.A.B.M. Ltd.; Ofer Bros. Engineering and Development Ltd.; Ofer Bros. (Ashkelon Industries) Ltd.; Ofer Bros. (Haifa 1974) Ltd.; Ofer Bros. (Jerusalem) Ltd.; Ofer Bros. Foreign Investments Ltd.; Melissa Ltd.; Mistletoe Holding B.V.; Ofer Merkazim Ltd.
Previous occupation (in past 5 years)	CEO, Meirav Managers Ltd.; Board member.; Ofer Brothers Holdings (1989) Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

Gideon Sitterman	
Membership of Board of Directors' committees	Remuneration-chairman, Audit, Risk Management
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	Yes
Has accounting and financial expertise?	Yes
Has professional qualifications?	Yes
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	07.07.2009
Education	Undergraduate degree in Economics and Accounting, Tel Aviv University; CPA.
Current occupation	Chairman of the board: Ashdod Port, External Board member, Economic and Financial Consultant, Chairman and Owner, Pninush Ltd.
Previous occupation (in past 5 years)	Business development, Central Bottling Company Ltd. (Coca Cola) 2001-2006; Director Manager, Ministry of Transportation and Road Safety 2006-2009.; Ceo Kal Binyan Ltd. Board member: Camor Ltd
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	Yes

Board of Directors (continued)

Liora Ofer	
Membership of Board of Directors' committees	Credit
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	No
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	Board member in companies of Ofer Group Investments Ltd. As described below , including companies which hold the bank shares(directly and indirectly).
Start date in office as member of the Bank's Board of Directors	23.1.2006
Education	High school – HaReali Haivri Haifa
Current occupation	Chairperson: Ofer Investments Ltd.; Chairperson, Melisaron Ltd. Board member: Oro Investments Ltd.; Oro Foreign Investments (1999); Helidor Entrepreneurs Ltd.; Ofer Bros. Properties (Ra'anana) Ltd(in voluntary dissolution).; Ramat Aviv Mall Ltd.; Mivnei Oferim Ltd.,Ofer Development and Investments Ltd.; Ofer Industrial Properties (Nazareth) Ltd., Ofer Commercial Centers Ltd., Ofer Commercial Centers Ltd., CID Israeli Company for Investment and Development Ltd.; Neot Coral Beach Ltd.; Residence Towers Ltd.; Carmeli Yuliad Ltd.; 10 Herbert Samuel (Management) Ltd.; Investments Energy Sources Ltd.; Ofer Investments Energy Enterprises (Management) Ltd.; A.A.B.M Ltd.;
Previous occupation (in past 5 years)	Managing real estate companies, investments companies and other companies and business, member in boards as described above
Family member of another interested party in the corporation?	Daughter of the late Mr. Yuli Ofer
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

Yossef Shachak	
Membership of Board of Directors' committees	Credit, Audit
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	Yes
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	26.4.2010
Education	Academic, Undergraduate degree in Accounting, Hebrew University, Jerusalem; CPA
Current occupation	Accounting and Financial Advisor to corporations and Boards Board member: Psagot Investment House Ltd.; Tafron Ltd.; HaBima National Theate (external board member); Peleg Nia Ltd.; Academic Track, Management College (external Board member); Yogi Consulting and Investments Ltd. - controlling shareholder; Shachak & Co. Assets Ltd. - shareholder; Campus Solutions Ltd. (external Board member); Y.S. Ltd. - shareholder; Member, Public Council of Accounting Standards Board.
Previous occupation (in past 5 years)	Member, Audit Committee of Bank of Israel; Board member, Dash Provident Fund Management Ltd., Board member of Elul Tamarind Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

Board of Directors (continued)

Jonathan Kaplan	
Membership of Board of Directors' committees	Risk management
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	12.5.2011
Education	Undergraduate degree in Economics and Accounting, Tel Aviv University; CPA; graduate degree in Political Science and National Security, Haifa University; National Security College, Tel Aviv.
Current occupation	Economic Advisor Board member: Vilar International Ltd.; Clal Biotechnology Industries Ltd.; Amir Agricultural Marketing and Investments Ltd.; Central Bottling Company Ltd.; International Breweries Ltd.; PharmUp Marketing (1966) Ltd.
Previous occupation (in past 5 years)	Board member: Solber Industries Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	Yes

Sabina Biran	
Membership of Board of Directors' committees	Audit, Risk management, Remuneration, Claims against the bank
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	Yes
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	No
Start date in office as member of the Bank's Board of Directors	27.2.2012
Education	Undergraduate degree in Political Science and Economics, Haifa University; MBA, Harriett-Watt University; MA studies in Political Studies and International Relations, Tel Aviv University.
Current occupation	Owner and Co-CEO of MVP-B Ltd. Board member: Shufersal Ltd.
Previous occupation (in past 5 years)	Tel-Aviv Jaffa Tourism Association chairperson.; Chim Nir Ltd chairprrson Board member: Leumi Partners Underwriters Ltd.; Rafael Advanced Defense Systems Ltd.; The Phoenix Pension and Provident Fund Ltd.; The Phoenix Insurance Co.Ltd.; Fox-Wizel Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

Board of Directors (continued)

Nahshon Yoav-Asher	
Membership of Board of Directors' committees	Credit, Claims against the Bank
Independent Board member as defined in Proper Conduct of Banking Business Regulation 301	No
Has accounting and financial expertise?	Yes
Has professional qualifications?	No
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	Yes
Start date in office as member of the Bank's Board of Directors	27.2.2012
Education	Academic, undergraduate degree in Economics and Accounting, Tel Aviv University; MBA (specialized in Strategy), Mt. Scopus University, Jerusalem
Current occupation	CFO; VP, Finance and Business Development; Central Bottling Company Ltd. (Coca Cola) Chairman of the Board of Directors, Neviot Teva HaGalil Ltd. Board member: Mey Galil Ltd., Central Beverage Distribution Company Ltd., Dairy Manufacturers Association Ltd. (in voluntary dissolution), Meshek Tzuriel Dairy Ltd., Tavor Winery (2005) Ltd., Meshek Tzuriel Distribution Ltd. (in voluntary dissolution), Keshet Broadcasting Ltd., Mira Trading Ltd., TURK TUBORG BIRA VE MALT, SANAYII A.S (Turkey), BIMPAS BIRA VE MESRUBAT PAZARLAMA A.S (Turkey), INTERNATONAL DAIRIES CORPORATION B.V. (Holland), AL BREWERIES B.V (Holland), UNITED ALBANIAN BREWERIES SH.P.K (Albania)
Previous occupation (in past 5 years)	Chairman of the Board of Directors, Dash Apex Holding Ltd. and Milco Industries Ltd. Board member: Meshek Tzuriel Dairy Ltd.
Family member of another interested party in the corporation?	No
Board member regarded by the corporation as having accounting and financial expertise or meeting the minimum quote specified by the Board?	No

Board of Directors (continued)

During 2012, the Bank Board of Directors held 24 plenary meetings and 82 committee meetings.

The permanent Board committees are: Audit Committee, Risk Management Committee, Credit Committee, Remuneration Committee and Committee for Claims Against the Bank

Presented below are the changes in composition of Board committees during 2012 and through publication of these financial statements:

A. On February 27, 2012, Ms. Sabina Biran was appointed external Board member of the Bank and member of the Audit Committee and of the Credit Committee. In addition, Mr. Yoav Nahshon was appointed Board member of the Bank.

B. The Board of Directors, at its meeting on March 25, 2012, resolved that Ms. Sabina Biran would conclude her term in office as member of the Audit Committee and of the Credit Committee, and would be appointed member of the Claims against the Bank Committee, Risk Management Committee, Remuneration Committee and the Financial Statements Review Committee. In addition, Mr. Yoav Nachshon was appointed member of the Credit Committee and of the Claims against the Bank Committee. At the same meeting. Mr. Yossi Shachak was appointed member of the Credit Committee, while Messrs. Avi Ziegelman, Jonathan Kaplan and Ron Gazit were appointed members of the Risk Management Committee. Mr. Ron Gazit concluded his term as member of the Credit Committee. Mr. Abraham (Beigah) Shochat concluded his term as member of the Financial Statements Review Committee. Messrs. Mordechai Meir, Dov Mishor and Yosef Shachak concluded their terms as members of the Risk Management Committee.

C. At the Board of Directors meeting held on August 27, 2012, Ms. Sabina Biran was appointed Member of the Audit Committee.

D. On September 20, 2012, Mr. Abraham (Beigah) Shochat concluded his term in office as Board Member of the Bank, as well as Member of the Audit Committee and of the Payroll and Remuneration Committee.

E. On October 16, 2012, the Bank was informed in writing by the Chairman of the Board of Directors, Mr. Jacob Perry, of his intended resignation from his office.

F. On October 31, 2012, Mr. Jacob Perry concluded his term in office as Bank Chairman.

G. At the Board of Directors meeting held on October 29, 2012, Mr. Moshe Vidman was appointed Member of the Payroll and Remuneration Committee.

H. On October 31, 2012, Mr. Moshe (Mosie) Wertheim was appointed Chairman of the Bank's Board of Directors, effective from November 1, 2012 through November 30, 2012.

I. The Board of Directors, at its meeting held on November 25, 2012, resolved to rename the Payroll and Remuneration Committee - the Remuneration Committee, and to appoint Board member Gideon Sitterman, Avi Ziegelman and Sabina Biran members of this committee. Furthermore, Messrs. Yoni Kaplan, Zvi Efrat, Yossi Shachak and Moshe Vidman concluded their office as members of the Payroll and Remuneration Committee.

J. At the Board of Directors meeting held on November 25, 2012, Mr. Moshe Vidman was appointed Chairman of the Board of Directors as from December 1, 2012.

Board of Directors (continued)

K. On December 24, 2012, the Bank of Israel approved the appointment of Mr. Avraham Noyman as independent Board member of the Bank. This appointment has yet to be approved by the General Meeting of shareholders.

L. The Board of Directors, at its meeting held on January 21, 2013, resolved to merge the Audit Committee and the Financial Statements Review Committee as from January 22, 2013.

M. On January 28, 2013, Mr. Dov Mishor resigned his position as member of the Bank Board of Directors and member of the Audit Committee and Committee for Claims Against the Bank. Upon his departure, the number of Board members having accounting and financial qualifications is 9.

Board members having accounting and financial qualifications

The Bank's Board of Directors prescribed that at least three directors should have accounting and finance skills. In the Board's opinion, this number enables it to meet all of the obligations imposed on it, especially with respect to its responsibility to examine the financial position of the corporation and to prepare and approve financial statements. The Board has also determined that the Audit Committee would have as members at least 2 Board members having accounting and financial qualifications. Upon publication of these financial statements, there are 9 Board members with accounting and finance skills: Messrs. Moshe (Mosie) Wertheim, Avi Ziegelman, Mordechai Meir, Gideon Sitterman, Yossef Shachak, Moshe Vidman, Jonathan Kaplan, Sabina Biran and Yoav-Asher Nahshon. The Audit Committee includes 5 Board members having accounting and financial qualifications.

Below are the facts related to each of the directors in the Bank named above, and by virtue of which they are to be deemed having accounting and financial skills:

Moshe (Mosie) Wertheim

Attorney, Bachelors of Law degree, certificate of business administration, serves as chairman of the board and CEO of Central Bottling Co. Ltd., director in Alony-Hetz Properties and Investments Ltd., in the Keshet Group companies and in other companies.

Avi Ziegelman

Holds undergraduate degree in Accounting and Economics and graduate degree in Business Economics (Finance). Licensed CPA. Provides financial consulting and serves as Board member with different companies. Was Senior Partner, Head of Professional Department with KPMG Somekh Chaykin CPA

Mordechai Meir

Undergraduate degree in Economics and Accounting, Tel Aviv University. CPA. Worked for nine years at Somekh Chaikin as Senior CPA, board member of public companies, consultant to interested parties in public companies. For the past 10 years: CEO of consulting firm, MERAV Management Ltd. - specialized in consulting to and representation of real estate and financials sectors for major corporations and enterprises.

Board of Directors (continued)

Gideon Sitterman

CPA, former member of Securities Authority, Director General of the Ministry of Transportation, has extensive accounting, economics and financial knowledge.

Yossef Shachak

Undergraduate degree in Accounting, Hebrew University, Jerusalem; CPA; accounting and financial advisor to private companies; Board member of private and public companies; previously - President, Institute of Certified Public Accountants in Israel.

Moshe Vidman

Undergraduate degree in Economics; Graduate degree in Business Administration; specialized in Financing; served as CEO of two industrial companies; Board member at leading companies for over 25 years; member, Finance Committee and Audit Committee, served as Chairman of multiple companies.

Jonathan Kaplan

Undergraduate degree in Economics and Accounting, Tel Aviv University; CPA; graduate degree in Political Science and National Security; Economic Advisor; Board member of private and public companies; formerly - Superintendent of Income Tax.

Sabina Biran

Undergraduate degree in Political Science and Economics, Haifa University; MBA; served as CEO of two airlines; Board member of private and public companies; formerly - Chairperson of the Board of Directors of an industrial company.

Nahshon Yoav-Asher

Undergraduate degree in Economics and Accounting, Tel Aviv University; MBA (specialized in Strategy); CFO, VP, Finance and Business Development; Chairman and Board member of private and public companies.

The Bank's Board of Directors thanks the Bank President, management and employees for their efforts to promote the Bank, the result of their diligent efforts to maintain the Bank's services with due responsibility. The Board of Directors appreciates the constant efforts of the President, the Bank's management and its employees to expand the business activities and client base.

M. Vidman

Moshe Vidman
Chairman of the Board of Directors

Eliezer Yones
President

Ramat Gan, March 17, 2013

Management Discussion of Group Business and Operating Results

Table of Contents

Management Discussion - Addendum A
Consolidated Balance Sheet – Multi-period information

As of year end, 2008-2012

Reported amounts (NIS in millions)

	2012	2011	2010	2009	2008
Assets					
Cash and deposits with banks	16,671	15,972	12,614	11,011	11,038
Securities	9,041	8,432	7,449	7,643	9,259
Securities loaned or sold in repurchase agreements	207	136	247	307	12
Loans to the public (1)	130,244	120,931	110,474	98,445	91,986
Provision for credit loss	(1,593)	(1,638)	(3,471)	(3,234)	(3,066)
Loans to the public, net	128,651	119,293	107,003	95,211	88,920
Loans to Governments	317	196	92	301	2
Investments in associates (1)	60	52	52	50	20
Buildings and equipment	1,658	1,616	1,546	1,522	1,476
Intangible assets and goodwill	87	87	87	101	109
Assets with respect to derivatives	3,518	(1) 3,115	(1) 3,405	1,491	(1) 3,383
Other assets	2,032	(1) 1,347	(1) 809	839	(1) 740
Total assets	**162,242**	**150,246**	**133,304**	**118,476**	**114,959**
Liabilities and Shareholders' Equity					
Deposits from the public	128,499	119,236	105,991	95,021	91,779
Deposits from banks	1,694	2,007	2,432	1,899	1,867
Deposits from the Government	107	152	172	209	242
Securities loaned or sold in conjunction with repurchase agreements	-	-	-	-	972
Debentures and subordinated notes	14,039	12,202	9,813	8,166	6,837
Liabilities with respect to derivatives	3,773	3,964	2,892	1,981	3,299
Other liabilities	4,878	4,631	4,508	4,407	3,834
Total liabilities	**152,990**	**142,192**	**125,808**	**111,683**	**108,830**
Equity attributable to equity holders of the banking corporation	8,811	7,666	7,130	6,447	5,781
Non-controlling interest	441	388	366	346	348
Total equity	**9,252**	**8,054**	**7,496**	**6,793**	**6,129**
Total liabilities and shareholders' equity	**162,242**	**150,246**	**133,304**	**118,476**	**114,959**

(1) Comparative figures were reclassified.

Management Discussion - Addendum B

Consolidated Statement of Profit and Loss – Multi-period information

For the years ended December 31, 2008-2012

Reported amounts (NIS in millions)

	2012	(1) 2011	(1) 2010	(1) 2009	(1) 2008
Interest revenues	6,591	6,840	5,509	4,892	5,552
Interest expenses	3,377	3,741	2,621	2,273	3,702
Interest revenues, net	3,214	3,099	2,888	2,619	1,850
Expenses with respect to credit loss	276	338	473	375	395
Interest revenues, net after expenses with respect to credit loss	**2,938**	**2,761**	**2,415**	**2,244**	**1,455**
Non-interest revenues					
Non-interest financing revenues (expenses)	95	18	(25)	(215)	393
Commissions	1,452	1,474	1,432	1,410	1,257
Other revenues	26	17	33	25	19
Total non-interest revenues	**1,573**	**1,509**	**1,440**	**1,220**	**1,669**
Operating and other expenses					
Payroll and associated expenses	1,701	1,615	1,529	1,504	1,273
Maintenance and depreciation of buildings and equipment	652	608	585	557	473
Amortization and impairment of intangible assets and goodwil	-	-	14	14	9
Other expenses	433	444	438	439	398
Total operating and other expenses	**2,786**	**2,667**	**2,566**	**2,514**	**2,153**
Pre-tax profit	1,725	1,603	1,289	950	971
Provision for taxes on profit	599	522	469	322	356
After-tax profit	1,126	1,081	820	628	615
Share in profits(losses) of associates, after tax	-	1	-	(1)	(1)
Net profit:					
Before attribution to non-controlling interest	1,126	1,082	820	627	614
Attributable to non-controlling interest	(50)	(38)	(19)	(11)	(12)
Attributable to equity holders of the banking corporation	**1,076**	**1,044**	**801**	**616**	**602**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. For details, see Note 1.D.1 in the financial statements.

Management Discussion - Addendum B (continued)

Consolidated Statement of Profit and Loss – Multi-period information

For the years ended December 31, 2008-2012

Reported amounts

	2012	2011	2010	2009	2008
Earnings per Ordinary share (in NIS)[(1)]					
Basic earnings per share (in NIS)					
Net profit attributable to ordinary shares holders of the banking corporation	4.77	4.65	3.63	2.76	2.71
Diluted earnings (in NIS)					
Net profit attributable to ordinary shares holders of the banking corporation	4.74	4.57	3.58	2.75	2.69

(1) Share of NIS 0.1 par value.

Management Discussion - Addendum C

Income and Expense Rates - of the Bank and its Subsidiaries (1)

For the year ended December 31,

Reported amounts (NIS in millions)

	2012				2011			
			Revenue (expense) rate				Revenue (expense) rate	
	Average balance (2)	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives(4)	Average balance (2)	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives(4)
			In %				In %	
Israeli currency - non-linked								
Assets(3)	79,713	3,480	4.37		75,255	3,395	4.51	
Effect of embedded and ALM derivatives (4)	60,798	961			63,170	1,650		
Total assets	**140,511**	**4,441**		**3.16**	**138,425**	**5,045**		**3.64**
Liabilities (3)	78,727	(1,503)	(1.91)		71,551	(1,542)	(2.15)	
Effect of embedded and ALM derivatives (4)	58,848	(1,084)			62,514	(1,445)		
Total liabilities	**137,575**	**(2,587)**		**(1.88)**	**134,065**	**(2,987)**		**(2.23)**
Interest margin			**2.46**	**1.28**			**2.36**	**1.41**
Israeli currency - linked to the CPI								
Assets (3)	47,648	2,289	4.80		43,833	2,665	6.08	
Effect of embedded and ALM derivatives (4)	4,964	30			4,283	137		
Total assets	**52,612**	**2,319**		**4.41**	**48,116**	**2,802**		**5.82**
Liabilities(3)	35,069	(1,619)	(4.62)		33,643	(1,974)	(5.87)	
Effect of embedded and ALM derivatives (4)	10,136	(109)			9,510	(360)		
Total liabilities	**45,205**	**(1,728)**		**(3.82)**	**43,153**	**(2,334)**		**(5.41)**
Interest margin			**0.18**	**0.59**			**0.21**	**0.41**

See remarks below.

Note: Complete data on income and expense rates for each sector, by balance sheet item, will be provided upon request.

Management Discussion - Addendum C (continued)

Income and Expense Rates - of the Bank and its Subsidiaries [1]

For the year ended December 31,

Reported amounts (NIS in millions)

	2012				2011			
			Revenue (expense) rate				Revenue (expense) rate	
	Average balance [2]	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives[4]	Average balance [2]	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives[4]
			In %				In %	
Foreign currency [5]								
Assets [3]	21,781	154	0.71		19,166	2,078	10.84	
Effect of derivatives [4]								
Hedging derivatives	3,109	(11)			2,642	308		
Embedded and ALM derivatives	51,470	(335)			52,894	2,412		
Total assets	**76,360**	**(192)**		**(0.25)**	**74,702**	**4,798**		**6.42**
Liabilities[3]	26,035	185	0.71		23,923	(2,067)	(8.64)	
Effect of derivatives [4]								
Hedging derivatives	3,109	(62)			2,642	(386)		
Embedded and ALM derivatives	48,531	437			48,364	(2,025)		
Total liabilities	**77,675**	**560**		**0.72**	**74,929**	**(4,478)**		**(5.98)**
Interest margin			**1.42**	**0.47**			**2.20**	**0.44**

See remarks below.

Note: Complete data on income and expense rates for each sector, by balance sheet item, will be provided upon request.

Management Discussion - Addendum C (continued)

Income and Expense Rates - of the Bank and its Subsidiaries [1]

For the year ended December 31,

Reported amounts (NIS in millions)

	2012				2011			
			Revenue (expense) rate				Revenue (expense) rate	
	Average balance [2]	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives[4]	Average balance [2]	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives[4]
			In %				In %	
Total								
Monetary assets generating financing revenues [3]	149,142	5,923	3.97		138,254	[8] 8,138	5.89	
Effect of derivatives [4]								
Hedging derivatives	3,109	(11)			2,642	308		
Embedded and ALM derivatives	117,232	656			120,347	[8] 4,199		
Total assets	**269,483**	**6,568**		**2.44**	**261,243**	**12,645**		**4.84**
Monetary liabilities generating financing expenses [3]	139,831	(2,937)	(2.10)		129,117	(5,583)	(4.32)	
Effect of derivatives [4]								
Hedging derivatives	3,109	(62)			2,642	(386)		
Embedded and ALM derivatives	117,515	(756)			120,388	(3,830)		
Total liabilities	**260,455**	**(3,755)**		**(1.44)**	**252,147**	**(9,799)**		**(3.89)**
Interest margin			**1.87**	**1.00**			**1.57**	**0.95**
On options		12				[8] 33		
With respect to other derivative instruments (excludes options, hedging and ALM derivatives and embedded derivatives that were detached [4])		26				[8] (5)		
Commissions from financing transactions and other financing revenues [6]		651				397		
Other financing expenses		(69)				(29)		
Profit from financing operations before expenses with respect to credit loss		3,433				3,242		
Expenses with respect to credit loss		(276)				(338)		
Profit from financing operations after expenses with respect to credit loss		3,157				2,904		

See remarks below.

Note: Complete data on income and expense rates for each sector, by balance sheet item, will be provided upon request.

Management Discussion - Addendum C (continued)

Income and Expense Rates - of the Bank and its Subsidiaries [1]

For the year ended December 31,

Reported amounts (NIS in millions)

	2012	2011
	Average balance [2]	Average balance [2]
Total		
Monetary assets generating financing revenues [3]	149,142	138,254
Assets derived from derivative instruments[7]	2,756	[8] 2,814
Other monetary assets [3]	1,530	904
Provision for credit loss	(1,629)	(2,206)
Total monetary assets	**151,799**	**139,766**
Total		
Monetary liabilities generating financing expenses [3]	139,831	129,117
Liabilities deriving from derivatives[7]	3,146	2,799
Other monetary liabilities [3]	1,446	1,731
Total monetary liabilities	**144,423**	**133,647**
Total excess monetary assets over monetary liabilities	7,376	6,119
Non-monetary assets	1,544	1,753
Non-monetary liabilities	249	293
Total capital resources	**8,671**	**7,579**

(1) The data in this table is provided before and after effect of derivatives (including off-balance sheet effects of financial derivatives).
(2) Based on monthly opening balances, except for non-linked Israeli currency, where average balance is calculated based on daily data net of average balance sheet balance of specific provisions for doubtful debts.
(3) Excludes financial derivatives.
(4) Hedging financial derivatives (other than options), embedded derivatives that were detached and derivatives (ALM) which comprise part of the Bank's asset and liability management system.
(5) Includes Israeli currency linked to foreign currency.
(6) Includes gain from sale of investments in debentures from adjustments to fair value of debentures held for trading.
(7) Average balance sheet balances of financial derivatives (excludes average off-balance sheet balances of financial derivatives).
(8) Reclassified.

Note: Complete data on income and expense rates for each sector, by balance sheet item, will be provided upon request.

Management Discussion - Addendum C (continued)

Income and Expense Rates - of the Bank and its Subsidiaries [1]

For the year ended December 31,

Nominal (US$ in millions)

	2012				2011			
			Revenue (expense) rate				Revenue (expense) rate	
	Average balance [2]	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives[4]	Average balance [2]	Financing revenues (expenses)	Excluding effect of derivatives	Including effect of derivatives[4]
			In %				In %	
Foreign currency [5]								
Assets [3]	4,652	113	2.43		5,420	144	2.66	
Effect of derivatives [4]								
Hedging derivatives	806	16			738	19		
Embedded and ALM derivatives	13,349	221			14,781	180		
Total assets	**18,807**	**350**		**1.86**	**20,939**	**343**		**1.64**
Liabilities [3]	7,058	(55)	(0.78)		6,847	(52)	(0.76)	
Effect of derivatives [4]								
Hedging derivatives	806	(18)			738	(37)		
Embedded and ALM derivatives	12,587	(177)			13,516	(143)		
Total liabilities	**20,451**	**(250)**		**(1.22)**	**21,101**	**(232)**		**(1.10)**
Interest margin			**1.65**	**0.64**			**1.90**	**0.54**

(1) The data in this table is provided before and after effect of derivatives (including off-balance sheet effects of financial derivatives).
(2) Net of the average balance sheet balance of specific provisions for doubtful debts.
(3) Excludes financial derivatives.
(4) Hedging financial derivatives (other than options), embedded derivatives that were detached and derivatives (ALM) which comprise part of the Bank's asset and liability management system.
(5) Includes Israeli currency linked to foreign currency.

Note: Complete data on income and expense rates for each sector, by balance sheet item, will be provided upon request.

Management Discussion - Addendum D

Exposure of the Bank and its Subsidiaries To changes in interest rates

As of December 31, 2012

Reported amounts (NIS in millions)

	On Call to 1 month	1-3 months	3 months to 1 year	1-3 years	3-5 years	5-10 years
Israeli currency - non-linked						
Financial assets, amounts receivable with respect to derivatives and to complex financial assets (2)						
Financial assets (1)	72,780	3,563	3,137	2,734	2,347	2,133
Financial derivatives (other than options)	8,383	4,223	24,821	10,826	5,040	11,272
Options (in terms of underlying asset)	942	521	1,838	78	47	114
Total fair value	**82,105**	**8,307**	**29,796**	**13,638**	**7,434**	**13,519**
Financial liabilities, amounts payable with respect to derivatives and to complex financial liabilities (2)						
Financial liabilities (1)	67,966	5,074	7,948	6,440	1,837	497
Financial derivatives (other than options)	11,504	11,069	14,785	8,215	5,339	11,075
Options (in terms of underlying asset)	1,009	1,117	1,730	75	47	114
Total fair value	**80,479**	**17,260**	**24,463**	**14,730**	**7,223**	**11,686**
Financial instruments, net						
Exposure to interest rate fluctuations in the sector	1,626	(8,953)	5,333	(1,092)	211	1,833
Cumulative exposure in sector	1,626	(7,327)	(1,994)	(3,086)	(2,875)	(1,042)

Specific remarks:

(1) Excludes balance sheet balances of financial derivatives, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Instruments classified by term based on average effective duration of each instrument, since exposure to their interest rates could not be reflected by classification by term to maturity of cash flows or term to next interest renewal date.

(3) Weighted average by fair value of average effective duration.

(4) Reclassified.

General remarks:

- Further details about exposure to changes in interest rates in each segment of financial assets and of financial liabilities, by balance sheet item, is available upon demand.
- In this table, data by term represents the present value of future cash flows from each financial instrument, discounted using the interest rate which discounts them to the fair value recognized for the financial instruments in Note 20.3) to the financial statements, consistent with assumptions used to calculate the fair value of the financial instrument. For further details of assumptions used in calculation of the fair value of financial instruments, see Note 20.2) to the financial statements. For further details of the effect of assumed early redemption on average effective duration and fair value, see above in Risk Management-Basel II: Pilars chapter of Board of Directors' Report.
- Internal rate of return is the interest rate which discounts the expected cash flows from a financial instrument to its fair value recognized under Note 20.3) to the financial statements.
- Average effective duration of a group of financial instruments is an approximation of the change, in percent, in fair value of the group of financial instruments which would be caused by a minor change (0.1% increase) in the internal rate of return of each of the financial instruments.
- Certain transactions conducted by the Bank constitute complex financial instruments, which include embedded derivatives not detached, in accordance with public reporting directives. These transactions include, inter alia, loans with exit points, deposits bearing gradual interest rates with withdrawal dates, credit and deposits with guaranteed minimum and deposits with optional linkage. The Bank reflects the interest rate risk with respect to these instruments in a reasonable manner, by spreading maturities of the cash flows in accordance with contract dates, and with various assumptions based on past experience. The instruments for which exposure to interest rate risk may not be reasonably reflected by spreading it over the appropriate contractual periods, are non-material in amount.

					2012			2011
10-20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective term to maturity	Total fair value	Internal rate of return	Average effective term to maturity
				In %	In years		In %	In years
192	(2)	476	87,360	3.76	0.55	(4) 79,294	4.37	0.46
-	-	-	64,565		1.22	67,668		1.10
-	-	-	3,540		1.12	(4) 4,027		0.68
192	**(2)**	**476**	**155,465**		**0.84**	**150,989**		**0.75**
261	(25)	-	89,998	1.59	0.39	78,478	2.75	0.41
-	-	-	61,987		1.69	65,125		1.42
-	-	-	4,092		1.10	5,860		0.56
261	**(25)**	**-**	**156,077**		**0.92**	**149,463**		**0.86**
(69)	23	476	(612)			1,526		
(1,111)	(1,088)	(612)	(612)					

Management Discussion - Addendum D (continued)

Exposure of the Bank and its Subsidiaries To changes in interest rates

As of December 31, 2012

Reported amounts (NIS in millions)

	On Call to 1 month	1-3 months	3 months to 1 year	1-3 years	3-5 years	5-10 years
Israeli currency - linked to the CPI						
Financial assets, amounts receivable with respect to derivatives and to complex financial assets [2]						
Financial assets [1]	987	2,594	10,690	15,798	14,290	5,175
Financial derivatives (other than options)	106	20	845	1,437	582	2,326
Total fair value	**1,093**	**2,614**	**11,535**	**17,235**	**14,872**	**7,501**
Financial liabilities, amounts payable with respect to derivatives and to complex financial liabilities [2]						
Financial liabilities [1]	(8)	1,991	6,193	10,251	8,698	7,565
Financial derivatives (other than options)	451	1,155	5,625	2,830	562	1,932
Total fair value	**443**	**3,146**	**11,818**	**13,081**	**9,260**	**9,497**
Financial instruments, net						
Exposure to interest rate fluctuations in the sector	650	(532)	(283)	4,154	5,612	(1,996)
Cumulative exposure in sector	650	118	(165)	3,989	9,601	7,605

Specific remarks:

(1) Excludes balance sheet balances of financial derivatives, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Instruments classified by term based on average effective duration of each instrument, since exposure to the interest rates there of could not be reflected by classification by term to maturity of cash flows or term to next interest renewal date.

(3) Weighted average by fair value of average effective duration.

General remarks:

- Further details about exposure to changes in interest rates in each segment of financial assets and of financial liabilities, by balance sheet item, is available upon demand.
- In this table, data by term represents the present value of future cash flows from each financial instrument, discounted using the interest rate which discounts them to the fair value recognized for the financial instruments in Note 20.3) to the financial statements, consistent with assumptions used to calculate the fair value of the financial instrument. For further details of assumptions used in calculation of the fair value of financial instruments, see Note 20.2) to the financial statements. For further details of the effect of assumed early redemption on average effective duration and fair value, see above in Risk Management-Basel II: Pillars chapter of Board of Directors' Report.
- Internal rate of return is the interest rate which discounts the expected cash flows from a financial instrument to its fair value recognized under Note 20.3) to the financial statements.
- Average effective duration of a group of financial instruments is an approximation of the change, in percent, in fair value of the group of financial instruments which would be caused by a minor change (0.1% increase) in the internal rate of return of each of the financial instruments.
- Certain transactions conducted by the Bank constitute complex financial instruments, which include embedded derivatives not detached, in accordance with public reporting directives. These transactions include, inter alia, loans with exit points, deposits bearing gradual interest rates with withdrawal dates, credit and deposits with guaranteed minimum and deposits with optional linkage. The Bank reflects the interest rate risk with respect to these instruments in a reasonable manner, by spreading maturities of the cash flows in accordance with contract dates, and with various assumptions based on past experience. The instruments for which exposure to interest rate risk may not be reasonably reflected by spreading it over the appropriate contractual periods, are non-material in amount.

				2012			2011		
	10-20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective term to maturity [(3)]	Total fair value	Internal rate of return	Average effective term to maturity [(3)]
					In %	In years		In %	In years
	1,507	8	299	51,348	2.63	3.08	46,950	3.10	3.11
	-	-	-	5,316		4.15	4,963		4.17
	1,507	**8**	**299**	**56,664**		**3.18**	**51,913**		**3.21**
	1,961	427	2	37,080	1.99	4.12	36,180	2.44	4.19
	-	-	-	12,555		1.68	10,742		1.63
	1,961	**427**	**2**	**49,635**		**3.50**	**46,922**		**3.60**
	(454)	(419)	297	7,029			4,991		
	7,151	6,732	7,029	7,029					

Management Discussion - Addendum D (continued)

Exposure of the Bank and its Subsidiaries To changes in interest rates

As of December 31, 2012

Reported amounts (NIS in millions)

	On Call to 1 month	1-3 months	3 months to 1 year	1-3 years	3-5 years	5-10 years
Foreign currency [4]						
Financial assets, amounts receivable with respect to derivatives and to complex financial assets [2]						
Financial assets [1]	9,345	5,272	2,337	937	562	880
Financial derivatives (other than options)	17,773	11,205	11,794	4,098	3,474	8,501
Options (in terms of underlying asset)	1,218	1,179	1,810	97	49	120
Total fair value	**28,336**	**17,656**	**15,941**	**5,132**	**4,085**	**9,501**
Financial liabilities, amounts payable with respect to derivatives and to complex financial liabilities [2]						
Financial liabilities [1]	13,498	5,893	4,770	270	31	15
Financial derivatives (other than options)	14,513	3,522	16,812	5,473	3,221	9,084
Options (in terms of underlying asset)	990	582	1,895	97	49	120
Total fair value	**29,001**	**9,997**	**23,477**	**5,840**	**3,301**	**9,219**
Financial instruments, net						
Exposure to interest rate fluctuations in the sector	(665)	7,659	(7,536)	(708)	784	282
Cumulative exposure in sector	(665)	6,994	(542)	(1,250)	(466)	(184)

Specific remarks:

(1) Excludes balance sheet balances of financial derivatives, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Instruments classified by term based on average effective duration of each instrument, since exposure to the interest rates there of could not be reflected by classification by term to maturity of cash flows or term to next interest renewal date.

(3) Weighted average by fair value of average effective duration.

(4) Includes Israeli currency linked to foreign currency.

General remarks:

- Further details about exposure to changes in interest rates in each segment of financial assets and of financial liabilities, by balance sheet item, is available upon demand.
- In this table, data by term represents the present value of future cash flows from each financial instrument, discounted using the interest rate which discounts them to the fair value recognized for the financial instruments in Note 20.3) to the financial statements, consistent with assumptions used to calculate the fair value of the financial instrument. For further details of assumptions used in calculation of the fair value of financial instruments, see Note 20.2) to the financial statements. For further details of the effect of assumed early redemption on average effective duration and fair value, see above in Risk Management-Basel II: Pillars chapter of Board of Directors' Report.
- Internal rate of return is the interest rate which discounts the expected cash flows from a financial instrument to its fair value recognized under Note 20.3) to the financial statements.
- Average effective duration of a group of financial instruments is an approximation of the change, in percent, in fair value of the group of financial instruments which would be caused by a minor change (0.1% increase) in the internal rate of return of each of the financial instruments.
- Certain transactions conducted by the Bank constitute complex financial instruments, which include embedded derivatives not detached, in accordance with public reporting directives. These transactions include, inter alia, loans with exit points, deposits bearing gradual interest rates with withdrawal dates, credit and deposits with guaranteed minimum and deposits with optional linkage. The Bank reflects the interest rate risk with respect to these instruments in a reasonable manner, by spreading maturities of the cash flows in accordance with contract dates, and with various assumptions based on past experience. The instruments for which exposure to interest rate risk may not be reasonably reflected by spreading it over the appropriate contractual periods, are non-material in amount.

						2012			2011
	10-20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective term to maturity (3)	Total fair value	Internal rate of return	Average effective term to maturity (3)
					In %	In years		In %	In years
	33	13	277	19,656	2.58	0.89	20,644	3.20	0.71
	-	-	-	56,845		1.71	55,682		1.68
	-	-	-	4,473		0.37	6,872		0.72
	33	**13**	**277**	**80,974**		**1.44**	**83,198**		**1.36**
	13	-	12	24,502	0.48	0.29	24,764	1.67	0.22
	-	-	-	52,625		1.46	53,368		1.39
	-	-	-	3,733		0.49	4,859		0.88
	13	**-**	**12**	**80,860**		**1.06**	**82,991**		**1.01**
	20	13	265	114			207		
	(164)	(151)	114	114					

Management Discussion - Addendum D (continued)

Exposure of the Bank and its Subsidiaries To changes in interest rates

As of December 31, 2012

Reported amounts (NIS in millions)

	On Call to 1 month	1-3 months	3 months to 1 year	1-3 years	3-5 years	5-10 years
Non-monetary						
Financial assets, amounts receivable with respect to derivatives and to complex financial assets [2]						
Options (in terms of underlying asset)	12	(13)	-	(1)	-	-
Total fair value	**12**	**(13)**	**-**	**(1)**	**-**	**-**
Total exposure to interest rate fluctuations						
Financial assets, amounts receivable with respect to derivatives and to complex financial assets [2]						
Financial assets [1]	83,112	11,429	16,164	19,469	17,199	8,188
Financial derivatives (other than options)	26,262	15,448	37,460	16,361	9,096	22,099
Options (in terms of underlying asset)	2,160	1,700	3,648	175	96	234
Total fair value	**111,534**	**28,577**	**57,272**	**36,005**	**26,391**	**30,521**
Financial liabilities, amounts payable with respect to derivatives and to complex financial liabilities [2]						
Financial liabilities [1]	81,456	12,958	18,911	16,961	10,566	8,077
Financial derivatives (other than options)	26,468	15,746	37,222	16,518	9,122	22,091
Options (in terms of underlying asset)	1,987	1,712	3,625	173	96	234
Total fair value	**109,911**	**30,416**	**59,758**	**33,652**	**19,784**	**30,402**
Financial instruments, net						
Total exposure to interest rate fluctuations	1,623	(1,839)	(2,486)	2,353	6,607	119
Total cumulative exposure	1,623	(216)	(2,702)	(349)	6,258	6,377

Specific remarks:

(1) Excludes balance sheet balances of financial derivatives, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Instruments classified by term based on average effective duration of each instrument, since exposure to the interest rates there of could not be reflected by classification by term to maturity of cash flows or term to next interest renewal date.

(3) Weighted average by fair value of average effective duration.

(4) Reclassified.

General remarks:

- Further details about exposure to changes in interest rates in each segment of financial assets and of financial liabilities, by balance sheet item, is available upon demand.
- In this table, data by term represents the present value of future cash flows from each financial instrument, discounted using the interest rate which discounts them to the fair value recognized for the financial instruments in Note 20.3) to the financial statements, consistent with assumptions used to calculate the fair value of the financial instrument. For further details of assumptions used in calculation of the fair value of financial instruments, see Note 20.2) to the financial statements. For further details of the effect of assumed early redemption on average effective duration and fair value, see above in Risk Management-Basel II: Pillars chapter of Board of Directors' Report.
- Internal rate of return is the interest rate which discounts the expected cash flows from a financial instrument to its fair value recognized under Note 20.3) to the financial statements.
- Average effective duration of a group of financial instruments is an approximation of the change, in percent, in fair value of the group of financial instruments which would be caused by a minor change (0.1% increase) in the internal rate of return of each of the financial instruments.
- Certain transactions conducted by the Bank constitute complex financial instruments, which include embedded derivatives not detached, in accordance with public reporting directives. These transactions include, inter alia, loans with exit points, deposits bearing gradual interest rates with withdrawal dates, credit and deposits with guaranteed minimum and deposits with optional linkage. The Bank reflects the interest rate risk with respect to these instruments in a reasonable manner, by spreading maturities of the cash flows in accordance with contract dates, and with various assumptions based on past experience. The instruments for which exposure to interest rate risk may not be reasonably reflected by spreading it over the appropriate contractual periods, are non-material in amount.

					2012			2011
10-20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective term to maturity [3]	Total fair value	Internal rate of return	Average effective term to maturity [3]
				In %	In years		In %	In years
-	-	-	(2)	-	-	(21)	-	-
-	**-**	**-**	**(2)**	**-**	**-**	**(21)**	**-**	**-**
1,732	19	1,052	158,364	3.24	1.41	[4] 146,888	3.80	1.34
-	-	-	126,726		1.56	128,313		1.47
-	-	-	8,013		0.70	[4] 10,874		0.70
1,732	**19**	**1,052**	**293,103**		**1.46**	**286,075**		**1.38**
2,235	402	14	151,580	1.51	1.28	139,422	2.48	1.35
-	-	-	127,167		1.59	129,235		1.43
-	-	-	7,827		0.81	10,719		0.70
2,235	**402**	**14**	**286,574**		**1.41**	**279,376**		**1.36**
(503)	(383)	1,038	6,529			6,699		
5,874	5,491	6,529	6,529					

Management Review - Addendum E

Credit Risk by Economic Sector - Consolidated

As of December 31, 2012

Reported amounts (NIS in millions)

	Off balance sheet debt[1] and credit risk (other than derivatives) [2]			Total credit risk	
	Debt [1]	Guarantees and other commitments on account of clients	Total	Debentures [4]	Fair value of derivatives
Agriculture	637	200	837	-	-
Industry	6,905	4,090	10,995	60	92
Construction and real estate - construction	8,742	13,949	22,691	31	4
Construction and real estate - real estate operations	1,442	286	1,728	-	-
Power and water	362	507	869	57	204
Commerce	7,113	2,061	9,174	-	23
Hotel and food services	374	133	507	-	4
Transport and storage	756	390	1,146	-	3
Communications and computer services	1,645	839	2,484	1	12
Financial services	4,699	6,945	11,644	-	640
Other business services	2,159	845	3,004	-	1
Public and community services	921	386	1,307	-	33
Total commercial credit risk	**35,755**	**30,631**	**66,386**	**149**	**1,016**
Private individuals - housing loans	79,361	4,267	83,628	-	-
Private individuals - other	12,402	9,624	22,026	-	3
Total	**127,518**	**44,522**	**172,040**	**149**	**1,019**
For borrowers' activities overseas	2,726	293	3,019	44	4
Total credit risk to public	**130,244**	**44,815**	**175,059**	**193**	**1,023**
Banking corporations	1,666	96	1,762	520	672
Government	1,153	169	1,322	8,209	-
Total credit risk	**133,063**	**45,080**	**178,143**	**8,922**	**1,695**

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with resale agreements.

(2) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits, except for derivatives.

(3) Includes with respect to off-balance sheet credit instruments (included on balance sheet under Other Liabilities).

(4) Includes borrowed securities amounting to NIS 207 million.

(5) On- and off-balance sheet credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer with respect to total credit risk and with respect to off-balance sheet debt and credit risk (other than derivatives).

	Total credit risk	Total troubled credit risk	Troubled off balance sheet debt [1] and credit risk (other than derivatives)			
				Credit loss [3]		
Future transactions	Total	Troubled [5]	Impaired	Expenses with respect to credit loss	Net accounting write-off	Balance of provision for credit loss
2	839	19	17	3	4	10
332	11,479	234	182	3	56	88
27	22,753	1,223	1,080	45	3	190
-	1,728	83	73	(8)	14	13
540	1,670	2	1	-	-	-
49	9,246	382	177	29	33	135
5	516	10	4	1	4	7
8	1,157	33	30	16	1	23
14	2,511	34	32	(11)	2	11
1,278	13,562	382	302	121	41	202
2	3,007	42	27	(5)	28	26
293	1,633	26	21	1	1	7
2,550	**70,101**	**2,470**	**1,946**	**195**	**187**	**712**
-	83,628	1,594	-	10	73	821
8	22,037	245	92	63	75	142
2,558	**175,766**	**4,309**	**2,038**	**268**	**335**	**1,675**
2	3,069	49	49	12	2	20
2,560	**178,835**	**4,358**	**2,087**	**280**	**337**	**1,695**
1,255	4,209	5	5	(4)	-	10
-	9,531	-	-	-	-	-
3,815	**192,575**	**4,363**	**2,092**	**276**	**337**	**1,705**

Management Discussion - Addendum E [(1)]- continued

Credit Risk by Economic Sector - Consolidated

As of December 31, 2011

Reported amounts (NIS in millions)

	Off balance sheet debt [(2)] and credit risk (other than derivatives) [(3)]			Total credit risk	
	Debt [(2)]	Guarantees and other commitments on account of clients	Total	Debentures [(5)]	Fair value of derivatives
Agriculture	664	202	866	-	2
Industry	6,365	3,358	9,723	94	191
Construction and real estate - construction	8,476	13,573	22,049	37	6
Construction and real estate - real estate operations	1,562	177	1,739	-	-
Power and water	374	610	984	48	76
Commerce	6,938	1,880	8,818	-	38
Hotel and food services	294	133	427	-	1
Transport and storage	827	354	1,181	-	11
Communications and computer services	1,667	1,144	2,811	23	7
Financial services	5,046	7,926	12,972	22	951
Other business services	2,173	615	2,788	-	14
Public and community services	931	337	1,268	-	5
Total commercial credit risk	**35,317**	**30,309**	**65,626**	**224**	**1,302**
Private individuals - housing loans	70,744	3,606	74,350	-	-
Private individuals - other	12,004	9,665	21,669	-	9
Total	**118,065**	**43,580**	**161,645**	**224**	**1,311**
For borrowers' activities overseas	2,866	329	3,195	15	7
Total credit risk to public	**120,931**	**43,909**	**164,840**	**239**	**1,318**
Banking corporations	2,545	292	2,837	551	1,420
Government	1,067	190	1,257	7,496	-
Total credit risk	**124,543**	**44,391**	**168,934**	**8,286**	**2,738**

(1) Reclassified.

(2) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with re-sale agreements.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits, except for derivatives.

(4) Includes with respect to off-balance sheet credit instruments (included on balance sheet under Other Liabilities).

(5) Includes borrowed securities amounting to NIS 136 million.

(6) On- and off-balance sheet credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer with respect to total credit risk and with respect to off-balance sheet debt and credit risk (other than derivatives).

		Total troubled credit risk	Troubled off balance sheet debt [2] and credit risk (other than derivatives)			
				Credit loss [4]		
Future transactions	Total	Troubled [6]	Impaired	Expenses with respect to credit loss	Net accounting write-off	Balance of provision for credit loss
3	871	10	5	7	12	11
322	10,330	215	176	59	92	141
8	22,100	1,268	1,160	71	104	148
1	1,740	96	94	20	12	35
554	1,662	-	-	-	-	-
48	8,904	191	107	89	60	139
1	429	18	5	8	5	10
11	1,203	10	5	1	5	8
22	2,863	18	15	5	5	24
918	14,863	211	121	(65)	37	122
11	2,813	40	47	(2)	(22)	59
246	1,519	69	24	(7)	18	7
2,145	**69,297**	**2,146**	**1,759**	**186**	**328**	**704**
-	74,350	1,712	-	2	57	884
15	21,693	237	54	88	84	154
2,160	**165,340**	**4,095**	**1,813**	**276**	**469**	**1,742**
4	3,221	73	71	57	68	10
2,164	**168,561**	**4,168**	**1,884**	**333**	**537**	**1,752**
2,688	7,496	4	4	6	-	14
-	8,753	-	-	(1)	-	-
4,852	**184,810**	**4,172**	**1,888**	**338**	**537**	**1,766**

Management Review - Addendum F

Exposure to Foreign Countries - Consolidated [(1)]

Reported amounts (NIS in millions)

Part A - Information regarding total exposure to foreign countries and exposure to countries for which total exposure to each country exceeds 1% of total consolidated assets or 20% of capital, whichever is lower:

	Balance sheet exposure [(2)]									Off-balance sheet exposure [(2)(3)]			
Country	Cross-border balance sheet exposure			Balance sheet exposure of affiliates of the banking corporation in foreign country to local residents								Cross-border balance sheet exposure	
	To governments [(4)]	To banks	To others	Balance sheet exposure before deduction of local liabilities	Deduction with respect to local liabilities	Net balance sheet exposure after deduction of local liabilities	Total balance sheet exposure	Off-balance sheet troubled commercial credit risk	Impaired debt [(5)]	Total off-balance sheet exposure	Includes: Off-balance sheet troubled commercial credit risk	Maturing in under 1 year	Maturing in over 1 year
As of December 31, 2012													
USA	-	991	1,079	1,131	1,131	-	2,070	29	21	1,752	-	1,074	996
UK	-	1,136	899	748	234	514	2,549	6	13	1,070	-	1,052	983
France	-	41	1,321	-	-	-	1,362	13	3	427	-	401	961
Other	1	1,099	2,533	-	-	-	3,633	15	2	2,445	-	1,534	2,099
Total exposure to foreign countries	**1**	**3,267**	**5,832**	**1,879**	**1,365**	**514**	**9,614**	**63**	**39**	**5,694**	**-**	**4,061**	**5,039**
Includes: Total exposure to LDC countries	-	81	391	-	-	-	472	1	2	166	-	130	342
Includes: Total exposure to Greece, Portugal, Spain, Italy and Ireland	-	3	26	-	-	-	29	-	-	3	-	4	25

The exposure presented above represents, in accordance with directives of the Supervisor of Banks, exposure based on final risk. The party bearing the final risk is an individual, business, institution or instrument which provides "credit reinforcement" to the bank, such as guarantees, collateral, insurance contracts or credit derivatives. When no "credit reinforcement" exists, the party bearing the final risk is the debtor.

(1) Based on final risk, after effect of guarantees, liquid collateral and credit derivatives.
(2) On- and off-balance sheet credit risk, troubled commercial credit risk and impaired debt are stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.
(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limits.
(4) Governments, official institutions and central banks.
(5) The Bank has started applying the Public Reporting Regulation on measurement and disclosure of impaired debt, credit risk and provision for credit loss as from January 1, 2011. For details see Note 1.J. and Note 4 to the financial statements.

Management Discussion - Addendum F (continued)

Exposure to Foreign Countries - Consolidated [(1)]

Reported amounts (NIS in millions)

Country	Balance sheet exposure [(2)]									Off-balance sheet exposure [(2)(3)]			
	Cross-border balance sheet exposure			Balance sheet exposure of affiliates of the banking corporation in foreign country to local residents								Cross-border balance sheet exposure	
	To governments [(4)]	To banks	To others	Balance sheet exposure before deduction of local liabilities	Deduction with respect to local liabilities	Net balance sheet exposure after deduction of local liabilities	Total balance sheet exposure	Off-balance sheet troubled commercial credit risk [(6)]	Impaired debt [(5)]	Total off-balance sheet exposure	Includes: Off-balance sheet troubled commercial credit risk	Maturing under 1 year	Maturing over 1 year
As of December 31, 2011													
USA	-	1,006	1,481	1,116	1,116	-	2,487	44	34	2,455	-	1,397	1,090
UK	-	670	1,138	652	320	332	2,140	2	28	1,529	-	577	1,231
France	-	103	1,130	-	-	-	1,233	10	3	383	-	388	845
Other	-	1,325	1,673	-	-	-	2,998	6	12	2,472	-	1,803	1,195
Total exposure to foreign countries	**-**	**3,104**	**5,422**	**1,768**	**1,436**	**332**	**8,858**	**62**	**77**	**6,839**	**-**	**4,165**	**4,361**
Includes: Total exposure to LDC countries	-	61	378	-	-	-	439	1	8	281	-	216	223
Includes: Total exposure to Greece, Portugal, Spain, Italy and Ireland	-	3	34	-	-	-	37	-	-	91	-	11	26

(1) Based on final risk, after effect of guarantees, liquid collateral and credit derivatives.

(2) On- and off-balance sheet credit risk, troubled commercial credit risk and impaired debt are stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limits.

(4) Governments, official institutions and central banks.

(5) The Bank has started applying the Public Reporting Regulation on measurement and disclosure of impaired debt, credit risk and provision for credit loss as from January 1, 2011. For details see Note 1.J. and Note 4 to the financial statements.

(6) Reclassified.

Management Discussion - Addendum F - continued

Exposure to Foreign Countries - Consolidated [(1)]

Reported amounts (NIS in millions)

Part B - Information regarding countries for which total exposure to each country is between 0.75%-1% of total consolidated assets or between 15%-20% of capital, whichever is lower:

As of December 31, 2012, there is no reportable exposure pursuant to the Supervisor of Banks' Public Reporting Regulations.

	As of December 31, 2011 [(2)]	
	Balance sheet exposure	Off-balance sheet exposure
Switzerland	445	898
Germany	599	798
Total	**1,044**	**1,696**

(1) Based on final risk, after effect of guarantees, liquid collateral and credit derivatives.
(2) Reclassified.

Part C - Information regarding balance sheet exposure to foreign countries facing liquidity issues

Movement in balance sheet exposure to foreign countries facing liquidity issues:

	For the year ended December 31, 2012			
	Greece	Ireland	Portugal	Total
Exposure at start of reported period	-	6	-	6
Net change in short-term exposure	-	-	-	-
Exposure at end of reported period	**-**	**6**	**-**	**6**

	For the year ended December 31, 2011 [(1)]			
	Greece	Ireland	Portugal	Total
Exposure at start of reported period	-	24	60	84
Net change in short-term exposure	-	(18)	(60)	(78)
Exposure at end of reported period	**-**	**6**	**-**	**6**

(1) Reclassified.

Management Review - Addendum G
Consolidated Balance Sheet – Multi-quarter information

As of the end of each quarter in 2012

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Assets				
Cash and deposits with banks	16,671	16,658	15,846	13,006
Securities	9,041	7,966	9,565	11,230
Securities loaned or sold in repurchase agreements	207	251	131	211
Loans to the public	130,244	(1) 128,220	(1) 125,025	(1) 122,033
Provision for credit loss	(1,593)	(1,654)	(1,639)	(1,664)
Loans to the public, net	128,651	126,566	123,386	120,369
Loans to the Government	317	313	209	190
Investments in associates	60	(1) 54	(1) 53	(1) 56
Buildings and equipment	1,658	1,601	1,594	1,605
Intangible assets and goodwill	87	87	87	87
Assets with respect to derivatives	3,518	2,780	2,964	2,199
Other assets	2,032	1,534	1,476	1,291
Total assets	**162,242**	**157,810**	**155,311**	**150,244**
Liabilities and Shareholders' Equity				
Deposits from the public	128,499	124,322	122,284	119,501
Deposits from banks	1,694	2,031	1,787	1,700
Deposits from the Government	107	119	137	143
Debentures and subordinated notes	14,039	14,186	13,873	12,722
Liabilities with respect to derivatives	3,773	3,553	3,959	3,244
Other liabilities	4,878	4,655	4,627	4,600
Total liabilities	**152,990**	**148,866**	**146,667**	**141,910**
Equity attributable to equity holders of the banking corporation	8,811	8,514	8,231	7,933
Non-controlling interest	441	430	413	401
Total equity	**9,252**	**8,944**	**8,644**	**8,334**
Total liabilities and shareholders' equity	**162,242**	**157,810**	**155,311**	**150,244**

(1) Reclassified.

Management Discussion - Addendum G (continued)
Consolidated Balance Sheet – Multi-quarter information

As of the end of each quarter in 2011

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Assets				
Cash and deposits with banks	15,972	16,987	15,477	14,669
Securities	8,432	5,879	5,431	5,726
Securities loaned or sold in repurchase agreements	136	34	99	173
Loans to the public [(1)]	120,931	119,295	114,113	111,074
Provision for credit loss	(1,638)	(1,708)	[(1)] (1,754)	[(1)] (1,718)
Loans to the public, net	119,293	117,587	112,359	109,356
Loans to the Government	196	146	106	96
Investments in associates [(1)]	52	50	48	51
Buildings and equipment	1,616	1,588	1,551	1,550
Intangible assets and goodwill	87	87	87	87
Assets with respect to derivatives [(1)]	3,115	3,160	2,553	2,760
Other assets[(1)]	1,347	1,359	1,521	1,717
Total assets	**150,246**	**146,877**	**139,232**	**136,185**
Liabilities and Shareholders' Equity				
Deposits from the public	119,236	116,497	111,496	109,029
Deposits from banks	2,007	1,874	1,903	2,306
Deposits from the Government	152	162	157	166
Debentures and subordinated notes	12,202	12,501	11,301	10,284
Liabilities with respect to derivatives	3,964	3,586	2,261	2,500
Other liabilities	4,631	4,521	4,610	4,658
Total liabilities	**142,192**	**139,141**	**131,728**	**128,943**
Equity attributable to equity holders of the banking corporation	7,666	7,359	7,139	6,886
Non-controlling interest	388	377	365	356
Total equity	**8,054**	**7,736**	**7,504**	**7,242**
Total liabilities and shareholders' equity	**150,246**	**146,877**	**139,232**	**136,185**

(1) Reclassified.

Management Review - Addendum H

Consolidated Statement of Profit and Loss – Multi-quarter information

Condensed Consolidated Statement of Profit and Loss by Quarter - for 2012

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest revenues	1,179	1,892	(1) 1,960	(1) 1,560
Interest expenses	536	992	(1) 1,089	(1) 760
Interest revenues, net	643	900	871	800
Expenses with respect to credit loss	48	116	45	67
Interest revenues, net after expenses with respect to credit loss	**595**	**784**	**826**	**733**
Non-interest revenues				
Non-interest financing revenues (expenses)	229	(98)	(1) (22)	(1) (14)
Commissions	367	378	(1) 348	(1) 359
Other revenues	6	7	7	6
Total non-interest revenues	**602**	**287**	**333**	**351**
Operating and other expenses				
Payroll and associated expenses	454	405	408	434
Maintenance and depreciation of buildings and equipment	171	163	160	158
Other expenses	115	108	108	102
Total operating and other expenses	**740**	**676**	**676**	**694**
Pre-tax profit	457	395	483	390
Provision for taxes on profit	176	121	174	128
After-tax profit	281	274	309	262
Net profit:				
Before attribution to non-controlling interest	281	274	309	262
Attributable to non-controlling interest	(11)	(14)	(14)	(11)
Attributable to equity holders of the banking corporation	**270**	**260**	**295**	**251**
Earnings per Ordinary share (in NIS) (2)				
Basic earnings				
Total net profit attributable to holders of ordinary shares of the banking corporation	1.19	1.15	1.31	1.12
Diluted earnings:				
Total net profit attributable to holders of ordinary shares of the banking corporation	1.17	1.14	1.29	1.11

(1) Reclassified.
(2) Share of NIS 0.1 par value each.

Management Discussion - Addendum H (continued)

Consolidated Statement of Profit and Loss – Multi-quarter information

Condensed Consolidated Statement of Profit and Loss by Quarter - for 2011

Reported amounts (NIS in millions)

	Fourth quarter [1]	Third quarter [1]	Second quarter [1]	First quarter [1]
Interest revenues	1,453	1,675	2,046	1,666
Interest expenses	719	784	1,253	985
Interest revenues, net	734	891	793	681
Expenses with respect to credit loss	62	142	80	54
Interest revenues, net after expenses with respect to credit loss	**672**	**749**	**713**	**627**
Non-interest revenues				
Non-interest financing revenues (expenses)	52	(48)	(26)	40
Commissions	359	366	367	382
Other revenues	7	3	1	6
Total non-interest revenues	**418**	**321**	**342**	**428**
Operating and other expenses				
Payroll and associated expenses	411	389	394	421
Maintenance and depreciation of buildings and equipment	153	155	152	148
Other expenses	125	106	109	104
Total operating and other expenses	**689**	**650**	**655**	**673**
Pre-tax profit	401	420	400	382
Provision for taxes on profit	93	154	138	137
After-tax profit	308	266	262	245
Share in profits of associates, after tax	-	-	-	1
Net profit:				
Before attribution to non-controlling interest	308	266	262	246
Attributable to non-controlling interest	(9)	(11)	(10)	(8)
Attributable to equity holders of the banking corporation	**299**	**255**	**252**	**238**
Earnings per Ordinary share (in NIS) [2]				
Basic earnings				
Total net profit attributable to holders of ordinary shares of the banking corporation	1.33	1.14	1.12	1.06
Diluted earnings:				
Total net profit attributable to holders of ordinary shares of the banking corporation	1.32	1.12	1.10	1.04

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. For details, see Note 1.D.1.

(2) Share of NIS 0.1 par value.

Certification

I, ELIEZER YONES, certify that:

1. I have reviewed the annual report of Mizrahi Tefahot Bank Ltd. ("the Bank") for the year 2012 ("the Report").

2. Based on my knowledge, this Report does not contain any untrue statement of a material fact or omit to state a material fact necessary so that the statements included therein, in light of the circumstances under which such statements were made, will not be misleading with respect to the period covered by the Report.

3. Based on my knowledge, the financial statements and other financial information included in the Report fairly present, in all material respects, the financial condition, results of operations, and changes in shareholders' equity and cash flows of the Bank as of the dates and for the periods presented in this Report.

4. I and others at the Bank who provide this certification, are responsible for determining and maintaining controls and procedures with regard to disclosure(1) and to the Bank's internal controls over financial reporting(1) as well as:

   A. We have determined such controls and procedures, or caused these controls and procedures to be determined under our supervision, for the purpose of ensuring that material information relating to the Bank, including its subsidiaries, is made known to us by others in the Bank and in those entities, particularly during the period in which the Report is being prepared;

   B. We have set such internal controls over financial reporting, or had them set under our supervision, intended to provide a reasonable degree of certainty with regard to the reliability of financial reporting and to the fact that the financial statements for external use are prepared in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks.

   C. We have evaluated the effectiveness of the Bank's disclosure controls and procedures and have presented in this report our conclusions about the effectiveness of the disclosure controls and procedures in this Report, as of the end of the period covered by this Report based on our evaluation; and

   D. We have disclosed in this Report any change in the Bank's internal controls over financial reporting that occurred during the fourth quarter, that has materially affected, or is reasonably likely to materially affect, the Bank's internal controls over financial reporting; and

5. I and others in the Bank who are declaring this certification, have disclosed, based on our most recent evaluation of the internal controls over financial reporting, to the Bank's independent auditors, the Board of Directors and the Audit Committee of the Board of Directors of the Bank:

   A. All significant deficiencies and material weaknesses in the determination or operation of internal control over financial reporting which are reasonably likely to impair the Bank's ability to record, process, summarize and report financial information; and

   B. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank's internal controls over financial reporting.

The aforesaid does not derogate from my responsibility or the responsibility of any other person according to the law.

Eliezer Yones
President

March 17, 2013

(1) As defined in public reporting regulations with regard to "Report of the Board of Directors".

Certification

I, MENAHEM AVIV, declare that

1. I have reviewed the annual report of Mizrahi Tefahot Bank Ltd. ("the Bank") for the year 2012 ("the Report").

2. Based on my knowledge, this Report does not contain any untrue statement of a material fact or omit to state a material fact necessary so that the statements included therein, in light of the circumstances under which such statements were made, will not be misleading with respect to the period covered by the Report.

3. Based on my knowledge, the financial statements and other financial information included in the Report fairly present, in all material respects, the financial condition, results of operations, and changes in shareholders' equity and cash flows of the Bank as of and for the periods presented in this Report.

4. I and others at the Bank who provide this certification, are responsible for determining and maintaining controls and procedures with regard to disclosure(1) and to the Bank's internal controls over financial reporting(1) as well as:

   A. We have determined such controls and procedures, or caused these controls and procedures to be determined under our supervision, for the purpose of ensuring that material information relating to the Bank, including its subsidiaries, is made known to us by others in the Bank and in those entities, particularly during the period in which the Report is being prepared;

   B. We have set such internal controls over financial reporting, or had them set under our supervision, intended to provide a reasonable degree of certainty with regard to the reliability of financial reporting and to the fact that the financial statements for external use are prepared in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks.

   C. We have evaluated the effectiveness of the Bank's disclosure controls and procedures and have presented in this report our conclusions about the effectiveness of the disclosure controls and procedures in this Report, as of the end of the period covered by this Report based on our evaluation; and

   D. We have disclosed in this Report any change in the Bank's internal controls over financial reporting that occurred during the fourth quarter, that has materially affected, or is reasonably likely to materially affect, the Bank's internal controls over financial reporting; and

5. I and others in the Bank who are declaring this certification, have disclosed, based on our most recent evaluation of the internal controls over financial reporting, to the Bank's independent auditors, the Board of Directors and the Audit Committee of the Board of Directors of the Bank:

   A. All significant deficiencies and material weaknesses in the determination or operation of internal control over financial reporting which are reasonably likely to impair the Bank's ability to record, process, summarize and report financial information; and

   B. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank's internal controls over financial reporting.

The aforesaid does not derogate from my responsibility or the responsibility of any other person according to the law.

Menahem Aviv
Vice-president, Chief Accountant

March 17, 2013

(1) As defined in public reporting regulations with regard to "Report of the Board of Directors".

Report of the Board of Directors and Management as to Internal Control of Financial Reporting

The Board of Directors and Management of Mizrahi Tefahot Bank Ltd. (hereinafter: "the Bank") are responsible for establishing and maintaining proper internal controls over financial reporting (as defined in public reporting regulations with regard to the "Report of the Board of Directors"). The Bank's internal control system has been designed to provide the Bank's Board of Directors and management with a reasonable degree of certainty as to proper preparation and presentation of the financial statements published in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks. Regardless of the quality of its design, all internal control systems have inherent limitations. Therefore, even should it be determined that these systems are effective, they may only provide a reasonable degree of certainty with regard to preparation and presentation of financial statements.

The management, under supervision of the Board of Directors, maintains a comprehensive system of controls intended to ensure that transactions are executed in line with management authorization, that assets are protected, and that accounting records are reliable. Furthermore, management under supervision of the Board of Directors, takes steps to ensure that information and communication channels are effective and monitor execution, including execution of internal control procedures.

The Bank's management, under supervision of the Board of Directors, has evaluated the effectiveness of the Bank's internal control system over financial reporting as of December 31, 2012 based on criteria stipulated in the internal control model of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on the aforementioned evaluation, management believes that as of December 31, 2012, the Bank's internal controls over financial reporting are effective.

The effectiveness of the Bank's internal controls over financial reporting as of December 31, 2012 was audited by the Bank's independent auditors, Brightman Almagor Zohar & Co. ,as noted in their report on page 240, which includes their unqualified opinion as to the effectiveness of the Bank's internal controls over financial reporting as of December 31, 2012.

Moshe Vidman	Eliezer Yones	Menahem Aviv
Chairman of the Board of Directors	President	Vice-president, Chief Accountant

Ramat Gan, March 17, 2013

Financial Statements

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Independent Auditors' Report to Shareholders of Bank Mizrahi-Tefahot Limited Pursuant to Public Reporting Directives of the Supervisor of Banks Concerning Internal Controls over financial Reporting

We have audited the internal controls over financial reporting at Bank Mizrahi-Tefahot Ltd. and subsidiaries (hereinafter jointly: "the Bank") as of December 31, 2012 based on criteria stipulated under the integrated framework for internal control published by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). The Bank's Board of Directors and management are responsible for maintaining effective internal controls over financial reporting, and for evaluating the effectiveness of these internal controls over financial reporting which is included in the attached report of the Board of Directors and management with regard to internal controls over financial reporting. We are responsible for our opinion on the Bank's internal controls over financial reporting, based on our audit.

We have not audited the effectiveness of internal controls over financial reporting at subsidiaries whose assets and whose net interest revenues before expenses with respect to credit loss included in consolidation account for 7.29% and 5.34%, respectively of the related amounts in the consolidated financial statements as of December 31, 2012 and for the year then ended. The effectiveness of internal controls over financial reporting at these companies was audited by other independent auditors whose reports have been provided to us and our opinion, in as much as it refers to effectiveness of internal controls over financial reporting at these companies, Is based on the reports of these other independent auditors.

We have conducted our audit in accordance with standards of the Public Company Accounting Oversight Board (PCAOB) in the USA with regard to audit of internal controls over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel. In accordance with these standards, we are required to design and execute the audit so as to achieve a reasonable degree of certainty as to the existence of effective internal controls over financial reporting, in all material aspects. Our audit included: understanding of the internal controls over financial reporting, evaluation of the risk of existence of any material weakness, testing and evaluation of the effective design and operation of internal control based on the evaluated risk. Our audit also included additional procedures which we believed to be necessary under the circumstances. We believe that our audits and the reports of the other independent auditors provide a reasonable basis for our opinion.

A bank's internal controls over financial reporting is a process designed to provide a reasonable degree of certainty as to the reliability of financial reporting and preparation of financial statements for external use in accordance with Israeli GAAP, directives and guidelines of the Supervisor of Banks. A bank's internal controls over financial reporting include policies and procedures which: (1) refer to record keeping which, with reasonable detail, accurately and properly reflects transactions and transfers of Bank assets (including their removal from Bank ownership); (2) provide a reasonable degree of certainty that transactions are properly recorded so as to allow for preparation of financial statements in accordance with Israeli GAAP and directives and guidelines of the Supervisor of Banks, and that the Bank's receipts and expenditures are made exclusively in line with authorizations of the Bank's management and Board members; and (3) provide a reasonable degree of certainty with regard to avoidance or timely discovery of any unauthorized acquisition, use or transfer of Bank assets (including removal from Bank ownership) which may materially impact the financial statements.

Due to their apparent limitations, internal controls over financial reporting may fail to prevent or discover any misrepresentation. Also, drawing conclusions about the future on the basis of any evaluation of current effectiveness is subject to the risk that controls may become inappropriate due to changes in circumstances or due to negative change in the extent to which policies or procedures are adhered to.

We believe that the Bank maintained, in all material aspects, effective internal controls over financial reporting as of December 31, 2012 based on criteria stated in the integrated framework for internal controls published by COSO.

We have also audited, in accordance with auditing standards generally accepted in Israel and certain auditing standards whose application to audits of banking corporations was stipulated in directives of and guidance from the Supervisor of Banks, the Bank's financial statements (and consolidated financial statements) as of December 31, 2012 and 2011 and for each of the three years ended December 31, 2012, and our report dated March 17, 2013 includes our unqualified opinion on the aforementioned financial statements, based on our audit and on reports of other independent auditors, as well as drawing attention with regard to claims filed against the Bank, including motions to grant class action status.

Brightman Almagor Zohar & Co.
Certified Public Accountants
Brightman Almagor Zohar & Co.
Tel Aviv, March 17, 2013

Independent Auditors' Report to Shareholders of Bank Mizrahi-Tefahot Limited

We have audited the accompanying balance sheets of Mizrahi Tefahot Limited ("the Bank") as of December 31, 2012 and 2011, and the consolidated balance sheets as of such dates, and the statements of profit and loss, changes in shareholders' equity and cash flows – of the Bank and on a consolidated basis – for each of the three years in the period ended December 31, 2012. These financial statements are the responsibility of the Bank's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audit.

We did not audit the financial statements of certain consolidated subsidiaries, whose assets included in consolidation constitute 7.29% and 7.69% of total consolidated assets as of December 31, 2012 and 2011, respectively, and whose net interest revenues before expenses with respect to credit loss included in the consolidated statements of profit and loss constitute 5.34%, 4.84% and 3.97% of total profit from financing operations before provision for doubtful debts included in the consolidated statement of profit and loss for the years ended December 31, 2012, 2011 and 2010, respectively. Furthermore, we have not audited the financial statements of affiliates, the investment in which amounts to NIS 17 million as of December 31, 2012 and NIS 15 million as of December 31, 2011. The financial statements of these companies were audited by other auditors, whose reports were furnished to us, and our opinion, insofar as it relates to amounts included with respect to these companies, is based on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards in Israel, including those prescribed by the Auditors' Regulations (Mode of Performance), 1973 and certain auditing standards, the application of which was mandated by the directives of the Supervisor of Banks. These regulations require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditors, the above financial statements present fairly, in all material respects, the financial position - of the Bank and on a consolidated basis – as of December 31, 2012 and 2011, and the results of operations, changes in shareholders' equity and cash flows – of the Bank and on a consolidated basis – for each of the three years in the period ended December 31, 2012, in conformity with generally accepted accounting principles in Israel (Israeli GAAP). Also, in our opinion, the financial statements have been prepared in accordance with the directives and guidelines of the Supervisor of Banks.

Without qualifying our aforementioned opinion, we draw your attention to Note 19.D.11)A.-E. with regard to lawsuits filed against the Bank, including motions for class action status.

We have also audited in accordance with PCAOB standards in the USA with regard to audit of internal controls over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel, the internal controls over financial reporting at the Bank as of December 31, 2012, based on criteria specified in the integrated framework for internal control published by COSO, and our report dated March 17, 2013 included an unqualified opinion of the effectiveness of internal controls over financial reporting at the Bank.

Brightman Almagor Zohar & Co.
Certified Public Accountants
Brightman Almagor Zohar & Co.
Tel Aviv, March 17, 2013

Balance sheet – consolidated and the Bank - as of December 31

Reported amounts (NIS in millions)

	Note	Consolidated		The Bank	
		2012	2011	2012	2011
Assets					
Cash and deposits with banks	2	16,671	15,972	13,586	12,874
Securities(1)	15, 3	9,041	8,432	6,284	5,730
Securities loaned or sold in repurchase agreements	15	207	136	207	136
Loans to the public		130,244	(3) 120,931	123,870	(3) 114,932
Provision for credit loss		(1,593)	(1,638)	(1,564)	(1,610)
Loans to the public, net	4	128,651	119,293	122,306	113,322
Loans to Governments	5	317	196	317	196
Investments in associates	6	60	(3) 52	2,131	(3) 1,964
Buildings and equipment	7	1,658	1,616	1,505	1,468
Intangible assets and goodwill		87	87	87	87
Assets with respect to derivatives	19.E.	3,518	(3) 3,115	3,518	(3) 3,108
Other assets	8	2,032	(3) 1,347	1,904	(3) 1,233
Total assets		**162,242**	**150,246**	**151,845**	**140,118**
Liabilities and Shareholders' Equity					
Deposits from the public	9	128,499	119,236	123,214	113,115
Deposits from banks	10	1,694	2,007	8,204	7,211
Deposits from the Government		107	152	93	141
Debentures and subordinated notes	11	14,039	12,202	4,125	4,575
Liabilities with respect to derivatives	19.E.	3,773	3,964	3,773	3,956
Other liabilities(2)	12	4,878	4,631	3,625	3,454
Total liabilities		**152,990**	**142,192**	**143,034**	**132,452**
Equity attributable to equity holders of the banking corporation		8,811	7,666	8,811	7,666
Non-controlling interest		441	388	-	-
Total equity	13	**9,252**	**8,054**	**8,811**	**7,666**
Total liabilities and shareholders' equity		**162,242**	**150,246**	**151,845**	**140,118**

(1) Includes: NIS 7,918 million at fair value on consolidated basis (December 31, 2011 - NIS 7,729 million) and for the Bank - NIS 6,284 million (December 31, 2011 - NIS 5,730 million).
(2) Includes: provision for credit loss with respect to off-balance sheet credit instruments, consolidated - NIS 102 million (on December 31, 2011 - NIS 114 million) and at the Bank - NIS 100 million (on December 31, 2011 - NIS 111 million).
(3) Reclassified.

The accompanying notes are an integral part of the financial statements.

M. Vidman

Moshe Vidman
Chairman of the Board of Directors

Eliezer Yones
President

Menahem Aviv
Vice-president, Chief Accountant

Approval date:
Ramat Gan, March 17, 2013

Statement of Profit and Loss - Consolidated and the Bank

For the year ended December 31,

Reported amounts (NIS in millions)

	Note	Consolidated			The Bank		
		2012	[(1)] 2011	[(1)] 2010	2012	[(1)] 2011	[(1)] 2010
Interest revenues		6,591	6,840	5,509	6,158	6,343	5,174
Interest expenses		3,377	3,741	2,621	3,355	3,606	2,563
Interest revenues, net	22	3,214	3,099	2,888	2,803	2,737	2,611
Expenses with respect to credit loss	4.A.	276	338	473	277	326	464
Interest revenues, net after expenses with respect to credit loss		**2,938**	**2,761**	**2,415**	**2,526**	**2,411**	**2,147**
Non-interest revenues							
Non-interest financing revenues (expenses)	23	95	18	(25)	82	(15)	(25)
Commissions	24	1,452	1,474	1,432	1,180	1,200	1,165
Other revenues	25	26	17	33	20	12	21
Total non-interest revenues		**1,573**	**1,509**	**1,440**	**1,282**	**1,197**	**1,161**
Operating and other expenses							
Payroll and associated expenses	26	1,701	1,615	1,529	1,474	1,394	1,327
Maintenance and depreciation of buildings and equipment		652	608	585	566	538	515
Amortization and impairment of intangible assets and goodwill		-	-	14	-	-	14
Other expenses	27	433	444	438	318	332	324
Total operating and other expenses		**2,786**	**2,667**	**2,566**	**2,358**	**2,264**	**2,180**
Pre-tax profit		1,725	1,603	1,289	1,450	1,344	1,128
Provision for taxes on profit	28	599	522	469	516	451	424
After-tax profit		1,126	1,081	820	934	893	704
Share in profits of associates, after tax	6.B	-	1	-	142	151	97
Net profit:							
Before attribution to non-controlling interest		1,126	1,082	820	1,076	1,044	801
Attributable to non-controlling interest		(50)	(38)	(19)	-	-	-
Attributable to equity holders of the banking corporation		**1,076**	**1,044**	**801**	**1,076**	**1,044**	**801**

(1) Data on the statement of profit and loss for previous periods were reclassified to adjust them for the new format adopted by the Supervisor of Banks. For details, see Note 1.D.1.

The accompanying notes are an integral part of the financial statements.

Statement of Profit and Loss - Consolidated and the Bank (continued)

For the year ended December 31,

Reported amounts

	Note	2012	2011	2010
Earnings per share[1]	1.W.			
Basic earnings per share (in NIS)				
Net profit attributable to equity holders of the banking corporation		4.77	4.65	3.63
Diluted earnings per share (in NIS)				
Net profit attributable to equity holders of the banking corporation		4.74	4.57	3.58

(1) Share of NIS 0.1 par value each.

The accompanying notes are an integral part of the financial statements.

Statement of Changes in Shareholders' Equity

Reported amounts (NIS in millions)

	Share capital and premium[(1)]	Capital reserve from benefit from share-based payment transactions	Treasury shares	Total paid-up share capital and capital reserves
Balance as of January 1, 2010	**1,963**	**105**	**(76)**	**1,992**
Net profit for the year	-	-	-	-
Dividends paid	-	-	-	-
Dividends declared after balance sheet date	-	-	-	-
Benefit from share-based payment transactions	-	44	-	44
Related tax effect	-	30	-	30
Realized share-based payment transactions[(5)]	23	(23)	-	-
Adjustments for presentation of securities available for sale at fair value	-	-	-	-
Adjustments for presentation of securities available for sale reclassified to statement of profit and loss	-	-	-	-
Related tax effect	-	-	-	-
Net gain from cash flow hedges	-	-	-	-
Net gain from cash flow hedges reclassified to the statement of profit and loss	-	-	-	-
Related tax effect	-	-	-	-
Balance as of January 1, 2011	**1,986**	**156**	**(76)**	**2,066**
Cumulative effect, net of tax, of initial application on January 1, 2011 of the directive concerning measurement of impaired debt and provision for credit loss [(6)]	-	-	-	-
Cumulative effect, net of tax, of initial application on January 1, 2011 of certain IFRS standards	-	-	-	-
Balance as of January 1, 2011, after reconciliation from application of new standards and directives	**1,986**	**156**	**(76)**	**2,066**
Net profit for the year	-	-	-	-
Dividends paid	-	-	-	-
Benefit from share-based payment transactions	-	43	-	43
Related tax effect	-	(27)	-	(27)
Realized share-based payment transactions[(5)]	17	(17)	-	-
Adjustments for presentation of securities available for sale at fair value	-	-	-	-
Adjustments for presentation of securities available for sale reclassified to statement of profit and loss	-	-	-	-
Related tax effect	-	-	-	-
Net gain from cash flow hedeges reclassified to the statement of profit and loss	-	-	-	-
Related tax effect	-	-	-	-
Balance as of December 31, 2011	**2,003**	**155**	**(76)**	**2,082**

(1) Share premium generated prior to March 31, 1986.
(2) Foreign currency translation adjustment of autonomous overseas units.
(3) For details on various limitations on dividend distributions, see Note 13 below.
(4) Retroactively adjusted as per directives of the Supervisor of Banks with regard to employee rights.
(5) In 2011, some 575,122 (in 2010 - 564,642) ordinary NIS 0.1 par value shares were issued for exercise of options in conjunction with the Employee Stock Option Plan, and 513,627 ordinary NIS 0.1 par value shares (in 2010 - 445,048) were issued to the President for exercise of options.
(6) For details, see Note 1.J. below.

he accompanying notes are an integral part of the financial statements.

Cumulative Other Comprehensive Income (Loss)							
Adjustments for presentation of securities available for sale at fair value	Translation adjustments[2]	Net gain from cash flow hedges	Retained earnings[3]	Dividends declared after balance sheet date	Total	Non-controlling interest	Total equity
(32)	**(51)**	**39**	[4] **4,499**	**-**	**6,447**	[4] **346**	**6,793**
-	-	-	[4] 801	-	801	[4] 19	820
-	-	-	(200)	-	(200)	-	(200)
-	-	-	(120)	120	-	-	-
-	-	-	-	-	44	-	44
-	-	-	-	-	30	-	30
-	-	-	-	-	-	-	-
16	-	-	-	-	16	2	18
7	-	-	-	-	7	-	7
(2)	-	-	-	-	(2)	(1)	(3)
-	-	32	-	-	32	-	32
-	-	(53)	-	-	(53)	-	(53)
-	-	8	-	-	8	-	8
(11)	**(51)**	**26**	[4] **4,980**	**120**	**7,130**	**366**	**7,496**
-	-	-	(359)	-	(359)	(16)	(375)
-	51	-	69	(120)	-	-	-
(11)	**-**	**26**	**4,690**	**-**	**6,771**	**350**	**7,121**
-	-	-	1,044	-	1,044	39	1,083
-	-	-	(120)	-	(120)	-	(120)
-	-	-	-	-	43	-	43
-	-	-	-	-	(27)	-	(27)
-	-	-	-	-	-	-	-
(65)	-	-	-	-	(65)	(2)	(67)
10	-	-	-	-	10	-	10
18	-	-	-	-	18	1	19
-	-	(12)	-	-	(12)	-	(12)
-	-	4	-	-	4	-	4
(48)	**-**	**18**	**5,614**	-	**7,666**	**388**	**8,054**

Statement of Changes in Shareholders' Equity (continued)

Reported amounts (NIS in millions)

	Shares capital and premium [1]	Capital reserve from benefit from share-based payment transactions	Treasury shares	Total paid-up share capital and capital reserves
Balance as of January 1, 2012	**2,003**	**155**	**(76)**	**2,082**
Net profit for the period	-	-	-	-
Benefit from share-based payment transactions	-	11	-	11
Related tax effect	-	28	-	28
Realized share-based payment transactions[3]	55	(55)	-	-
Adjustments for presentation of securities available for sale at fair value	-	-	-	-
Adjustments for presentation of securities available for sale reclassified to statement of profit and loss	-	-	-	-
Related tax effect	-	-	-	-
Net gain from cash flow hedges reclassified to the statement of profit and loss	-	-	-	-
Related tax effect	-	-	-	-
Balance as of December 31, 2012	**2,058**	**139**	**(76)**	**2,121**

(1) Share premium generated prior to March 31, 1986.

(2) For details on various limitations on dividend distributions, see Note 13 below.

(3) In 2012, some 1,948,544 (in 2011 - 575,122) ordinary NIS 0.1 par value shares were issued for exercise of options in conjunction with the Employee Stock Option Plan, and 413,036 ordinary NIS 0.1 par value shares (in 2011 - 513,627) were issued to the President for exercise of options.

The accompanying notes are an integral part of the financial statements.

Cumulative Other Comprehensive Income (Loss) Adjustments for presentation of securities available for sale at fair value	Net gain from cash flow hedges	Retained earnings[(2)]	Total	Non-controlling interest	Total equity
(48)	**18**	**5,614**	**7,666**	**388**	**8,054**
-	-	1,076	1,076	50	1,126
-	-	-	11	-	11
-	-	-	28	-	28
-	-	-	-	-	-
61	-	-	61	6	67
8	-	-	8	(2)	6
(24)	-	-	(24)	(1)	(25)
-	(22)	-	(22)	-	(22)
-	7	-	7	-	7
(3)	**3**	**6,690**	**8,811**	**441**	**9,252**

Statement of Cash Flows - Consolidated and the Bank [(1)]

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
Cash flows provided by current operations						
Net profit for the period	1,126	1,082	820	1,076	1,044	801
Adjustments:						
Share of corporation in un-distributed earnings of associates	-	(1)	-	(142)	(152)	(97)
Depreciation of buildings and equipment	230	219	221	207	201	203
Expenses with respect to credit loss	276	338	473	277	326	464
Net profit (loss) from revaluation of securities held to maturity, from revaluation and sale of securities available for sale.	(244)	(419)	119	(160)	(352)	182
Impairment of securities held for sale	8	10	7	8	10	7
Realized and unrealized gain from adjustment to fair value of securities held for trading	(44)	(19)	(9)	(44)	(19)	(9)
Net loss (gain) from sale of buildings and equipment	-	(5)	2	-	(5)	2
Benefit from share-based payment transactions	11	43	44	11	43	44
Deferred taxes, net	17	(105)	61	6	(62)	61
Severance pay - decrease (increase) in excess of amount funded over liability	(8)	123	(34)	(8)	119	(34)
Accrual differences included under investment and financing operations	73	213	162	(36)	76	67
Effect of change in exchange rate on cash balances	66	(234)	314	63	(215)	289
Net change in current assets						
Deposits with banks, net	(1,296)	1,798	(1,174)	(39)	(139)	129
Loans to the public, net	(9,669)	(13,318)	(12,264)	(9,296)	(12,944)	(12,075)
Loans to the Governments, net	(121)	(104)	209	(121)	(104)	209
Securities loaned or sold in repurchase agreements, net	(71)	111	60	(71)	111	60
Assets with respect to derivatives, net	(425)	-	(1,957)	(432)	(3)	(1,946)
Securities held for trading, net	(1,064)	(878)	(23)	(1,065)	(880)	(23)
Other assets, net	(689)	191	24	(660)	135	35
Net change in current liabilities						
Deposits from banks, net	(313)	(425)	533	993	(63)	878
Deposits from the public, net	9,263	13,245	10,970	10,099	14,231	12,397
Deposits from the Government, net	(45)	(20)	(37)	(48)	(28)	(38)
Liabilities with respect to derivatives, net	(191)	1,072	911	(183)	1,071	914
Other liabilities, net	285	(35)	108	203	(145)	78
Deferred income, net	11	(45)	44	14	(47)	43
Net cash provided by current operations	**(2,814)**	**2,837**	**(416)**	**652**	**2,209**	**2,641**

(1) Data for prior periods was restated due to initial adoption of IAS 7 "Statement of cash flows". For details see Note 1.C.

The accompanying notes are an integral part of the financial statements.

Statement of Cash Flows - Consolidated and the Bank (continued)

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
Cash flows provided by investment operations						
Acquisition of debentures held to maturity	(420)	(703)	-	-	-	-
Proceeds from redemption of debentures held to maturity	25	8	-	-	-	-
Acquisition of securities available for sale	(7,479)	(8,265)	(6,759)	(6,581)	(7,145)	(4,974)
Proceeds from sale and redemption of securities available for sale	8,717	9,159	6,883	7,392	7,721	5,185
Acquisition of buildings and equipment	(316)	(252)	(263)	(288)	(231)	(250)
Proceeds from sale of buildings and equipment	-	14	16	-	14	16
Purchase of shares in associates	(8)	(1)	(3)	(25)	(30)	(69)
Net cash provided by investment operations	**519**	**(40)**	**(126)**	**498**	**329**	**(92)**
Cash flows provided by financing operations						
Issuance of debentures and subordinated notes	2,161	2,620	1,786	-	57	90
Redemption of debentures and subordinated notes	(397)	(375)	(301)	(414)	(239)	(301)
Dividends paid to shareholders	-	(120)	(200)	-	(120)	(200)
Net cash provided by financing operations	**1,764**	**2,125**	**1,285**	**(414)**	**(302)**	**(411)**
Increase (decrease) in cash	(531)	4,922	743	736	2,236	2,138
Cash balance at beginning of year	14,991	9,835	9,406	12,269	9,818	7,969
Effect of change in exchange rate on cash balances	(66)	234	(314)	(63)	215	(289)
Cash balance at end of period	**14,394**	**14,991**	**9,835**	**12,942**	**12,269**	**9,818**
Interest and taxes paid / received and divdends received						
Interest received	6,602	6,827	5,496	6,139	6,330	5,086
Interest paid	3,270	3,605	2,485	3,301	3,552	2,509
Dividends received	24	1	1	24	1	1
Taxes on income received	-	59	179	-	58	179
Taxes on income paid	556	512	450	528	489	422
Appendix A - Non-cash Transactions						
Acquisition of buildings and equipment	44	67	2	44	67	2

Notes to financial statements as of December 31, 2012

Note 1 - Reporting Principles and Accounting Policies

A. General

1) The financial statements are compiled in accordance with generally accepted accounting policies in Israel (Israeli GAAP) and in accordance with directives and guidance from the Supervisor of Banks.

2) The notes to the financial statements refer to the financial statements of the Bank, as well as to the consolidated financial statements of the Bank and its subsidiaries, unless a note explicitly states that it refers only to the statements of the Bank, or to the consolidated statements.

3) Definitions:

"Generally Accepted Accounting Practices" Accounting rules which American banks traded in the USA are required to apply at US banks as stipulated by the ASC 105 codification.

"International Financial Reporting Standards"

Standards and interpretations adopted by IASB, including International Financial Reporting Standards (hereinafter: "IFRS") and International Accounting Standards (IAS), including interpretations of these standards by the International Financial Reporting Interpretations Committee (IFRIC) or interpretations by the Standing Interpretations Committee (SIC), respectively.

"IASB"	International Accounting Standards Board.
"FASB"	Financial Accounting Standards Board in the USA.
“Subsidiaries”	Companies controlled by the banking corporation.
“Affiliates”	Entities in which the Group has material influence over financial and operational policy, but over which it has no control. Investment in associates is included on the financial statements using the equity method.
“Investees”	Subsidiaries and associates.
"Overseas affiliates"	Representatives, agencies, branches or subsidiaries of the Bank outside Israel.
"Functional currency"	The currency of the major economic environment in which the Bank operates. Usually, this is the currency of the environment in which a corporation generates and expends most of the cash.
"Reporting currency"	The currency in which the financial statements are presented.
“Adjusted amount”	The historical nominal amount that was adjusted to the CPI for December 2003, in conformity with the opinions of the Institute of Certified Public Accountants in Israel.

Note 1 - Reporting Principles and Accounting Policies - (continued)

“Reported amount”	An amount adjusted as of December 31, 2003 (hereinafter: "the transition date"), plus amounts in nominal values that were added after the transition date, minus amounts deducted after the transition date. After the transition date, the amounts are deducted in historical nominal values, in adjusted amounts at the transition date or a combination of historical nominal values and adjusted amounts as of the transition date, as applicable.
“Cost”	Cost in reported amount.
"Related parties"	As defined in IAS 24 "Related party disclosures", other than interested parties.
"Interested parties"	As defined in Paragraph 1 of the definition of "Interested party in a corporation" in Section 1 of the Securities Act, 1968.

B. Principles of financial reporting

These condensed financial statements have been prepared as follows:

1. As for core banking business issues - the accounting treatment is in accordance with directives of the Supervisor of Banks and in accordance with generally accepted accounting principles for US banks, as adopted in the Supervisor of Banks' Public Reporting Regulations.
2. As for non-core banking business issues - the accounting treatment is in accordance with Israeli GAAP and in accordance with certain International Financial Reporting Standards (IFRS) and the relevant IFRIC interpretations.

   International standards are applied in accordance with the following guidelines:

   - In cases where a material issue arises, which is not addressed by the international standards or by application directives issued by the Supervisor of Banks, the Group shall handle the issue in accordance with generally accepted accounting principles at US banks which specifically apply to these issues.
   - In cases where the adopted international standard makes reference to another international standard adopted under the public reporting directives, the Group shall act in accordance with provisions of the international standard.
   - In cases where the adopted international standard makes reference to an international standard not adopted under the public reporting directives, the Group shall act in accordance with reporting directives and in accordance with generally accepted accounting principles in Israel.
   - In cases where the adopted international standard makes reference to definition of a term also defined in the public reporting directives, the reference to the definition in the directives shall replace the original reference.

Note 1 - Reporting Principles and Accounting Policies

3. Use of estimates

In preparing the consolidated financial statements in accordance with directives and guidelines of the Supervisor of Banks, Bank management is required to use judgment, assessments, estimates and assumptions which impact policy implementation and amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

These estimates and assumptions are regularly reviewed, and changes to accounting estimates are recognized in the period in which these estimates were revised and in any affected future period.

C. Reclassification

Following initial application of certain accounting standards and directives by the Supervisor of Banks, as described below in section d. below, certain sections of the financial statements and comparative figures were reclassified to align them with section headings and with reporting requirements in the current period.

Reclassification of items included on the consolidated statement of profit and loss:

- Revenues included under "Profit from financing operations", amounting to NIS 18 million, and expenses amounting to NIS 25 million for the years ended December 31, 2011 and 2010, respectively, were reclassified under "Non-interest financing revenues (expenses)".
- Gain from investment in shares, net amounting to NIS 6 million, and loss amounting to NIS 1 million for the years ended December 31, 2011 and 2010, respectively, were reclassified under "Non-interest financing revenues".
- Commissions from financing business, amounting to NIS 131 million and NIS 95 million for the years ended December 31, 2011 and 2010, respectively, were reclassified under "Commissions".
- After-tax loss from extraordinary items, resulting from sale of buildings and equipment, amounting to NIS 2 million in the nine-month period ended December 31, 2011 and in all of 2010, were reclassified under "Other revenues".

Reclassification of items included on the statement of cash flows:

- Decrease in cash flow with respect to current assets (such as: deposits with banks, loans to the public, securities loaned or sold in conjunction with repurchase agreements, assets with respect to derivative instruments, securities held for trade and other assets), previously included under investment operations (previously - "activities in assets"), amounting to NIS 12,200 million and NIS 15,125 million for the years ended December 31, 2011 and 2010, respectively, were reclassified under "Current operations".

Note 1 - Reporting Principles and Accounting Policies - (continued)

Increase in cash flow with respect to current liabilities (such as: deposits from banks, deposits from the public, deposits from the Government, securities loaned or sold in conjunction with repurchase agreements, liabilities with respect to derivative instruments and other liabilities), previously included under financing operations (previously - activities in liabilities and equity), amounting to NIS 13,837 million and NIS 12,485 million for the years ended December 31, 2011 and 2010, respectively, were reclassified under "Current operations".

Reclassification of items included on notes to the financial statements:
Data in certain Notes to the financial statements were reclassified to align with new definitions, headings and presentation in the current reported period.

D. Initial application of accounting standards, accounting standard updates and directives of the Supervisor of Banks As from periods starting on January 1, 2012, the Bank applies accounting standards and directives as follows:

1. Directives included in the Supervisor of Banks' circular on the format of the statement of profit and loss for banking corporations and adoption of generally acceptable accounting practices by US banks for measurement of interest revenues.

   In accordance with the Supervisor of Banks' circular dated December 29, 2011 concerning the format of the statement of profit and loss for banking corporations and adoption of generally acceptable accounting practices by US banks for measurement of interest revenues, the Bank applies the provisions related to the presentation of the statement of profit and loss. According to these directives, the Bank has adjusted the presentation of financing profit items on the statement of profit and loss and associated Notes as follows:

   – Profit from financing operations before expenses with respect to credit loss - was divided into three individual items: interest revenues, interest expenses and non-interest financing revenues - which are presented on separate lines.
   – Items of financing profit other than interest and gain from investment in shares were classified under "Non-interest financing revenues", with a distinction between trade operations and non-trade operations.
   – The definition of "Interest" was amended to include CPI linkage differentials on interest, exchange rate differentials on interest and CPI linkage differentials on principal (this component was previously not considered part of interest).
   – The distinction between commissions from financing business, previously included under financing profit, and operating commissions, was eliminated. Consequently, all commission revenues are included under "Commissions" on the statement of profit and loss (previously - under "Operating commissions").
   – The item "Profit from extraordinary operations" was eliminated, and the approach commonly used in the USA, whereby extraordinary items are classified as "Non-ordinary" and "Non-recurring" items, was adopted. Consequently, any event would only be classified as a special (extraordinary) item on the statement of profit and loss by prior approval of the Supervisor of Banks.

Note 1 - Reporting Principles and Accounting Policies - (continued)

The Bank retroactively applies the directives on layout of the statement of profit and loss as from January 1, 2012. Initial application of this directive had no effect, other than the change in presentation.

The updates related to adoption of interest revenue measurement issues will be applied as from January 1, 2014. For details see section AA.3) below.

2. Certain International Financial Reporting Standards (IFRS) and interpretations by the International Financial Reporting Interpretations Committee (IFRIC) concerning application of these standards, as listed below:
   - IAS 7 "Statement of Cash Flows";
   - IAS 12 "Income taxes";
   - IAS 23 "Borrowing costs";
   - IAS 24 "Related party disclosures".

3. Supervisor of Banks' directives with regard to transactions between a banking corporation and their controlling shareholder and a company controlled by the banking corporation:

   According to the Supervisor of Banks' circular dated November 30, 2011 on adoption of certain IFRS standards, the Bank applies, as from January 1, 2012, US GAAP for accounting treatment of transactions between a banking corporation and their controlling shareholder and a company controlled by the banking corporation. In cases where the aforementioned rules do not refer to the accounting treatment, the Bank applies the rules prescribed by Standard 23 of the Israel Accounting Standards Board concerning accounting treatment of transactions between an entity and the controlling shareholder there of, consistently with the principles of adopting IFRS standards for non core banking issues.

   Assets and liabilities subject to a transaction with a controlling shareholder are measured at fair value as of the transaction date. Since this is an equity transaction, the Group recognizes the difference between fair value and transaction proceeds to equity.

   The amount of liability, indemnification or waiver assumed by the Bank is charged to a capital reserve.

   A loan granted to the controlling shareholder, or deposit received from the controlling shareholder, are stated on the Bank's financial statements upon initial recognition at their fair value, as an asset or liability - as the case may be. The difference between the amount of the loan granted or deposit received, and their fair value upon initial recognition, is charged to equity. In reporting periods subsequent to initial recognition, the loan or deposit are stated on the Bank's financial statements at their amortized cost, applying the effective interest method - except for cases where, in accordance with generally accepted accounting practices, they are stated at fair value.

   The Bank applies the provisions of these directives prospectively to transactions between the Bank and its controlling shareholder made after January 1, 2012, as well as to loans extended to or deposits received from the controlling shareholder prior to the start date of applying these directives - as from their start date.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Since transactions between the Bank and controlling shareholders are made at similar terms and conditions to those extended to similar clients who are not controlling shareholders - initial application of these directives has no impact on the Bank's financial statements.

4. Accounting standard update, ASU 2011-03, on reconsideration of effective control for repurchase agreements, which is an update to rules stated in FAS 166 (ASC 860).
5. Accounting standard update ASU 2011-04 on fair-value measurement (ASC 820): Amendments to achieve uniform fair value measurement and disclosure requirements in US GAAP and in IFRS.
6. Directives of the Supervisor of Banks with regard to update of disclosure of credit quality of debt and of provision for credit loss, to adopt accounting standard update ASU 2010-20 .
7. Clarifications by the Supervisor of Banks with regard to implementation of certain IFRS:
   - Functional currency of overseas affiliates.

The Group's accounting policies, as described below, incorporates the new accounting policy with regard to application of these accounting standards, accounting standard updates and directives of the Supervisor of Banks, and presents the manner and effect of initial application, if any.

E. Foreign currency and linkage:

1) Foreign currency transactions

Foreign currency transactions are translated into the functional currency of the Bank and its affiliates (NIS) using the exchange rate as of the transaction date. Monetary assets and liabilities denominated in foreign currency as of the reporting date are translated into the functional currency at the exchange rate as of that date. Exchange rate differences with respect to monetary items are the differences between the amortized cost in the functional currency as of the start of the year, adjusted for the effective interest and installments during the year, and the amortized cost in foreign currency, translated at the exchange rate as of the end of the year.

Non-monetary assets and liabilities denominated in foreign currency and measured at fair value, are translated into the functional currency using the exchange rate as of the date on which the fair value is determined. Exchange rate differences arising from translation into the functional currency are recognized on the statement of profit and loss, other than differences arising from translation into the functional currency of cash flow hedges, which are recognized on the statement of Other Comprehensive Income.

Non-monetary items denominated in foreign currency and measured at historical cost, are translated at the exchange rate as of the transaction date.

Exchange rate differences arising from translation to the functional currency are recognized on the statement of profit and loss.

Note 1 - Reporting Principles and Accounting Policies - (continued)

2) Overseas banking affiliates

According to directives by the Supervisor of Banks prior to adoption of IFRS, an overseas banking affiliate of a banking corporation was classified as a foreign operation whose functional currency is the same as that of the banking corporation.

Pursuant to IAS 21 and to the Supervisor of Banks' circular on this matter, dated February 14, 2012, in order to determine the functional currency, the banking corporation is required to consider, inter alia, the following:

- The currency which primarily affects the selling price of goods and services (usually this would be the currency in which selling prices of goods and services are denominated and settled), and the currency of the country whose competitive forces and regulation primarily determine the selling prices of goods and services.
- The currency which primarily affects labor costs, material and other costs for delivery of goods or services (usually, this would be the currency in which these costs are denominated and settled).
- Other factors which may serve as evidence of the entity's functional currency, such as: The currency in which monetary resources are generated by financing operations, and the currency in which receipts from current operations are usually kept.
- Relations of the affiliate with the Bank - is the foreign operation significantly independent, do transactions between the affiliate and the Bank constitute a large or small percentage of the foreign operation, do cash flows from the foreign operation directly affect the cash flows of the Bank and are readily available to be transferred to it, and are cash flows from the foreign operation sufficient to fund its current and anticipated liabilities in the normal course of business of the entity, without resources being provided by the Bank.
- Affiliate clients were recruited independently by the affiliate, and its operations with Bank clients (not recruited by the affiliate) is not significant.
- Affiliate operations with the Bank, such as asset and liability balances or revenues and expenses, are not significant.
- Affiliate operations are essentially independent, stand alone and are not an extension of or complementary to the Group's domestic operations. Furthermore, the affiliate conducts its operations with significant autonomy.

Based on review of these criteria, the Bank continues to treat its overseas banking affiliates as foreign operations whose functional currency is the same as the Bank's.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Below is information about official exchange rates, the Consumer Price Index and changes there to:

	As of December 31			Change in %		
	2012	2011	2010	2012	2011	2010
Consumer Price Index:						
CPI for December (points)	105.7	104.0	101.8	1.6	2.2	2.7
Known CPI for November (points)	105.5	104.0	101.4	1.4	2.6	2.3
Exchange rate of:						
USD (in NIS)	3.733	3.821	3.549	(2.3)	7.7	(6.0)
EUR (in NIS)	4.921	4.938	4.738	(0.4)	4.2	(12.9)

F. Consolidation basis

1) Subsidiaries

Financial statements of subsidiaries are included on the consolidated financial statements from the date control is achieved and through the date control is terminated. Control is the power to determine financial and operational policy of an entity to achieve benefits from operations there of. The Bank exercises judgment in determining the acquisition date and whether or not control has been achieved.

Accounting policies of subsidiaries was modified as needed, to align them with the accounting policies adopted by the Group.

2) Attribution of Profit and of Other Comprehensive Income items among shareholders

Profit or loss and any Other Comprehensive Income item is attributed to the controlling shareholder of the Bank and to non-controlling interest. Total profit, loss and Other Comprehensive Income are attributed to the controlling shareholder of the Bank and to non-controlling interest, even if this results in a negative balance of non-controlling interest.

3) Investments in affiliates

When testing the existence of material influence, there is an assumption that controling between 20% to 50% in investees grant material influence in an investment.

Pursuant to IAS 28, Investment in associates is accounted for using the equity method and is initially recognized at cost. The investment cost includes transaction costs.

The consolidated financial statements include the Group's share of income and expenses, profit or loss and Other Comprehensive Income of investees accounted for using the equity method, after required adjustments to the accounting policies of the associate to align it with that of the Group, as from the date on which material influence or joint control exists until such material influence or joint control ceases to exist.

The Bank does not make adjustments to accounting policies with regard to core banking business issues (issues where IFRS are yet to be adopted by the Public Reporting Regulations) applied by a non-banking associate.Which is reported pursuant to the International Financial Reporting Standards.

When the Group's share of loss exceeds the value of Group interest in an entity accounted for using the equity method, the carrying amount of these rights (including any long-term investment) is fully amortized, and the Group recognizes no further loss, unless the Group is committed to support the investee, or if the Group has paid any amounts in consideration there for.

Note 1 - Reporting Principles and Accounting Policies - (continued)

4) Inter-company transactions

Mutual balances within the Group and unrealized revenues and expenses arising from inter-company transactions have been cancelled in the course of preparing the consolidated financial statements. Unrealized gain from transactions with associates and joint ventures have been cancelled against the investment, in accordance with Group rights in these investments. Unrealized losses haves been cancelled in the same manner as cancellation of unrealized gains, provided there was no evidence of impairment.

5) Business combinations

The Bank applies the acquisition method to all business combinations.

The acquisition date is the date on which the acquiring entity achieves control over the acquired entity. Control is the power to determine financial and operational policy of an entity to achieve benefits from its operations. When testing for existence of control, immediately realizable potential voting rights are taken into account. The Bank exercises judgment in determining the acquisition date and whether or not control has been achieved.

Pursuant to directives of the Supervisor of Banks, the Bank has elected to apply the standard prospectively to financial statements for periods starting on January 1, 2011, so that no reattribution of excess cost was made for acquisitions prior to application of the standard. Amortization of goodwill with respect to investments made prior to application of the standard were discontinued, and in lieu, the need for making a provision for impairment of other-than-temporary nature is periodically reviewed.

For acquisitions made after January 1, 2011, the Bank would recognize goodwill as of the acquisition date at fair value of the consideration, including amounts with respect to any non-controlling interest in the acquired entity, and the fair value as of the acquisition date of equity interest in the acquired entity previously held by the Bank, less the net amount attributed upon acquisition to identifiable assets acquired and liabilities assumed.

The Bank recognizes upon acquisition a contingent liability assumed upon business combination, if there is a present obligation due to past events, and its fair value may be reliably measured.

G. Set-off of financial instruments

Financial assets and liabilities are set off when there is an enforceable legal right of set-off between them and intent to set-off the amounts on the maturity dates. Assets and liabilities with two different counter-parties will only be set off subject to an additional condition: existence of an agreement between the three parties which clearly stipulates the Bank's set-off rights with regard to said liabilities. Accordingly, designated deposits for which repayment to the depositor is contingent upon the collection of the loan (when the Bank Group is not at risk of credit loss) were set off against the loans issued out of these deposits. The interest margins from this activity are presented in the statement of profit and loss under “commissions”.

Note 1 - Reporting Principles and Accounting Policies - (continued)

H. Statement of cash flows

The statement of cash flows is presented classified under cash flows from current operations, from investment operations (previously - activities in assets) and from financing operations (previously - activities in liabilities and equity). Cash flows from major Bank operations are classified under current operations. Cash and cash equivalents includes cash, deposits with banks, negotiable deposit notes and deposits with central banks with an original term of up to three months.

The Bank retroactively applies the rules prescribed by IAS 7 as from January 1, 2012. Initial application of the standard did not impact the Bank's financial statements, other than the change in presentation.

I. Securities

1) Investments in securities were classified into three categories, as follows:

a) Debentures held to maturity - debentures that the Bank has the intention and ability to hold until maturity date. These debentures are presented by their amortized cost their nominal value plus accrued interest and linkage or exchange rate differentials, plus or minus the discount or premium component generated upon acquisition and not yet amortized. Income from bonds held to maturity is recorded to the statement of profit and loss on the accrual basis.

b) Securities held for trade - securities acquired or held in order to be sold in the near term, or securities which the Bank has elected to measure at fair value through profit & loss using the fair value alternative, except for shares for which no fair value is available. These securities are included in the balance sheet at their fair value on the reporting date. Unrealized gains or losses from the adjustment to fair value are charged to the statement of profit and loss.

c) Securities available for sale – securities not classified under the two preceding categories. Securities available for sale are presented on the balance sheet at fair value. Shares having no available fair value, including shares of credit card company received in conjunction with a long-term contractual agreement, are presented at fair value as of the date they were received – which does not exceed their cost – and net of provision for impairment which is not of a temporary nature, which is charged to the statement of profit and loss. Unrealized profit or loss from fair value adjustment is not included on the statement of profit and loss, and are recognized - net of tax reserve - on the statement of changes in shareholders' equity under Adjustments for Presentation of Available-for-Sale Securities at Fair Value, under Other Comprehensive Income - pending the realization there of. Exchange rate differences, interest and dividend income is recognized on the statement of profit and loss. Dividends received from an investment in shares available for sale, originating in the profits of the distributing company after the acquisition date, were charged to the statement of profit and loss.

For securities which include embedded derivatives – see section S.3) below.

Note 1 - Reporting Principles and Accounting Policies - (continued)

When a security is other than temporarily impaired, its cost is written down to its fair value and serves as the new cost basis. The accumulated loss related to an available-for-sale security, previously charged to a separate item under shareholders' equity under Other Comprehensive Income, is transferred to the Statement of Profit and Loss when its impairment is other than of a temporary nature. Appreciation in subsequent reported periods are charged to a separate item under shareholders' equity under Accumulated Other Comprehensive Income, and are not recognized on the Statement of Profit and Loss (using the new cost basis). For details of determination of fair value and provision for impairment, see sections 4) and 5) below.

2) Bank investments in venture capital funds and other investment funds are stated at cost net of any other-than-temporary impairment loss. Gain from venture capital investments are recognized on the Statement of Profit and Loss upon realization of the investment. Dividends received from Bank investments in these funds are charged to profit & loss when the Bank has the right to receive them, up to the amount of accumulated gain since this investment was acquired.

3) The cost of realized securities is calculated on FIFO basis, except for securities acquired as part of a hedge, or in conjunction with creating a strategic position or for any other specific purpose, which is separately identified.

4) With regard to calculation of fair value, see section T. below.

5) Impairment:

Pursuant to directives and guidelines of the Supervisor of Banks, the Bank periodically reviews whether impairment of the fair value of securities classified under the available-for-sale portfolio or the held-to-maturity portfolio, below its cost, is of an other-than-temporary nature. To this end, the following indicators, inter alia, are reviewed:

- Intent and capacity of the Bank to hold the securities for a sufficient period which would allow the security to recover its original cost.
- The value of collateral which guarantees the security.
- The time period during which the value of the security was lower than its cost.
- The ratio of impairment to total cost.
- Adverse change in the issuer status or in the stock situation
- Review of conditions reflecting the financial standing of the issuer, including whether or not the impairment is due to individual reasons related to the issuer, or to any macro-economic conditions.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Furthermore, in any of the following situations, the Bank recognizes an other-than-temporary impairment:

- The security was sold prior to publication of the financial statements for that period.
- The Bank intends, as of the publication of the financial statements for that period, to sell the security within a short time.
- Debenture is significantly impaired between its rating upon acquisition by the Bank and its rating upon publication of the financial statements for said period.
- Debenture classified by the Bank as troubled after its acquisition.
- Debenture which is in payment default after its acquisition.
- Security where, in general, its fair value as of the end of the reported period and soon prior to publication of the financial statements, is significantly lower than its cost (amortized cost), or where any payment failure has occurred after the acquisition there of, unless proven with a high degree of confidence and based on objective evidence, that the impairment is merely of a temporary nature.

If the impairment of fair value is deemed to be other-than-temporary in nature, the cost of the security is written-off to its fair value, such that any loss amounts accrued in equity under Other Comprehensive Income, would be classified upon impairment to the statement of profit and loss. This value would serve as the new cost basis, and would not be revised even if in subsequent reporting periods (after recognizing the impairment) the fair value should increase.

Subsequently to impairment recognition any interest revenues from investments in securities which are debt instruments would generally be recognized on accrual basis, based on the difference between expected cash flows of the debt instrument and the fair value of the instrument upon impairment (new cost basis).

J. Impaired debt, credit risk and provision for credit loss

1) Pursuant to the Supervisor of Banks' directive on measurement and disclosure of impaired debt, credit risk and provision for credit loss, the Bank applies as from January 1, 2011 the rules stipulated by codification of US accounting standards ASC 310 and the opinion of the US banking supervision authorities and of the US SEC, as adopted in the Public Reporting Regulations. Moreover, as from the aforementioned date, the Bank applies the Supervisor of Banks' directive with regard to treatment of troubled debt. Moreover, as from the 2012 financial statements, the Bank applies the Supervisor of Banks' directive with regard to updated disclosure of credit quality of debt and of provision for credit loss.

2) Loans to the public and other debt balances

The directive is applied to all debt balances, including deposits with banks, debentures, securities borrowed or purchased in repurchase agreements, loans to the public, loans to the government etc. Loans to the public and other debt balances for which no specific rules on measurement of provision for credit loss were specified in the Public Reporting Regulations (such as: loans to the government, deposits with banks etc.) are reported on the Bank's accounts at their recorded debt balance. The recorded debt balance is defined as the debt balance after accounting write-offs but before deduction of the provision for credit loss for that debt. The recorded debt balance does not include any accrued interest not recognized, or previously recognized and then reversed.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Note that prior to January 1, 2011, the Bank applied different rules. Therefore, debt balances presented in periods preceding the initial implementation period are not comparable with debt balances reported after the implementation. As for other debt balances for which specific rules on measurement and recognition of provision for credit loss exist (such as: debentures), the Bank continues to apply the same measurement rules.

3) Identification and classification of impaired debt

Debt is classified as impaired when, based on current information and events, it is expected that the Bank would be unable to collect all amounts due pursuant to contractual terms of the debt contract. In any case, debt is classified as impaired when its principal or interest is in arrears over 90 days, unless the debt is well secured and is in collection proceedings. Further, any debt whose terms and conditions have been changed in conjunction with restructuring of troubled debt would be classified as impaired debt, unless prior to and following such restructuring, a provision for credit loss by extent of arrears was made with respect to the debt pursuant to the appendix to Proper Conduct of Banking Business Regulation 314 on troubled debt in housing loans at mortgage banks.

Restructing of troubled debt - Debt which has been formally restructured as troubled debt is defined as debt for which, for economic or legal reasons related to financial difficulties of the debtor, the Bank has made a concession by way of modification to terms and conditions of the debt, designed to make it easier for the debtor to make cash payments in the near term (reduction or postponement of cash payments due from the debtor), or by way of receiving other assets as debt repayment (in whole or in part).
In order to determine whether debt restructuring by the Bank constitutes troubled debt restructuring, the Bank conducts a qualitative review of all restructuring terms and circumstances in order to determine whether the debtor is in financial duress and whether: (1) the creditor is in financial duress; and (2) the Bank made a concession to the debtor in conjunction with the restructuring.
In order to determine whether the creditor is in financial duress, the Bank reviews for indications of the creditor being in financial duress at the time of restructuring, or for reasonable likelihood that the creditor would be in financial duress if not for the restructuring. Inter alia, the Bank reviews the existence of one or more of the following circumstances: As of the debt restructuring date, the borrower is in default, including when any other debt of the borrower is in default; for debt which, as of the restructuring date, is not in arrears, the Bank assesses whether, based on the current repayment capacity, it is likely that in the foreseeable future the borrower would be in default and would fail to comply with original contractual conditions of the debt; the creditor has declared bankruptcy, is in Receivership or there is significant doubt as to the borrower continuing as a going concern; and without changes to debt terms, the debtor would not be able to raise funds from other sources at market interest typical for debtors not in default.

Note 1 - Reporting Principles and Accounting Policies - (continued)

The Bank concludes that a concession was made to the creditor in conjunction with the restructuring, even if the contractual interest rate was increased in the restructuring - if one or more of the following exists: Due to the restructuring, the Bank does not expect to collect all debt amounts (including accrued interest pursuant to contractual terms); the current fair value of collateral, for debt contingent on collateral, does not cover the contractual debt balance and indicates inability to collect all debt amounts; the creditor is unable to raise funds at market rates for debt with similar terms and conditions to those of the restructured debt.

The Bank does not classify debt as restructured troubled debt, if in conjunction with the restructuring, it granted to the creditor a delay in payments which is not material considering the payment frequency, the contractual term to maturity and the expected effective maturity of the original debt. For this matter, if multiple restructurings took place involving changes to debt terms, the Bank accounts for the accumulated effect of previous restructurings in order to determine whether the delay in payments is not material.

Restructured debt, including debt assessed on group basis prior to restructuring, shall be classified as impaired debt and shall be individually assessed for making a provision for credit loss or accounting write-off. Since the debt being restructured would not be repaid as per its original contractual terms, the debt continues to be classified as impaired debt even after the debtor resumes repayments pursuant to the new terms and conditions.

Reinstatement of impaired debt to non-impaired status - impaired debt is reclassified as non-impaired debt upon one of these conditions occurring:

- It includes no principal or interest components which are past due, and the Bank anticipates payment of the outstanding principal and interest in full according to contractual terms (includes amounts subject to accounting write-off or provision).
- When the debtor has become well-secured and is in collection proceedings.

Reinstatement of impaired debt to impaired and accruing status - debt which has been formally restructured, such that after restructuring all of the following conditions are fulfilled::

- There is reasonable certainty that the debt would be repaid and will perform according to its new terms and conditions, based on a current, well-documented credit evaluation of the debtor's financial situation and repayment schedule according to its new terms and conditions.
- The debtor has made cash and cash equivalent payments over a reasonable period of at least six months for loans repaid (principal and interest) by monthly installments, or has repaid 20% of the re-structured debt for loans with longer repayment schedules.
- The loan, after restructuring, is not in arrears of 90 days or more.

Note 1 - Reporting Principles and Accounting Policies - (continued)

4) Provision for credit loss

The Bank has put in place procedures for classification of credit and for measurement of provision for credit loss, in order to maintain an appropriate provision to cover expected credit loss with regard to the Bank's loan portfolio. Further, the Bank has put in place procedures required to maintain, as a separate liability account, an appropriate provision to cover expected credit loss with regard to off-balance sheet credit instruments (such as: commitment to provide credit, un-utilized credit facilities and guarantees).

The required provision to cover expected credit losses from the credit portfolio is estimated under one of the following tracks: "individual provision" or "group provision". Further, the Bank reviews the overall appropriateness of the provision for credit loss.

An individual provision for credit loss is applied for any debts determined to be impaired, whose contractual balance (including accounting write-offs, unrecognized interest, provisions for credit losses and collateral) is NIS 700 thousand or higher.

For other debt, the Bank may decide whether to make an individual assessment. The individual provision for credit loss is estimated based on expected future cash flows, discounted using the effective interest rate of the original debt. Where debt collection is contingent upon collateral, or if the Bank determines that an asset is expected to be seized, the individual provision for credit loss is estimated based on fair value of the collateral securing said credit. For this matter, the Bank defines debt as debt contingent upon collateral, when it is expected to be entirely repaid by pledged collateral, or when the Bank expects repayment from an asset even with no specific pledge on such asset, provided that the borrower has no other reliable sources available for repayment.

The Bank regularly reviews the forecasted expected credit loss, based on actual cash flows, and adjusts the individual provision to the current forecast. The actuall individual provision loss can be different from the original estimates.

Group provision for credit loss - is applied for large, homogeneous groups of small debts (whose balance is below NIS 700 thousand, as determined by the Bank) (such as: credit card debts, housing loans and consumer debts repaid by installments) as well as for large, non-impaired debts. The provision for credit losses from debts based on group estimate, except for loans for which a specific minimum provision by extent of arrears has been calculated as per directives of the Supervisor of Banks, is calculated based on rules stipulated in USA Accounting Standard FAS 5: "Accounting for Contingencies" (hereinafter "FAS 5"), based on a formula prescribed in the interim directive issued by the Supervisor of Banks, in effect through December 31, 2012. This formula is based on past loss rates by economic sector, as well as rates of on net accounting write-offs actually recognized as from January 1, 2011. In addition to calculating the range of historic loss rates for various economic sectors, as per the above, for determining the appropriate rate of provision, the Bank also accounts for other data, including trends in credit volume for each sector as well as sector condition, macro-economic data and general quality assessment of credit to each economic sector.

Note 1 - Reporting Principles and Accounting Policies - (continued)

For large debt, the actual write-off rate is doubled, so that the estimated group provision is higher than actual write-offs made in the following year. The Bank carefully reviews the level of group provision compared to actual write-offs.

Pursuant to provisions determined by the interim directive, as from January 1, 2011 the Bank does not maintain general and supplementary provisions, but continued to calculate the supplementary provision and to verify that in any case, the amount of group provision at the end of each reporting period shall be no less than the sum of general and supplementary provisions which would have been calculated as of the same date, gross of tax.

The required provision with regard to off-balance sheet credit instruments is assessed as per rules stipulated in FAS 5. The provision estimated on group basis for off-balance sheet credit instruments is based on provision rates specified for on-balance sheet credit (as stated above), accounting for expected credit realization rate for the off-balance sheet credit risk. The credit realization rate is calculated by the Bank based on credit conversion factors, as stipulated in Proper Conduct of Banking Business Regulation 203 "Measurement and capital adequacy - Credit risk - Standard approach".

A minimum provision with respect to housing loans is calculated based on the formula stipulated by the Supervisor of Banks, by extent of arrears, so that the provision rate is higher the longer the arrears. Upon the start date of application of the new directive, the amendment to appendix to Proper Conduct of Banking Business Regulation 314 "Troubled debt in housing loans at mortgage banks" became effective, expanding the scope of calculation of provision by extent of arrears to all housing loans, other than loans not repaid by periodic installments and loans used to finance activity of a business nature.

In addition, the Bank records a group provision for housing loans as well, except for provision by extent of arrears. The Bank has put in place a methodology for calculating the group provision with respect to housing loans, whereby the provision amount is derived from the increase in current credit grant volume compared to past periods. The amendment is applied prospectively starting with financial statements for periods starting on January 1, 2011.

The Bank classifies all troubled debt and troubled off-balance sheet credit items under: special supervision, inferior or impaired. Debt under special supervision is debt with potential weaknesses, which require special attention by Bank management. Should these weaknesses not be addressed, the likelihood of debt repayment may deteriorate. Inferior debt is debt insufficiently secured by collateral or by debtor repayment capacity, and for which the Bank may incur a loss if faults are not corrected, including debt over NIS 700 thousand which is 60-89 days in arrears. Impaired debt is debt which the Bank anticipates not being able to collect all amounts due pursuant to the debt contract, including debt in arrears 90 days or more.

Note 1 - Reporting Principles and Accounting Policies - (continued)

5) Revenue recognition

Upon classification of debt as impaired, the Bank classifies the debt as non-accruing debt and discontinues accrual of relevant interest revenues, except as stated above for certain restructured debt. Further, upon classification of debt as impaired, the Bank reverses all accrued and uncollected interest revenues recognized as income on profit and loss. The debt continues to be classified as non-accruing debt for as long as it is classified as impaired debt. For further information about revenue recognition on the cash basis with respect to debt classified as impaired, see section u.1)a) below.

For debt reviewed and provided for on group basis, the Bank discontinues accrual of interest revenues when conditions for accounting write-off of the debt are fulfilled, usually after 150 days in arrears, unless the debt is well-secured and in collection proceedings. Such debt is subject to assessment of provision for credit loss, which ensures that Bank profit is not skewed upwards. Commissions for delinquency of such debt is included as income when the Bank has the right to receive them from the client, provided that collection is reasonably secured.

6) Accounting write-off

The Bank makes accounting write-offs of any debt, or part there of, individually assessed as not collectible and of low value, so that maintaining it as an asset is not justified, or any debt which is subject to long-term collection effort by the Bank (typically defined as terms in excess of two years). For debt assessed on a group basis, write-off rules have been put in place based on extent of arrears (mostly - over 150 consecutive days in arrears) and on other problem parameters. Note that accounting write-offs do not involve any legal concession, and merely reduce the debt balance reported for accounting purposes, while creating a new cost basis for the debt on Bank accounts.

7) Policy on provision for doubtful debts prior to application of directives on impaired debt, credit risk and provision for credit losses.

Prior to January 1, 2011, the provision for doubtful debts was specifically determined, and a general provision and supplementary provision were also included, as per directives of the Supervisor of Banks.

The specific provision for doubtful debts was made based on careful assessment by management of any loss inherent in the loan portfolio, including liabilities under off-balance sheet items. In this assessment, management accounted for, inter alia, the degree of risk associated with financial robustness of borrowers, based on information available to it with regard to their financial position, business operations, compliance with obligations and evaluation of relevant collateral received. interest revenues received with respect to debt classified as doubtful is not recognized as from the start of the quarter in which the debt was classified as doubtful. Upon collection of interest, interest revenues were recorded to Other Financing Revenues.

A specific provision with respect to housing loans originated by the Bank and banking investees in Israel, was calculated according to directives of the Supervisor of Banks, considering the extent of arrears, with larger provision percentage as the arrears are longer.

Note 1 - Reporting Principles and Accounting Policies - (continued)

The supplementary provision for doubtful debts is based on the quality of client indebtedness portfolio, based on risk attributes as defined in directives of the Supervisor of Banks. The supplementary provision for doubtful debts is calculated using percentages specified for each of these risk attributes. The general provision is in amounts adjusted for the end of 2004, an amount which constituted 1% of total indebtedness under responsibility of the Bank and banking investees as of December 31, 1991.

Bad debts are written off whent the Bank concludes the debt is uncollectable, following legal proceedings conducted or agreements reached, usually when no legal proceedings took place, and the debt is uncollectable, or for other causes whereby the debt is uncollectable.

8) Effect of initial application of the Supervisor of Banks' directives with regard to updated disclosure of credit quality of debt and of provision for credit loss, to adopt accounting standard update ASU 2010-20.

On March 25, 2012, the Supervisor of Banks issued a directive with regard to update of disclosure of credit quality of debt and of provision for credit loss, to adopt accounting standard update ASU 2010-20, which stipulates wider disclosure of debt balances, movement in balance of provision for credit loss, any material acquisition and sale of debt during the reported period and disclosures with regard to credit quality.

Inter alia, banking corporations are required to provide quantitative disclosure of indicated credit quality, at least for the troubled debt balance in each debt group. Disclosure of credit quality of housing loans are also to be included. The new disclosure is required for each credit segment (such as: commercial credit, individuals – housing loans, individuals – other, banks and governments) and for each major debt group, as defined in the directive, with distinction between borrower activity in Israel and overseas, if this is material.

The Bank applies the directives prospectively as from the 2012 financial statements for balance sheet data first required pursuant to this directive, with reclassification of comparative figures in as much as possible. Note that in financial statements for 2012, no new disclosure was required with regard to restructuring of troubled debt. All other disclosures required pursuant to this directive will be applied as from financial statements for March 31, 2013. Initial application of the directive had no effect on the Bank's financial statements, other than a change in presentation.

K. Transfer and service of financial assets and discharge of liabilities

The Bank applies measurement and disclosure rules specified in US Accounting Standard FAS 140 (ASC 860-10), "Transfer and service of financial assets and discharge of liabilities", as amended by FAS 166, "Transfer and service of financial assets" (ASC 860-10), for handling the transfer of financial assets and discharge of liabilities.

Under these rules, the accounting treatment of transfer of a financial asset would only be deemed a sale if all of these conditions are fulfilled: (1) the transferred financial asset was separated from the transferring entity, even in case of bankruptcy or other form of Receivership; (2) any recipient (or, if the recipient is an entity designed to engage in securitization or asset-backed financing operations, and that entity is prohibited from pledging or exchanging the financial assets it received - any third party holding beneficiary interests) may pledge or replace the assets (or the beneficiary interests) received, and there is no condition which limits the recipient (or third party holding beneficiary interests) from exercising their right to pledge or exchange, and grants the transferror a non-trivial benefit; (3) the transferror, or subsidiaries consolidated on the financial statements there of, or agents there of, do not retain effective control over the financial assets or beneficiary interests related to these transferred assets.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Moreover, for the transfer of part of a financial asset to be considered a sale, the transferred part must fulfill the definition of participatory interests.

Participatory interests must fulfill the following criteria: the interest should represent an interest proportionate to the complete financial asset; all cash flows received from the assets are divided among the participatory interests pro-rata to their ownership stake; interests are not subordinated to other interests; there is no recourse to the transferror or to other holders of participatory interests (other than in case of breach of representation or obligation, current contractual obligations to service the financial asset as a whole and management of the transfer contract, and contractual obligations to share in offset of any benefits received by any holder of participatory interests); and the transferror and the holder of participatory interests have no right to pledge or replace the financial asset in whole, unless all holders of participatory interests agree to pledge or replace the financial asset in whole.

If the transaction fulfills the conditions for treating it as a sale, the transferred financial assets are removed from the Bank's balance sheet. If the sale conditions are not fulfilled, the transfer is treated as secured debt. Sale of part of a financial asset, other than a participatory interest, is treated as secured debt - that is, the transferred assets remain on the Bank's balance sheet and proceeds from the sale are recognized as a Bank liability.

The Bank applies specific provisions stipulated in Public Reporting Regulations for handling transactions to borrow or loan securities, in which lending is made against the borrower's general credit and collateral quality, where the borrower does not provide as collateral for the lender any liquid instruments specifically related to the securities loan transaction, which the lender may sell or pledge.

Such loaning and borrowing are treated as credit or deposit, measured at fair value of the related security.

As from January 1, 2012, the Bank applies Accounting Standard Update ASU 2011-03, on reconsideration of effective control for repurchase agreements, which is an update to rules stated in FAS 166 (ASC 860).

Evaluation of existence of effective control is focused on contractual rights and contractual obligations of the transferor, and therefore does not take into consideration the criterion requiring that the transferor would be capable of acquiring transferred securities even in case of default by the transferee, and does not take into consideration directives with regard to required collateral with respect to that criterion.

In transactions involving transfer of financial assets, the Bank determines that the transferor maintains effective control over transferred assets (and therefore the asset transfer shall be accounted for as secured debt) if all of the following conditions are fulfilled:

- The assets repurchased or redeemed are identical or essentially identical to the transferred assets;
- The agreement is to repurchase or redeem them prior to maturity, at a fixed or fixable price; and
- The agreement is made simultaneously with the transfer.

The Bank prospectively applies the rules stipulated in ASU 2011-03, as from January 1, 2012. Upon the transition date, there was no impact on the Bank's financial statements.

Note 1 - Reporting Principles and Accounting Policies - (continued)

L. Buildings and equipment

This item includes investments by the Bank in fixed assets (including payments on account), assets leased by the Bank under a financing lease, and cost of software for its own use, recognized as an asset.

Fixed assets:

a) A fixed asset is a tangible item held for use in production or delivery of goods or services, for renting to others or for administrative needs, which is expected to be used for more than one period.

b) Fixed assets are initially recognized at cost, including cost directly attributable to acquisition of the fixed asset and to bringing it to the location and state required for their operation.

Cost of software for the Bank's own use, incurred during the development phase, are presented under "Buildings and equipment" if the following conditions are fulfilled:

a) Technical feasibility is provable with regard to completion of the software so as to be available for use.

b) The Bank intends to complete development and use the software.

c) The Bank is able to use the software.

d) The Bank can prove the manner in which the software would produce the expected economic benefits.

e) There are technical, financial and other resources available for completing development and use of the software.

The initial recognition, as described above, is based on costs directly attributable to and required for software development, to be used in the manner intended by the Bank.

c) In periods subsequent to initial recognition, fixed assets are stated at cost net of accumulated depreciation and net of any accumulated impairment loss.

d) Depreciation and depreciation method:

1) According to the component method, the Bank depreciates separately any component of a fixed asset whose cost is significant relative to the total item cost. Depreciation expense for each period is recognized on the statement of profit and loss.

2) The depreciable amount of the fixed asset item is methodically allocated across its useful life. The depreciation method used reflects the expected pattern of consumption of future economic benefits from the asset. For additional details, see Note 7.A.

3) The Bank reviews the residual value, the useful life of the fixed asset and the depreciation method used - at least at the end of each fiscal year. Any changes required are treated as changes in accounting estimate.

e) Current maintenance cost for an item is recognized in the statement of profit and loss when incurred.

f) As for impairment, see Note 1.O. below.

g) The carrying amount of a fixed asset item is derecognized upon realization, or when no future economic benefits are expected from use or realization therfe of. The difference between net proceeds from realization, if any, and the carrying amount of the derecognized asset, is recognized on the statement of profit and loss under "After-tax profit from extraordinary operations".

Note 1 - Reporting Principles and Accounting Policies - (continued)

M. Intangible assets and goodwill

This item includes goodwill and will include any intangible assets acquired separately or as part of a business combination, intangible assets developed by the Bank (other than development cost of software for own use, included under "Buildings and equipment") and service assets.

Goodwill is not systematically depreciated. As for impairment of intangible assets, see Note 1.O. below.

N. Leases

Leases, including land leases from the Israel Land Administration ("ILA") or from third parties, where the Bank essentially bears all risk and reward associated with the property, are classified as financing leases. Upon initial recognition, leased assets are measured at their fair value or the present value of the minimum future leasing fee, whichever is lower. Future payments for exercising an option to extend the lease term with the Israel Land Administration are not recognized as part of the asset and the related liability since they constitute contingent lease fees, derived from the fair value of the land upon future renewal dates of the lease Subsequent to initial recognition, the asset is treated as per the accounting policy applicable for such asset. Other leases are classified as operating leases, and the leased assets are not recognized on the Bank's balance sheet.

Prepaid leasing fee paid to the ILA with respect to land leases classified as operating leases are presented on the balance sheet as prepaid expenses, and are recognized on the statement of profit and loss over the lease term. The lease term and amortization amounts account for any option to extend the lease term, if upon contracting the lease it was reasonably certain that the option would be exercised.

In a lease of land and buildings, the land and building components are individually reviewed for the purpose of classifying such leases; the key consideration in classification of the land component is the fact that land typically has an unspecified useful life.

Payments for an operating lease are charged to the statement of profit and loss using the straight line method over the lease term. Lease incentives received are recognized as an integral part of all lease expenses using the straight line method over the lease term.

Minimum leasing fees payable for a financing lease are divided into financing expenses and reduction of the liability balance. Financing expenses are allocated for all periods in the lease term, so as to obtain a fixed periodic interest rate for the outstanding liability balance. Minimum leasing fees with respect to contingent leasing fees are updated when the contingency is resolved.

O. Impairment of non-financial assets

1) General

Upon each balance sheet date, a review is made for indications of impairment of various assets within the scope of IAS 36. For some assets, the review for impairment is annual if there are no indications of impairment, namely:

a) Intangible asset not yet ready for use;

b) Assets with unspecified useful life; and

c) Goodwill acquired upon business combination.

Note 1 - Reporting Principles and Accounting Policies - (continued)

For review of impairment, the Bank estimates the recoverable amount of the asset or of the cash-generating unit. The recoverable amount is the higher of the fair value net of selling cost of the asset (or cash-generating unit) or its value in use. Value in use is the present value of future cash flows expected from an asset or cash-generating unit.

Should the recoverable amount be lower than the carrying amount for the asset, the Bank recognizes an impairment loss and writes down the asset on its books to its recoverable amount. Impairment loss is immediately recognized on the statement of profit and loss.

If it is not possible to estimate the recoverable amount of an individual asset, the Bank calculates the recoverable amount of the cash-generating unit to which the asset belongs.

For review of impairment, goodwill acquired in a business combination is allocated, as from the acquisition date, to each of the cash-generating units expected to benefit from the synergy of the business combination.

The Bank recognizes an impairment loss for a cash-generating unit when the unit's recoverable amount is lower than its carrying amount. In such case, the Bank allocates the impairment loss to reducing the value of unit assets, first against goodwill allocated to the unit and then to all assets pro-rata to their carrying amounts (subject to their recoverable amount). Such loss is immediately recognized on the statement of profit and loss.

The Bank estimates, at the end of each reported period, if there are indications that any impairment loss for the asset, except for goodwill, recognized in previous periods, no longer exists or is reduced. When such indications exist, the Bank calculates the recoverable amount of the asset. Impairment loss for an asset, except for goodwill, is only reversed in case of changes to estimates used to determine the recoverable amount of the asset, since the date on which impairment loss was most recently recognized. The carrying amount of an asset, except for goodwill, which increased due to reversal of an impairment loss, shall not exceed the carrying amount assigned (net of depreciation or amortization), had no impairment loss been recognized in previous periods. Reversal of an impairment loss for an asset, except for goodwill, is immediately recognized on the statement of profit and loss. Reversal of impairment loss for a cash-generating unit is allocated to unit assets, except goodwill, pro-rata to their carrying amounts. Due to reversal, the carrying amount of an asset shall not exceed the lower of its recoverable amount or its carrying amount if no impairment loss had been recognized. Impairment loss with respect to goodwill is not reversed.

2) In addition, when reviewing for impairment of capitalized development cost of software for own use, the Bank also applies the following criteria:

a) Use of the software is not expected to provide significant potential service;
b) Significant change has been or is expected to be made to the software; and
c) The cost of software development significantly exceeds the amount budgeted by the entity for such development.

Moreover, if development of the software is not expected to be completed, based on certain indications (such as programming challenges which may not be resolved within a reasonable time), the Bank writes off the entire carrying amount of software development.

Note 1 - Reporting Principles and Accounting Policies - (continued)

3) Impairment of investment in affiliates:

Impairment of investment in an affiliate is reviewed when evidence indicates potential impairment of the investment, as stated in sections 58-70 of IAS 39 "Financial Instruments: Recognition and Measurement". In addition, the Bank reviews the indications listed in resolution 4-1 of the Israeli Securities Authority "Guidelines for review of need to write down permanent investments". Impairment is measured pursuant to provisions of IAS 36, by comparing the recoverable amount of the investment to its carrying amount. When determining the value in use of the investment, the Bank estimates its share of the present value of estimated future cash flows to be produced by the affiliate, or alternatively, the present value of estimated future cash flows expected from dividends received from this investment and from its final realization. Any impairment loss incurred is allocated to the investment as a whole.

In subsequent reporting periods after the period in which the Bank was first required to record a provision for impairment, the investment in an affiliate would be stated at the lower of the recoverable amount and the carrying amount using the equity method. The recoverable amount is calculated in each reported period in which indications exist of change in the recoverable amount. If, at a later date, the recoverable amount should increase, the recognized impairment would be reversed.

P. Contingent liabilities

The financial statements include appropriate provisions to cover possible damage, where, in the estimation of the Bank's management, based on the opinion of its legal counsel, a provision is required.

In accordance with the directives of the Supervisor of Banks, claims have been classified according to the range of probability of realization of the risk exposure, as follows:

1) Probable risk: there is a probability of more than 70% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Probable, an appropriate provision was made in the financial statements.

2) Reasonably Possible risk: there is a probability of between 20% and 70% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Reasonably Possible, an appropriate provision is sometimes made on the financial statements, at the discretion of Bank management and based on the opinion of legal counsel.

3) Remote risk: there is a probability of less than 20% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Remote, no provision was made in the financial statements.

See Note 19 D for disclosure of material claims (whose amount, excluding interest and expenses, is over 1% of equity).

Note 1 - Reporting Principles and Accounting Policies - (continued)

Likewise, disclosure is given to motions for recognition as class actions, when the amount claimed in them is material, and to appeals to the High Court of Justice when, in the estimation of the Bank's management, based on the opinion of its legal counsel, it is not possible at this stage to estimate their possible outcome, and therefore, no provision was recorded for them.

In accordance with the directives of the Supervisor of Banks, the Bank is permitted to determine for class actions that it is not possible to estimate the prospects for realization of the exposure to risk in the four financial statements published since the claim was filed, or in case of delay of proceedings by decision of the Court. Beyond this, only in rare cases is the Bank permitted to determine that the prospects for realizing the exposure cannot be determined.

Q. Employee rights

1) Pension and severance pay liability

Pension and severance pay liabilities are covered by regular deposits to funds and by appropriate provisions. The financial statements included all of the liabilities for employee rights, including appropriate provisions for severance pay and for voluntary retirement programs, which are recorded in accordance with the law, agreement, custom and management's expectations. The future contractual pension liabilities are calculated based on regular actuarial consultation, based on recommendations of the Supervisor of Insurance. Also, see Note 16 below.

2) Updated mortality tables

In July 2012, the Bank of Israel instructed banks to update the actuarial provisions based on a draft update of mortality tables, issued by the Capital Market Division on July 11, 2012 - reasoning that this draft is the best estimate available to the Bank. The total impact of the Bank of Israel directive included on financial statements for the second quarter of 2012 amounted to NIS 3 million.

3) Supervisor of Banks' directives with regard to strengthening internal controls over financial reporting of employee rights.

On March 27, 2011, the Supervisor of Banks published directives with regard to strengthening internal controls over financial reporting of employee rights. These directives provide several clarifications with regard to assessment of liabilities with respect to employee rights, as well as directives concerning internal control over the financial reporting process for employee rights, including a requirement to include a qualified actuary, identify and classify liabilities with respect to employee rights, maintain internal controls for reliance on their actuarial assessment and validation, as well as certain disclosure requirements.

In accordance with these directives, a banking corporation which expects payments to be made to a group of employees in excess of contractual terms, shall take into account the expected number of departing employees (including employees expected to retire under voluntary retirement plans or upon receiving other beneficial terms) and the benefits expected to be paid to them upon departure.

Note 1 - Reporting Principles and Accounting Policies - (continued)

The severance pay liability for this group of employees shall be stated on the financial statements at the amount of liability calculated on actuarial basis, accounting for the additional cost expected to be incurred by the banking corporation with respect to providing such benefits, or the liability amount calculated as the product of the employee's monthly salary and their number of years in service, as required by Accounting Opinion 20 of the Institute of Certified Public Accountants in Israel - whichever is higher.

R. Share-based payment transactions

The fair value, upon award, of share-based payment awards to employees is recognized as payroll expense, against an increase in equity, over the period in which non-contingent eligibility for such award is gained, pursuant to IFRS2. The amount charged as an expense with respect to share-based payment awards contingent on vesting conditions, which are service or performance conditions other than market conditions, is adjusted to reflect the number of awards expected to vest. As for share-based payment awards contingent on non-vesting conditions, or on vesting conditions which are performance conditions that are market conditions, the Bank accounts for these conditions when estimating the fair value of equity instruments awarded. Therefore, the Bank recognizes an expense with respect to these awards, regardless of fulfillment of these conditions.

For transactions in which the Bank awards to employees of subsidiaries rights to equity instruments of the Bank, the award is accounted for by the Bank as a share-based payment transaction discharged using equity instruments.

S. Derivative instruments and hedging activities

1) The Bank trades in financial derivatives, including currency and interest contracts and credit derivatives. The currency contracts include forwards, futures, swaps and options. These trades are executed in all linkage sectors. The trades are executed with the public and with banks in Israel and overseas, as part of the Bank's day-to-day activities as a market maker, and as part of the overall strategy of managing the expedient level of exposure for the various market risk, including basis and interest risk – risk to which the Bank is exposed in its day-to-day activities.

2) Derivatives are stated at fair value on the Bank's balance sheet, under Assets or Liabilities, as the case may be. Changes to fair value of derivatives, other than derivatives used as cash flow hedges, are recognized on the dtatement of profit and loss.

3) It is possible that the Bank will enter into a contract, which by itself is not a derivative, but contains an embedded derivative. When an embedded derivative has economic characteristics that are not clearly and closely tied to the economic characteristics of the host contract, and a separate instrument with the same conditions as the embedded derivative would qualify as a derivative instrument, then the embedded derivative is detached from the host contract and is treated as a hedge by itself.

Note 1 - Reporting Principles and Accounting Policies - (continued)

A detached embedded derivative is stated in the balance sheet together with the host contract. When the host contract is measured at fair value and changes in its fair value are reported currently in the statement of profit and loss, or when the Bank is unable to reliably identify and measure the embedded derivative for the purpose of detaching it from the host contract, the entire contract is measured at fair value on the balance sheet.

4) In certain cases, in which the embedded derivative must be detached from the host contract, the Bank adopts a policy of measuring the entire contract according to its fair value, and records the changes in its fair value in the statement of profit and loss. This policy was adopted for structured securities in the available-for-sale portfolio.

5) The Bank designates certain derivates as fair value hedges or as cash flow hedges. The Bank documents in writing all of the hedging relationships between the hedging financial derivatives and the hedged items, as well as the objective and strategy of the management of risk through the creating of a hedge transaction. The documentation includes specific identification of the asset designated as the hedged item and states the manner in which the hedging instrument is expected to hedge the risk related to the hedged item. The Bank estimates the effectiveness of the hedging relationship at the inception of the hedge and continuously, in accordance with its risk management policies. Based on the above, a determination is made as to whether the derivative qualifies as a hedge in accordance with public reporting directives.

6) Changes in the fair value of an item hedged by a fair value hedge using a derivative that meets the above conditions, arising from changes in the specified risk factors, are recorded currently to the statement of profit and loss, concurrent with the changes in the fair value of the hedging derivative.
Changes in the fair value of a derivative which qualifies as a cash flow hedge, which arise from changes in the risk factor being hedged (which impacts the cash flows resulting from the hedged instrument), are charged to the capital reserve from cash flow hedging, in the other comprenensive income under shareholders' equity.

7) The Bank discontinues hedge accounting immediately, when:

   a) It is determined that a hedge is no longer effective for offsetting the changes in the fair value or cash flow of the hedged item, as the case may be;
   b) The derivative expires, is sold, cancelled or realized;
   c) Management revokes the designation of the derivative as a hedging instrument.

   When a fair value hedge is discontinued because it is determined that the hedge no longer qualifies as an effective fair value hedge, the derivative will continue to be recorded in the balance sheet at its fair value, but the hedged asset or liability will no longer be adjusted for changes in fair value. When a cash flow hedge is discontinued because it is determined that the hedge no longer qualifies as an effective cash flow hedge, changes in the fair value of the derivative since the date of discontinuation of hedging are recorded in the statement of profit and loss.

Note 1 - Reporting Principles and Accounting Policies - (continued)

T. Fair value

1) As from January 1, 2011, the Bank applies FAS 157 (ASC 820-10) which defines fair value, and determines a consistent work framework for fair value measurement, by defining valuation techniques and a fair value ranking. Moreover, as from January 1, 2012, the Bank applies the Supervisor of Banks' directive on fair value measurement, which includes in the Public Reporting Regulations the rules stipulated by Accounting Standard Update ASU 2011-04 with regard to fair value measurement (ASN 820): Amendments to achieve uniform fair value measurement and disclosure requirements in US GAAP and in IFRS.

The ranking divides instruments measured at fair value into three levels:

Level 1 - fair value measured using prices quoted for identical instruments on an active market accessible by the Bank upon the measurement date.

Level 2 - fair value measured using observed data, either direct or indirect, which are not quoted prices as stated under Level 1. Level 2 data include quoted market data on active markets, or on non active markets, if they exist, or data derived from or based upon such observed market data.

Level 3 - fair value measured by using non-observed data.

FAS 157 expands the disclosure requirements for fair value measurements. Application of the standard allows recognition of "first day" gains, and eliminates the obligation to determine the fair value of derivative instruments not traded on an active market based on the transaction price. (See also the Bank of Israel directive from June 2012, as follows)

For the purpose of fair value measurement, the basic "in use" assumption is not applied to financial instruments. However, under certain conditions, financial assets and financial liabilities held and managed within a portfolio, are measured at fair value using the price which would have been received or paid upon sale or transfer of the net position in such groups of financial assets or financial liabilities.

Moreover, fair value of financial instruments is measured without accounting for the "block" factor (holding size), both for financial instruments measured based on Level 1 data and for financial instruments measured based on Level 2 or 3, except for cases where a premium or discount would have been accounted for in fair value measurement by market players, in the absence of Level 1 data.

The standard stipulates that the Bank should reflect credit risk and non-performance risk in measuring the fair value of debt that it issues, including derivatives, and measured at fair value. Non-performance risk includes the Bank's credit risk, but is not limited to this risk alone.

Note 1 - Reporting Principles and Accounting Policies - (continued)

The Bank assesses credit risk in derivatives as follows:

- When there is sufficient liquid collateral with respect to the exposure, which specifically secures the derivative, the Bank assumes that credit risk is zero, and does not adjust the fair value with respect to credit quality of the counter-party.
- In other cases, the Bank estimates the fair value based on indications from transactions on an active market of the credit quality of the counter party, if such indications are available at reasonable effort. The Bank derives these indications, inter alia, from prices of debt instruments of the counter-party traded on an active market, and from prices of credit derivatives based on the credit quality of the counter-party. In the absence of such indications, the Bank calculates the adjustments based on internal ratings.

When the counter-party exposure, on consolidated basis, is not material, the Bank calculates the aforementioned adjustment on group basis, using a benchmark for credit quality by groups of similar counter-parties, e.g. based on internal ratings.

Further, the Bank conducts reasonability testing of results obtained from internal assessment with regard to changes in market spreads, and makes the required adjustments, if any.

In order to adapt the Bank's valuation methods to the exit price principle and to provisions stipulated in the standard, the Bank is required to review the valuation methods applied there by for measuring fair value, taking into consideration the relevant circumstances of the various transactions, including recent transaction prices on the market, indicative prices from valuation services and results of back testing of similar transaction types.

In June 2012, the Bank of Israel directed the Bank (in conjunction with a review of the banking system), that fair value measurement of a derivative instrument, when no quoted prices, liquid collateral or offset agreements exist which adequately secure the derivative's credit quality, and when no market information exists as to the credit quality of the counter-party (such as CDS or negotiable debentures of the counter-party) – shall be classified as a Level 3 fair value measurement. According to this directive, the aforementioned classification requirement shall apply to financial statements as from September 30, 2012, including an update of comparison figures.
For details of the effect of reclassification of derivatives to the different levels, see Note 20

How fair value is determined:

a) Securities

The fair value of securities held for trade and securities available for sale is determined based on quoted market prices on a major market. When there are multiple markets on which the security is traded, and there is no primary market. the estimate is based on the quoted market price on the most effective market. In such cases, the fair value of the Bank's investment in securities is the product of the number of units and the aforementioned quoted market price. If a quoted market price is not available, the fair value estimate is based on the best available information, with maximum use of observed data and taking into account the risk inherent in the financial instrument (market risk, credit risk, non-negotiability etc.)

Note 1 - Reporting Principles and Accounting Policies - (continued)

b) Financial derivatives

Financial derivatives with an active market are valued based on market value, determined on the primary market, or in the absence of a primary market - using a quoted market price on the most effective market. Non-negotiable financial derivatives are valued using models which take into account the risk inherent in the derivative instrument (market risk, credit risk etc.)

c) Financial instruments other than derivatives

Most of the financial instruments in this category (such as: loans to the public and loans to the Government, deposits from the public and deposits with banks, non-negotiable subordinated notes and bonds) no "market price" is quotable, since there is no active market on which they are traded. Therefore, the fair value is estimated using acceptable pricing models, such as present value of future cash flows, discounted at an interest rate that reflects the level of risk inherent in the instrument.

To this end, the future cash flows for impaired and other debt have been calculated net of effects of accounting write-offs and provision for credit loss with respect of this debt.

In May 2011, FASB issued an update to ASC 820 - "fair value measurement and disclosure". This is part of a FASB-IASB joint project designed to achieve compatibility in this regard. For entities applying the American standard, the new disclosure does not significantly alter prior requirements, but mostly clarifies prior requirements and provides new guidance.

The update clarifies that the main market used for measurement will be the market where most of the volume and transactions for this asset or liability take place, rather than the market which the entity considers to be such. The update also stipulates that the prohibition to apply a holding size factor shall apply not only to negotiable instruments classified under Level 1 of the fair value ranking, as is the case currently, but shall also apply to all other instruments under Levels 2 and 3. However, the update stipulates that a quantity or premium assumption may be used for measurements not classified under Level 1, if they are consistent with attributes of the measured asset or liability, and provided that market participants would account for such assumptions when measuring fair value.

Additional guidance relates to measuring fair value of financial instrument portfolios. The update allows for measurement of fair value based on net exposure for a group of financial instruments. Such measurement is contingent on the exposure to market risk or to credit risk being managed on net basis, items being measured at fair value, and information based on net exposure being presented to management. Note that additional guidance relates only to measurement of fair value, and not to net presentation on the balance sheet.

The update applies new disclosure requirements whereby, inter alia, disclosure is required for all transfers between Level 1 and Level 2, rather than for significant transfers only, as well as expanded disclosure requirements for instruments classified under Level 3, and disclosure is required of classification by level on the fair value hierarchy of items not measured at fair value on the balance sheet, but which require disclosure of their fair value.

Note 1 - Reporting Principles and Accounting Policies - (continued)

The Bank prospectively applies the amendments stipulated in ASU 2011-04, as from January 1, 2012. There is no mandatory application of the new disclosure requirements for financial statements for periods prior to initial application. Therefore, these financial statements include no comparison figures for these new disclosures. Initial application of ASU 2011-04 had no material impact on the Bank's financial statements, other than the change in presentation due to the new disclosure requirements.

2) Fair value alternative

FAS 159 (ASC 825-10) allows banking corporations to elect, upon specified election dates, to measure at fair value financial instruments and certain other items ("qualified items") which, according to public reporting directives, are not required to be measured at fair value. Unrealized gain and loss due to changes in fair value of items for which the fair value option has been selected, are recognized on the statement of profit and loss at each subsequent reporting date. Furthermore, prepaid costs and commissions related to items for which the fair value option has been elected, are recognized on the statement of profit and loss as they are incurred. Election of the fair value option, as stated above, is made for each instrument individually, and may not be cancelled.

Further, FAS 159 (ASC 825-10) stipulates presentation and disclosure requirements designed to assist in comparing banking corporations which elect different measurement bases for similar types of assets and liabilities.

Notwithstanding the foregoing, the Supervisor of Banks' directives with regard to application of the standard have clarified that a banking corporation may not elect the fair value option, unless the banking corporation had previously developed knowledge, systems, procedures and high-level controls which would allow it to measure the item with a high degree of reliability. Therefore, the Bank may not elect the fair value option for any asset which may be classified under Level 2 or Level 3 of the fair value ranking, nor for any liability, without prior consent of the Supervisor of Banks.

U. Basis of recognition of income and expenses

1) Interest revenues and expenses are included on accrual basis, except as follows:

a) Interest accrued on troubled debt classified as non-performing debt is recognized as revenue on cash basis when there is no doubt about collection of the outstanding recorded balance of the impaired debt. In such cases, the amount collected on account of interest to be recognized as interest revenues, is limited to the amont which would have accrued in the reported period for the outstanding recorded debt balance at the contractual interest rate. Interest revenues on cash basis are classified as interest revenue under the relevant item on the statement of profit and loss. When collection of the outstanding recorded balance is doubtful, all payments collected serve to decrease the loan principal. Moreover, interest on amounts in arrears with respect to housing loans are recognized on the statement of profit and loss based on actual collection.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Impaired debt under restructuring is treated as debt accruing interest revenues if all of the following conditions are fulfilled:

- After restructuring, the debt is reasonably certain to be fully repaid under the new terms.
- The agreement is complied with for at least six months for debt repaid by monthly installments, or over 20% for debt repaid by longer installment periods.
- The restructured debt is not 90 days or more in arrears.

b) Revenues from early repayment fees for loans, after deduction of the portion related to financial capital, are recognized on the statement of profit and loss at equal annual installments over the remaining term to maturity of the loan, or over three years from the date of early repayment, whichever is shorter.

c) Commissions for allocation of credit facilities, as well as commissions from financing business (such as: commissions with respect to acceptances, guarantees and documentary credit) are recognized on the statement of profit and loss pro-rata to the transaction terms.

d) securities - see section i) above.

e) financial derivatives - see section s) above.

2) Commission revenues with respect to services rendered (such as: activities in securities and derivatives, credit cards, account management, handling of credit, conversion differences and foreign trade activities) are recognized on the statement of profit and loss when the Bank becomes eligible to receive them. Commissions from financing transactions, such as commissions with respect to acceptances, guarantees and documentary credit are recognized pro-rata to the transaction terms.

3) In subsequent periods to other-than-temporary impairment. Revenue accrual in the reported period is based on excess expected cash flows from the debt instrument (the base amount of debt instrument upon other-than-temporary impairment is its fair value).

4) Other revenues and expenses - are recognized on accrual basis.

V. Taxes on income

Taxes on income include current and deferred taxes. Current and deferred taxes are charged to the statement of profit & loss, unless the taxes arise from a business combination, or charged directly to equity if they arise from items directly recognized under equity.

1) Current taxes

Current tax is the tax amount expected to be payable (or receivable) on taxable income for the year, calculated using tax rates which apply pursuant to statutes enacted, or essentially enacted, as of the reporting date, including changes to tax payments with regard to previous years.

The provision for taxes on income of the Bank and its subsidiaries that are financial institutions for VAT purposes includes profit tax levied on earnings under the Value Added Tax Act. The value added tax levied on the salaries of financial institutions is included under “Payroll and associated expenses”.

Note 1 - Reporting Principles and Accounting Policies - (continued)

2) Deferred taxes

Deferred taxes are recognized with respect to temporary difference between the carrying amount of asset and liabilities for the purpose of financial reporting, and their value for tax purposes.

Deferred tax are measured so as to reflect the tax implications expected to arise from the manner in which the Bank, at the end of the reported period, anticipates recovering or discharging the carrying amount of assets and liabilities.

Deferred taxes are measured using tax rates expected to apply to temporary differences when realized, based on statutes enacted, or essentially enacted, as of the balance sheet date.

As from January 1, 2012, the Bank applies IAS 12 "Taxes on income". The standard, as adopted by the Supervisor of Banks, contains similar provisions to those of Israeli Accounting Standard 19 "Income Taxes", applied by the banking system to date. However, along with adoption of the international standard, specific provisions issued by the Supervisor of Banks have been modified. In general, deferred taxes are recognized with respect to carry-forward loss, tax credits and deductible temporary differences, when taxable revenue is expected in future which may be used to utilize them. According to the Supervisor of Bank's directive, definition of the term "probable" is "more likely than not", as in generally accepted accounting principles for US banks for handling income taxes, rather than the translation of the term "probable" in Public Reporting Regulations with regard to deferred tax assets, which is "beyond any reasonable doubt". Initial application of the standard had no material impact on the Bank's financial statements.

3) Offset of deferred tax assets and liabilities

The Bank offsets deferred tax assets and liabilities when there is an enforceable legal right of set-off between them, and they are attributed to the same taxable income, taxed by the same tax authority with respect to the same entity, or to consolidated companies, which intend to discharge current tax assets and liabilities on net basis, or with tax assets and liabilities settled concurrently.

4) Additional tax on income with respect to dividend distributions

The earnings of certain investees may be subject to additional taxes if distributed by them as a dividend. No provision for tax is recorded for the profits of subsidiaries, when dividend distributions are not expected in the foreseeable future.

5) Unertain tax positions

In cases where there is uncertainty with regard to taxes on income, banking corporations would be required to apply the rules listed in clarification FIN 48 with regard to uncertainty concerning taxes on income, provided these are not in contradiction to International Financial Reporting Standards, by way of setting policy, procedures and applying documentation requirements with regard to tax positions with varying degrees of uncertainty.

In this context, the Bank rcognizes the effect of tax positions only if it is more likely than not that these positions would be accepted by the Tax Authority or by the Court. Recognized tax positions are measured at he maximum amount which is over 50% likely to materialize. Changes to recognition or measurement are reflected in the period in which changes occurred to assumptions, resulting in a change in judgment.

Note 1 - Reporting Principles and Accounting Policies - (continued)

W. Earnings per share

The Bank states earnings per share data, both basic and diluted, for its ordinary share capital. Basic earnings per share is calculated by dividing the earnings attributable to holders of ordinary shares of the Group, by the weighted average number of ordinary shares outstanding during the period, after adjustment for treasury shares.

Diluted earnings per share is calculated by adjusting earnings (such as adjustment for after-tax effect of dividends, financing costs and other changes, if any) related to holders of ordinary shares, and adjusting the weighted average number of ordinary shares outstanding, after adjustment for treasury shares and for the effect of all potentially dilutive ordinary shares, including debentures convertible into shares, stock option warrants and stock option warrants awarded to employees.

X. Segment reporting

An operating segment is a component of the Bank engaged in operations from which it may derive revenues and incur expenses, its operating results are regularly reviewed by management and by the Board of Directors for the purpose of making decisions about resource allocation and for assessing performance, and separate relevant financial information is available. The format for reporting Bank operating segments was stated in public reporting directives by the Supervisor of Banks, and is based on client attributes.

Y. Related party disclosures

IAS 24 stipulates the required disclosure by an entity of its relations with any related party, as well as of transactions and outstanding balances with any related party. Further disclosure is required of remuneration of key executives. Key executives are defined as persons having the authority and responsibility for planning, directing and controlling entity operations, either directly or indirectly, including any (active or inactive) Board member of such entity.

In conjunction with adoption of this standard by the Supervisor of Banks, the required disclosure format of the financial statements has been adapted to comply with both IAS 24 disclosure requirements and the additional disclosure required pursuant to Securities Regulations, 2010.

The Bank applies the standard retroactively starting with financial statements as of December 31, 2012.

Initial application of the standard did not materially impact the Bank's financial statements, other than the change in presentation.

Z. Capitalized borrowing costs

IAS 23 stipulates that an entity should capitalize borrowing costs related directly to acquisition and setup or production of a qualified asset. A qualified asset is one which requires a significant time period to prepare for designated use or sale, including fixed assets, software assets and other assets which require a prolonged time period to be brought to a state ready for use or sale. However, directives by the Supervisor of Banks have clarified that a banking corporation shall not capitalize borrowing costs prior to setting clear policy, procedures and controls with regard to criteria for recognizing qualified assets and for the borrowing costs capitalized.

The Bank applies the standard as from January 1, 2012. Initial application of the standard had no impact on the Bank's financial statements.

Note 1 - Reporting Principles and Accounting Policies - (continued)

AA. New accounting standards and new directives by the Supervisor of Banks prior to their application:

1) Standards with regard to non-core banking business issues – were gradually adopted in 2011 and 2012. However, IAS 19 "Employee benefits" has yet to become effective, and will be adopted in accordance with the Supervisor of Banks' directives, when published, with regard to timing and manner of initial application of this standard.

2) New IFRS set with regard to consolidation of financial statements and related matters

In May 2011, IASB published the new set of standards, which is part of the joint IASB-FASB convergence program, and essentially supersedes existing standards on consolidation of financial statements and joint transactions, as well as several revisions with regard to associates. According to guidance from the Supervisor of Banks, banking corporations should regularly update their accounting treatment of issues adopted in the Public Reporting Regulations. Such updates are required based on the start date and transition provisions to be specified in new IFRS to be published on these matters, and in accordance with adoption principles and clarifications by the Supervisor of Banks.

Therefore, application of rules stipulated in the new set of standards on consolidation of financial statements and related matters, will be subject to guidelines stated in the Public Reporting Regulations, inter alia, with regard to application of the standard to matters where specific rules had been stipulated in or adopted by the Public Reporting Regulations, which differ from those provide by the standard and/or related guidance.

In December 2012, the Supervisor of Banks issued a circular concerning "Adoption of Certain International Financial Reporting Standards (IFRS)", which stipulated that as from January 01, 2013, banking corporations should apply the following IFRS standards concerning consolidation of financial statements and related matters:

IFRS 10 "Consolidated financial statements"

. IFRS 12 "Disclosure of interests in other entities"

IAS 28 (2011 revision) "Investments in associates and joint ventures"

Initial application of these standards, as stipulated by the Supervisor of Banks, is in accordance with transition provisions determined by these standards, including by way of retroactive application and adjustment of comparison figures as needed.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Below is additional information about standards to be adopted and their potential effect:

a) IFRS 10 "Consolidated financial statements"

The standard redefines the term "control over subsidiaries".

The major changes in the standard include:

- IFRS 10 stipulates that control is the sole basis for consolidation of entities, and the definition of control has been expanded compared to existing standards.
- Consolidation of entities in which de-facto control exists.
- Potential voting rights shall be accounted for when reviewing control, if they may be immediately realized and are real, as stated in the standard. However, rights not immediately realizable may also need to be accounted for.
- Added guidance with regard to identification of agent-principal relations.

IFRS 10 will be retroactively applied to financial statements for annual periods starting on or after January 1, 2013, in accordance with transition provisions in this standard.

The Bank believes that the effect of IFRS 10 on its financial statements should not be material.

b) IFRS 12 “Disclosure of interests in other entities”

The standard incorporates disclosure requirements with regard to investment in interests in subsidiaries, associates, interests in joing ventures and structured entities not consolidated.

IFRS 12 will be retroactively applied to financial statements for annual periods starting on or after January 1, 2013, in accordance with transition provisions in this standard.

IFRS 12 will affect the Notes to the financial statements upon initial application.

c) IAS 28 (2011 revision) "Investments in associates and joint ventures"

The following major changes appear in the standard:

- Accounting treatment of joint venture.
- An entity which invests in an associate which is partly held, indirectly, through venture capital funds or mutual funds, trusts composed of similar units and entities, including insurance funds linked to investments, may elect to measure this portion of the associate at fair value through profit and loss, regardless of whether these entities have or do not have a material effect on the share of the investment.
- Required classification as held-for-sale of any portion of investment in associate, or if realization of that portion meets the criteria for classification as held-for-sale under IFRS 5.
- Explicit provision stipulating that when investment in an associate becomes an investment in a joint venture, or vice versa, the entity should continue to apply the equity method and shall not remeasure the remaining balance of the interest.

IAS 28 (2011 revision) will be retroactively applied to financial statements for annual periods starting on or after January 1, 2013.

The Bank believes that application of IAS 28 (2011 revision) should not materially impact the financial statements.

Note 1 - Reporting Principles and Accounting Policies - (continued)

3) Format of statement of profit and loss for banking corporations and adoption of generally acceptable accounting practices by US banks for measurement of interest revenues

On December 29, 2011, the Supervisor of Banks published a circular designed to adapt the Public Reporting Regulations for adoption of rules specified in US GAAP with regard to non-refundable fees and other costs.

Below are the changes arising from adoption of ASC 310-20 "Non-refundable fees and other costs".

When calculating the effective interest rate for a loan, the banking corporation should account for the net amount of fees or costs incurred. These costs will include direct costs of loan origination incurred with a third party, as well as certain costs expended by the banking corporation as lender for that loan (currently, costs incurred by the banking corporation as lender are recognized in the statement of profit and loss under "Payroll and associated expenses". Commissions from loan generation include commissions charged to the borrower with respect to loan origination activities (currently, some of these commissions are included under "Operating commissions" and some – under "Commissions from financing transactions").

The updates related to adoption of interest revenue measurement issues will be applied as from January 1, 2014. The Bank is reviewing the effect of adopting this directive on its financial statements.

4) Directive on the Statement of Comprehensive Income

On December 9, 2012, the Supervisor of Banks issued a circular revising the Public Reporting Regulations with regard to the Statement of Comprehensive Income. The circular modifies the presentation of other comprehensive income items on the financial statements, so that other comprehensive income items would be reported on a separate statement named "Statement of Comprehensive Income", to be presented immediately following the statement of profit and loss. Furthermore, the composition and movement in Cumulative Other Comprehensive Income are to be presented in a new note on Cumulative Other Comprehensive Income.

The revisions included in this directive will be retroactively applied to financial statements for the first quarter of 2013 and thereafter. Initial application of the standard is not expected to materially impact the Bank's financial statements, other than the change in presentation.

5) Directive with regard to offset of assets and liabilities

On December 12, 2012, the Supervisor of Banks issued a draft circular revising the Public Reporting Regulations with regard to offset of assets and liabilities. As for offset of derivative instruments, the draft stipulates that banking corporations should offset assets and liabilities arising from the same counter-party and present their net balance on the balance sheet, when all of the following conditions are met:

(1) The banking corporation has an enforceable legal right to offset assets against liabilities with regard to said liabilities;

(2) The banking corporation intends to repay the liabilities and realize the assets on net basis or concurrently;

(3) Both the banking corporation and the counter-party owe each other amounts which may be determined.

Note 1 - Reporting Principles and Accounting Policies - (continued)

Moreover, the draft stipulates that under certain conditions, a banking corporation may offset fair value amounts recognized with respect to derivative instruments and fair value amounts recognized with respect to the right to call cash collateral (receivables) or the commitment to reimburse cash collateral (payables) arising from derivative instruments transacted with the same counter-party in accordance with a master netting arrangement – even if there is no intention to repay on net basis or concurrently. The banking corporation is required to set accounting policies to be consistently applied with respect to offset of such fair value amounts.

With regard to repurchase transactions, the draft stipulates that banking corporations may offset securities purchased in conjunction with repurchase agreements against securities sold in conjunction with repurchase agreements, if certain conditions specified in US GAAP on this matter are fulfilled.

The circular clarifies certain consideratios to be accounted for by banks in order to determine if there is any doubt about meeting the conditions for offset. Inter alia, as for the right to offset, a new requirement was added whereby the independent auditor of the banking corporation should verify existence of an enforceable legal right to offset (for offset) mutatis mutandis, in the same manner they currently verify whether transferred financial assets have been isolated beyond the reach of the transferor and the creditors (for derecognition of financial assets).

In addition, the circular includes comprehensive disclosure requirements, including disclosure of the banking corporation policy which determines whether such derivative instruments are to be or not to be offset as described above.

It was further stipulated that any banking corporation intending to offset on its balance sheet amounts significantly higher than the amounts offset through June 30, 2012 by that corporation, should apply to the Supervisor of Banks to obtain preliminary directives.

The revisions included in this directive will be retroactively applied to financial statements for reporting periods starting on or after January 1, 2013. However, in quarterly financial statements in 2013 banking corporations are allowed not to provide disclosure initially required due to application of this directive for comparative figures referring to corresponding periods in 2012.

The retroactively adjustment does not suppose to have material impact on the bank's financial statements.

Note 2 - Cash and Deposits with Banks

As of December 31

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	2012	2011	2012	2011
Cash and deposits with central banks	15,005	13,427	12,333	11,135
Deposits with commercial banks	1,589	2,419	1,180	1,623
Deposits with special banking entities	77	126	73	116
Total cash and deposits with banks	**16,671**	**15,972**	**13,586**	**12,874**
Includes - cash, deposits with banks and deposits with central banks for an original period of up to three months	14,394	14,991	12,942	12,269

Note 3 - Securities – Consolidated

As of December 31, 2012

Reported amounts (NIS in millions)

A. Composition:

	Carrying amount	Amortized cost (for shares - cost)	Unrecognized profit from adjustments to fair value	Unrecognized loss from adjustments to fair value	Fair value (1)
(1) Government of Israel debentures held to maturity	**1,123**	**1,123**	**3**	**-**	**1,126**

	Carrying amount	Amortized cost (for shares - cost)	Cumulative other comprehensive income Gain	Cumulative other comprehensive income Loss	Fair value (1)
(2) Securities available for sale					
Debentures and bonds -					
Of the Government of Israel (2)	4,700	4,705	46	(51)	4,700
Of foreign governments (2)(6)	95	95	-	-	95
Of banks and financial institutions in Israel	123	123	2	(2)	123
Of banks and financial institutions overseas	394	392	2	-	394
Of others in Israel	25	24	1	-	25
Of others overseas	168	166	2	-	168
Total debentures available for sale	**5,505**	**5,505**	**53**	**(53)**	**5,505**
Shares (3)	119	120	-	(1)	119
Total securities available for sale	**5,624**	**5,625**	(4) **53**	(4) **(54)**	**5,624**

	Carrying amount	Amortized cost (for shares - cost)	Unrealized profit from adjustments to fair value	Unrealized loss from adjustments to fair value	Fair value (1)
(3) Securities held for trade					
Debentures -					
Of the Government of Israel (7)	2,291	2,272	39	(20)	2,291
Of banks and financial institutions overseas	3	3	-	-	3
Total securities held for trade	**2,294**	**2,275**	(5) **39**	(5) **(20)**	**2,294**
Total securities	**9,041**	**9,023**	**95**	**(74)**	**9,044**

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities.

(2) See Note 15.A-E for information on liens on securities held by the Bank.

(3) Includes shares for which a fair value is not available, that are stated at cost, net of a provision for decline in value that is not temporary, amounting to NIS 115 million.

(4) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".

(5) Charged to statement of profit and loss but not yet realized.

(6) US government debentures.

(7) Of which, securities amounting to NIS 1,106 million are classified as held for trade, because the Bank elected to present them in accordance with the fair value alternative in Section 20 of Public Reporting Regulations, even though they had not been acquired for trade.

Note: For details of results of trading in investments in debentures – see Notes 22(d), 23(a)(2) and 23(b); for details on results of trading in shares - see Note 23(a)(4).

Note 3 - Securities - Consolidated (continued)

As of December 31, 2011

Reported amounts (NIS in millions)

A. **Composition –** (continued):

	Carrying amount	Amortized cost (for shares - cost)	Unrecognized profit from adjustments to fair value	Unrecognized loss from adjustments to fair value	Fair value [1]
(1) Government of Israel debentures held to maturity	**703**	**703**	**-**	**(5)**	**698**

	Carrying amount	Amortized cost (for shares - cost)	Cumulative other comprehensive income		Fair value [1]
			Gain	Loss	
(2) Securities available for sale					
Debentures and bonds -					
Of the Government of Israel [2]	5,524	5,586	19	(81)	5,524
Of foreign governments[2][6]	86	86	-	-	86
Of banks and financial institutions in Israel	159	164	1	(6)	159
Of banks and financial institutions overseas	412	413	2	(3)	412
Asset-backed (ABS)	61	68	5	(12)	61
Of others in Israel	81	81	-	-	81
Of others overseas	135	135	1	(1)	135
Total debentures available for sale	**6,458**	**6,533**	**28**	**(103)**	**6,458**
Shares[3]	85	85	-	-	85
Total securities available for sale	**6,543**	**6,618**	[4] **28**	[4] **(103)**	**6,543**

	Carrying amount	Amortized cost (for shares - cost)	Unrealized profit from adjustments to fair value	Unrealized loss from adjustments to fair value	Fair value [1]
(3) Securities held for trade					
Debentures -					
Of the Government of Israel [7]	1,183	1,177	7	(1)	1,183
Of banks and financial institutions overseas	3	3	-	-	3
Total securities held for trade	**1,186**	**1,180**	[5] **7**	[5] **(1)**	**1,186**
Total securities	**8,432**	**8,501**	**35**	**(109)**	**8,427**

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities.
(2) See Note 15.A-E to the 2011 financial statements for information on liens on securities held by the Bank.
(3) Includes shares for which a fair value is not available, that are stated at cost, net of a provision for decline in value that is not temporary, amounting to NIS 79 million.
(4) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".
(5) Charged to statement of profit and loss but not yet realized.
(6) US government debentures.
(7) Of which, securities amounting to NIS 531 million are classified as held for trade, because the Bank elected to present them in accordance with the fair value alternative in Section 20 of Public Reporting Regulations, even though they had not been acquired for trade.

Note: For details of results of trading in investments in debentures – see Notes 22(d), 23(a)(2) and 23(b); for details on results of trading in shares - see Note 23(a)(4).

Note 3 - Securities – the Bank (continued)

As of December 31, 2012

Reported amounts (NIS in millions)

A. **Composition – (continued):**

	Carrying amount	Amortized cost (for shares - cost)	Cumulative other comprehensive income		Fair value [1]
			Gain	Loss	
(1) Securities available for sale					
Debentures and bonds -					
Of the Government of Israel [2]	3,257	3,268	40	(51)	3,257
Of foreign governments [2][6]	95	95	-	-	95
Of banks and financial institutions overseas	364	362	2	-	364
Of others overseas	158	156	2	-	158
Total debentures available for sale	**3,874**	**3,881**	**44**	**(51)**	**3,874**
Shares[3]	119	120	-	(1)	119
Total securities available for sale	**3,993**	**4,001**	[4] **44**	[4] **(52)**	**3,993**

	Carrying amount	Amortized cost (for shares - cost)	Unrealized profit from adjustments to fair value	Unrealized loss from adjustments to fair value	Fair value [1]
(2) Securities held for trade					
Debentures -					
Of the Government of Israel [7]	2,291	2,272	39	(20)	2,291
Total securities held for trade	**2,291**	**2,272**	[5] **39**	[5] **(20)**	**2,291**
Total securities	**6,284**	**6,273**	**83**	**(72)**	**6,284**

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities.
(2) See Note 15.A-E for information on liens on securities held by the Bank.
(3) Includes shares for which a fair value is not available, that are stated at cost, net of a provision for decline in value that is not temporary, amounting to NIS 115 million.
(4) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".
(5) Charged to statement of profit and loss but not yet realized.
(6) US government debentures.
(7) Of which, securities amounting to NIS 1,106 million are classified as held for trade, because the Bank elected to present them in accordance with the fair value alternative in Section 20 of Public Reporting Regulations, even though they had not been acquired for trade.

Note: For details of results of trading in investments in debentures – see Notes 22(d), 23(a)(2) and 23(b); for details on results of trading in shares - see Note 23(a)(4).

Note 3 - Securities – the Bank (continued)

As of December 31, 2011

Reported amounts (NIS in millions)

A. Composition – (continued):

	Carrying amount	Amortized cost (for shares - cost)	Cumulative other comprehensive income		Fair value [1]
			Gain	Loss	
(1) Securities available for sale					
Debentures and bonds -					
Of the Government of Israel [2]	3,808	3875	12	(79)	3808
Of foreign governments [2][6]	86	86	-	-	86
Of banks and financial institutions overseas	381	382	2	(3)	381
Asset-backed (ABS)	61	68	5	(12)	61
Of others overseas	126	126	1	(1)	126
Total debentures available for sale	**4,462**	**4,537**	**20**	**(95)**	**4,462**
Shares[3]	85	85	-	-	85
Total securities available for sale	**4,547**	**4,622**	[4]**20**	[4] **(95)**	**4,547**

	Carrying amount	Amortized cost (for shares - cost)	Unrealized profit from adjustments to fair value	Unrealized loss from adjustments to fair value	Fair value [1]
(2) Securities held for trade					
Debentures -					
Of the Government of Israel [7]	1,183	1,177	7	(1)	1,183
Total securities held for trade	**1,183**	**1,177**	[5] **7**	[5] **(1)**	**1,183**
Total securities	**5,730**	**5,799**	**27**	**(96)**	**5,730**

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities.
(2) See Note 15.A-E to the 2011 financial statements for information on liens on securities held by the Bank.
(3) Includes shares for which a fair value is not available, that are stated at cost, net of a provision for decline in value that is not temporary, amounting to NIS 79 million.
(4) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".
(5) Charged to statement of profit and loss but not yet realized.
(6) US government debentures.
(7) Of which, securities amounting to NIS 531 million are classified as held for trade, because the Bank elected to present them in accordance with the fair value alternative in Section 20 of Public Reporting Regulations, even though they had not been acquired for trade.

Note: For details of results of trading in investments in debentures – see Notes 22(d), 23(a)(2) and 23(b); for details on results of trading in shares - see Note 23(a)(4).

Note 3 - Securities (continued)

Reported amounts (NIS in millions)

B. Further details with regard to the time period in which asset-backed securities available for sale, which include unrealized loss:

In 2012, the Bank realized the remaining asset-backed securities available for sale.

	As of December 31, 2012			
	Less than 12 months		12 months or more	
	Fair value	Unrealized loss	Fair value	Unrealized loss
Asset-backed securities (ABS):				
CLO	-	-	-	-
Total	**-**	**-**	**-**	**-**

	As of December 31, 2011			
	Less than 12 months		12 months or more	
	Fair value	Unrealized loss	Fair value	Unrealized loss
Asset-backed securities (ABS):				
CLO	-	-	37	(12)
Total	**-**	**-**	**37**	**(12)**

Note 4 - Credit risk, loans to the public and provision for credit loss

Reported amounts (NIS in millions)

A. Off balance sheet debt [(1)] and credit instruments

1. Change in balance of provision for credit loss

Consolidated

						December 31, 2012
						Provision for credit loss
	Loans to the public					
	Commercial	Housing	Individual - other	Total	Banks and govern-ments	Total
Balance of provision for credit loss at year start	714	884	154	1,752	14	1,766
Expenses with respect to credit loss	207	10	63	280	(4)	276
Accounting write-offs	(230)	(73)	(138)	(441)	-	(441)
Recovery of debt written off in previous years	41	-	63	104	-	104
Net accounting write-offs	(189)	(73)	(75)	(337)	-	(337)
Balance of provision for credit loss at year end	**732**	**821**	**142**	**1,695**	**10**	**1,705**
Includes: With respect to balance sheet credit instruments	85	-	17	102	-	102
						December 31, 2011[(2)]
Balance of provision for credit loss at year start	2,388	846	369	3,603	3	3,606
Net accounting write-offs recognized as of January 1, 2011	(2,165)	-	(395)	(2,560)	-	(2,560)
Other changes to provision as of January 1, 2011 (charged to shareholders' equity)	644	93	176	913	6	919
Expenses with respect to credit loss	243	2	88	333	5	338
Accounting write-offs	(438)	(57)	(169)	(664)	-	(664)
Recovery of debt written off in previous years	42	-	85	127	-	127
Net accounting write-offs	(396)	(57)	(84)	(537)	-	(537)
Balance of provision for credit loss at year end	**714**	**884**	**154**	**1,752**	**14**	**1,766**
Includes: With respect to balance sheet credit instruments	90	-	24	114	-	114

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with re-sale agreements. And except from deposits with bank of israel.

(2) As from the 2012 financial statements, the Bank initially applies supervision of banks' directive with regard to update disclosure of credit quality of debt and of provision for credit loss. The Bank applies the directives prospectively as from the 2012 financial statements for balance sheet data first required pursuant to this directive with reclassification of comparative figures in as much as possible. For details see note 1.J.8.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

A. Off balance sheet debt [(1)] and credit instruments

1. Change in balance of provision for credit loss - continued

The Bank

						December 31, 2012
						Provision for credit loss
	Loans to the public					
	Commercial	Housing	Individual - other	Total	Banks and governments	Total
Balance of provision for credit loss at year start	714	884	123	1,721	12	1,733
Expenses with respect to credit loss	221	10	50	281	(4)	277
Accounting write-offs	(244)	(73)	(111)	(428)	-	(428)
Recovery of debt written off in previous years	41	-	49	90	-	90
Net accounting write-offs	(203)	(73)	(62)	(338)	-	(338)
Balance of provision for credit loss at year end	**732**	**821**	**111**	**1,664**	**8**	**1,672**
Includes: With respect to balance off sheet credit instruments	85	-	15	100	-	100

						December 31, 2011[(2)]
Balance of provision for credit loss at year start	2,388	846	318	3,552	-	3,552
Net accounting write-offs recognized as of January 1, 2011	(2,165)	-	(332)	(2,497)	-	(2,497)
Other changes to provision as of January 1, 2011 (charged to shareholders' equity)	644	93	134	871	6	877
Expenses with respect to credit loss	243	2	75	320	6	326
Accounting write-offs	(438)	(57)	(145)	(640)	-	(640)
Recovery of debt written off in previous years	42	-	73	115	-	115
Net accounting write-offs	(396)	(57)	(72)	(525)	-	(525)
Balance of provision for credit loss at year end	**714**	**884**	**123**	**1,721**	**12**	**1,733**
Includes: With respect to balance sheet credit instruments	90	-	21	111	-	111

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with re-sale agreements. And except from deposits with bank of israel.

(2) As from the 2012 financial statements, the Bank initially applies supervision of banks' directive with regard to update disclosure of credit quality of debt and of provision for credit loss. The Bank applies the directives prospectively as from the 2012 financial statements for balance sheet data first required pursuant to this directive with reclassification of comparative figures in as much as possible. For details, see note 1.J.8.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

A. Off balance sheet debt [1] and credit instruments

2. Additional information about calculation of the provision for credit loss with respect to debt, and debt for which the provision has been calculated

Consolidated

						December 31, 2012
	Loans to the public					
	Commercial	Housing	Individual - other	Total	Banks and govern-ments	Total
Recorded debt balance of debt [1]						
Reviewed on individual basis	30,372	5	617	30,994	2,819	33,813
Reviewed on group basis	6,277	80,864	12,109	99,250	-	99,250
Total debt	**36,649**	[4] **80,869**	**12,726**	**130,244**	**2,819**	**133,063**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	79,970	-	79,970	-	79,970
Provision for credit loss with respect to debt [1]						
Reviewed on individual basis	595	2	23	620	10	630
Reviewed on group basis	52	819	102	973	-	973
Total provision for credit loss	**647**	**821**	**125**	**1,593**	**10**	**1,603**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	[3] 819	-	819	-	819

						December 31, 2011[2]
Recorded debt balance of debt [1]						
Reviewed on individual basis	30,222	17	631	30,870	3,612	34,482
Reviewed on group basis	5,768	72,252	12,041	90,061	-	90,061
Total debt	**35,990**	[4] **72,269**	**12,672**	**120,931**	**3,612**	**124,543**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	70,494	-	70,494	-	70,494
Provision for credit loss with respect to debt [1]						
reviewed on individual basis	562	15	28	605	14	619
reviewed on group basis	62	869	102	1,033	-	1,033
Total provision for credit loss	**624**	**884**	**130**	**1,638**	**14**	**1,652**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	[3] 869	-	869	-	869

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with resale agreements. And except from deposits with bank of israel.

(2) As from the 2012 financial statements, the Bank initially applies supervision of banks' directive with regard to update disclosure of credit quality of debt and of provision for credit loss. The Bank applies the directives prospectively as from the 2012 financial statements for balance sheet data first required pursuant to this directive with reclassification of comparative figures in as much as possible. For details, see note 1.J.8.

(3) Includes balance of provision in excess of that required by extent of arrears assessed on group basis, amounting to NIS 98 million (as of December 31, 2011 - NIS 91 million).

(4) includes general –purpose loans secured by lieb on residential apatment amounting to NIS 5,037 (as of December 31, 2011 - NIS 4,388 million.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

A. Off balance sheet debt [(1)] and credit instruments

2. Additional information about calculation of the provision for credit loss with respect to debt, and debt for which the provision has been calculated - continued

The Bank

						December 31, 2012
	Loans to the public					
	Commer-cial	Housing	Individual - other	Total	Banks and govern-ments	Total
Recorded debt balance of debt [(1)]						
Reviewed on individual basis	30,372	5	350	30,727	2,349	33,076
Reviewed on group basis	6,277	80,864	6,002	93,143	-	93,143
Total debt	**36,649**	[(4)] **80,869**	**6,352**	**123,870**	**2,349**	**126,219**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	79,970	-	79,970	-	79,970
Provision for credit loss with respect to debt [(1)]						
Reviewed on individual basis	595	2	18	615	8	623
Reviewed on group basis	52	819	78	949	-	949
Total provision for credit loss	**647**	**821**	**96**	**1,564**	**8**	**1,572**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	[(3)] 819	-	819	-	819

						December 31, 2011[(2)]
Recorded debt balance of debt [(1)]						
Reviewed on individual basis	30,222	17	405	30,644	2,806	33,450
Reviewed on group basis	5,768	72,252	6,268	84,288	-	84,288
Total debt	**35,990**	[(4)] **72,269**	**6,673**	**114,932**	**2,806**	**117,738**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	70,494	-	70,494	-	70,494
Provision for credit loss with respect to debt [(1)]						
Reviewed on individual basis	562	15	23	600	12	612
Reviewed on group basis	62	869	79	1,010	-	1,010
Total provision for credit loss	**624**	**884**	**102**	**1,610**	**12**	**1,622**
Includes: Loans for which a provision for credit loss is assessed by extent of arrears	-	[(3)] 869	-	869	-	869

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with resale agreements. And except from deposits with bank of israel.

(2) As from the 2012 financial statements, the Bank initially applies supervision of banks' directive with regard to update disclosure of credit quality of debt and of provision for credit loss. The Bank applies the directives prospectively as from the 2012 financial statements for balance sheet data first required pursuant to this directive with reclassification of comparative figures in as much as possible. For details, see note 1.J.8.

(3) Includes balance of provision in excess of that required by extent of arrearsassessed on group basis, amounting to NIS 98 million (as of December 31, 2011 - NIS 91 million).

(4) Includes: general-purpose loans secured by lieh on residential apartment amounting to Nis 5,037 (as of December 31, 2011– Nis 4,388 million).

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

B. Debt [1]

1. Credit quality and arrears

Consolidated

					As of December 31, 2012	
		Troubled [2]			Non impaired debt - additional information	
	Non troubled	Non impaired	Impaired [3]	Total	In arrears 90 days or longer [4]	In arrears 30 to 89 days [5]
Borrower activity in Israel						
Public-commercial						
Construction and real estate – construction	6,678	32	737	7,447	7	5
Construction and real estate - real estate operations	1,411	8	23	1,442	1	2
Financial services	4,373	24	302	4,699	2	13
Commercial-other	20,144	264	464	20,872	22	201
Total commercial	**32,606**	**328**	**1,526**	**34,460**	**32**	**221**
Private individuals – housing loans	79,052	[6]1,599	5	80,656	1,599	869
Private individuals - other	12,157	161	84	12,402	28	109
Total public – activity in Israel	**123,815**	**2,088**	**1,615**	**127,518**	**1,659**	**1,199**
Banks in Israel	512	-	-	512	-	-
Government of Israel	1	-	-	1	-	-
Total activity in Israel	**124,328**	**2,088**	**1,615**	**128,031**	**1,659**	**1,199**
Borrower activity overseas						
Public - commercial						
Construction and real estate	756	-	38	794	-	-
Commercial – other	1,390	-	5	1,395	-	-
Total commercial	**2,146**	**-**	**43**	**2,189**	**-**	**-**
Private individuals	531	-	6	537	-	-
Total public – overseas activity	**2,677**	**-**	**49**	**2,726**	**-**	**-**
Overseas banks	1,149	-	5	1,154	-	-
Overseas governments	1,152	-	-	1,152	-	-
Total activity overseas	**4,978**	**-**	**54**	**5,032**	**-**	**-**
Total public	126,492	2,088	1,664	130,244	1,659	1,199
Total banks	1,661	-	5	1,666	-	-
Total governments	1,153	-	-	1,153	-	-
Total	**129,306**	**2,088**	**1,669**	**133,063**	**1,659**	**1,199**

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with re-sale agreements. And except from deposits with bank of israel.
(2) Credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer.
(3) Generally, impaired debt does not accrue interest revenues. For information about certain impaired debt restructured using troubled debt restructuring, see Note 4.B.2.c below.
(4) Classified as troubled non-impaired debt. Accruing interest revenues.
(5) Accruing interest revenues. Debt in arrears 30 to 89 days amounting to NIS 70 million was classified as troubled non-impaired debt.
(6) Includes balance of housing loans amounting to NIS 311 million (as of December 31, 2011 - NIS 324 million) provided for by extent of arrears, for which an agreement has been signed for repayment of arrears by the borrower, where a change was made to the repayment schedule for the outstanding loan balance not yet due.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

B. Debt [(1)]

1.A Credit quality and arrears – continued.

Consolidated

	As of December 31, 2011				
				Non impaired debt - additional information	
	Non impaired	Impaired [(2)]	Total	In arrears 90 days or longer [(3)]	In arrears 30 to 89 days [(4)]
Loans to the public					
Reviewed on individual basis	30,608	[(5)] 1,587	32,195	56	53
Housing loans by extent of arrears	71,486	-	71,486	1,716	893
Reviewed on group basis - other	17,250	-	17,250	42	81
Total public	119,344	1,587	120,931	1,814	1,027
Total banks	2,541	4	2,545	-	-
Total governments	1,067	-	1,067	-	-
Total	**122,952**	**1,591**	**124,543**	**1,814**	**1,027**

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with re-sale agreements. And except from deposites with Bank of israel.
(2) Generally, impaired debt does not accrue interest revenues. For information about certain impaired debt restructured using troubled debt restructuring, see Note 4.B.2.c below.
(3) Classified as troubled non-impaired debt. Accruing interest revenues.
(4) Accruing interest revenues. Debt in arrears 30 to 89 days amounting to NIS 70 million was classified as troubled non-impaired debt.
(5) Reclassified.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

1.B. Credit quality

The state of debt arrears is monitored daily and automatically, providing one of the key indications of credit quality. The state of arrears, and consequently classification of the debt, are based on the actual number of days in arrears for each debt.

Debt is classified as non-performing debt, i.e. debt not accruing interest revenues, after 90 days in arrears for debt measured on individual basis, and after 150 days in arrears for debt measured on group basis.

Debt is clasifitied as inferior debt after 60 days in arrears for debt measured on indvidual basis, and after 90 days in arrears for debt measured on group basis.

Housing loans are measured using extent of arrears with respect to such loans.

Credit risk attributes, including specific risk for housing loans, are included on the Board of Directors' Report under Risk management, Basel II: Pillar 3.

Below is disclosure of the recorded debt balance as of December 31, 2012, by credit quality and by credit segment of the Bank:

Consolidated

						Credit segment
Debt quality	Commercial	Housing	Individuals	Governments	Banks	Total
Trouble-free debt, investment grade	34,443	79,265	12,475	1,153	1,650	128,986
Trouble-free debt, other than investment grade	309	-	-	-	11	320
Troubled non-impaired debt.	328	1,599	161	-	-	2,088
Impaired debt	1,569	5	90	-	5	1,669
Total	**36,649**	**80,869**	**12,726**	**1,153**	**1,666**	**133,063**

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

B. Debt [1]

2. Additional information about impaired debt

A. Impaired debt and individual provision

Consolidated

					December 31, 2012
	Balance of impaired debt for which an individual provision has been made [2] [3]	Balance of individual provision [2]	Balance of impaired debt for which no individual provision has been made [2]	Total balance of impaired debT[2]	Contractual principal balance of impaired debt
Borrower activity in Israel					
Public-commercial					
Construction and real estate-construction	682	31	55	737	1,494
Construction and real estate - real estate operations	22	1	1	23	46
Financial services	274	91	28	302	371
Commercial – other	359	107	105	464	909
Total commercial	**1,337**	**230**	**189**	**1,526**	**2,820**
Private individuals-housing loans	5	2	-	5	5
Private individuals-other	21	11	63	84	129
Total public – activity in Israel	**1,363**	**243**	**252**	**1,615**	**2,954**
Banks in Israel	-	-	-	-	-
Government of Israel	-	-	-	-	-
Total activity in Israel	**1,363**	**243**	**252**	**1,615**	**2,954**
Borrower activity overseas					
Public - commercial					
Construction and real estate	36	-	2	38	102
Commercial – other	5	-	-	5	5
Total commercial	**41**	**-**	**2**	**43**	**107**
Private individuals	6	-	-	6	6
Total public – activity overseas	**47**	**-**	**2**	**49**	**113**
Overseas banks	5	-	-	5	5
Overseas governments	-	-	-	-	-
Total activity overseas	**52**	-	**2**	**54**	**118**
Total public	1,410	243	254	1,664	3,067
Total banks	5	-	-	5	5
Total governments	-	-	-	-	-
Total	**1,415**	**243**	**254**	**1,669**	**3,072**
Includes:					
Measured at present value of cash flows	1,279	241	176	1,455	
Debt under troubled debt restructuring	736	56	124	860	

				December 31, 2011
Total public	[4] 1,351	215	236	1,587
Total banks	4	-	-	4
Total governments	-	-	-	-
Total	**1,355**	**215**	**236**	**1,591**
Includes:				
Measured at present value of cash flows	1,291	211	208	1,499
Debt under troubled debt restructuring	796	25	34	830

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with resale agreements. And except from deposites with Bank of Israel
(2) Recorded debt balance.
(3) Debt balance net of accounting write-off, if any was made.
(4) Reclassified.

.Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

B. Debt [(1)]

2. Additional information about impaired debt

B. Average balance and interest revenues

Consolidated

	2012	2011
Average recorded debt balance of impaired loans to the public during reported period	1,562	[(2)] 1,443
Total interest revenues recognized in the reported period with respect to such loans in the period in which it was classified as impaired [(3)]	126	73
Total interest revenues which would have been recognized in the reported period had this credit accrued interest at its original terms	78	[(2)] 73
[(3)]Includes: Interest revenues recognized in accordance with cash basis accounting policy	120	62

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with resale agreements, and except from deposits with Bank of Israel.

(2) Reclassified.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

B. Debt [(1)]
2. Additional information about impaired debt
C. Troubled debt under restructuring
Consolidated

					December 31, 2012
					Recorded debt balance
	Not accruing interest revenues	Accruing [(2)] interest revenues, in arrears 90 days or longer	Accruing [(2)] interest revenues, in arrears 30-89 days	Accruing [(2)] not in arrears	Total [(3)]
Borrower activity in Israel					
Public-commercial					
Construction and real estate - construction	704	-	-	-	704
Construction and real estate - real estate operations	14	-	3	-	17
Financial services	11	-	-	1	12
Commercial - other	47	-	-	10	57
Total commercial	**776**	**-**	**3**	**11**	**790**
Private individuals - housing loans	-	-	-	-	-
Private individuals - other	29	-	3	36	68
Total public - activity in Israel	**805**	**-**	**6**	**47**	**858**
Banks in Israel	-	-	-	-	-
Government of Israel	-	-	-	-	-
Total activity in Israel	**805**	**-**	**6**	**47**	**858**
Borrower activity overseas					
Public - commercial					
Construction and real estate	-	-	-	2	2
Commercial – other	-	-	-	-	-
Total commercial	**-**	**-**	**-**	**2**	**2**
Private individuals	-	-	-	-	-
Total public – overseas activity	**-**	**-**	**-**	**2**	**2**
Overseas banks	-	-	-	-	-
Overseas activity	-	-	-	-	-
Total activity overseas	**-**	**-**	**-**	**2**	**2**
Total public	805	-	6	49	860
Total banks	-	-	-	-	-
Total governments	-	-	-	-	-
Total	**805**	**-**	**6**	**49**	**860**
					December 31, 2011
Total public	[(4)] 728	-	9	[(4)] 93	830
Total banks	-	-	-	-	-
Total governments	-	-	-	-	-
Total	**728**	**-**	**9**	**93**	**830**

(1) Loans to the public, loans to governments, deposits with banks and other debt, except for debentures and securities borrowed or acquired in conjunction with re-sale agreements and except from deposits with bank of Israel.
(2) Accruing interest revenues.
(3) Included in impaired debts.
(4) Reclassified.

As of December 31, 2012, the Bank had no commitments to provide additional credit to debtors subject to troubled debt restructuring, in which credit terms have been revised.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

Reported amounts (NIS in millions)

B. Debt

3. Additional information about housing loans

Balance at year end by loan-to-value ratio (LTV) (1), repayment type and interest type

Consolidated

					December 31, 2012
		Housing loan balance			Off-balance sheet credit risk
		Total (1)	(1) Includes: Bullet / balloon	(1) Includes: Variable interest	Total
Senior lien: LTV ratio	Up to 60%	40,382	1,066	30,227	2,339
	Over 60%	40,392	527	31,084	1,719
Junior lien or no lien		95	2	59	1,440
Total		**80,869**	**1,595**	**61,370**	**5,498**
					December 31, 2011(2)
Senior lien: LTV ratio	Up to 60%	35,232	745	25,691	2,426
	Over 60%	36,957	453	27,878	1,930
Junior lien or no lien		80	-	44	986
Total		**72,269**	**1,198**	**53,613**	**5,342**

(1) Ratio of approved facility upon extending the facility to the property value, as approved by the Bank upon extending the facility.
(2) As from the 2012 financial statements, the Bank applies the Supervisor of Banks' directives with regard to updated disclosure of credit quality of debt and of provision for credit loss. Comparative figures for the previous year were re-classified, in as much as possible, to adapt them to the format required pursuant to the aforementioned directives. For details, see Note 1.J.(8) above.

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

As of December 31, 2012 - Consolidated

Reported amounts (NIS in millions)

F. Balances of loans to the public and off-balance sheet credit risk according to extent of borrower credit risk:

Loan ceiling and credit risk (in NIS thousands)		Number of Borrowers (1)	Credit (2)	On-balance sheet credit risk (3)
	Up to 10	185,675	573	260
Above 10	Up to 20	70,242	489	557
Above 20	Up to 40	109,570	1,547	1,681
Above 40	Up to 80	132,223	4,294	3,347
Above 80	Up to 150	91,057	7,371	2,668
Above 150	Up to 300	69,588	13,372	1,602
Above 300	Up to 600	60,938	25,047	1,935
Above 600	Up to 1,200	39,889	30,068	3,320
Above 1,200	Up to 2,000	8,326	10,862	1,565
Above 2,000	Up to 4,000	2,992	6,859	1,173
Above 4,000	Up to 8,000	1,007	4,181	1,253
Above 8,000	Up to 20,000	531	4,608	1,846
Above 20,000	Up to 40,000	220	3,884	2,220
Above 40,000	Up to 200,000	234	9,680	10,183
Above 200,000	Up to 400,000	43	4,373	7,840
Above 400,000	Up to 512,898	18	3,036	5,925
Total		**772,553**	**130,244**	**47,375**

(1) Number of borrowers is based on total loans and off-balance sheet credit risk.

(2) Off-balance sheet credit and credit risk is stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limitation. Data is in accordance with definition of indebtedness in Regulation 313

Note 4 - Credit risk, loans to the public and provision for credit loss - continued

As of December 31, 2011 - Consolidated

Reported amounts (NIS in millions)

F. Balances of loans to the public and off-balance sheet credit risk according to extent of borrower credit risk - continued:

Loan ceiling and credit risk (in NIS thousands)		Number of Borrowers (1)	Credit (2)(4)	On-balance sheet credit risk (3)
	Up to 10	178,016	251	241
Above 10	Up to 20	69,430	496	534
Above 20	Up to 40	108,576	1,554	1,665
Above 40	Up to 80	124,371	3,923	3,231
Above 80	Up to 150	93,549	7,677	2,566
Above 150	Up to 300	69,706	13,450	1,568
Above 300	Up to 600	57,554	23,563	1,867
Above 600	Up to 1,200	33,162	24,658	2,973
Above 1,200	Up to 2,000	7,209	9,217	1,572
Above 2,000	Up to 4,000	2,788	6,255	1,263
Above 4,000	Up to 8,000	963	3,956	1,257
Above 8,000	Up to 20,000	544	4,552	2,064
Above 20,000	Up to 40,000	201	3,454	2,079
Above 40,000	Up to 200,000	239	9,343	9,596
Above 200,000	Up to 400,000	49	5,696	7,691
Above 400,000	Up to 539,267	20	2,886	5,906
Total		**746,377**	**120,931**	**46,073**

(1) Number of borrowers is based on total loans and off-balance sheet credit risk.

(2) Off-balance sheet credit and credit risk is stated before impact of provision for credit loss, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limitation. Data is in accordance with definition of indebtedness in Regulation 313.

(4) Reclassified

G. In the reported period, the Bank had no debt sales or purchases.

Note 5 - Loans to Governments

As of December 31

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	2012	2011 [(1)]	2012	2011 [(1)]
Loans to Government of Israel	1	3	1	3
Loans to foreign governments	316	193	316	193
Total loans to governments	**317**	**196**	**317**	**196**

Note 6 - Investments in Investees including Details

As of December 31

Reported amounts (NIS in millions)

A. Consolidated

			2012			2011
	Affiliates	Subsidiaries	Total	Affiliates[2]	Subsidiaries	Total
Investment in shares stated on equity basis	27	-	27	21	-	21
Other investments	-	-	-		-	-
Subordinated notes and capital notes	33	-	33	31	-	31
Total investments	**60**	**-**	**60**	**52**	**-**	**52**
Includes:						
Losses accrued since acquisition date	(15)	-	(15)	(15)	-	(15)

B. The Bank

			2012			2011
	Affiliates	Subsidiaries	Total	Affiliates[2]	Subsidiaries	Total
Investment in shares stated on equity basis	27	1,592	1,619	21	1,447	1,468
Other investments	-	-	-	-	-	-
Subordinated notes and capital notes	33	479	512	31	465	496
Total investments	**60**	**2,071**	**2,131**	**52**	**1,912**	**1,964**
Includes:						
Profits (losses) accrued since acquisition date	(15)	820	805	(15)	678	663
Post-acquisition items accrued in shareholders' equity:						
Capital reserve from implementation of directive on impaired debt	-	(16)	(16)	-	(16)	(16)

Bank's share in profits (losses) of investees:

			Consolidated			The Bank
	2012	2011	2010	2012	2011	2010
Bank's share in after-tax operating profit (loss) of investees [1]	-	1	-	142	151	97

(1) No loss from impairment of investees.
(2) Reclassified

Note 6 - Investment in Investees (continued)

Reported amounts (NIS in millions)

	Company detail	Share in capital conferring rights to profits		Share in voting rights	
		As of December 31			
		2012	2011	2012	2011
C. Details of principal investees [(2)]					
1) Subsidiaries					
Bank Yahav for Government Employees Ltd. [(3)]	The Bank	50%	50%	50%	50%
Tefahot Insurance Agency (1989) Ltd.	Insurance agency	100%	100%	100%	100%
Mizrahi International Holding Company Ltd. (B.V. Holland) [(4)]	International holding company.	100%	100%	100%	100%
Mizrahi-Tefahot Factoring Ltd.	Equipment leasing and factoring	100%	100%	100%	100%
Mizrahi Tefahot Underwriting and Issuance (1980) Ltd.	Issuance underwriting	100%	100%	100%	100%
Mizrahi-Tefahot Management Ltd.	Previously managed provident funds	100%	100%	100%	100%
Etgar Investment Portfolio Management Company of the Mizrahi Tefahot Group Ltd.	Portfolio management	100%	100%	100%	100%
Mizrahi Tefahot Issue Company Ltd.	Issuance company	100%	100%	100%	100%
2) Associates					
Psagot Jerusalem Ltd. ("Psagot")	Land for construction	[(9)] 20%	[(9)] 20%	20%	20%
Rosario Capital Ltd. ("Rosario") [(6)]	Underwriting company	19.99%	19.99%	19.99%	19.99%
Mustang Mezzanine Fund	Credit granting	20%	20%[(11)]	-	-
3) Main subsidiary of a subsidiary of United Mizrahi Overseas International Holding Ltd. (BV Holland)					
United Mizrahi Bank (Switzerland) Ltd. [(7)]	Commercial bank	100%	100%	100%	100%

(1) Includes capital notes.
(2) The above list does not include wholly owned and controlled subsidiaries constituting property companies that provide services to the Bank, or companies that provide services to the Bank, and whose assets and liabilities and operating results are included in the Bank's financial statements.
(3) Balance of goodwill with respect to acquisition of Bank Yahav is included on the consolidated balance sheet under Intangible Assets and Goodwill.
(4) The company is incorporated in Holland; for a subsidiary of the Company, see section C. 3).
(5) Includes loss due to devaluation of the shekel, relative to foreign currency exchange rates, totaling NIS 2 million (2011 – profit of NIS 22 million).
(6) Rosario was acquired on October 19, 2010 for consideration of NIS 2 million.
(7) United Mizrahi Bank (Switzerland) Ltd. is a commercial bank registered in Switzerland, and is presented at arm's length on Bank financial statements.
(8) Includes profit due to devaluation of the shekel, relative to CHF exchange rate, amounting to NIS 1 million (2011 – NIS 15 million).
(9) Share of contribution in case of loss is 27%.
(10) Includes goodwill balance included on the consolidated balance sheet under "Intangible assets and goodwill".
(11) Reclassified

Investment in shares at equity value [10]		Goodwill balance [3]		Other capital investments [1]		Contribution to net profit (loss) attributable to equity holders of the banking corporation		Dividends recorded		Other items accrued under shareholders' equity	
As of December 31						For the year ended December 31		As of December 31			
2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011
509	456	69	69	479	452	50	38	-	-	3	(17)
598	529	-	-	-	-	69	71	-	-	-	-
324	321	-	-	-	-	[5] 2	[5] 31	-	-	-	-
					-		1		-		
59	59	-	-	-		1		-		-	-
					-		1		-		
34	33	-	-	-		1		-		-	-
					-		-		-		
28	28	-	-	-		-		-		-	-
					-		3		-		
24	22	-	-	-		2		-		-	-
39	37	-	-	-	-	2	2	-	-	-	-
(16)	(16)	-	-	33	31	-	-	-	-	-	-
2	2	-	-	-	-	-	-	-	-	-	-
40	[11] 32	-	-	-	-	-	-	-	-	-	-
227	223	-	-	-	-	[8] 3	[8] 21	-	-	-	-

Note 6 - Investment in Investees (continued)

Reported amounts (NIS in millions)

D. Balance of goodwill related to subsidiaries – consolidated and the Bank: [(1)]

			December 31, 2012
	Cost	Accumulated amortization	Unamortized balance
Consolidated [(2)]	140	53	87
The Bank	140	53	87

			December 31, 2011
	Cost	Accumulated amortization	Unamortized balance
Consolidated [(2)]	140	53	87
The Bank	140	53	87

(1) The goodwill balance includes goodwill with respect to the acquisition of Tefahot Mortgage Bank Ltd., whose amortized balance as of December 31, 2012 amounted to NIS 14 million (similar to amortized balance as of December 31, 2011 and as of December 31, 2010), and with respect to the acquisition of Adanim Mortgage Bank Ltd., whose amortized balanced as of December 31, 2012 amounted to NIS 4 million (similar to amortized balance as of December 31, 2011 and as of December 31, 2010).

(2) Balance of goodwill with respect to subsidiaries is included on the consolidated balance sheet under Intangible Assets and Goodwill.

Note 7 - Buildings and Equipment

Reported amounts (NIS in millions)

	Consolidated				The Bank			
	Buildings and land (including installations and leasehold improvements)	Equipment, furniture, and vehicles	Software cost	Total	Buildings and land (including installations and leasehold improvements)	Equipment, furniture, and vehicles	Software cost	Total
A. Composition								
Average depreciation rate:	4.4%	14.1%	21.6%		4.1%	16.1%	21.7%	
Cost of the assets -								
December 31, 2011	1,405	880	1,132	3,417	1,219	716	1,112	3,047
Additions in 2012	75	77	120	272	64	64	116	244
Disposals in 2012	-	(23)	-	(23)	-	(23)	-	(23)
Cost of assets as of December 31, 2012	**1,480**	**934**	**1,252**	**3,666**	**1,283**	**757**	**1,228**	**3,268**
Depreciation								
Accrued as of December 31, 2011 (2)	503	659	639	1,801	434	519	626	1,579
Depreciation	47	38	145	230	35	30	142	207
Disposals	-	(23)	-	(23)	-	(23)	-	(23)
Accumulated depreciation as of **December 31, 2012**	**550**	**674**	**784**	**2,008**	**469**	**526**	**768**	**1,763**
Net book value								
As of December 31, 2012 (1)	**930**	**260**	**468**	**1,658**	**814**	**231**	**460**	**1,505**
As of December 31, 2011 (1)	**902**	**221**	**493**	**1,616**	**785**	**197**	**486**	**1,468**

(1) Includes amortized capitalized cost of independently developed computer software as of December 31, 2012 amounting to NIS 35 million - consolidated and for the Bank (December 31, 2011 - NIS 39 million, consolidated and for the Bank).

(2) Accumulated depreciation includes accumulated loss from impairment.

Note 7 - Buildings and Equipment (continued)

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	December 31,		December 31,	
	2012	2011	2012	2011
B. The above assets include assets not used by the Group:				
Not designated for sale	5	6	5	6
Includes - leased to others	5	5	5	5
Designated for sale	-	-	-	-

	Lease term end dates (In years)	Consolidated		The Bank	
		December 31,		December 31,	
		2012	2011	2012	2011
C. Leasing rights to buildings					
Capitalized lease	6-12	76	70	76	70
Non-capitalized lease	6-60	26	11	26	11

D. Management estimates that, on the basis of decisions taken, a loss on realization of the buildings intended for sale is not anticipated beyond the relevant provision recorded.

E. This item includes installations, leasehold rights and payments on account. Part of the buildings and leasing rights, amounting to NIS 297 million on consolidated and to NIS 270 million for the Bank (as of December 31, 2011 - NIS 448 million consolidated and NIS 420 million for the Bank), have yet to be recorded at the Land Registry Office in the name of the Bank or its subsidiaries. Most of these properties are in the process of being registered.

Note 8 - Other Assets

As of December 31

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	December 31,		December 31,	
	2012	2011	2012	2011
Deferred tax asset, net [1]	772	776	721	710
Excess of advance tax payments over current provisions	77	69	75	68
Income receivable	83	97	45	46
Other receivables and debit balances	1,100	[2] 405	1,063	[2] 409
Total other assets	**2,032**	**1,347**	**1,904**	**1,233**

(1) See Note 28.

(2) Reclassified.

Note 9 - Deposits from the Public

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	December 31,		December 31,	
	2012	2011	2012	2011
On-call deposits	19,499	14,633	16,117	11,935
Time and other deposits	106,731	101,668	105,462	98,876
Deposits to savings plans	2,269	2,935	1,635	2,304
Total deposits from the public	**128,499**	**119,236**	**123,214**	**113,115**

Note 10 - Deposits from Banks

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	December 31,		December 31,	
	2012	2011	2012	2011
Commercial banks:				
On-call deposits	284	167	289	768
Term deposits	1,119	1,490	7,624	6,093
Acceptances	291	348	291	348
Special banking entities:				
On-call deposits	-	2	-	2
Total deposits from banks	**1,694**	**2,007**	**8,204**	**7,211**

Note 11 - Debentures and Subordinated Notes

As of December 31

Reported amounts (NIS in millions)

	Average maturity in years [1]	Internal rate of return [2]	Consolidated		The Bank	
			2012	2011	2012	2011
Debentures and subordinated notes not convertible into shares:						
In Israeli currency - non-linked						
Debentures	2.18	5.08%	2,094	2,145	-	-
In Israeli currency, CPI-linked						
Debentures	2.74	2.34%	5,316	3,088	-	-
Subordinated notes [3]	5.78	4.64%	6,629	6,969	4,125	4,575
Total debentures and subordinated notes	**4.35**	**4.08%**	**14,039**	**12,202**	**4,125**	**4,575**

(1) Average maturity is the average of the repayment periods, weighted by the cash flows discounted according to the internal rate of return.
(2) Internal rate of return is the interest rate used to discount the projected flow of payments to the carrying value in the financial statements.
(3) Upon dissolution, the subordinated notes issued by the Bank and included under this item are repayable after all other liabilities.

A. On October 30, 2006, the Bank's Board of Directors approved the issuance of Bank subordinated notes (Series A) which will be deemed complex capital instruments ("Upper Tier II capital"), as the term is defined in Regulation 311 of Proper Banking Conduct Regulations, and in accordance with the approval received from the Supervisor of Banks on November 12, 2006), amounting up to NIS 500 million. The subordinated notes are bonds that, if certain events specified in advance in their terms, will be converted in a forced conversion, according to a formula prescribed in advance, into shares of the Bank. On November 15, 2006, Ma'alot Israel Securities Rating Company Ltd. issued a rating of AA- for the subordinated notes issued. The rating of the subordinated notes in its offering is based on the rating of the Bank's debentures, including subordinated notes, which are rated AA+, with the changes required by the terms of the subordinated notes. Note, that should the Bank issue in the future complex tier I capital, the Bank would maintain an original tier I capital ratio (excluding the complex tier I capital) of no less than 6%. On May 16, 2007, the same rating was approved for capital notes allocated, pursuant to the published prospectus for listing them for trading. On April 5, 2009, Ma'alot announced that in conjunction with a review by S&P of ratings of hybrid instruments world wide, including in Israel, in view of the global financial crisis, the rating of the subordinated capital notes was lowered from AA- to A+.

On September 15, 2009, the Bank and the Trustee for the Bank's subordinated capital notes (Series A) signed an addendum, revising the Deed of Trust dated November 16, 2006, which is effective as of the signing date there of ("the revision"). According to the revision, the capital note section stipulating that interest payment to holders of capital notes would be suspended, inter alia, in case "within a period of six consecutive quarters, the financial statements for the most recent of which was published prior to the date set for payment of such interest, the Bank has not reported a cumulative net profit" (i.e. if the simple summation of quarterly net profit or loss amounts stated on the Bank's financial statements, with respect to six consecutive quarters, should be negative).

Note 11 - Debentures and Subordinated Notes (continued)

As of December 31

Reported amounts (NIS in millions)

The Bank has issued to the public, pursuant to a prospectus dated May 20, 2007, subordinated capital notes (Series A) whose balance as of December 31, 2012 amounted to NIS 1,946 million par value for consideration of NIS 1,644 million.

B. Mizrahi Tefahot Issue Company ("the Company"), a company wholly-owned and controlled by the Bank, issued debentures and subordinated notes links to the costumer price index under the terms of a prospectus to the public, with a par value of NIS 6,809 million and non-links to the consumer price index debenture with a par value of NIS 2,119 as of December 31, 2012. Deposited the proceeds in the Bank earmarked for its day-to-day activities.

To secure fulfillment of the Company's obligations deriving from some of the debentures and subordinated notes (totaling NIS 496 million), the Company undertook to assign all of its rights in each of the deposits that it had deposited in the Bank from the proceeds of securities offered pursuant to the Prospectus in favor of the Trustee of the issued securities.

Additionally, the Bank holds NIS 55 million par value of debentures that were issued by the Company. The Bank is allowed to sell the debentures, at its discretion, on the TASE or off-exchange, and when sold, their terms will be the same as the debentures in circulation.

The Company issued in 2012 additional debentures Series 33 and 35 of NIS 2,057 million par value for consideration of NIS 2,161 million.

On January 21, 2013, after the balance sheet date, the Company issued further debentures Series 29 and 35, amounting to NIS 1,305 million par value for consideration of NIS 1,509 million.

Note 12 - Other Liabilities

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	December 31,		December 31,	
	2012	2011	2012	2011
Provision for deferred taxes, net [(1)]	34	28	34	28
Excess of current provisions for income taxes over advances paid	3	8	-	-
Excess of provision over funding severance pay, retirement and pension [(2)]	669	677	652	660
Deferred income	259	248	259	245
Accrued expenses	204	235	169	207
Provision for unutilized vacations and long- service bonus	113	110	93	93
Guarantees payable	60	52	60	52
Provision for doubtful debts for off-balance sheet and other items	102	114	100	111
Payables for credit card operations	2,889	2,736	1,766	1,680
Other payables and credit balances	545	423	492	378
Total other liabilities	**4,878**	**4,631**	**3,625**	**3,454**

(1) See Note 28.
(2) See Note 16.

Note 13 - Share capital and shareholders' equity [(1)]

A. Details on share capital of the Bank (in NIS):

	Registered		Issued and paid-in	
	December 31,		December 31,	
	2012	2011	2012	2011
Ordinary shares, NIS 0.1 par value [(2)]	40,000,000	40,000,000	[(3)] 22,959,950	[(3)] 22,723,792

(1) For allotment of stock options – see Note 16.A.
(2) The shares are listed for trading on the Tel Aviv Stock Exchange.
(3) Includes 2,500,000 dormant shares, acquired and held by the Bank. For details, see section D. below.

B. On April 3, 2006, the Bank's Board of Directors adopted a resolution on a dividend distribution policy, whereby, provided that the Bank's capital ratio is not less than 10%, dividends will be distributed every year at the rate of 40% of the net operating profit and 80% of the profit from extraordinary items of that year. The dividend distribution policy is in effect as from the year 2006.
On July 23, 2012, the Bank Board of Directors determined, in conjunction with approval of the new strategic five-year plan for 2013-2017, that during the plan term, the Bank's adopted dividend distribution policy would be maintained.
It should be noted that a dividend distribution by the Bank is subject, in addition to the aforesaid, to the provisions of the law and additional limitations.

C. Information on dividend distribution limitations is provided below:

- According to the directives of the Supervisor of Banks with respect to a dividend distribution by banking corporations, a bank may not distribute cash dividends, as long as its non-monetary assets exceed its adjusted shareholders' equity. As of December 31, 2012, the Bank's reported capital exceeds its non-monetary assets by NIS 5,430 million.
- The permit issued to the purchasers of the controlling interest by the Governor of the Bank of Israel stipulates that dividends will not be distributed out of profits accumulated through September 30, 1994, amounting to NIS 100 million (after capitalization into capital reserves in 1998).

D. On May 27, 2009, the Bank received the Supervisor's approval, allowing the Bank to buy back on a non-recurring basis 2,500,000 shares of NIS 0.1 par value of the Bank's issued share capital, subject to statute and to conditions stated in the Supervisor's approval. On July 20, 2009 the Bank's Board of Directors approved a share buy-back plan by the Bank, to acquire up to 2,500,000 shares of NIS 0.1 par value each, subject to terms and conditions stated in the Supervisor's approval. On September 24, 2009, the Bank completed the buy-back, purchasing in total 2,500,000 shares at a cost of NIS 76 million.

Note 13 - Share capital and shareholders' equity [1] - (continued)

The shares held by the Bank are designated to be provided as consideration for exercise of stock options under the stock option plan for VPs - for details see Note 16.A. In accordance with the condition stated in the Supervisor's approval, the Bank would sell all excess shares (if any) immediately after the end of the exercise period of all options allotted pursuant to the stock option plan, i.e. immediately after the seventh anniversary of the date of allotment of options in accordance with the stock option plan. In accordance with a pre-ruling obtained from the Tax Authority, the Bank would not incur any tax liability upon purchase of shares as stated above. The Bank Board of Directors has concluded that buy-back of Bank shares in accordance with the aforementioned buy-back program meets the distribution criteria stipulated in the Corporate Act and is compliant with terms and conditions stipulated in Proper Conduct of Bank Businesses Regulation No. 331. The Board of Directors has reexamined Bank compliance with distribution tests stipulated by in the Corporate Act, as well as compliance with conditions determined by Regulation 331, immediately prior to these acquisitions.

On January 30, 2013, the Bank of Israel allowed the Bank to use the excess shares for its 2013 stock option plan for managers who are not part of Bank management nor Bank officers. The Bank should sell the remaining excess shares (if any) immediately after the end of the exercise period of options pursuant to the stock option plan for managers who are not part of Bank management nor Bank officers, or pursuant to the original plan - whichever is later.

Note 14 – Capital adequacy pursuant to directives of the Supervisor of Banks

Calculated in accordance with Proper Conduct of Banking Business Regulation No. 201-211 "Measurement and Capital Adequacy"

Reported amounts (NIS in millions)

A. Capital adequacy information

		December 31,
	2012	2011
1. Consolidated data		
A. Capital for purpose of calculating minimum capital ratio		
Tier I capital, after deductions	9,145	7,912
Tier II capital, after deductions	5,129	5,722
Total capital	**14,274**	**13,634**
B. Weighted risk asset balances		
Credit risk	98,736	92,973
Market risk	1,119	947
Operating Risk (1)	7,093	7,851
Total weighted risk asset balances	**106,948**	**101,771**

	2012	2011
	In percentage	
C. Ratio of capital to risk elements		
Ratio of Tier I capital to risk elements	8.55	7.77
Ratio of total capital to risk elements	13.35	13.40
Total minimum capital ratio required by the Supervisor of Banks	9.00	9.00
2. Significant subsidiaries		
Bank Yahav for Government Employees Ltd. and subsidiaries there of		
Ratio of Tier I capital to risk elements	9.45	9.04
Total ratio of capital to risk elements	14.22	13.55
Total minimum capital ratio required by the Supervisor of Banks	9.00	9.00

(1) Calculation of cpital adequacy from December 31, 2012 using the standard approach.Until December 31, 2012 the Bank used the basic indicator approach for calculation of operating risk, in accordance with provisions of Proper Conduct of Banking Business Regulation 206 concerning "Measurement and capital adequacy – operating risk". Application of the standard approach to calculation of capital requirement with respect to operating risk has reduced risk assets by NIS 1,348 million, and concurrently increased the Tier I capital ratio by 0.11%, and the overall capital ratio by 0.17%.

Note 14 – Capital adequacy pursuant to directives of the Supervisor of Banks- (continued)

Calculated in accordance with Proper Conduct of Banking Business Regulation No. 201-211 "Measurement and Capital Adequacy"

Reported amounts (NIS in millions)

	December 31,	
	2012	2011
3. Capital components for calculation of capital ratio (on consolidated basis)		
A. Tier I capital		
Paid-up share capital and capital reserves	2,121	2,082
Total cumulative other loss (1)	(3)	(48)
Retained earnings	6,690	5,614
Non-controlling interest of external shareholders in equity of consolidated subsidiaries	441	388
Less:		
Goodwill	(87)	(87)
Tier I capital after Tier I deductions alone	**9,162**	**7,949**
Less:		
Investments in supervisory capital components of banking corporations	(17)	(19)
Other deductions from Tier I capital	-	(18)
Total Tier I capital	**9,145**	**7,912**
B. Tier II capital		
1. Upper Tier II capital		
General provision for doubtful debts (2)	110	110
Complex capital instruments	1,896	1,869
2. Lower Tier II capital		
Subordinated notes	3,140	3,780
3. Deductions from Tier II capital		
Investments in supervisory capital components of banking corporations	(17)	(19)
Other deductions from Tier II capital	-	(18)
Total Tier II capital	**5,129**	**5,722**

(1) Excludes net gain from cash flow hedges.

(2) The amount defined, through December 31, 2010, as a general provision for doubtful debts, is part of upper Tier II capital and is not deducted from loans to the public.

Note 14 – Capital adequacy pursuant to directives of the Supervisor of Banks- (continued)

B. On June 30, 2010, the Supervisor of Banks issued a letter to banking corporations, on capital policy for interim periods, in which they are required to adopt a target for Tier I capital ratio by December 31, 2010, to be no less than 7.5%. Concurrently, the banks are required to submit to the Supervisor a work plan for achieving this target. The letter further stipulates that in absence of prior approval by the Supervisor of Banks, the bank shall not distribute dividends if the target has not been achieved, or if such dividend distribution would cause the bank not to achieve the target. This directive is intended to clarify the expectations of the Supervisor of Banks from banking corporations in the interim period, pending adaptation of the Supervisor's directives to emerging changes in recommendations of the Basel Committee.

C. On October 25, 2010, the Bank's Board of Directors decided that the target core capital ratio would be no less than 7.5%. Further, the Board of Directors resolved to direct Bank management to act so as to maintain appropriate safety margins, in order to ensure that the core capital ration shall be no less than the foregoing. The Bank Board of Directors further resolved that the overall capital adequacy ratio shall be no less than 12.5%.

D. The Bank is in compliance with all capital requirements pursuant to directives of the Supervisor of Banks, and in accordance with limits set by the Board of Directors. Bank policy requires regular review of the ration of capital to risk elements, and taking action whenever this ratio approached the limits set by the Board of Directors, in order to minimize the risk of exceeding said limits. Failure to comply with minimum capital requirements would require the Bank or Group companies to reduce risk exposure, in order to reduce the capital requirement in line with existing capital. Reducing risk exposure may be associated with a cost, due to the need to enter into transactions under sub-optimal conditions.

E. On March 28, 2012, the Supervisor of Banks issued a directive to all banking corporations, citing a higher minimum core capital ratio than the one currently required. According to the directive, all banking corporations would be required to achieve a minimum core capital ratio of 9% by January 1, 2015. In addition, large banking corporations, whose total consolidated balance sheet assets exceed 20% of total balance sheet assets for the Israeli banking sector, would be required to achieve a minimum core capital ratio of 10% by January 1, 2017. The directive with regard to a minimum core capital ratio of 10% does not apply to the Bank.

F. On December 31, 2012, the Advisory Committee on Banking Business received draft amendments to Proper Conduct of Banking Business Regulations 201-211 (concerning adoption of Basel III directives with regard to supervisory capital and with regard to risk assets). Proper Conduct of Banking Business Regulation 202 (Capital measurement and adequacy - supervisory capital) adopts the Basel III recommendations in Israel.

The Bank is preparing for immediate application of the Supervisor of Banks' anticipated requirements, as listed in the draft regulations.

Note 14 – Capital adequacy pursuant to directives of the Supervisor of Banks- (continued)

G. Upper Tier II capital includes complex capital notes amounting to NIS 1,896 million as of December 31, 2012, and to NIS 1,869 million as of December 31, 2011. A summary of terms and conditions there of follows:

- Capital notes bear interest and are linked to the CPI.
- Capital notes are not secured by liens on Bank assets or by any other collateral.
- Under certain circumstances, the Bank may suspend interest payments for the notes.
- The Bank would be required to convert the subordinated capital notes into ordinary Bank shares, using a pre-determined formula, if the Bank's ratio of Tier I capital to risk elements would decrease significantly, if the Bank's retained earnings balance would turn negative, or if the Bank's external auditors should raise significant doubt with regard to the continued status of the Bank as a going concern - all under conditions stipulated in the capital note terms.
- The Bank's obligation to make payments for the subordinated capital notes would be subordinate to all other Bank obligations to creditors of all types, including to holders of subordinated capital notes issued or to be issued by the Bank and/or its subsidiaries, and would only outrank the rights of shareholders to a refund of excess Bank assets upon its dissolution.

H. Tier II capital includes subordinated notes amounting to NIS 3,140 million as of December 31, 2012, compared to NIS 3,780 million as of December 31, 2011. A summary of terms and conditions follows:

- Subordinated notes bear interest and are linked to the CPI.
- The notes shall rank below all other Bank liabilities which are not specified as having an equal or lower ranking, as stated above.
- The notes are not secured by any collateral, are not subject to any lien, and the Bank may not receive any lien with respect there to, to secure any loan granted by the Bank or by its subsidiary.
- The notes are not subject to early repayment nor to any change in terms, without prior written consent of the Supervisor of Banks.

I. For details of issuance of complex capital notes and subordinated notes, see Note 11 above.

Note 15 - Liens

A. Stock exchange members are required to deposit a system of collateral to secure the fulfillment of all the obligations of their customers and the obligations of the other stock exchange members that are not members of the clearinghouse and their customers, to the stock exchange clearinghouse, with respect to transactions executed through the stock exchange clearinghouse, and to secure their share in the risks fund for this activity as discussed below in Note 19.D.1).
In the framework of system of collateral, the Bank deposits liquid collateral, as provided below:

1) Government debentures of the Bank were deposited in the account opened by the stock exchange clearinghouse in its name ("collateral account in clearinghouse") as collateral in favor of the stock exchange clearinghouse, at the full value of the customers' obligations plus the Bank's share in the risk fund. As of December 31, 2012, no debentures were deposited with the clearinghouse (as of December 31, 2011 – NIS 103 million).

2) Additionally, in the account opened by the stock exchange clearinghouse in its name for the Bank in another bank, cash is deposited that the Bank furnishes as collateral, as well as the cash to be paid as income on securities that were deposited in the account, the clearinghouse's collateral or cash originating in any other financial right deriving from the said securities, including cash proceeds from their sale. As of December 31, 2012, deposits to this account amounted to NIS 34 million (as of December 31, 2011 - NIS 21 million).

3) The accounts discussed in Par. 1 and 2 above have been pledged under a first-level fixed lien in favor of the stock exchange clearinghouse.

B. Stock exchange members are required to deposit a system of collateral that secures the fulfillment of their obligations relating to MAOF transactions that are executed by them or their customers or by stock exchange members that are not members of the MAOF Clearinghouse, and to secure their share in the risks fund covering this activity, as provided below in Note 19.D. 2).
Accordingly, the Bank was required to deposit only liquid collateral, for the full exposure of activity in derivatives and for its share in the risks fund, as provided below:

1) In the account opened in the TASE Clearinghouse in the name of the MAOF Clearinghouse ("main MAOF collateral account"), government bonds of the Bank were deposited as security in favor of the MAOF Clearinghouse, at the full value of the requirements for customers' collateral plus the Bank's share in the risks fund. The value of debentures deposited as of December 31, 2012 is NIS 387 million (as of December 31, 2011 – NIS 980 million).

2) Additionally, in the account opened by the MAOF clearinghouse in its own name on behalf of the Bank with another bank, cash is deposited that the Bank furnishes as collateral, as well as the cash to be paid as income on securities that will be deposited in a major clearinghouse collateral account or cash originating in any other financial right deriving from these securities, including cash proceeds from their sale. As of December 31, 2012, deposits to this account amounted to NIS 99 million (as of December 31, 2011 - NIS 95 million).

3) The aforementioned accounts in sections 1-2 are pledged under a floating and fixed lien to benefit the MAOF clearinghouse.

Note 15 - Liens (continued)

C. The Bank of Israel operates the Real Time Gross Settlement system (RTGS) - a system which allows customers to transfer in real time NIS-denominated amounts between bank accounts in the same bank or between banks.

The Bank of Israel provides daily and intra-day credit for participants in the RTGS system against specific liens on Bank debentures in the Bank of Israel account with the stock exchange clearinghouse. As of December 31, 2012 and as of December 31, 2011, no debentures were deposited in this account.

D. In accordance with the requirement of the regulatory agencies in the U.S., the Bank's branch there pledged securities worth USD 25 million as of the balance sheet date (as of December 31, 2011– USD 22 million), used to secure deposits of the public or to comply with other government regulations, or to fulfill other government directives. Most of the amount pledged, which as of December 31, 2012 amounted to USD 15 million (as of December 31, 2011 – USD 21 million), relates to a demand by U.S. regulatory agencies to secure 7.5% of the branch's liabilities, as defined by the authorities there.

E. To secure credit facilities provided to the Bank by the Bank of Israel, the Bank has pledged an account containing foreign securities. As of December 31, 2012 the Bank didn't pledge foreign securities(as of December 31,20111-USD 100 thousand).

F. Debentures acquired by Bank Yahav, held at Bank HaPoalim, are pledged by a floating lien in favor of the Bank of Israel.

G.

		December 31,
	2012	2011
Sources of securities which have been received and which the Bank may sell or pledge, at fair value excluding set-offs:		
Securities received in transactions for borrowing securities against cash	207	136

These securities have been provided as collateral to the Bank, which may sell or pledge them.

Note 16 - Employees' Rights

A. The employment terms of the vast majority of the Group's employees and managers (except for those detailed in paragraphs B - I below) are determined in accordance with the provisions of collective labor agreements. Liabilities to these employees are covered by regular deposits to pension, provident and severance-pay funds, which release the Bank from severance-pay liabilities provided for those employees by law. With respect to several previous Tefahot employees, the Bank is legally absolved from making compensation payments only for the period commencing on February 1, 2006 (with respect to previous Tefahot management, the Bank is absolved from its obligation commencing January 1, 2006). with respect to the Banks' obligation until the end of 2005 (until January 2006 for previous Tefahot management), the Bank has contributed to pension and retirement funds and has recorded a provision for the difference between liability and contributions.

B. A small group of employees who retired in the past is entitled to a fixed monthly pension from the Bank. Employees who retired from the Bank prior to June 30, 1997 are entitled to pension payments from the Bank for certain salary components. Bank retirees are also eligible to receive non-pension benefits. The Bank's liability for these payments is covered by provisions, based on an actuarial calculation.

C. The Bank's President ("the President") entered into an agreement with the Bank ("the agreement") whereby he would be employed by the Bank for a term of 5 years and 4 months starting December 1, 2008 and ending April 1, 2014. The current agreement is further to the previous 5-year agreement commencing on March 29, 2004. The agreement was approved by the Bank Board of Directors on November 30, 2008, after receiving approval of the Bank Audit Committee and then accepting the recommendation by the Compensation Committee concerning the principles of major terms of employment of the President.

Pursuant to the agreement, the President is entitled to receive upon termination of his employment for any reason whatsoever (other than termination under specific circumstances determined in the employment agreement) severance pay equal to 200% of his most recent monthly salary upon termination of his employment for each year of service to the Bank, a 3-month adjustment period as well as current amounts with respect to pension payments deposited on his behalf at the usual rates. The financial statements included provisions for these liabilities.

The Bank may terminate the agreement with the President with 4 months' prior notice (instead of six months under the previous agreement).

In the agreement, the President waived the annual bonus to which he is entitled under the previous agreement, starting on the termination date of the previous agreement.

For details of options to acquire Bank shares allotted to the President under the new agreement see Note 16.A. 1.

Note 16 - Employees' Rights (continued)

D. Personal employment contracts have been signed with a group of senior employees, entitling them to a special bonus upon termination, under the circumstances prescribed in the agreements that could, in a few years' time, reach seventeen months' salary for certain employees with high seniority. These employees are also eligible, upon retirement, to other sums and rights, as accrued in their favor in various funds. The Bank has no intention to terminate any of these senior Bank employees.
The Bank's liability for these payments is covered by provisions, based on an actuarial calculation.

E. Several senior employees are eligible upon their retirement to an acclimation grant of six months' salary, for which a provision was recorded in the financial statements.

F. Two senior employees are eligible upon their retirement to increased severance pay of 150% of their last monthly salary multiplied by the number of their years of employment in the Bank, beyond the amounts deposited in funds, as required by law. Alternatively, these employees are entitled, provided they have passed age 55, to budgetary pension until they reach retirement age. for which a provision was recorded in the financial statements.

G. A pension agreement was signed with an employee of an overseas affiliate of the Bank, whereby they would be entitled to a monthly pension for 180 months from retirement, after aggregating 20 years' seniority in the Bank, and under certain other circumstances prescribed in the agreements. The actuarial value of the provision recorded in the financial statements for this liability was calculated using a discount rate of 6%, which corresponds with the yield on the monies deposited for payment of these pension rights, and assuming that the annual pay raise will be at a rate of 3.5%.

H. Some Bank employees who take early retirement, sometimes receive, upon retirement, higher amounts than their entitlement pursuant to the law and to agreements. Sometimes the Bank pays these employees a pension until they reach the full retirement age. According to the Supervisor of Banks' directive, an actuarial reserve with respect to these payments is included on the financial statements.

I. On September 16, 2009, a special collective bargaining agreement was signed with the employee union - clerks sector, whereby the special collective bargaining agreement signed on April 27, 2006 was extended by a further 5 years, from January 1, 2011 through December 31, 2015. This agreement was approved by the Bank Board of Directors on October 19, 2009.

Highlights of this agreement are as follows:

- Extension of the "employment constitution" through December 31, 2015.
- Maintaining absolute calm labor relations during the agreement period. The obligation to maintain calm labor relations shall not apply in case of a labor dispute involving all bank sector employees in Israel.
- Specification of dispute resolution mechanisms: negotiation, facilitation, arbitration.

Note 16 - Employees' Rights (continued)

- The Bank committed not to terminate for economic reasons any permanent employees during the term of the agreement. This commitment does not apply to individual termination for cause, incompatibility or regulatory changes.
- Enactment of a voluntary retirement program by up to 200 employees during the term of the agreement, starting in 2011. Management has the right to veto any specific voluntary retirement application without being required to provide any justification.
- Management has the option of terminating up to 50 permanent employees during the term of the agreement period, for incompatibility reasons, starting in 2011.

The cost of the voluntary retirement program is covered by an actuarial reserve.

J. Long-service bonuses

Bank employees are entitled to special lump-sum bonuses upon attaining thirteen and eighteen years of service. A provision for these liabilities was recorded in the financial statements according to an actuarial calculation based on past experience and the likelihood that the employee will still be employed by the Bank on the vesting date.

K. Provisions for long-service bonuses and the voluntary retirement agreement were based on actuarial calculations using a 4% discount rate. taking into account a future real pay increase of 2.5% except for retired employees who are not entitled to a real increase in the pension paid to them.

L. Bonuses for officers

1. On May 19, 2008, the Board of Directors, after receiving approval of the Audit Committee, resolved to approve a bonus framework for Bank officers, other than Board members including the Chairman of the Board of Directors and other than the Bank President (hereinafter in this section "the officers") for each of the years 2008-2012 (inclusive) (each of these years hereinafter in this section "report year") inter alia by way of creating a pool for bonus payments to officers. On March 2, 2009, an amendment to the bonus plan was approved, concerning the date on which the Board of Directors would discuss bonus payments pursuant to the aforementioned plan (hereinafter: "the bonus plan"). On October 26, 2010, an amendment of the bonus plan was approved, with regard to the annual rate of return for each of the years 2010 through 2012.
2. In accordance with the bonus plan, the Board of Directors would determine in each reported year, the number of monthly salaries to be deposited for each officer of the Bank, to a fund designated for bonus payment to officers. For any reported year, the number of monthly salaries would be based on the Bank's average operating net profit return on equity, as defined in the bonus plan (hereinafter: "the annual return ratio"). Accordingly, the Board of Directors shall determine in each report year the number of salaries to be transferred to the pool, if the annual return ratio should range from 10.5% (12% prior to the amendment dated October 26, 2010) to the maximum return ratio to be determined by the Board of Directors for that report year (hereinafter in this section: "the maximum return ratio") based on a scale to be determined by the Board of Directors for this purpose.

Note 16 - Employees’ Rights (continued)

3. Shortly prior to publication of the Bank's annual report for the report year, and based on the expected annual return ration for the report year, pursuant to the Bank's draft annual statements for the report year, subject to approval there of by law, the Board of Directors shall decide, after discussing recommendations of the Bank President and subject to approval by the Audit Committee (in as much as required by law), as stated below -

   a) Should the annual return ratio for the report year range from 10.5% (12% prior to the amendment dated October 26, 2010) to the maximum return ratio set by the Board of Directors for that report year, the Board of Directors shall determine the bonus amount to be paid out of the bonus payment pool, for the report year, provided that no single officer be paid a bonus higher than 12 salaries for the report year.

   b) Should the annual return ratio for the report year be lower than 10.5% (12% prior to the amendment dated October 26, 2010), the Board of Directors shall determine the bonus amount to be paid (if any). Furthermore, should the annual return ratio for the report year be higher than the maximum ratio set by the Board of Directors for the report year, then the Board shall determine the bonus amount to be paid for the report year.

4. Furthermore, in accordance with the bonus plan, the Board of Directors may decide, at its discretion, to have bonuses paid to officers with respect to net profit from extraordinary items at the Bank for any report year.

5. For details of the stock option plan for VPs, in which the offerees waived their right to receive a bonus as mentioned above, see Note 16.A.2).

M. At Bank Yahav, the Bank customarily makes up the difference, for employees eligible to receive severance pay, between the employee's most recent salary multiplied by their number of years in service and the amount accrued in their name in provident funds. Retiring Bank Yahav employees are also entitled, under the labor agreement, to partial redemption of unused sick days.

To some of its employees, Bank Yahav committed to deliver, upon termination of their employment for any reason, the severance pay component of recognized provident funds (pursuant to Section 14 of the Severance Pay Act). The Bank is not required to make up the difference for these employees between the employee's most recent salary multiplied by their number of years in service and the amount accrued in their name in the aforementioned provident funds.

Bank Yahav has committed to pay senior executives' salary during an adjustment period, should their employment be terminated by the Bank. To some, the Bank has committed to release to them the severance pay component accrued in the pension fund, in addition to their final salary multiplied by their number of years in service.

Bank Yahav committed to make monthly payments through the official retirement age to two senior executives who retired from Bank Yahav, with this payment linked to changes in the salary of Bank Yahav's CEO.

Bank Yahav's commitments are covered by appropriate reserves and provisions based on actuarial calculation.

Note 16 - Employees' Rights (continued)

N. The provisions and deposits for employees' rights to pension, severance pay and acclimation grants are included in "other liabilities", as follows (reported amounts, NIS in millions):

	Consolidated		The Bank	
	2012	2011	2012	2011
Amount of provision	781	777	662	669
Amount of reserve[1]	112	100	10	9
Excess of provision over funding	**669**	**677**	**652**	**660**

(1) The Bank and its subsidiaries may not withdraw the funded amounts other than for severance payment.

O. Provisions for employees' rights to paid leave, redemption of unused sick leave and seniority grants are included in "other liabilities" as follows (in reported amounts, NIS in millions):

	Consolidated		The Bank	
	2012	2011	2012	2011
Provision for vacation	91	88	83	81
Provision for seniority bonuses	22	22	10	12
Provision for redemption of sick leave [1]	14	12	-	-

(1) Presented under Other Liabilities, under Other Accounts Payable.

Note 16.A. – Share-based Payment Transactions

1. Stock option plan for the President

On November 30, 2008, the Bank Board of Directors, following approval by the Bank Audit Committee at its meeting on November 30, 2008, resolved to approve the new stock option plan for allotment of options by private offer to the Bank President.

In conjunction with the stock option plan, the Bank allotted to a trustee on February 1, 2009, on behalf of the President, at no cost 5,571,381 options, each exercisable into one Bank ordinary share of NIS 0.1 par value, subject to adjustment for distribution of bonus shares, rights issuance, split or reverse split of shares or dividend distribution. Assuming full exercise of all options, and assuming allotment of the maximum possible number of exercised shares, all options allotted under the stock option plan would be equal to 2.44% of the Bank's issued share capital and voting rights (after allotment of the full number of exercised shares), and assuming full dilution – 1.54% of the Bank's issued share capital and voting rights.

Should the President elect to exercise the options, in whole or in part, by way of allotment against the benefit amount, as stated below, then the assumption with regard to allotment of the maximum number of exercised shares is merely theoretical, since in this way the full amount of resulting exercised shares would not be allotted, but rather only enough shares to reflect the monetary benefit amount inherent in the options, as stated below.

The trustee would grant the options to the President, subject to provisions of the stock option plan, in 5 lots (4 equal lots of 1,114,276 options each, and one lot of 1,114,277 options) on April 1 of each year between 2010-2014. Should employment of the President by the Bank be terminated prior to April 1, 2014 (i.e. prior to conclusion of the term of the new employment agreement), not by the President and not under specific circumstances set forth in the employment agreement, the President would be eligible to receive on his final day in office as Bank President the remainder of the options included in the lots not yet granted to him by that date.

The President may exercise the options as from the grant date through April 1, 2014 or through the second anniversary of his last day in office as Bank President, whichever is later, but no later than April 1, 2016.

The exercise price for each option is NIS 21.18, plus linkage differentials to the Consumer Price Index starting on the date on which the Board of Directors approved the stock option plan and up to the CPI known upon the exercise date. The exercise price has been determined based on the closing price of Bank shares on the stock exchange on November 9, 2008 (the trading day preceding the date on which the recommendation by the Compensation Committee was received, as stated above). Note that the exercise price is higher by 9.5% than the closing price of Bank shares on the stock exchange on November 27, 2008 (NIS 19.35), when the exercise price was discussed by the Audit Committee, which was the trading day preceding the date on which the Board of Directors approved the employment agreement and the stock option plan.

Note 16.A. – Share-based Payment Transactions (continued)

The options may be exercised, in whole or in part, in any of the following ways:

1) Each option would be exercised into one Bank share (subject to adjustments), in exchange for payment of the full exercise price.

2) The Bank would allot, at no cost, a number of shares whose market value based on the closing price for Bank shares on the stock exchange on the trading day preceding the exercise date would be equal to the monetary benefit amount inherent in the options upon the exercise date.

The Bank applies IFRS 2 "Share-based Payment". In accordance with provisions of this standard, the Bank records in its financial statements an expense equal to the fair value of the options. The expense, for each of the 5 lots, is allocated over the period from the allotment date to the grant date for that lot. The theoretical fair value of the options was calculated using the Black & Scholes model. Calculation of the fair value accounts for terms and conditions of the plan as well as for the following data and assumptions:

1) Calculation of the fair value does not account for the fact that the options would not be listed for trading on the stock exchange, nor does it account for blocking of the options, as prescribed bythe stock option plan.

2) The exercise price for each option, for the purpose of this calculation, is NIS 21.18 as stated above.

3) It was assumed that all options would be exercised on the last day of the exercise period, i.e. expected duration of 7 years and 4 months.

4) The standard deviation used for this calculation was 27.06%, which was calculated by measuring the historic standard deviation of share prices on the stock exchange over a period equal to the expected duration of the options, ending on November 27, 2008.

5) The risk-free interest rate used for the calculation - 3.88% - was calculated based on interest rate quotes for risk-free, CPI-linked NIS-denominated assets traded on the stock exchange as of November 27, 2008 for a term equal to the expected duration for exercise of each option.

6) The exercise price is adjusted for dividends, hence the dividend yield assumed for this calculation is %.

Based on the assumptions described above, the fair value of all options to be granted to the President under the new stock option plan is NIS 38.6 million (NIS 44.6 million, including payroll tax at a rate of 15.5% as it stood at that time).

The options would be allotted under the "wages" track, pursuant to the Section 102 of the Income Tax Ordinance. Therefore, any benefit arising to the President from exercise of these options shall be taxed at the marginal tax rate applicable to the President upon exercise of the options. The Bank would be required to pay the payroll tax with respect to the benefit arising to the President from exercise of the options under the new stock option plan. Furthermore, upon payment of the tax with respect to this benefit by the President, the Bank may make a deduction for tax purposes with respect to the aforementioned options based on the effective tax rate applicable upon the exercise date.

Note 16.A. – Share-based Payment Transactions (continued)

2. Stock option plan for VPs

On March 29, 2009, the Bank Board of Directors, after obtaining approval of the Bank Audit Committee, decided to approve a plan for allotment of options by a private placement which does not constitute a material private placement (hereinafter: "the plan") to nine officers of the Bank who are VP members of Bank management (of which one offeree who had served as VP, took unpaid leave from the Bank and currently serves as the CEO of Bank Yahav for Government Employees Ltd.) (hereinafter: "the offerees"). The Board of Directors further decided, after obtaining approval of the Audit Committee, that allotment of the options is contingent on the Supervisor of Banks allowing the Bank to buy back at least 1,400,000 shares of NIS 0.1 par value in the Bank's issued share capital. For details of 2,500,000 Bank shares bought back by the Bank in accordance with approval of the Supervisor of Banks, see Note 13.D.

Each offeree pursuant to the stock option plan consented, by their own choice, that should the Bank allot to them stock options pursuant to the plan, they would be excluded from the framework bonus plan for Bank officers for each of the years 2009 through 2012, and would not be included in a bonus plan for Bank officers for 2013, should such plan be approved by the Bank.

In conjunction with the stock option plan, the Bank allotted on June 23, 2009 to the trustee, on behalf of the offerees, 5,850,000 options which would not be listed for trading on the stock exchange. The options may each be exercised for one Bank ordinary share of NIS 0.1 par value for no consideration, subject to terms and conditions of the plan. Allotment of the maximum number of exercise shares is only theoretical. Upon the exercise date of the options, offerees would not be allotted the full number of exercised shares arising from the options which the offerees may exercise, pursuant to plan terms, but rather only the number of shares reflecting the monetary benefit inherent in the aforementioned options.

The exercise price for each option allotted to offerees pursuant to the plan is NIS 21.18, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was determined based on the closing price of Bank shares on the stock exchange on November 9, 2008 - which was also the basis for the exercise price of options allotted to the Bank President as stated above. Note that the exercise price is higher than the closing price of Bank shares on the stock exchange on March 26, 2009 - the most recent trading day prior to the date on which the Board of Directors approved the stock option plan.

The options allotted to the trustee for each offeree, in accordance with the plan, were allotted in 5 equal lots. Each lot shall vest upon vesting dates on each anniversary of the allotment date, from the first anniversary (for the first lot) to the fifth anniversary (for the fifth lot).

Note 16.A. – Share-based Payment Transactions (continued)

In accordance with the original plan, each offeree would be eligible to exercise options included in the exercise lot which vested on any date, provided that the net operating profit return on the Bank's average shareholders' equity for the reported year preceding said vesting date should be 10% or higher. Should the aforementioned rate of return for the reported year prior to this vesting date be lower than 10%, the offeree may not exercise at any time the lot vested on that vesting date. The Bank's Board of Directors would be qualified, at its own discretion and subsequent to approval by the Audit Committee, to exclude the impact of non-recurring or extraordinary events from calculation of the annual rate of return for any reported period.

On October 26, 2010, the Board of Directors resolved, after receiving approval of the Audit Committee, to update the vesting eligibility rate for each of the stock option plans for VPs for lots vesting in 2011, 2012, 2013 and 2014, where the vesting eligibility would be determined based on annual rate of return in reported fiscal 2010, 2011, 2012 and 2013, respectively. Accordingly, it was resolved that the vesting eligibility rate for each of the stock option Plans for VPs would be reduced from 10% to 9%.

The fair value (theoretical benefit value) of a single option in any lot of options was calculated in accordance with IFRS 2, using the Black & Scholes model. The theoretical benefit value of each lot is recognized in the Bank's accounts over the vesting term. The following assumptions were used for calculation of fair value:

- The exercise price for each option , for the purpose of this calculation, is NIS 21.18.
- The expected term to exercise of each lot was assumed to be the average of the vesting period of each lot (from one year for lot 1, to five years for lot 5) and the plan term (7 years).
- Standard deviation for each lot was calculated using historical daily returns of the share price on the stock exchange over a period equal to the expected term of each lot.
- The risk-free interest rate was calculated based on quoted yield to maturity information for CPI-linked government debentures traded on the stock exchange, as published on March 26, 2009.
- The exercise price is adjusted for dividends, hence the dividend yield assumed for this calculation is 0%.
- For calculation of fair value, it was assumed that net operating profit return on the Bank's average shareholders' equity in each plan year would be 10% or higher.
- Calculation of the fair value does not account for the fact that the options would not be listed for trading on the stock exchange.

The number of options which the offerees may exercise shall be reviewed upon each reporting date, based on information available at that time. The results of this review may reduce the expense charged in the Bank's financial statements with respect to options over plan years, but may not change the fair value of each option included in each lot.

Note 16.A. – Share-based Payment Transactions (continued)

On November 9, 2009, the Bank Board of Directors, after obtaining approval by the Bank Audit Committee, resolved to approve allotment of a further 1,104,999 options, under identical terms and conditions with the exception of the exercise price, to two VPs appointed subsequent to the approval date of the stock option plan for VPs. The exercise price for each option allotted to the two additional offerees pursuant to the plan is NIS 29.85, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was based on the closing price of Bank shares on the stock exchange on November 8, 2009, the most recent trading day prior to the date of plan approval by the Board of Directors. The fair value (theoretical benefit value) of a single option warrant in any lot of additional options approved was calculated in accordance with IFRS 2, using the Black & Scholes model. The theoretical benefit value of each lot is recognized in the Bank's accounts over the vesting period.

On March 21, 2010, the Bank's Board of Directors, after receiving approval of the Bank's Audit Committee, resolved to approve allotment of a further 520,000 options, under identical terms and conditions with the exception of the exercise price, to a VP appointed on January 18, 2010. The exercise price for each option allotted to the additional offeree pursuant to the plan is NIS 35.35, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was based on the closing price of Bank shares on the stock exchange on March 21, 2010, the most recent trading day prior to the date of plan approval by the Board of Directors. The plan consists of 4 lots, vesting concurrently with lots 2-5 of the original plan for VPs. The fair value (theoretical benefit value) of a single option in any lot of the additional options approved was calculated in accordance with Accounting Standard no. 24, using the Black & Scholes model. The theoretical benefit value of each lot is recognized in the Bank's accounts over the vesting period.

On April 30, 2012, the Bank's Board of Directors resolved, after approval by the Bank Audit Committee, to approve a plan for award of 238,333 options to an officer who was hired by the Bank in March 2012. The option plan is based on the principles of the stock option plan for VPs at the Bank, as described above.

Options would be awarded in 2 lots vesting on three dates ("vesting dates") starting on the first anniversary (lot 1) and second anniversary (lot 2) of the award date, subject to net profit rate of return on average equity for each year preceding each vesting date, as stated above. The exercise price for each option pursuant to the plan is NIS 33.79, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was based on the closing price of Bank shares on the stock exchange on April 29, 2012, the most recent trading day prior to the date of plan approval by the Board of Directors. The fair value (theoretical benefit value) of a single option in any lot of the additional options approved was calculated in accordance with IFRS 2, using the Black & Scholes model. The theoretical benefit value of the options in this allotment, calculated in accordance with accounting rules of IFRS 2, amounts to NIS 1.7 million (NIS 1.9 million including Payroll Tax).

Calculation of the total theoretical benefit value for the allotment is based on assumptions regarding the number of options that the offeree would be eligible to exercise based on management estimate of the range of annual rates of return, as stated above, as well as based on Bank management assessment with regard to the average resignation rate of plan offerees, meaning that some of the options to be granted would expire due to the offerees retirement. The theoretical benefit value of each lot is recognized in the Bank's accounts over the vesting period.

Note 16.A. – Share-based Payment Transactions (continued)

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted:

	Lot 1	Lot 2	Lot 3	Lot 4	Lot 5	Total
Allotment approved on March 29, 2009						
Number of options (in thousands)	910	910	910	650	650	(1) 4,030
Annualized standard deviation	32.75%	32.04%	30.95%	30.11%	30.27%	
Exercise price (in NIS)	21.18	21.18	21.18	21.18	21.18	
Risk-free interest rate	0.65%	0.77%	0.92%	1.09%	1.28%	
Term to exercise (in years)	4.1	4.6	5.1	5.6	6.1	
Fair value per single option	4.78	5.02	5.19	5.39	5.77	
Total fair value per lot (NIS in thousands)	4,346	4,569	4,724	3,504	3,751	20,894
Allotment approved on November 9, 2009						
Number of options (in thousands)	65	260	260	260	260	1,105
Annualized standard deviation	35%	34%	33%	33%	32%	
Exercise price (in NIS)	29.85	29.85	29.85	29.85	29.85	
Risk-free interest rate	0.46%	0.65%	0.83%	1.02%	1.20%	
Term to exercise (in years)	3.6	4.1	4.6	5.1	5.6	
Fair value per single option	8.00	8.39	8.73	9.16	9.44	
Total fair value per lot (NIS in thousands)	520	2,181	2,270	2,381	2,455	9,807
Allotment approved on March 21, 2010						
Number of options (in thousands)	130	-	-	-	-	(2) 130
Annualized standard deviation	34.9%	33.9%	33.2%	32.6%	-	
Exercise price (in NIS)	35.35	35.35	35.35	35.35	-	
Risk-free interest rate	0.85%	1.10%	1.17%	1.38%	-	
Term to exercise (in years)	3.8	4.3	4.8	5.3	-	
Fair value per single option	9.77	10.28	10.72	11.24	-	
Total fair value per lot (NIS in thousands)	1,270	-	-	-	-	1,270
Allotment approved on April 30, 2012						
Number of options	108,333	130,000	-	-	-	238,333
Annualized standard deviation	30.23%	32.27%	-	-	-	
Exercise price (in NIS)	33.79	33.79	-	-	-	
Risk-free interest rate	0.2%	0.3%	-	-	-	
Term to exercise (in years)	2.7	3.2	-	-	-	
Fair value per single option	6.63	7.75	-	-	-	
Total fair value of award (NIS in thousands)	718	1,008	-	-	-	1,726

(1) After expiration of 1,820 thousand options with respect to four VPs who resigned from the Bank.
(2) After expiration of 390 thousand options with respect to a VP who resigned from the Bank.

Note 16.A. – Share-based Payment Transactions (continued)

Details of the number of stock options and their exercise price are as follows:

	2012		2011		2010	
	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)
Outstanding at year start	4,804,999	23.65	5,656,999	24.76	5,654,999	23.32
Granted during the year (1)	238,333	33.85	-	-	520,000	35.60
Forfeited during the year	520,000	22.07	520,000	35.96	-	-
Exercised during the year(2)	1,671,666	22.58	332,000	21.73	518,000	21.75
Outstanding at year end	2,851,666	25.46	4,804,999	23.65	5,656,999	24.76

(1) The weighted average fair value of stock options granted in 2012 was NIS 7.24 and in 2010 - NIS 10.50.

(2) The weighted average share price upon exercise of options into shares during 2012 was NIS 34.37 (2011 – NIS 36.01; 2010 - NIS 35.24).

Stock options in circulation at year end by exercise price range:

	December 31, 2012			December 31, 2011			December 31, 2010		
Exercise price range (NIS)	17-25	26-32	33-42	17-25	26-32	33-42	17-25	26-32	33-42
Number of options	1,790,000	823,333	238,333	3,700,000	1,104,999	-	4,032,000	1,104,999	520,000
Weighted average exercise price (in NIS)	22.07	30.42	33.85	21.76	29.98	-	21.75	30.68	35.60
Weighted average remaining contractual term (in years)	3.48	3.48	3.48	-	-	-	5.48	5.48	5.48
Of which vested:				4.49	4.48	-	-	-	-
Number of options	490,000	303,333	-	970,000	324,999	-	392,000	64,999	-
Weighted average exercise price (in NIS)	22.07	30.42	-	21.76	29.98	-	21.75	30.68	-

3. Stock option plan for employees

A. On July 19, 2005, after approval by the Bank's Audit Committee and Board of Directors, stock options were granted to Executive Management, division and sector managers, and department and branch managers of the Bank and its subsidiaries ("the offerees") in conjunction with a compensation planned aimed at encouraging them to contribute to business development of the Bank and its subsidiaries, and to align interests of the offerees with that of the Bank and its subsidiaries. Allotted in accordance with the plan will be up to 12,000,000 options, which may be exercised for shares, NIS 0.1 par value each. As of December 31, 2009, a total of 11,379,103 options have been allotted to 338 offerees.

Note 16.A. – Share-based Payment Transactions (continued)

The options will vest in 3 annual installments (25%, 35% and 40%), each at the end of every year from the date the options are granted. For some of the offerees, the number of options that will vest in each installment will be determined subject to meeting certain threshold conditions of “quality level”.

The offerees will be eligible to exercise the options until the end of four years from the date granted, and to receive for them shares in the Bank at a value totaling the balance of the theoretical profit included in the options on the exercise date. The exercise price of the shares will be based, for each grant, on the stock market value of the Bank’s shares on the grant date plus linkage to the CPI, and is subject to adjustments deriving from the distribution of cash dividends and/or bonus shares, as well as issuance of rights of the Bank.

The theoretical value of the benefit for the 12,000,000 options that were approved, in accordance with accounting treatment rules of Accounting Standard 24, is estimated at NIS 53 million. The value of the benefit, which includes salary tax, as recorded on the Bank’s financial statements, is estimated at June 30, 2005 at NIS 62 million. The value of this benefit will be included in the Bank’s books of account, beginning from the third quarter of 2005 and will be spread over 3 years.

The theoretical value of the benefit was determined using the Black and Scholes model. Annualized standard deviation for the 4-year period preceding the original allocation date is 22.5%. The option term in the model was set at 4 years (based on the last exercise date). The risk-free interest rate was based on the gross yield to maturity for “Galil” and “Sagi” government bonds, CPI-linked and bearing fixed interest, as published by the Bank of Israel in June 2005 near the allocation date, and based on the option term, amounting to 2.7%. No assumptions were made as to dividend distribution.

On March 2, 2009, the Bank Board of Directors, having received approval from the Bank Audit Committee dated March 2, 2009, resolved to extend the exercise period of all options granted to employees and officers of the Bank and its subsidiaries in accordance with this stock option plan, not yet exercised into Bank shares, by a further 2 years. The extension of the exercise period for these options is only a benefit to offerees who own the options under the plan.

Pursuant to Accounting Standard no. 24 "Share-based Payment", the Bank is required to recognize the impact of extension of option exercise periods, which increases their fair value, equal to the difference between the option's fair value immediately after extension of the exercise period and their fair value immediately before the decision by the Board of Directors (hereinafter: "the additional fair value").

Note 16.A. – Share-based Payment Transactions (continued)

The additional fair value for the options has been calculated using the Black & Scholes model, based on the following data and assumptions:

- The exercise price for the options are as determined upon the original grant date, adjusted for the Consumer Price Index known upon approval of the extension.
- The share price was determined using the closing price for Bank shares on the stock exchange on the trading day preceding the data of approval by the Board of Directors of this extension.
- The expected duration to exercise for the options included in lots fully vested as of the valuation date were assumed to be half of the remaining period from the date of approval of this extension until expiration of the options included in said lot.
- The standard deviation is based on historical volatility of Bank shares, in accordance with the expected terms to option exercise, and has been calculated separately for each lot.
- The interest rate for calculation of the option fair value is based, in accordance with Accounting Standard no. 24, on interest rates for risk-free, CPI-linked NIS-denominated assets as published by the Bank of Israel from time to time, for a term equal to the expected duration until each lot is exercised.
- The exercise price is adjusted for dividends, hence the dividend yield assumed for this calculation is 0%.
- The fair value calculation assumes that the options would not be listed for trading on the stock exchange.

Below are data used for this calculation:

			As of March 01, 2009
	Original exercise period	Modified exercise period	Total change
Annualized standard deviation	41.1% - 57.4%	34.6% - 44.1%	
Bank share price (in NIS)	17.80	17.80	
Average effective exercise price (in NIS)	19.03	19.03	
Discount rate	1.84%	1.64%	
Average expected duration to exercise (in years)	0.31	1.31	
Average value per 1 option (in NIS)	1.59	3.30	1.71
Number of options (in millions)	6.6	6.6	
Total option value (NIS in millions)	10.5	21.9	11.4

The additional fair value of the options due to extension of their exercise period (6,632,256 options allotted in accordance with the plan and not yet then exercised or expired), amounting to NIS 11.4 million (NIS 13.2 million including payroll tax), was recorded as an expense on the Bank's 2009 financial statements.

Note 16.A. – Share-based Payment Transactions (continued)

Details of the number of stock options and their exercise price are as follows:

	2012		2011		2010	
	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)
Outstanding at year start	393,922	28.24	1,049,492	22.18	1,810,704	22.36
Granted during the year	-	-	-	-	-	-
Forfeited during the year	-	-	-	-	-	-
Exercised during the year [(1)]	393,922	28.37	655,570	18.51	761,212	21.67
Outstanding at year end	-	-	393,922	28.24	1,049,492	22.18

(1) The weighted average share price upon exercise of options into shares during 2012 was NIS 34.07 (2011 – NIS 36.01; 2010 - NIS 35.24).

Stock options outstanding at year end by exercise price range:

	December 31, 2012		December 31, 2011		December 31, 2010	
Exercise price range (NIS)	17-25	26-32	17-25	26-32	17-25	26-32
Number of options	-	-	100,740	293,182	754,043	295,449
Weighted average exercise price (in NIS)	-	-	23.44	29.88	19.25	29.65
Weighted average remaining contractual term (in years)	-	-	0.6	0.9	0.7	1.9
Of which vested:						
Number of options	-	-	100,740	293,182	754,043	295,449
Weighted average exercise price (in NIS)	-	-	23.44	29.88	19.25	29.65

B. On May 19, 2008, the Bank Board of Directors resolved, after obtaining approval of the Bank Audit Committee and the recommendations of the Bank Board's Compensation and Management Committees with regard to principles of the stock option plan, to approve a stock option plan ("the plan" or "the option plan") for Bank officers, branch-, department- and affiliate managers as well as for other employees of the Bank and its subsidiaries – as provided by the option plan and in the outline published on June 8, 2008 ("the outline"). No stock options would be granted, pursuant to the plan, to members of the Bank's Board of Directors, including the Chairman of the Board, nor to the Bank's President.

The option plan is for a term of 5 years and 90 days, starting on the date of option allotment in accordance with the plan. In conjunction with approval of the plan, the Board of Directors resolved that the number of options to be used as a pool for allotment of options pursuant to the plan, would include 32,500,000 options, registered in the owner's name, not listed for trading on the Tel Aviv Stock Exchange, which would be granted at no cost to offerees, and which may be exercised for up to 32,500,000 Bank ordinary shares, NIS 0.1 par value each, subject to adjustments as stated in the plan, and subject to achieving the stated eligibility conditions.

Note 16.A. – Share-based Payment Transactions (continued)

The options allotted to the trustee for each offeree, in accordance with the plan, will be allotted in 5 equal lots. The vesting period for each such lot would be at the end of each of the 1st, 2nd, 3rd, 4th and 5th anniversaries of the allotment date of options pursuant to the plan, respectively. The number of exercised shares, as stated above, is the maximum number of shares arising from exercise of all options which may be allotted pursuant to the plan. However, the number of options which the offerees may actually exercise, pursuant to terms of the plan, will be based on the net operating profit return on the Bank's average shareholders' equity, up to an annual rate of return equal to 18% (under the original plan), based on the exercise eligibility formula, as prescribed by the option plan.

The personal eligibility rate for each offeree included in the group of branch-, department- and affiliate managers (as defined in the plan) to exercise the options granted to them in accordance with the plan will be determined, in addition to the aforementioned, also by the quality rating assigned to them, as stated in the option plan.

Furthermore, allotment of the full number of exercised shares is merely theoretical, since in actual fact the offerees would not be allotted the full number of exercised shares arising from the options which the offerees may exercise, pursuant to plan terms, but rather only the number of shares reflecting the monetary benefit inherent in the aforementioned options, as stated in the option plan.

The exercise price for each of the options allotted pursuant to the plan was determined based on the closing price of the Bank's ordinary shares on the stock exchange on July 7, 2008 – the final trading day preceding the allotment date of options to the offeree. The exercise price is NIS 25.15 plus linkage differentials to the Consumer Price Index starting on the allotment date, adjusted for dividends to be distributed by the Bank.

On July 8, 2008, 28,625,300 options were allotted, in accordance with the plan, at no cost to 313 offerees who are Bank officers, branch-, department- and affiliate managers, as well as other employees of the Bank and its subsidiaries, as stated in the option plan.

The options pursuant to the plan were allotted in accordance with terms of the work income track, via a trustee, pursuant to provisions of Section 102 of the Profit Tax Ordinance (New Version), 1961 including all relevant regulations, rules, circulars and guidelines issued.

On November 24, 2008, the Board of Directors resolved, after receiving approval of the Bank's Audit Committee dated November 23, 2008, to extend the exercise periods of all options allotted in accordance with the plan and the framework, and which would be allotted thereby in the future, by 24 months.

Accordingly, the exercise period for each lot of the options allotted or to be allotted pursuant to the option plan, including all options allotted on July 8, 2008, would be extended by 24 months, to end after 7 years and 90 days from the date of allotment, rather than after 5 years and 90 days from the date of allotment, as stated in the original plan.

For recording the expense in the Bank's financial statements, and based on the strategic 5-year plan, as stated above, management has estimated a range of annual rates of return (though not linear) for each plan year (2008-2012) up to an 18% annual rate of return in 2012. Using this range, the number of options each offeree may exercise out of the total number of options granted to them in accordance with the plan has been estimated, as stipulated by the framework.

Note 16.A. – Share-based Payment Transactions (continued)

On November 24, 2008, the Bank Board of Directors approved an updated strategic plan, whereby the Bank's objective is to achieve an annual rate of return of 18% in 2013, rather than in 2012, as determined by the strategic plan prior to its update. Accordingly, management estimate with regard to the framework of annual rates of return has been updated for the purpose of recording this expense in the Bank's financial statements.

On October 26, 2010, the Board of Directors resolved, after receiving approval of the Audit Committee, to update the vesting eligibility formula for each of the stock option plans for VPs for lots vesting in 2011, 2012 and 2013, where the vesting eligibility would be determined based on the annual rate of return in reported fiscal 2010, 2011 and 2012, respectively. In accordance with the updated formula, the offerees would be eligible to exercise in full the options in each lot, provided that the average net profit rate of return on equity would be 15%, compared to 18% in the original formula, all as stated in the update to the stock option plan. For recording the expense on the Bank's financial statements, Bank management has estimated the trend of annual rates of return (though not linear) for each of the years 2010, 2011 and 2012. Using this trend, the number of options each offeree may exercise out of the total number of options granted to them in accordance with the plan were reestimated for lots vesting in 2011 through 2013. The update to the vesting eligibility formula, as well as management estimates with regard to the trend of annual rates of return, are arithmetical results of the Board of Directors' decision with regard to the capital adequacy target. Pursuant to this reestimation, it is expected that the number of options exercisable by each offeree, as stated above, would be similar to the number of options exercisable by each offeree based on previous estimates by management, and that the change would not materially impact the Bank's financial statements.

The theoretical benefit value of the options currently allotted, as stated above, calculated in accordance with accounting principles in IFRS 2, including adjustment of option value with respect to the change in option terms and the impact of change in number of options expected to vest, as of December 31, 2012 amounted to NIS 154 million (NIS 179 million including payroll tax); Calculation of the total theoretical benefit value for the allotment is based on assumptions regarding the number of options that offerees would be eligible to exercise based on management estimate of the range of annual rates of return, as stated above, as well as based on Bank management assessment with regard to the average resignation rate of plan offerees, meaning that some of the options to be granted would expire due to the offerees retirement. Adjustment of the benefit value with respect to the change in option terms is the difference between the fair value of the options, under their original terms, upon the date of change in these terms, and their fair value under the new terms upon the same date. The theoretical benefit value is recorded in the Bank's accounts starting on the grant date and over a 5-year period. Management estimates with regard to the range of annual rates of return and resignation rates are reviewed and updated on an on-going basis, and the extent of total expenditure recorded in the financial statements is updated accordingly.

The theoretical benefit value of the options was determined using the Black and Scholes model. Standard deviation was separately calculated for each lot, based on daily share prices in a period equal to the expected life of each lot. The option term in the model was determined based on the average time between the vesting period and the option expiration date (Simplified Approach). The rate of risk-free interest is determined based on gross yield to maturity for CPI-linked government bonds bearing fixed interest ("Galil"), for a term equal to the expected life to exercise of each lot.

Note 16.A. – Share-based Payment Transactions (continued)

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted on July 8, 2008, as of the grant date and as of the date of modification of terms:

	Lot 1	Lot 2	Lot 3	Lot 4	Lot 5
As of July 8, 2008 – the grant date					
Annualized standard deviation	26.05%	26.23%	25.44%	24.71%	24.98%
Exercise price (in NIS)	25.15	25.15	25.15	25.15	25.15
Interest	2.03%	2.20%	2.34%	2.47%	2.58%
Term to exercise (in years)	3.10	3.60	4.10	4.60	5.10
Fair value per single option	5.25	5.79	6.13	6.45	6.95
As of November 24, 2008 – for the original exercise period (exercise price unchanged)					
Annualized standard deviation	29.84%	29.22%	28.76%	28.35%	27.43%
Share price	15.70	15.70	15.70	15.70	15.70
Exercise price	25.70	25.70	25.70	25.70	25.70
Interest	4.08%	4.11%	4.13%	4.15%	4.16%
Term to exercise (in years)	2.75	3.25	3.75	4.25	4.75
Fair value per single option	1.17	1.43	1.69	1.94	2.12
As of November 24, 2008 – for the updated exercise period (exercise price unchanged)					
Annualized standard deviation	28.76%	28.35%	27.43%	26.77%	27.18%
Share price	15.70	15.70	15.70	15.70	15.70
Exercise price	25.70	25.70	25.70	25.70	25.70
Interest	4.13%	4.15%	4.16%	4.18%	4.19%
Term to exercise (in years)	3.75	4.25	4.75	5.25	5.75
Fair value per single option	1.69	1.94	2.12	2.32	2.66
Value of change per single option	0.52	0.51	0.43	0.38	0.54
Cumulative value per single option	5.77	6.30	6.56	6.83	7.49

On June 29, 2009, the Bank Board of Directors approved allotment of a further 2,263,700 options, under identical terms and conditions except for the exercise price, to two officers and 37 additional employees. The exercise price for each option allotted to offerees pursuant to the plan is NIS 23.6, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was based on the closing price of Bank shares on the stock exchange on June 28, 2009, the most recent trading day prior to the date of plan approval by the Board of Directors.

Based on assumptions with regard to number of options which offerees would be eligible to exercise, as stated above, the theoretical benefit value of the options amounted to NIS 11 million (NIS 12 million including payroll tax).

Note 16.A. – Share-based Payment Transactions (continued)

On November 9, 2009, the Bank Board of Directors, after receiving approval of the Bank Audit Committee, resolved to approve allotment of a further 1,085,432 options, under identical terms and conditions with the exception of the exercise price, to four officers of the Bank. The exercise price for each option allotted to the four additional offerees pursuant to the plan is NIS 29.85, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was based on the closing price of Bank shares on the stock exchange on November 8, 2009, the most recent trading day prior to the date of plan approval by the Board of Directors. The fair value (theoretical benefit value) of a single option in any lot of the additional options approved was calculated in accordance with Accounting Standard no. 24, using the Black & Scholes model. The theoretical benefit value of each lot is recognized in the Bank's accounts over the vesting period.

Based on assumptions with regard to number of options which offerees would be eligible to exercise, as stated above, the theoretical benefit value of the options amounted to NIS 6 million (NIS 7 million including payroll tax).

On October 26, 2010, the Bank's Board of Directors, after receiving approval of the Bank's Audit Committee, resolved to approve a plan for allotment of a further 1,652,500 options, under identical terms and conditions with the exception of the exercise price, to 41 employees, including one officer of the Bank. Options would be allotted in 3 equal lots vesting on three dates ("vesting dates") starting on the first anniversary (lot 1), second anniversary (lot 2) and third anniversary (lot 3) of the allotment date, subject to net profit rate of return on average equity for each year preceding each vesting date, as stated above. The exercise price for each option allotted to the additional offerees pursuant to the plan is NIS 35.40, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank.

The exercise price was based on the closing price of Bank shares on the stock exchange on October 25, 2010, the most recent trading day prior to the date of plan approval by the Board of Directors. The fair value (theoretical benefit value) of a single option in any lot of the additional options approved was calculated in accordance with Accounting Standard no. 24, using the Black & Scholes model. The theoretical benefit value of each lot is recognized in the Bank's accounts over the vesting period.

Based on assumptions with regard to number of options which offerees would be eligible to exercise, as stated above, the theoretical benefit value of the options amounted to NIS 11 million (NIS 13 million including payroll tax).

On October 3, 2011, the Bank's Board of Directors, after receiving approval of the Bank's Audit Committee, resolved to approve a plan for allotment of a further 701,300 options, under identical terms and conditions with the exception of the exercise price, to 31 employees, including one officer of the Bank. Options would be allotted in 2 equal lots vesting on three dates ("vesting dates") starting on the first anniversary (lot 1) and second anniversary (lot 2) of the allotment date, subject to net profit rate of return on average equity for each year preceding each vesting date, as stated above. The exercise price for each option allotted to the additional offerees pursuant to the plan is NIS 31.62, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank.

The exercise price was based on the closing price of Bank shares on the stock exchange on October 2, 2011, the most recent trading day prior to the date of plan approval by the Board of Directors. The fair value (theoretical benefit value) of a single option in any lot of the additional options approved was calculated in accordance with IFRS 2, using the Black & Scholes model.

The theoretical benefit value of the options in this allotment, calculated in accordance with accounting rules of Accounting Standard no. 24, amounts to NIS 4.4 million (NIS 5 million including Payroll Tax).

The options were allotted to employees on November 17, 2011.

Note 16.A. – Share-based Payment Transactions (continued)

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted on June 28, 2009, on November 9, 2009, on October 26, 2010 and on October 3, 2011:

	Lot 1	Lot 2	Lot 3	Lot 4	Total
Allotment approved on June 29, 2009					
Number of options (in thousands)	566	566	566	566	2,264
Annualized standard deviation	34.27%	33.29%	32.65%	31.55%	
Exercise price (in NIS)	23.60	23.60	23.60	23.60	
Risk-free interest rate	0.91%	1.20%	1.50%	1.71%	
Term to exercise (in years)	3.7	4.2	4.7	5.2	
Fair value per single option	6.40	8.75	7.15	7.45	
Total fair value per lot, NIS in thousands	3,622	3,820	4,046	4,194	15,682
Allotment approved on November 9, 2009					
Number of options (in thousands)	248	279	279	279	1,085
Annualized standard deviation	34.88%	33.92%	33.15%	32.45%	
Exercise price (in NIS)	29.85	29.85	29.85	29.85	
Risk-free interest rate	0.49%	0.68%	0.87%	1.05%	
Term to exercise (in years)	3.7	4.2	4.7	5.2	
Fair value per single option	8.05	8.43	8.82	9.21	
Total fair value per lot, NIS in thousands	2,000	2,352	2,461	2,569	9,382

	Lot 2	Lot 3	Lot 4	Total
Allotment approved on October 26, 2010				
Number of options (in thousands)	551	551	551	1,653
Annualized standard deviation	36.73%	35.07%	33.88%	
Exercise price (in NIS)	35.40	35.40	35.40	
Risk-free interest rate	0.22%	0.38%	0.53%	
Term to exercise (in years)	3.2	3.7	4.2	
Fair value per single option	9.23	9.55	9.92	
Total fair value per lot (NIS in thousands)	5,084	5,260	5,464	15,808
Allotment approved on October 3, 2011				
Number of options (in thousands)		351	351	702
Annualized standard deviation		31.93%	36.90%	
Exercise price (in NIS)		31.62	31.62	
Risk-free interest rate		1.07%	1.13%	
Term to exercise (in years)		2.71	3.21	
Fair value per single option		6.93	8.63	
Total fair value per lot (NIS in thousands)		1,700	2,783	4,483

Note 16.A. – Share-based Payment Transactions (continued)

Details of the number of stock options and their exercise price are as follows:

	2012		2011		2010	
	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)
Outstanding at year start	15,841,665	27.24	20,342,887	27.05	25,275,389	26.42
Granted during the year(1)	-	-	701,300	31.59	1,652,500	35.43
Forfeited during the year	1,033,267	26.94	4,732,979	27.26	6,242,656	26.28
Exercised during the year(2)	5,547,512	26.68	469,543	6.79	342,346	26.21
Outstanding at year end(3)	9,260,886	28.22	15,841,665	27.24	20,342,887	27.05

(1) The weighted average fair value of stock options granted in 2011 , upon the measurement date, was NIS 7.30 and in 2010 - NIS 8.49.
(2) The weighted average share price upon exercise of options into shares during 2012 was NIS 36.26 (2011 – NIS 36.16; 2010 - NIS 36.34).
(3) Stock options outstanding at year end by exercise price range:

	December 31, 2012			December 31, 2011			December 31, 2010		
Exercise price range (NIS)	17-25	26-32	33-42	17-25	26-32	33-42	17-25	26-32	33-42
Number of options	704,422	6,730,713	1,735,751	1,323,678	13,346,010	1,171,977	1,716,153	16,974,234	1,652,500
Weighted average exercise price (in NIS)	24.28	26.99	34.79	23.93	26.82	35.79	24.77	26.46	35.43
Weighted average remaining contractual term (in years)	2.98	2.80	3.17	3.98	3.81	4.18	4.98	4.79	5.18
Of which vested:									
Number of options	255,522	1,998.733	900,603	245,878	2,357,790	182,978	601,528	856,434	-
Weighted average exercise price (in NIS)	24.28	27.09	34.99	23.93	26.56	35.79	24.77	26.39	-

Note 17 - Assets and Liabilities by Linkage Basis - Consolidated

As of December 31, 2012

Reported amounts (NIS in millions)

	Israeli currency		In foreign currency [1]			Non-monetary items [2]	Total
	Non-linked	CPI-linked	US dollars	Euro	Other currencies		
Assets							
Cash and deposits with banks	14,068	170	1,802	166	465	-	16,671
Securities	5,487	251	2,396	757	31	119	9,041
Securities borrowed or bought in conjunction with repurchase agreements	15	192	-	-	-	-	207
Loans to the public, net	66,160	49,221	8,908	2,568	1,794	-	128,651
Loans to Governments	-	-	103	213	1	-	317
Investments in investees	33	-	-	-	-	27	60
Buildings and equipment	-	-	-	-	-	1,658	1,658
Intangible assets and goodwill	-	-	-	-	-	87	87
Assets with respect to derivatives	2,653	318	358	74	115	-	3,518
Other assets	1,525	388	51	2	16	50	2,032
Total assets	**89,941**	**50,540**	**13,618**	**3,780**	**2,422**	**1,941**	**162,242**
Liabilities							
Deposits from the public	83,411	21,823	16,369	4,179	2,717	-	128,499
Deposits from banks	196	532	688	222	56	-	1,694
Deposits from the Government	13	62	32	-	-	-	107
Debentures and subordinated notes	2,094	11,945	-	-	-	-	14,039
Liabilities with respect to derivatives	2,645	271	572	269	16	-	3,773
Other liabilities	3,846	663	58	8	19	284	4,878
Total liabilities	**92,205**	**35,296**	**17,719**	**4,678**	**2,808**	**284**	**152,990**
Difference	**(2,264)**	**15,244**	**(4,101)**	**(898)**	**(386)**	**1,657**	**9,252**
Impact of hedging derivatives:							
Derivatives (other than options)	400	(400)	-	-	-	-	-
Non-hedging financial derivatives:							
Derivatives (other than options)	2,342	(6,886)	3,984	355	205	-	-
Net in-the-money options (in terms of underlying asset)	(577)	-	91	381	89	16	-
Net out-of-the-money options (in terms of underlying asset)	(147)	-	64	94	7	(18)	-
Total	**(246)**	**7,958**	**38**	**(68)**	**(85)**	**1,655**	**9,252**
Net in-the-money options (capitalized par value)	88	-	370	(394)	(64)	-	-
Net out-of-the-money options (capitalized par value)	(457)	-	(141)	538	60	-	-

(1) Includes linked to foreign currency.
(2) Includes derivatives whose base relates to a non-monetary item.

Note 17 - Assets and Liabilities by Linkage Basis - Consolidated (continued)

As of December 31, 2011

Reported amounts (NIS in millions)

	Israeli currency		In foreign currency [1]			Non-monetary items [2]	
	Non-linked	CPI-linked	US dollars	Euro	Other currencies		Total
Assets							
Cash and deposits with banks	12,273	418	2,816	158	307	-	15,972
Securities	5,128	302	1,835	1,051	31	85	8,432
Securities borrowed or bought in conjunction with repurchase agreements	12	124	-	-	-	-	136
Loans to the public, net	60,559	44,651	[3] 10,064	2,004	2,015	-	119,293
Loans to Governments	-	-	-	196	-	-	196
Investments in investees	31	-	-	-	-	[3] 21	52
Buildings and equipment	-	-	-	-	-	1,616	1,616
Intangible assets and goodwill	-	-	-	-	-	87	87
Assets with respect to derivatives	[3] 1,591	162	1,117	23	222	-	3,115
Other assets	[3] 1,018	199	97	-	5	28	1,347
Total assets	**80,612**	**45,856**	**15,929**	**3,432**	**2,580**	**1,837**	**150,246**
Liabilities							
Deposits from the public	72,554	23,046	16,832	4,272	2,532	-	119,236
Deposits from banks	283	681	844	212	(13)	-	2,007
Deposits from the Government	11	107	34	-	-	-	152
Debentures and subordinated notes	2,075	10,127	-	-	-	-	12,202
Liabilities with respect to derivatives	1,772	187	1,710	172	123	-	3,964
Other liabilities	3,521	711	50	2	25	322	4,631
Total liabilities	**80,216**	**34,859**	**19,470**	**4,658**	**2,667**	**322**	**142,192**
Difference	**396**	**10,997**	**(3,541)**	**(1,226)**	**(87)**	**1,515**	**8,054**
Impact of hedging derivatives:							
Derivatives (other than options)	670	(670)	-	-	-	-	-
Non-hedging financial derivatives:							
Derivatives (other than options)	2,125	(5,084)	2,416	511	32	-	-
Net in-the-money options (in terms of underlying asset)	(1,712)	-	1,018	724	(7)	(23)	-
Net out-of-the-money options (in terms of underlying asset)	(274)	-	371	(39)	(56)	(2)	-
Total	**1,205**	**5,243**	**264**	**(30)**	**(118)**	**1,490**	**8,054**
Net in-the-money options (capitalized par value)	6	-	103	(118)	(67)	76	-
Net out-of-the-money options (capitalized par value)	(92)	-	(337)	448	32	(51)	-

(1) Includes linked to foreign currency.
(2) Includes derivatives whose base relates to a non-monetary item.
(3) Reclassified.

Note 17 - Assets and Liabilities by Linkage Basis - Consolidated (continued)

As of December 31, 2012

Reported amounts (NIS in millions)

	Israeli currency		In foreign currency [1]			Non-	
		CPI-	US		Other	monetary	
	Non-linked	linked	dollars	Euro	currencies	items [2]	Total
Assets							
Cash and deposits with banks	11,378	93	1,612	121	382	-	13,586
Securities	2,787	238	2,383	757	-	119	6,284
Securities borrowed or bought in conjunction with repurchase agreements	15	192	-	-	-	-	207
Loans to the public, net	60,663	48,591	8,766	2,527	1,759	-	122,306
Loans to Governments	-	-	103	213	1	-	317
Investments in investees [3]	33	478	-	-	-	1,620	2,131
Buildings and equipment	-	-	-	-	-	1,505	1,505
Intangible assets and goodwill	-	-	-	-	-	87	87
Assets with respect to derivatives	2,653	318	358	74	115	-	3,518
Other assets	1,401	393	51	2	7	50	1,904
Total assets	**78,930**	**50,303**	**13,273**	**3,694**	**2,264**	**3,381**	**151,845**
Liabilities							
Deposits from the public	74,017	26,954	15,742	3,924	2,577	-	123,214
Deposits from banks	3,243	3,228	1,211	405	117	-	8,204
Deposits from the Government	-	61	32	-	-	-	93
Debentures and subordinated notes	-	4,125	-	-	-	-	4,125
Liabilities with respect to derivatives	2,645	271	572	269	16	-	3,773
Other liabilities	2,615	657	48	2	19	284	3,625
Total liabilities	**82,520**	**35,296**	**17,605**	**4,600**	**2,729**	**284**	**143,034**
Difference	**(3,590)**	**15,007**	**(4,332)**	**(906)**	**(465)**	**3,097**	**8,811**
Impact of hedging derivatives:							
Derivatives (other than options)	400	(400)	-	-	-	-	-
Non-hedging financial derivatives:							
Derivatives (other than options)	2,342	(6,886)	4,089	367	88	-	-
Net in-the-money options (in terms of underlying asset)	(578)	-	92	381	89	16	-
Net out-of-the-money options (in terms of underlying asset)	(146)	-	64	94	7	(19)	-
Total	**(1,572)**	**7,721**	**(87)**	**(64)**	**(281)**	**3,094**	**8,811**
Net in-the-money options (capitalized par value)	88	-	370	(394)	(64)	-	-
Net out-of-the-money options (capitalized par value)	(457)	-	(141)	538	60	-	-

(1) Includes linked to foreign currency.
(2) Includes derivatives whose base relates to a non-monetary item.
(3) Includes investments in overseas subsidiaries totaling NIS 325 million.

Note 17 - Assets and Liabilities by Linkage Basis - Consolidated (continued)

As of December 31, 2011

Reported amounts (NIS in millions)

	Israeli currency		In foreign currency [1]			Non-monetary items [2]	Total
	Non-linked	CPI-linked	US dollars	Euro	Other currencies		
Assets							
Cash and deposits with banks	9,690	142	2,740	149	153	-	12,874
Securities	2,549	223	1,822	1,051	-	85	5,730
Securities borrowed or bought in conjunction with repurchase agreements	12	124	-	-	-	-	136
Loans to the public, net	55,481	43,937	[4] 9,991	1,927	1,986	-	113,322
Loans to Governments	-	-	-	196	-	-	196
Investments in investees [3]	31	452	13	-	-	[4] 1,468	1,964
Buildings and equipment	-	-	-	-	-	1,468	1,468
Intangible assets and goodwill	-	-	-	-	-	87	87
Assets with respect to derivatives	1,591	162	1,117	23	215	-	3,108
Other assets	907	199	97	1	1	28	1,233
Total assets	**70,261**	**45,239**	**15,780**	**3,347**	**2,355**	**3,136**	**140,118**
Liabilities							
Deposits from the public	64,427	25,887	16,340	4,061	2,400	-	113,115
Deposits from banks	2,591	2,851	1,322	384	63	-	7,211
Deposits from the Government	-	107	34	-	-	-	141
Debentures and subordinated notes	-	4,575	-	-	-	-	4,575
Liabilities with respect to derivatives	1,771	187	1,710	172	116	-	3,956
Other liabilities	2,370	700	41	2	19	322	3,454
Total liabilities	**71,159**	**34,307**	**19,447**	**4,619**	**2,598**	**322**	**132,452**
Difference	**(898)**	**10,932**	**(3,667)**	**(1,272)**	**(243)**	**2,814**	**7,666**
Impact of hedging derivatives:							
Derivatives (other than options)	670	(670)	-	-	-	-	-
Non-hedging financial derivatives:							
Derivatives (other than options)	2,125	(5,084)	2,434	555	(30)	-	-
Net in-the-money options (in terms of underlying asset)	(1,712)	-	1,018	724	(7)	(23)	-
Net out-of-the-money options (in terms of underlying asset)	(274)	-	371	(39)	(56)	(2)	-
Total	**(89)**	**5,178**	**156**	**(32)**	**(336)**	**2,789**	**7,666**
Net in-the-money options (capitalized par value)	6	-	103	(118)	(67)	76	-
Net out-of-the-money options (capitalized par value)	(92)	-	(337)	448	32	(51)	-

(1) Includes linked to foreign currency.
(2) Includes derivatives whose base relates to a non-monetary item.
(3) Includes investments in overseas subsidiaries totaling NIS 337 million.
(4) Reclassified.

Note 18 - Assets and Liabilities Classified by Term to Maturity and Linkage Basis [(1)] - consolidated

As of December 31, 2012

Reported amounts (NIS in millions)

	Expected contractual future cash flows				
	On-call to 1 month	1-3 months	3-12 months	1-2 years	2-3 years
Israeli currency - non-linked					
Assets [(3)]	37,587	2,461	8,475	4,697	3,732
Liabilities	47,257	13,319	17,731	7,936	2,860
Difference	**(9,670)**	**(10,858)**	**(9,256)**	**(3,239)**	**872**
Derivatives (other than options)	(3,008)	(6,593)	9,846	2,387	287
Options (in terms of underlying asset)	(213)	(587)	76	2	-
Israeli currency - linked to the CPI					
Assets	848	885	4,162	5,175	5,275
Liabilities	1,702	1,486	4,809	5,415	4,862
Difference	**(854)**	**(601)**	**(647)**	**(240)**	**413**
Derivatives (other than options)	(339)	(1,130)	(4,850)	(1,341)	(72)
Options (in terms of underlying asset)	-	-	-	-	-
Foreign currency - Israeli operations [(4)]					
Assets	5,104	1,269	2,445	1,359	1,000
Liabilities	11,218	4,863	5,176	488	129
Difference	**(6,114)**	**(3,594)**	**(2,731)**	**871**	**871**
Derivatives (other than options)	3,347	7,723	(4,995)	(1,045)	(215)
Options (in terms of underlying asset)	201	600	(76)	(1)	-
Foreign currency - overseas operations					
Assets	1,906	213	597	593	1,073
Liabilities	1,852	927	892	143	139
Difference	**54**	**(714)**	**(295)**	**450**	**934**
Non-monetary items					
Assets	-	-	-	-	-
Liabilities	-	-	-	-	-
Difference	-	-	-	-	-
Derivatives (other than options)	-	-	-	-	-
Options (in terms of underlying asset)	12	(13)	-	(1)	-
Total					
Assets	45,445	4,828	15,679	11,824	11,080
Liabilities	62,029	20,595	28,608	13,982	7,990
Difference	**(16,584)**	**(15,767)**	**(12,929)**	**(2,158)**	**3,090**

(1) Presented in this note are expected contractual future cash flows with respect to assets and liabilities, according to linkage basis, according to the remaining contractual period to maturity of each flow. The data is stated net of provisions for credit loss.
(2) Includes assets totaling NIS 352 million which are past due.
(3) Includes NIS 6,459 million of loans at debitory account terms and NIS 284 million exceeding limits in debitory account facilities.
(4) Includes linkage to foreign currency.
(5) As in Note 17 "Assets and Liabilities Classified by Linkage Basis", includes off-balance sheet items related to derivatives.
(6) Contractual rate of return is the interest rate which discounts the expected contractual future cash flows, as presented in this Note, for the monetary item to its balance sheet balance.

Expected contractual future cash flows - continued						Balance sheet balance [5]		
3-4 years	4-5 years	5-10 years	10-20 years	Over 20 years	Total cash flows	Without maturity	Total	Contractual rate of return(6)
3,715	4,438	15,074	13,662	3,494	97,335	[2] 900	89,941	4.42%
1,761	854	574	469	941	93,702	38	92,205	2.59%
1,954	**3,584**	**14,500**	**13,193**	**2,553**	**3,633**	**862**	**(2,264)**	
(340)	40	231	(84)	-	2,766	-	2,742	
-	-	-	-	-	(722)	-	(724)	
4,249	4,015	14,840	18,543	6,141	64,133	[2] 299	50,540	4.63%
5,253	3,933	8,667	3,742	1,035	40,904	48	35,296	3.37%
(1,004)	**82**	**6,173**	**14,801**	**5,106**	**23,229**	**251**	**15,244**	
107	(98)	390	-	-	(7,333)	-	(7,286)	
-	-	-	-	-	-	-	-	
1,184	561	3,199	2,140	631	18,892	[2] 182	14,757	3.65%
129	61	270	18	-	22,352	12	20,557	2.50%
1,055	**500**	**2,929**	**2,122**	**631**	**(3,460)**	**170**	**(5,800)**	
233	58	(621)	84	-	4,569	-	4,544	
-	-	-	-	-	724	-	726	
115	140	906	167	-	5,710	-	5,063	2.90%
101	16	1,031	-	-	5,101	-	4,648	1.03%
14	**124**	**(125)**	**167**	**-**	**609**	**-**	**415**	
-	-	-	-	-	-	1,941	1,941	
-	-	-	-	-	-	284	284	
-	**-**	**-**	**-**	**-**	**-**	**1,657**	**1,657**	
-	-	-	-	-	-	-	-	
-	-	-	-	-	(2)	-	(2)	
9,263	9,154	34,019	34,512	10,266	186,070	3,322	162,242	4.47%
7,244	4,864	10,542	4,229	1,976	162,059	382	152,990	3.11%
2,019	**4,290**	**23,477**	**30,283**	**8,290**	**24,011**	**2,940**	**9,252**	

Note 18 - Assets and Liabilities Classified by Term to Maturity and Linkage Basis (1) - the Bank (continued)

As of December 31, 2012

Reported amounts (NIS in millions)

	Expected contractual future cash flows				
	On-call to 1 month	1-3 months	3-12 months	1-2 years	2-3 years
Israeli currency - non-linked					
Assets (3)	33,581	1,851	6,840	3,688	3,068
Liabilities	37,970	12,285	17,048	8,465	2,921
Difference	**(4,389)**	**(10,434)**	**(10,208)**	**(4,777)**	**147**
Derivatives (other than options)	(3,008)	(6,593)	9,846	2,387	287
Options (in terms of underlying asset)	(213)	(587)	76	2	-
Israeli currency - linked to the CPI					
Assets	823	776	3,976	4,983	5,140
Liabilities	(313)	1,459	6,377	5,362	4,865
Difference	**1,136**	**(683)**	**(2,401)**	**(379)**	**275**
Derivatives (other than options)	(339)	(1,130)	(4,850)	(1,341)	(72)
Options (in terms of underlying asset)	-	-	-	-	-
Foreign currency - Israeli operations (4)					
Assets	5,076	1,269	2,435	1,359	1,000
Liabilities	10,732	4,984	5,509	488	129
Difference	**(5,656)**	**(3,715)**	**(3,074)**	**871**	**871**
Derivatives (other than options)	3,347	7,723	(4,995)	(1,045)	(215)
Options (in terms of underlying asset)	201	600	(76)	(1)	-
Foreign currency - overseas operations					
Assets	1,246	178	750	593	1,073
Liabilities	1,396	927	1,097	143	139
Difference	**(150)**	**(749)**	**(347)**	**450**	**934**
Non-monetary items					
Assets	-	-	-	-	-
Liabilities	-	-	-	-	-
Difference	**-**	**-**	**-**	**-**	**-**
Derivatives (other than options)	-	-	-	-	-
Options (in terms of underlying asset)	12	(14)	-	(1)	-
Total					
Assets	40,726	4,074	14,001	10,623	10,281
Liabilities	49,785	19,655	30,031	14,458	8,054
Difference	**(9,059)**	**(15,581)**	**(16,030)**	**(3,835)**	**2,227**

(1) Presented in this note are expected contractual future cash flows with respect to assets and liabilities, according to linkage basis, according to the remaining contractual period to maturity of each flow. The data is stated net of provisions for doubtful debts.
(2) Includes assets totaling NIS 337 million which are past due.
(3) Includes NIS 5,530 million of loans at debitory account terms and NIS 220 million exceeding limits in debitory account facilities.
(4) Includes linkage to foreign currency.
(5) As in Note 17 "Assets and Liabilities Classified by Linkage Basis", includes off-balance sheet items related to derivatives.
(6) Contractual rate of return is the interest rate which discounts the expected contractual future cash flows, as presented in this Note, for the monetary item to its balance sheet balance.

	Expected contractual future cash flows - continued						Balance sheet balance (5)		Contractual rate of return(6)
	3-4 years	4-5 years	5-10 years	10-20 years	Over 20 years	Total cash flows	Without maturity	Total	
	3,204	3,236	13,044	13,648	3,494	85,654	(2) 794	78,930	4.47%
	1,760	880	658	469	941	83,397	-	82,520	2.57%
	1,444	**2,356**	**12,386**	**13,179**	**2,553**	**2,257**	**794**	**(3,590)**	
	(340)	40	231	(84)	-	2,766	-	2,742	
	-	-	-	-	-	(722)	-	(724)	
	4,176	3,968	15,464	18,543	6,141	63,990	(2) 292	50,303	4.69%
	5,252	3,927	9,346	3,742	1,035	41,052	48	35,296	3.84%
	(1,076)	**41**	**6,118**	**14,801**	**5,106**	**22,938**	**244**	**15,007**	
	107	(98)	390	-	-	(7,333)	-	(7,286)	
	-	-	-	-	-	-	-	-	
	1,184	561	3,199	2,140	631	18,854	(2) 182	14,746	3.67%
	129	61	270	18	-	22,320	12	20,540	2.53%
	1,055	**500**	**2,929**	**2,122**	**631**	**(3,466)**	**170**	**(5,794)**	
	233	58	(621)	84	-	4,569	-	4,544	
	-	-	-	-	-	724	-	727	
	115	140	906	167	-	5,168	-	4,485	2.90%
	101	16	1,031	-	-	4,850	-	4,394	1.01%
	14	**124**	**(125)**	**167**	**-**	**318**	**-**	**91**	
	-	-	-	-	-	-	3,379	3,381	
	-	-	-	-	-	-	284	284	
	-	**-**	**-**	**-**	**-**	**-**	**3,095**	**3,097**	
	-	-	-	-	-	-	-	-	
	-	-	-	-	-	(3)	-	(3)	
	8,679	7,905	32,613	34,498	10,266	173,666	4,647	151,845	4.52%
	7,242	4,884	11,305	4,229	1,976	151,619	344	143,034	3.41%
-	**1,437**	**3,021**	**21,308**	**30,269**	**8,290**	**22,047**	**4,303**	**8,811**	

Note 18 - Assets and Liabilities Classified by Term to Maturity and Linkage Basis - Consolidated and the Bank (continued)

As of December 31, 2011

Reported amounts (NIS in millions)

	Expected contractual future cash flows				
	On-call to 1 month	1-3 months	3-12 months	1-2 years	2-3 years
Consolidated					
Assets (1)	30,432	5,603	20,173	16,409	13,833
Liabilities	61,155	22,138	23,430	8,048	7,645
Difference	**(30,723)**	**(16,535)**	**(3,257)**	**8,361**	**6,188**
The Bank					
Assets (2)	26,211	4,704	17,890	14,952	12,961
Liabilities	50,357	21,742	24,072	8,233	7,683
Difference	**(24,146)**	**(17,038)**	**(6,182)**	**6,719**	**5,278**

(1) Includes NIS 6,331 million of loans at debitory account terms and NIS 193 million exceeding limits in debitory account facilities.
(2) Includes NIS 5,577 million of loans at debitory account terms and NIS 138 million exceeding limits in debitory account facilities.
(3) Includes assets totaling NIS 345 million which are past due.
(4) Includes assets totaling NIS 304 million which are past due.
(5) As included in Note 17 "Assets and liabilities by linkage basis".
(6) Rate of return is the interest rate which discounts the expected contractual future cash flows, as presented in this Note, for the monetary item to its balance sheet balance.

Expected contractual future cash flows - continued						Balance sheet balance [5]		Contractual rate of return[6]
3-4 years	4-5 years	5-10 years	10-20 years	Over 20 years	Total cash flows	Without maturity	Total	
10,724	9,206	31,996	32,587	9,050	180,013	[3] 2,759	150,246	4.49%
7,293	4,268	9,967	5,538	1,513	150,995	432	142,192	3.92%
3,431	**4,938**	**22,029**	**27,049**	**7,537**	**29,018**	**2,327**	**8,054**	
10,163	8,822	30,773	32,565	9,050	168,091	[4] 3,962	140,118	4.54%
7,340	4,262	10,663	5,538	1,513	141,403	387	132,452	3.97%
2,823	**4,560**	**20,110**	**27,027**	**7,537**	**26,688**	**3,575**	**7,666**	

Note 19 - Contingent Liabilities and Special Commitments

As of December 31

Reported amounts (NIS in millions)

Consolidated

	As of December 31			
	2012		2011	
	Balance [1]	Provision [2]	Balance [1]	Provision [2]
A. Off-balance sheet financial instruments				
Contractual balances or their denominated amounts at the end of the year				
Transactions in which the balance represents a credit risk:				
- Documentary credit	387	1	340	3
- Loan guarantees	2,705	21	3,195	27
- Guarantees to home buyers	8,096	7	6,810	9
- Other guarantees and liabilities [3]	3,281	23	2,923	17
- Unutilized revolving credit card facilities	6,718	6	6,628	7
- Unutilized debitory account and other credit facilities in accounts available on demand	16,313	21	16,994	34
- Irrevocable commitments for loans approved but not yet granted	9,724	17	9,449	14
- Commitments to issue guarantees	5,198	6	5,127	3

The Bank

A. Off-balance sheet financial instruments				
Contractual balances or their denominated amounts at the end of the year				
Transactions in which the balance represents a credit risk:				
- Documentary credit	387	1	340	3
- Loan guarantees	2,690	21	3,180	27
- Guarantees to home buyers	8,096	7	6,810	9
- Other guarantees and liabilities [3]	3,252	22	2,897	17
- Unutilized revolving credit card facilities	4,499	5	4,408	6
- Unutilized debitory account and other credit facilities in accounts available on demand	14,640	21	15,458	32
- Irrevocable commitments for loans approved but not yet granted	9,724	17	9,449	14
- Commitments to issue guarantees	5,198	6	5,127	3

(1) Contract balances or their stated amounts at the end of the period, before effect of provision for credit loss.
(2) Balance of provision for credit loss at end of period.
(3) Includes the Bank's liabilities for its share in the risks fund of the MAOF Clearinghouse of NIS 127 million. (on December 31, 2011 - NIS 176 million) see Note 19.D. 2) and Note 15.B.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

B. Off-balance sheet liability for activities based on extent of collection at year end [(1)]

1. Balance of loans from deposits based on extent of collection [(2)]

	Consolidated	
	2012	2011 [(5)]
Israeli currency - linked to the CPI	13,198	14,879
Israeli currency - non-linked	1,863	1,740
Foreign currency	171	259
Total	**15,232**	**16,878**

2. Cash flows with respect to collection commissions on activities based on extent of collection [(3)]

Consolidated	2012							2011
	Up to 1 year	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years to 10 years	Over 10 years to 20 years	Over 20 years	Total	Total
Cash flows of futures contracts	63	123	128	227	85	3	629	750
Expected future cash flows net of management's estimate of early repayments	63	122	115	208	65	1	574	701
Discounted expected future flows net of management's estimate of early repayments [(4)]	62	117	106	179	50	1	515	600

3. Information on loans made available during the year

	Consolidated	
	2012	2011
Loans out of deposits according to extent of collection	186	90
Standing loans and grants	213	102

(1) Loans and deposits from deposits the repayment of which to the depositor is contingent upon collection of the loans (or deposits), with margin or with collection commission (instead of margin).
(2) Standing loans and Government deposits given with respect there to totaling NIS 3,015 million (2011 - NIS 3,380 million) are not included in this table.
(3) Includes unlinked shekel sector and foreign currency sector.
(4) Discounted at the rate of 2.05% (2011 - 2.85%).
(5) Reclassified.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

	Consolidated		The Bank	
	2012	2011	2012	2011
C. Special commitments:				
Obligations with respect to:				
Long-term rental contracts [(1)]	624	532	489	466
Computerization and software service contracts	178	148	178	148
Acquisition and renovation of buildings	18	5	18	5
Receipt of deposits on future dates [(2)]	400	405	400	405

(1) The Bank and subsidiaries have long-term leases on buildings and equipment for which the rental payments are as follows (subject to linkage conditions):

	Consolidated		The Bank	
	2012	2011	2012	2011
First year	66	58	46	44
Second year	58	50	43	40
Third year	50	46	36	37
Fourth year	47	37	33	29
Fifth year	44	35	30	28
Sixth year and thereafter	359	306	301	288
Total	**624**	**532**	**489**	**466**

(2) Transactions with institutional depositors to receive deposits at future dates at fixed interest rates set upon the contract date.

Note 19 - Contingent Liabilities and Special Commitments (continued)

D. Contingent liabilities and other special commitments

1) In accordance with a resolution of the Board of Directors of the Tel Aviv Stock Exchange ("TASE"), a risk fund was established, which totaled NIS 536 million as of December 31, 2012. The Bank's share of the fund as of December 31, 2012 is estimated at NIS 34 million (as of December 31, 2011 – NIS 76 million). The size of the risk fund is updated semi-annually based on the average daily total clearing volume - but no less than NIS 150 million. Each member's share in the risk fund will be determined by a ratio between the member's clearing volume and the total clearing volume of all members (except for the Bank of Israel) during that period, but no less than NIS 500 thousand.
In accordance with a decision by the stock exchange clearinghouse Board of Directors, starting on December 15, 2008 each member of the clearing house deposits in cash at least 25% of their share in the risk fund.
See Note 15.A regarding liens that the Bank has undertaken to furnish for this liability.

2) The Bank has undertaken toward the MAOF Clearinghouse Ltd., a subsidiary of the TASE ("MAOF Clearinghouse"), to pay any monetary charge deriving from transactions in derivatives traded on the TASE, executed through it by its customers, and from such transactions executed by several members of the TASE that are not members of the MAOF Clearinghouse, for their customers.

The amount of the liability for these customers, as of the balance sheet date, amounts to NIS 225 million (as of December 31, 2011 – NIS 374 million).
Likewise, the Bank has undertaken to refund its share in the risk fund of the MAOF Clearinghouse, which totaled NIS 757 million as of December 31, 2012. The Bank's share of the fund as of December 31, 2012 is estimated at NIS 127 million (as of December 31, 2011 – NIS 176 million).
In accordance with a decision by the MAOF clearinghouse Board of Directors, starting on December 15, 2008 each member of the clearing house deposits in cash at least 25% of their share in the risk fund.

For information regarding charges that the Bank undertook to furnish with respect to these liabilities, see Note 15.B.

3) The Bank has made undertakings to the Tel Aviv Stock Exchange ("TASE") for operations of a company which is a member of the stock exchange but not a member of the clearinghouse. The undertaking is to honor any monetary charge arising from transactions executed by said company.

4) In 1992, a General Meeting of the Bank's shareholders ratified a resolution to indemnify officers of the Bank with the following wording:

- The Bank will indemnify in full each of the officers for financial liabilities and legal expenses incurred for actions, acts, and omissions performed within the framework stipulated in the Companies Ordinance and the Bank's by-laws, and subject to the above provisions.
- These officers will be indemnified whether the claim is brought against them during their employment period at the Bank, or whether subsequently and refers to an act performed in their capacity as officers.

There are differing legal opinions regarding a company's authority to approve such broad indemnification, and whether invoking it in a specific case requires additional approval, in a manner stipulated by law. Should the Bank be required to pay any amounts on the basis of the above decision, it will seek advice from its legal counsel regarding its obligation, taking into consideration the specific and special circumstances of each incident, if applicable.

Note 19 - Contingent Liabilities and Special Commitments (continued)

5) In December 2001, a General Meeting of the Bank's shareholders ratified the granting a waiver in advance (as described below) as well as advance commitment by the Bank to indemnify Board members and other officers (hereinafter jointly: "the officers"). Pursuant to the resolution by the General Meeting of shareholders, the Bank waives in advance any liability by officers of the Bank towards the Bank with respect to any damage incurred by the Bank due to breach of the officer's duty of care towards the Bank in the former's conduct, arising from their position as officer of the Bank; the Bank also committted to indemnify officers of the Bank for any liability or expense incurred by the officer in conjunction with his action in the course of their office, all as stated in the letter of commitment to indemnify, including with regard to actions by officers who are not Board members in conjunction with their action as Board member on behalf of the Bank, or at the Bank's request, of another company whose shares are owned by the Bank (hereinafter: "the original letter of indemnification").

According to the original letter of indemnification, the amount if indemnification paid by the Bank to all officers on aggregate shall not exceed 25% of the Bank's shareholder equity on the Bank's 2000 financial statements, adjusted for the CPI as from December 2000 (hereinafter: ("total indemnification amount). This indemnification applies to action related, directly or indirectly, to one or more of the event types listed in the Addendum to the letter of commitment to indemnify.

On October 28, 2004, the General Meeting of Bank shareholders resolved to add to the list of events for which the Bank granted a commitment to indemnify to its officers, pursuant to the original letter of indemnification, a merger event, as defined in the Corporate Act, including any decision, action or reporting with regard to a merger.

It was resolved that in all that relates to indemnification resulting from a merger event, the maximum amount of the indemnification will be the lesser of: 25% of the Bank's shareholders' equity according to its financial statements as of December 31, 2000, plus linkage differentials beginning from the CPI for December 2000, or 25% of the Bank's shareholders' equity according to the last financial statements published in proximity to the actual payment date with respect to the indemnification.

On May 14, 2006, the General Meeting of Bank shareholders resolved to adapt the wording of the letter of indemnification to the provisions of the Corporate Act (Amendment 3), 2005 and resolved to grant advance commitment to indemnify, of identical wording, to Bank employees serving as Board member on a company in which the Bank owns some shares, and to those serving, from time to time at the Bank's request, as Board member on a company controlled by the Bank.

On November 9, 2011, the General Meeting of Bank shareholders resolved to add a commitment by the Bank to indemnify Bank employees who are not officers of the Bank, who serve from time to time, upon request by the Bank, as officers of companies controlled by the Bank (such a resolution was also passed by the Bank's Board of Directors on February 16, 2009 - resolving to provide a letter of indemnification identical to the one granted to Bank officers), and to those who are not employees or officers of the Bank, who serve from time to time as officers of a company, other than a banking corporation, wholly-owned by the Bank (jointly: "the parties eligible for indemnification").

Note 19 - Contingent Liabilities and Special Commitments (continued)

The General Meeting of Bank shareholders further decided to add a commitment by the Bank to indemnify the parties eligible for indemnification for any monetary liability arising from payment to any party injured by the breach and with respect to expenses related to any administrative proceeding, including reasonable litigation expenses - all as specifief in the ISA Enforcement Proceeding Streamlining Act (Legislative Amendments), 2011.

The General Meeting of Bank shareholders also resolved that the maximum indemnification amount payable by the Bank, on aggregate to all those eligible for indemnification pursuant to the letter of commitment to indemnify, shall not exceed 25% of the Bank's shareholders equity, based on its most recent financial statements published soon prior to the actual payment date of the indemnification amount ("maximum indemnification amount"). Should the total indemnification amount exceed the maximum indemnification amount specified above, the maximum amount payable by the Bank on aggregate to all those eligible for indemnification shall not exceed the total indemnification amount, but the differences between these two amounts would only be used for indemnification with respect to action taken before November 9, 2011.

On September 20, 2012, the General Meeting of Bank shareholders further decided to add a commitment by the Bank to indemnify the parties eligible for indemnification for any monetary liability arising from payment to any party injured by the breach and with respect to expenses related to any administrative proceeding, including reasonable litigation expenses - all as specified in the ISA Enforcement Proceeding Streamlining Act (Legislative Amendments), 1981 and in the Financial Services Supervision Act (Provident Funds), 2005 and with respect to expenses related to any administrative proceeding, including reasonable litigation expenses - all as specified in the Restrictive Trade Practices Act, 1988.

The General Meeting of Bank shareholders further decided to add a commitment by the Bank to indemnify the parties eligible for indemnification for any monetary liability arising from payment to any party injured by the breach or similar, pursuant to any other statute, including reasonable litigation expenses, including attorneys' fees, with regard to any administrative proceeding pursuant to any other statute, provided that such indemnification is not prohibited by law.

6) In May 1998, General Meetings of the shareholders of the Bank and of Bank Tefahot ratified an undertaking to indemnify officers, which had previously been approved by their Audit Committees and Boards of Directors as follows:

The Bank and Bank Tefahot will irrevocably indemnify any of their officers for any action taken in their capacity as officers, in connection with the causes of action listed below, and for any financial obligation to be imposed by a court judgment, including a compromise, or arbitrator’s decision that is subsequently approved by a court, and also for any reasonable legal expenses for which they may be indemnified in accordance with provisions of the Companies Ordinance.

Note 19 - Contingent Liabilities and Special Commitments (continued)

The indemnification will be made for all the officers on a cumulative basis, up to a sum not to exceed – for each bank separately - NIS 750 million (linked to the CPI of March 1998), for any financial liability that the officer incurs as a result of an action that he took that is directly or indirectly connected to the prospectus published in 1998, or to the draft prospectus that was filed in that year, in connection with the offer of sale of the Bank's securities by the State, including in connection with the reports submitted by the banks subsequent to the date of the prospectus regarding any matter that occurred before the date of the prospectus.

Furthermore, the total cumulative amount of indemnification to be paid for all officers for any action or matter related to the insurance of borrowers by mortgage banks mentioned in the above prospectus included in the letter of indemnification – by each bank separately - will not exceed NIS 750 million (linked to the CPI of March 1998).

The letters of undertaking for indemnification stipulated further that, notwithstanding the aforesaid, the total cumulative amount of indemnification to be paid for all the officers with regard to all the causes of action included in the letter of indemnification – by each bank separately - will be limited to NIS 1,000 million (linked to the CPI of March 1998).

Under terms and conditions of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

7) In November 2001, approval was given by General Meetings of the shareholders of Bank Tefahot and of a wholly-owned and controlled subsidiary of Bank Tefahot ("Tefahot Issuance"), in connection with the prospectus for issuance of debentures and subordinated notes of Bank Tefahot from November 2001, that Tefahot Issuance irrevocably undertakes to indemnify all of its officers, for any action taken in connection with matters detailed in the letter of indemnity, by virtue of his being an officer ("indemnification").

   The indemnification will be given for any financial debt, if imposed by a judgment, including a judgment issued in a compromise or arbitration that was approved by a court, and with respect to any reasonable legal expenses (including fees to attorneys and other experts), which may be indemnified in accordance with the provisions of the Corporate Act, all up to a limit of NIS 1 billion, linked to the CPI.

   Bank Tefahot undertook vis-à-vis Tefahot Issuance that, should it be unable to fulfill its obligations to the indemnity recipients, or any one of them, Bank Tefahot would pay to Tefahot Issuance any amount that Tefahot Issuance will be found liable to indemnify, beyond the amounts paid by Tefahot Issuance.

   Under terms and conditions of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

8) In October 2002, the Board of directors of Bank Tefahot, following the approval of the Audit Committee, approved the bestowing of an advance undertaking for indemnification of directors and other officers of Bank Tefahot (together – "the officers"). Accordingly, Bank Tefahot undertakes, subject to the conditions detailed in the letter of undertaking and to the provisions of the Companies Law, to indemnify the officers for any liabilities or expenses imposed on the officer due to his capacity as an officer in Bank Tefahot, provided that these activities are related, directly or indirectly, to one or more of the events listed in the addendum to the letter of undertaking the indemnification.

Note 19 - Contingent Liabilities and Special Commitments (continued)

The cumulative amount of the indemnification to be paid by Bank Tefahot to all the officers will not exceed 25% of the shareholders' equity of Bank Tefahot according to its annual financial statements for 2001, adjusted for the CPI, beginning from December 2001, or 25% of the shareholders' equity of Bank Tefahot according to the latest financial statements published as of the actual payment date of the indemnification, whichever is lower.

In November 2002, a General Meeting of the shareholders of Bank Tefahot ratified this resolution.

Under terms and conditions of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

9) On June 30, 1998, an extraordinary general meeting of Bank Adanim, following approval by its Board of Directors and approval of its Audit Committee, ratified an undertaking to indemnify ("indemnification letter") the officers in Bank Adanim. The indemnification letter will apply to officers, as defined in Section 96(24) of the Companies Ordinance, who, on the approval date of the indemnification by the General Meeting ("date of record"), are serving in Bank Adanim or whose tenure ended in a period not earlier than 4 years from the date of record.

   Pursuant to the indemnification letter, Bank Adanim will indemnify any officers in Bank Adanim for any financial liabilities imposed on them by a ruling, including legal expenses, for an act or omission done directly or indirectly in the matters itemized in the letter of indemnification, namely the offer of sale to the public of securities of Mizrahi Tefahot by the State, pursuant to a prospectus published in May 1998.

   Pursuant to the indemnification letter, the amount of the indemnification to be paid by Bank Adanim (in addition to the amounts to be received according to the officers' insurance policy as detailed below) to all officers, on a cumulative basis will not exceed NIS 70 million, with the amount linked to the last CPI published before the date of record until the CPI published before the date of payment.

   Bank Adanim will take action, to the extent possible, so that during the 10-year period beginning on the date of record, an officers' insurance policy will be purchased by or for Bank Adanim, which will cover the matters covered by the indemnification, the amount of which, including restitution/reinstatement will not be lower than the aforementioned amounts.

   On December 16, 2002, a General Meeting of Bank Adanim, following approval by the Audit Committee and ratification by its Board of Directors, ratified the letter of indemnification undertaking ("indemnification letter") for officers in Bank Adanim. The indemnification letter will apply to officers, as defined in Section 1 of the Companies Law, 1999, who, on the approval date of the indemnification letter by the general meeting ("date of record") serve in Bank Adanim. Pursuant to the indemnification letter, Bank Adanim will indemnify all of the officers in Bank Adanim for all the financial liabilities to be imposed on them by a ruling, including legal expenses, relating to an act or omission done directly or indirectly in matters listed in the indemnification letter, up to the indemnification amounts.

Note 19 - Contingent Liabilities and Special Commitments (continued)

The indemnification amounts to be paid by Bank Adanim for each officer, on a cumulative basis, for one or more of the types of events provided in the addendum to the letter of undertaking, shall not exceed 25% of the shareholders' equity of Bank Adanim according to its financial statements for the year 2001, adjusted from time to time, according to the rate of increase in the CPI compared with the CPI for December 2001 that was published in January 2002 ("total indemnification amount). In the event the officer will receive indemnification from the insurer of the officers' insurance policy for the matter covered by the indemnification, the indemnification will be provided by Bank Adanim in the amount of the difference between the amount of financial liabilities imposed on the officer and/or legal expenses incurred by or charged to the officer, and between the amount received from the insurer on this matter, provided that the amount of indemnification for which Bank Adanim will be charged will not exceed the total indemnification amount.

Beginning December 2002, Bank Adanim was one of the insured parties in the officers' insurance policy purchased by the Bank for itself and its subsidiaries and related companies, which is in effect until April 5, 2007.

Under terms and conditions of the merger of Bank Adanim into the Bank, the Bank assumed this commitment.

10) Various claims are pending against the Bank and its subsidiaries, namely, claims of customers, as well as motions for recognition of various class actions. In the estimation of the management of the Bank, based on the estimation of the managements of its subsidiaries and on the opinion of their legal counsel as to the possible outcome of the pending claims and motions for approval of claims as class actions, the financial statements include fair provisions, where necessary, to cover possible damages.

Below are details of significant actions in which the amount claimed (excluding interest and fees) exceeds 1% of the Bank's shareholders' equity, and for motions for recognition as class action lawsuits:

A. Two motions were pending and open in District Court and the Supreme Court to recognize as class actions two legal actions against the Bank and other mortgage banks totaling more than one and one-half billion NIS. The specific amount demanded from each bank was not stated. In the actions, it was principally argued that the banks unlawfully collected commissions on property insurance and life insurance of borrowers and engaged in insurance brokerage, that the mortgage banks over-charged for insurance premiums, and that the banks and insurers are parties to a cartel which results in borrowers having to pay higher insurance premiums than they would pay for similar policies on the free market.

The banks denied all plaintiffs' claims and rejected them out of hand. The banks claimed, inter alia, that their actions were lawful both in charging the commissions and in the rates of these commissions.

The parties to the first motion to grant class action status submitted to a reconciliation proceeding heard by the Deputy Chief Justice, Justice Theodore Or (Retired). As the reconciliation process progressed, the parties to the additional motion for class action status filed on the same matter against two insurance companies were added to the process, in view of the parties' desire to reach a comprehensive agreement to conclude all proceedings on this issue.

Note 19 - Contingent Liabilities and Special Commitments (continued)

Upon conclusion of the reconciliation process, the parties reached a reconciliation agreement. According to the reconciliation agreement, ratified by a verdict handed down in December 2011, in conjunction with the first motion, the banks would donate a total of NIS 17 million to organizations acting for public causes. Furthermore, the parties recommended that the petitioners in the two motions be compensated, including their attorneys' legal fees, amounting in total to NIS 4 million. According to the reconciliation agreement, the Bank's share of these payments amounts to NIS 8 million.

In May 2012, payment was made to the various organizations, in accordance with the verdict. This concluded legal proceedings for these two motions.

B. In December 2001, a statement of claim was filed against the Bank in Tel Aviv District Court in the amount of NIS 80 million. The plaintiffs allege that a bank clerk (who was suspended), when he was an employee of the Bank, executed numerous unlawful transactions in their accounts, without their permission and without their knowledge. The plaintiffs allege that as a result of these acts, they experienced a credit crisis, which required them to effect financial transactions that would not have been effected otherwise, as a result of which they allege that they sustained direct and indirect losses, in tens of millions of NIS.

In January 2002, the Bank filed a statement of defense, in which it argued as preliminary arguments, inter alia, that the statue of limitations had expired for all of the plaintiffs' allegations relating to transactions executed more than seven years prior to the filing of the claim.

It was also argued that the plaintiffs had received statements on what was occurring in their accounts, and that they cannot deny the accuracy of the contents of the Bank's books of account. In the body of the statement of defense, it was argued that the plaintiffs knew and/or should have known what was done in their accounts, and that unfortunately they were very negligent in examining their account statements, thus enabling the alleged transactions, which are denied by the Bank, to be executed in their accounts. It was further argued that the improper transactions, to the extent they were executed, were executed by a bank clerk at that time, acting on his own, and exceeding authority, and the Bank could not have prevented them with the reasonable means available to it.

In May 2008, the plaintiff filed an amended statement of claim in the amount of NIS 102 million, and consequently the Bank has filed an amended statement of defense. The evidentiary hearings and parties' summations were concluded in July 2010.

In February 2012, a verdict was given which recognizes some of the causes for claim, and instructs recalculation of the corresponding financial values.

The Court appointed an expert, consented to by both parties, to quantify and calculate the amount due to the plaintiff.

Note 19 - Contingent Liabilities and Special Commitments (continued)

C. In March 2004, an action and a motion for recognition as a class action were filed in Nazareth District Court against Bank Tefahot ("the Action"). The action was filed on behalf of borrowers of Bank Tefahot, in the amount of NIS 69 million. The action alleges that Bank Tefahot overcharged interest on arrears beyond that permitted by law, and that it charged a commission for non-payment of a standing order for current repayments of a loan drawn by borrowers of Bank Tefahot. The action alleges that this commission should be deemed to be interest on the loan in arrears, such that this commission, together with the interest on arrears that Bank Tefahot charges for the period in arrears, exceeds the ceiling of permitted interest on arrears under the Interest Law, 1957, and the related legislation.

In January 2007, the Supreme Court ruled to dismiss outright the motion for recognition as a class action, and ordered the parties to file their positions on the issue of the implications of the Class Actions Law, 2006, on this case. The plaintiffs have appealed the Court's' decision. In May 2007, the Supreme Court ruled that processing of this appeal would be suspended pending a court decision in the action based on the same claim against the Bank, which was filed with the Haifa District Court by some of the plaintiffs in these proceedings, in June 2006.The ruling further stipulates that should the decision in the identical case under way at the Haifa District Court be appealed, both appeals may be reviewed concurrently when such a decision is handed down.

In February 2013, the Supreme Court denied both appeals filed by the plaintiffs.

D. In April 2006, a claim was lodged with Tel-Aviv District Court in the amount of NIS 100 million for damages allegedly sustained by the plaintiffs as a result of an alleged misrepresentation made to them by an employee of the Bank's Givatayim branch who has since been dismissed from employment with the Bank. Plaintiffs claim that they have deposited with the Bank over years large amounts totaling NIS millions, and made many investment transactions in various asset classes, mainly by daily telephone contact with an employee at the Bank branch, who carried out their instructions and reported to them on execution of their instructions and the balances in their accounts. The plaintiffs claim that according to reports of the Bank branch employee who handled their accounts, at end of 2003 the balance of their accounts amounted to NIS 91 million. Based on this information, the plaintiffs claim they entered into a contract to purchase a house at a cost of over NIS 10 million. However, the plaintiffs claim, in retrospect after signing the contract to buy the house, they discovered that reports made by the Bank employee were false, and in actual fact no investment actions were taken in their accounts, which in fact had a debit balance.

Therefore, the plaintiffs claim, they have sustained heavy damages, and the amount claimed by them is composed of the last reported balance in their Bank accounts of NIS 91 million, damage sustained by them due to cancellation of the house purchase contract and claimed damages for distress.

Note 19 - Contingent Liabilities and Special Commitments (continued)

In July 2006, the Bank filed a statement of defense arguing, inter alia, that plaintiffs were unable to provide details or proof of the investment instructions they had given, and in fact not a single investment transaction was made in the plaintiffs' accounts in the capital market during the alleged period, and therefore the alleged balances did not accrue in their accounts. The Bank also argued that returns claimed by the plaintiffs – amounting to thousands of percent, at a growth rate of over NIS 30 million per year – are unreasonable, let alone for investors who have no relevant expertise and with the plaintiffs' initial equity at the Bank amounting to only NIS 150 thousand.

The Bank further argues that reports provided to plaintiffs by the Bank employee with regard to enormous amounts accumulated in their accounts, in as much as such reports were provided, are also unreasonable and were provided only at the Bank employee's discretion, using false pretenses and acts of fraud and deception, without the Bank's consent or knowledge, and with the Bank being incapable of preventing it by reasonable means available to it. In September 2010, the plaintiff filed an amended claim, reducing the claim amount by half to NIS 50 million.

Preliminary proceedings in this case have been concluded and the parties have filed primary testimonial affidavits and expert opinions. The case is scheduled for evidentiary hearing at the Court in June 2013.

In June 2006, an action and a motion for recognition as a class action in the amount of NIS 57 million were lodged in Haifa District Court against the Bank for charges to borrowers whose loans (linked to the CPI) are in arrears and bear delinquent interest, the rate of which allegedly exceeds the rate stipulated in the Interest Law, 1957 and the Interest Order enacted accordingly. The plaintiffs allege that the arrears clause in the loan agreement, which stipulates that at the time of arrears, the Bank will provide the borrowers with unlinked loans, is apparently illegal, since it contradicts the Interest Order. The plaintiffs also claim that their being charged commissions for not honoring automatic debits, in addition to the delinquent interest, is allegedly illegal, since a commission for not honoring an automatic debit is essentially arrears interest in all respects.

The Bank filed a motion to dismiss out of hand the plaintiffs' motion for class action status, arguing that its actions were and are lawful. In November 2010, the evidence was heard in this motion, and as decided by the Court, the parties filed their summary claims in conclusion.

On March 7, 2011 the Haifa District Court dismissed the plaintiffs' motion for class action status. The plaintiffs have appealed the decision by the District Court to the Supreme Court.

In February 2013, the Supreme Court denied the plaintiffs' appeal.

F. In June 2006, an action and a motion for recognition as a class action in the amount of NIS 233 million were lodged in Tel Aviv District Court against the State of Israel – Court Order Execution Service, banking corporations, insurance companies and provident funds.

Note 19 - Contingent Liabilities and Special Commitments (continued)

The plaintiffs allege that since they were awarded judgments, they opened files against various debtors in the Execution Office, within the framework of which, through the Execution Office, they attached various assets held by third parties (banks, insurance companies and provident funds). However, it claims, that they provided them with partial, misleading and incomplete information, as they were apparently unprepared to provide answers through electronic media, even though they collected from the awardees (the plaintiffs) payment for each answer, which they allege is unlawful.

The defendants, including the Bank, have filed a motion to dismiss out of hand the motion for class action status. The Court rejected the Bank motion to reject the claim out of hand, but accepted the motion by the insurance companies and rejected out of hand the motion against them. The Bank has filed a motion for the right to appeal to the Supreme Court. The Supreme Court refused the right to appeal.

In April 2012, the District Court dismissed the plaintiffs' claim and motion for class action status.

G. In July 2006, an action and motion for recognition as a class action were lodged in Tel Aviv District Court against the Bank in an amount exceeding NIS 2.5 million, for management fees commissions on securities deposits charged to customers, as defined in the Bank's commissions price list, at amounts above those to which the Bank is entitled according to its own price list and allegedly in violation of the law.

In January 2007, the Bank filed its response to the motion for class action status. In response, the Bank argued, inter alia, that the plaintiff's claims are diametrically opposed to content of the Bank's price list, that the plaintiff has no cause for claim and that, prima facie, the claim is not appropriate for class action status, and that the plaintiff has failed to meet even a single criterion required by the Class Action Act for his motion for class action status to be accepted.

On November 10, 2010, the Tel Aviv District Court granted class action status to this lawsuit, and determined that the class on behalf of which this class action suit would be heard includes all clients who had owned a securities deposit in the seven-year period preceding the filing of the motion (July 2006), and who were over-charged by the Bank with respect to minimum client commission. The remedy sought by the class in the class action suit is refund of the over-charged amounts.

In accordance with the decision by the court, the cause for the class action suit is breach of contract, and the legal issue common to class members is the issue of interpretation of price list provisions with regard to charging of minimum quarterly commission. The Court has instructed the plaintiff to file a statutory notice with the Court, which is to be published, after being approved by the Court, in newspapers as determined by the Court.

The Bank has filed a motion to appeal the Court's decision, and the Supreme Court has ordered a stay of the decision to approve the lawsuit pending a decision on the motion to appeal.

Concurrently, a motion was filed for approval of a settlement agreement in this case. The settlement agreement is subject to approval by the Court and to accepting the position of the Government's Legal Counsel.

In June 2012, the District Court approved the settlement agreement, which was adopted as a verdict.

Note 19 - Contingent Liabilities and Special Commitments (continued)

H. In January 2008, a claim against the Bank was filed with the Central District Court at Petah-Tikva, along with a motion for class action status, amounting to NIS 237 million.

The plaintiff claims that the Bank lowers interest rates paid on renewable short-term deposits based on a non-binding outlook for reduction of the Bank of Israel interest rate. By contrast, when a similar outlook existed for raising the Bank of Israel interest rate, interest rates on deposits were only raised by the Bank after the date on which the Bank of Israel actually raised its interest rate.

The plaintiff further claims that the Bank acted arbitrarily and misled its customers in the pre-contract stage – by not disclosing to customers that it used different criteria for raising the Bank of Israel interest rate compared to those for lowering the Bank of Israel interest rate, as well as during the contract stage - by not informing its customers that it had lowered interest rates for such deposits based on the outlook for a reduction in Bank of Israel interest rates rather than on actual reduction thereof.

The plaintiff claims that the Bank was also in breach of its duty to disclose, imposed by the Banking Act (Customer Service). The plaintiff further claims that should it be determined that under terms of the contract between the Bank and the customer, the Bank may lower interest rates at will, according to the plaintiff, this is a discriminatory condition in a uniform contract.

In May 2008, the Bank filed its response to the motion, in which it rejected the claims made by the customer, and stated that the claim whereby the Bank had to modify interest rates on fixed-rate deposits exclusively in accordance with Bank of Israel interest rates was counter to agreements between the customer and the Bank and contrary to reason. The Bank further claimed that the plaintiff's claim with regard to expectations was also unfounded, since interest on deposits was based on a range of economic and macro-economic considerations, commercial considerations by the Bank and considerations with regard to actual customers. Evidence in this case was heard in 2010.

In May 2011, the parties filed a motion with the Court, seeking approval of a settlement whereby the fixed interest deposit form would be amended to include clarification of the circumstances of change in interest rate for renewed deposits as stated above. The Court has yet to decide on this motion.

In February 2012, the District Court approved the settlement agreement between the parties to this case, which was adopted as a verdict.

I. In March 2008, a claim against the Bank was filed with the Tel Aviv District Court, including an application for class action status, amounting to over NIS 2.5 million (as set forth in the claim). The plaintiffs claim that banks are in breach of restrictive trade practices statutes, with restrictive practices leading to reduced competition among banks with regard to various commissions. The banks, according to the claim, have shared information with regard to the various commissions they charge. The plaintiffs claim that this impacted competition in the banking sector, and customers, such as the plaintiffs, have been charged higher commissions than they would have paid had the banks acted lawfully. In November 2009, the Court handed down its decision, whereby legal proceedings would currently be put on hold for at least two years.

Note 19 - Contingent Liabilities and Special Commitments (continued)

In January 2012, a hearing was held by the Court with regard to continued stay of proceedings. In February 2012, the Court decided that the hearing of this claim and another claim filed in the same matter, would be delayed pending a resolution by the Anti-Trust Court of an appeal filed by the Bank of the decision by the Anti-Trust Supervisor, whereby the Bank was party to a restrictive trade practice concerning transfer of information with regard to commissions applicable to households and small businesses.

J. In November 2008, a claim was filed with the Tel Aviv District Court, including an application for class action status, amounting to NIS 68 million, against the Bank, Bank Leumi Le-Israel Ltd., First International Bank of Israel Ltd. and Bank Igud Le-Israel Ltd. for alleged over collection of tax on interest and dividend revenues by way of tax withholding. The plaintiff claims that the banks named in the claim over charge their customers who own debentures or shares (the source of revenue) by not deducting the commission on said revenue prior to withholding tax. The Bank and the other banks have yet to file their response to the motion. The parties are in discussions outside the Court, but have yet to reach any agreement.

K. In May 2009, the Bank received a statement of claim and application for approval of class action suit submitted to the Tel Aviv District Court against the Bank and against Bank Leumi Le-Israel Ltd., Bank Discount Le-Israel Ltd. and First International Bank of Israel Ltd. (hereinafter: "the defendant banks").

The claim is based on the determination by the Anti-Trust Supervisor dated April 26, 2009 headed "Re: restrictive trade practices existed between the Bank and Bank HA-POALIM Ltd., Bank LEUMI LE-ISRAEL Ltd., Bank Discount LE-ISRAEL Ltd. and First International Bank of Israel Ltd., with regard to commission-related information sharing" (see section 12 below). The claim alleges, based on the determination by the Supervisor, that the defendant banks were party to a restrictive trade practice, which affected competition and caused coordination of commissions, such that the plaintiffs paid excessive prices for services rendered to them.

The plaintiffs have set the amount of their claim against all defendant banks at NIS 1 billion based, according to the plaintiffs, only on an estimation so as to place the issue under the material jurisdiction of the District Court.

In November 2009, the Court handed down its decision, whereby legal proceedings would currently be put on hold for at least two years. In January 2012, a hearing was held by the Court with regard to the stay of proceedings. In February 2012, the Court decided that the hearing of this claim and another claim filed in the same matter, would be delayed pending a resolution by the Anti-Trust Court of an appeal filed by the Bank of the decision by the Anti-Trust Supervisor, whereby the Bank was party to a restrictive trade practice concerning transfer of information with regard to commissions applicable to households and small businesses.

Note 19 - Contingent Liabilities and Special Commitments (continued)

L. In November 2009, the Bank received a claim of NIS 804 million filed, by way of originating motion, with the Central District Court in PETACH TIKVA, against the Bank, Bank HA-POALIM, BANK LEUMI, First International Bank of Israel, Discount Bank, Mercantile Discount Bank and BANK IGUD (hereinafter: "the defendant banks"). The background for this claim is a loan obtained by the plaintiffs from the banks in 1999 for purchase of shares (of which the Bank's share was 10%), with the plaintiffs pledging their shares to the banks to secure the loan. Since the plaintiffs were unable to repay their debt, a receiver was appointed for the shares at the request of the defendant banks.

The plaintiffs claim that once a receiver was appointed for the shares, these shares were no longer under their control, and although the decision concerning the sale date of the shares was in the hands of the defendant banks and of the receiver, the defendant banks continued to charge, allegedly unlawfully, "arrears interest" to the plaintiffs throughout the receivership period, with respect to the arrears in loan repayment, which over the years amounted, according to the claim, to the total claim amount. The response of the defendant banks to the claim has yet to be filed.

In January 2010, the Court decision was handed down, whereby the lawsuit would be referred for resolution in the course of a regular claim for monetary remedy, and the Court fee with respect there to would be paid by the plaintiffs. Accordingly, the plaintiffs filed in February 2010 a statement of claim in the amount of NIS 829 million.

In March 2010,the plaintiffs, including the Bank, filed their statements of defense.

Evidence in this case has been heard by the Court between March 2011 and April 2012.

The parties have filed their summations with the Court.

M. In February 2010, a claim and motion for class action status was filed with the Central District Court, in the non-specific amount of tens of millions of NIS. The plaintiff asks the Court to determine that the lawsuit is to be filed in the name of all Bank clients who have repaid a loan granted by the Bank, to buy a residential apartment or secured by a residential apartment (housing loan) before its scheduled maturity, by means of another loan granted by the Bank (refinancing loan), and whose account was charged a fee for lack of advance notice, in the period started 7 years prior to filing the motion. The plaintiff claims that the Bank is in breach of provisions of the Banking Ordinance (Early Repayment Commission), 2002 and charges its clients a commission for lack of advance notice, even when the early repayment is made by means of another loan granted by the Bank.

Note 19 - Contingent Liabilities and Special Commitments (continued)

The plaintiff further claims that the Bank does not provide clients with commission details after such repayment, and therefore the clients are allegedly unaware of the components included in the commission amount charged by the Bank.

In May 2010, the Bank filed its response with the Court, claiming that the Bank acts in compliance with provisions of the Banking Ordinance, and that this was a specific error and not a method of action, so that the claim should not be granted class action status. The parties have filed a motion with the Court to approve a settlement agreement, which was published in two daily newspapers. The settlement amount is small and is not material.

In February 2012, the District Court approved the settlement agreement, which was adopted as a verdict.

N. In May 2011, the Bank received a claim and motion for approval of class action in the amount of NIS 181 million. The claim involves alleged unlawful charging of early repayment commission for additional housing loans. The plaintiff claims that the Bank allegedly unlawfully charges an early repayment commission for additional loans, without the reduction required by law.

In March 2011, The Bank has filed its response to the motion, in which it claimed that according to a decision by the Bank of Israel, the Bank recognizes as additional loans any loans granted prior to as well as after granting the directed loan.

The parties are in discussions to settle their differences.

O. In May 2011, the Bank received a claim and motion for approval of class action status. The claim concerns two alleged claims made against the Bank - firstly, late reporting to the Court Order Execution Service of payments made to reduce debt which is subject to proceedings at the Court Order Execution Service. Secondly, failure to indicate on the reporting forms the number of the principal to be reduced by the reported credit, and the number of the interest calculation rule applied to the reported payment amount.

The lawsuit and motion allege that, by late reporting to the Court Order Execution Service and by failure to provide the aforementioned indications on the reporting forms, the Bank misleads clients, causes clients not to be credited with interest in line with the date of their payment and in accordance with the correct interest rate, creates a situation in which the debt on Court Order Execution Service files is higher than the real debt, and over-charges in payments. The lawsuit and motion further allege that the Enforcement and Collection Authority and the Court Order Execution Service admit that under crediting occurs in case of late reporting and failure to provide the required indications on the reporting form.

The plaintiff claims he is unable to estimate the damage incurred by the entire class of plaintiffs, but believes (on a basis which is not clear to the Bank) that it amounts to hundreds of millions of NIS.

Note 19 - Contingent Liabilities and Special Commitments (continued)

On January 9, 2012, the Bank filed its response to the motion, describing in detail the factual and legal defense claims made by the Bank. On May 20, 2012, the plaintiff filed their response to the Bank's response to the motion. In view of new claims made by the plaintiff in their response to the Bank's response, the Bank filed a further, more detailed response on August 15, 2012. On October 17, 2012 and on October 29, 2012, the Court held preliminary hearings in this case.

The parties have agreed to launch a reconciliation process aimed to try and resolve their differences.

P. In July 2011, a claim was filed with the Central District Court in the amount of NIS 81.8 million for alleged forward transactions made in the plaintiffs' account, which allegedly caused the plaintiffs to incur a loss. The plaintiffs claim that the Bank acted unilaterally in the account and without prior notification about collateral calculation, causing the plaintiffs to incur losses by taking risky positions. The plaintiffs claim that the Bank, by deed or omission, caused the account and the investment portfolio to collapse.

In January 2012, the Bank filed a statement of defense.

The Bank claims that the plaintiff is skilled and familiar with the capital market, and the Bank acted professionally, thoroughly and skillfully at all times.

In February 2012, a pre-trial hearing was conducted in this case.

In November 2012, the plaintiffs filed their evidence with the Court.

The Bank is to file its evidence in March 2013. The parties have agreed that once the Bank has filed its evidence, the parties would launch a reconciliation process designed to try and resolve their differences outside the Court.

Q. In August 2011, a claim and motion for class action status was filed with the Central District Court amounting to hundreds of millions of NIS (as per the claim statement); no specific amount was claimed. The plaintiff seeks a verdict, pursuant to the Class Action Lawsuit Act, whereby the claim would be made on behalf of all Bank clients whose account was charged legal fees not approved by any legal jurisdiction, or whose account was charged unlawful interest with respect to approved legal fees.

This proceeding is in early stages.In November 2012, The parties have agreed to launch a reconciliation process designed to try and resolve their differences outside the Court.

R. In August 2011, a claim and motion for class action status was filed with the Tel Aviv District Court amounting to hundreds of millions of NIS (as per the claim statement); no specific amount was claimed. The plaintiff seeks a verdict, pursuant to the Class Action Lawsuit Act, whereby the claim would be made on behalf of all Bank clients whose account was charged legal fees not approved by any legal jurisdiction, or whose account was charged unlawful interest with respect to approved legal fees.

In October 2012, the plaintiff filed with the Court a motion to withdraw its claim.

In December 2012, the Court accepted this motion and ordered the claim to be erased, and for the motion for approval in this matter to be rejected.

Note 19 - Contingent Liabilities and Special Commitments (continued)

S. In September 2011, a claim and motion for class action status was filed with the Central District Court amounting to NIS 927 million on adjusted basis, for alleged unlawful charging of compounded interest, in contravention of statutes and agreements, on housing loans - including targeted loans, eligibility loans and additional loans, excluding standing loans.
The motion was also filed against Bank Leumi LeMashkantaot and Bank HaPoalim. According to the statement of claim, the amount claimed from the Bank is NIS 364 million.
In May 2012, The Bank has filed its response to this claim, claiming that it was unfounded, that the Bank acted in accordance with statutory provisions and did not charge any compounded interest in the manner in which banks in general and the Bank, in particular, acted.
The position of the Supervisor of Banks, which supports the banks' position, was also filed in this case.
In October 2012, A first pre-trial hearing took place in this case.

T. In November 2011, Bank Yahav received a claim filed with the Haifa District Court, against Bank Yahav and Bank Benleumi. As alleged in the claim, the banks over-charged a cash handling commission in alleged contravention of the law, and in particular - in contravention of Banking Rules (Commissions). The plaintiff also filed a motion for class action status, for a total amount of NIS 200 million.
Bank Yahav has filed its response to this motion. In a pre-trial hearing held in this case, the plaintiff withdrew all of his claims, except for the claim alleging unlawful charging of the commission.
The case is scheduled for summation hearing in March 2013.

U. In December 2011, a claim was filed with the Tel Aviv District Court, along with a motion for class action status, in the amount of NIS 26 million, for commission charged for the service "cash handling by teller". The plaintiff claims that the Bank may only charge a commission for withdrawals in excess of NIS 10,000.
In November 2012, the Bank filed its response to the motion with the Court, in which the Bank rejected the plaintiff's claims.

For all claims against the Bank Group in individual amounts over NIS 2 million, excluding claims listed in section 11 below, there is additional, non-remote exposure for which no provision was made, amounting to NIS 106 million.

11) Motions for recognition as class actions are pending against the Bank, where the amount claimed is material, as well as appeals to the High Court of Justice, as itemized below, which, in the opinion of the Bank's management, based on the opinion of the managements of its subsidiaries, and on the opinion of their legal counsel, the prospects for which cannot be estimated at this stage, so that no provision was made for these.

A. In August 2012, a claim against the Bank was filed with the Tel Aviv District Court, including an application for class action status, amounting to NIS 2.3 billion against Automated Bank Services Ltd. (hereinafter: "ABS"), major banks including the Bank and others, with regard to alleged unlawful charging of commissions upon cash withdrawal from ATMs operated by ABS and located on premises of the defendant banks. Four banks are named as defendants for being shareholders of ABS, while the Bank is named as defendant, even though its ABS shares were transferred to other shareholders in 1980, but the Bank retained the right to appoint an observer to OBS Board of Directors meetings.
The Bank has yet to file a response to this motion.

Note 19 - Contingent Liabilities and Special Commitments (continued)

B. In September 2012, a claim and motion for class action status were filed with the Tel Aviv District Court, with regard to charging VAT on attorneys' fees in Court Order Execution Service cases filed against debtors. The plaintiff has not stated a specific amount claimed in its class action lawsuit.
In March 2013, the Bank filed its respnse to the motion with the court.

C. In October 2012, a claim with motion for class action status was filed with the Tel Aviv District Court, against the five large banks - including the Bank - alleging failure to match the client debt amount on Bank accounts and the debt amount indicated in Court Order Execution Service files. The plaintiffs indicate that the claim amount cannot be estimated at this stage. The Bank has yet to file a response to this motion.

D. In December 2012, a claim and motion for class action status were filed with the Tel Aviv District Court, in the amount of NIS 6 billion, alleging that no notice was given to mortgage borrowers that provisions of a HEYTER ISKA ("transaction permit") apply to their loans and therefore, the Bank over-charged arrears interest on these loans.
The plaintiffs claim that the Bank has failed to fulfill its obligations pursuant to the HEYTER ISKA, and charged the plaintiffs arrears interest which was 10% higher than regular interest.
The Bank has yet to file a response to this motion.

E. In December 2012, an action and a motion for recognition as a class action were filed with the Tel Aviv District Court, with regard to setting rates of arrears interest charged by the Bank in Court Order Execution Service cases filed against debtors. According to the plaintiff, the Bank charges interest significantly higher than the maximum interest rate on checking accounts.
The plaintiff is currently unable to estimate the amount claimed. The Bank has yet to file a response to this motion.

12) On April 26, 2009, the Bank received a determination by the Anti-Trust Supervisor pursuant to Section 43(a)(1) of the Restrictive Trade Practices Act, 1988, whereby restrictive trade practices existed between the Bank and Bank Hapoalim Ltd., Bank Leumi Le-Israel Ltd., Bank Discount Le-Israel Ltd. and First International Bank of Israel Ltd., with regard to commission-related information sharing, since the early 1990s through commencement of the Supervisor inquiry into this matter, in November 2004. This is a civil determination which constitutes a-priori evidence of the content there of in any legal proceeding.
On March 24, 2010, the Bank appealed this ruling to the Anti-Trust Court. On February 22, 2011, the Anti-Trust Supervisor filed their response to appeals filed by the banks. As suggested by the Court, all parties consented to hand over the discussion to arbitration, but on December 25, 2011, the arbitrator informed the Court that he was unable to have the parties reach an agreed settlement, and therefore the case is still pending before the Court.
For details of a claim filed against the Bank based on the determination by the Anti-Trust Supervisor, see Note 10)N. above.

Note 19 - Contingent Liabilities and Special Commitments (continued)

13) On November 18, 2008, the Bank entered into an agreement with Israel Credit Cards Ltd. (hereinafter: "CAL") and with Diners Club Israel Ltd., a company controlled by CAL (hereinafter: "Diners") - (hereinafter jointly: "CAL Group") with regard to jointly providing Visa, MasterCard and Diners Club charge cards, including cards under the Bank brand, to be distributed by the Bank to its customers (hereinafter, respectively: "the agreement" and "the cards"). The agreement sets forth the parties' rights as well as operating arrangements and service provision by CAL Group for the cards, as well as all other terms and conditions related there to. The agreement supersedes current agreements between the Bank and CAL Group in effect since July 26, 1995.

In conjunction with the agreement, the Bank received an option to acquire from CAL, by way of allotment, up to 121,978 ordinary CAL shares, which if allotted upon the date of signing the agreement would have constituted up to 10% of CAL's ordinary share capital, fully diluted (hereinafter: "the option"). The number of shares allotted upon exercise of the option may be adjusted for certain changes in CAL's capital, as set forth in the agreement. The number of shares allotted may be larger if, prior to exercise of the option, CAL would allot shares at a price reflecting a price below the market value, in accordance with a formula prescribed by the agreement.

Furthermore, the number of shares may change accordingly, should CAL decide on a reverse split of its ordinary shares into shares of higher par value, or on a split of its ordinary shares into shares of lower par value, or on distribution of bonus shares – all from the date of signing the agreement and through a date prior to the option exercise date. The option may be exercised one time, no later than 5 years from the date of signing the agreement (or, under certain circumstances, a slightly longer period), at any time after the average monthly credit utilization volume by Bank customers on their cards has reached a minimum volume stated in the agreement. The number of ordinary shares to be allotted in conjunction with exercise of the option shall be calculated using a formula stated in the agreement, in accordance with transactions made by card holders.

In return for exercising the option, the Bank shall pay an exercise price based on a formula prescribed by the agreement, based on the current company value. The option may be converted into a cash payment to the Bank should there by any hindrance to exercising the option by way of allotment of CAL shares as stated above, or should CAL elect to do so.

The agreement is effective for a 5-year term from the date of signing. Should the option be exercised or cashed as stated above, the agreement term shall be extended to 10 years from its signing date, and may be further extended. The agreement is subject to all regulatory requirements required by statute, if any.

The signed agreement and the related option granted to the Bank have no material impact on the Group's financial statements.

Note 19 - Contingent Liabilities and Special Commitments (continued)

14) On May 9, 2012, the Bank received a letter from the Supervisor of Banks, which announces the filing of a motion to impose a monetary sanction on the Bank for an alleged breach of provisions of the Prohibition on Money Laundering Act, 2000. The motion to impose a monetary sanction is based on findings in an audit report by the Supervisor of Banks with regard to AML, which refers to the period from 2007 through mid-2010.

    The Bank has reviewed the findings listed in the audit report. The Bank has accepted some of these, with regard to the period under review. Moreover, in early 2010 the Bank replaced the person in charge of implementing the Bank's obligations pursuant to the Act, and since then the Bank has expanded its activity, including with regard to training and deployment of the relevant directives, and has taken extensive measures to amend the shortcomings listed in the audit report, which were mostly relevant only for the period under review.

    The Bank filed its response to this motion on June 9, 2012.

    On July 24, 2012, the Committee for Imposing Monetary Sanctions on Banking Corporations (hereinafter: "the committee") held a meeting at which the Bank concluded its verbal claims, in conformity with the committee's operating procedure.

    On September 19, 2012, the Bank received a letter from the Supervisor of Banks, informing the Bank of a monetary sanction imposed on the Bank, amounting to NIS 3.8 million - paid on October 9, 2012.

15) A trust company that is a subsidiary of the Bank executes trust transactions that include primarily trusteeships for trust funds, for debenture holders, for owners of restricted shares and for the maintenance of bank accounts.

16) In a labor agreement signed between the Bank and its employee representatives on December 30, 1993, the Bank made available long-term loans to its employees, to finance the retroactive purchase of pension rights from certain pension funds with which the Bank had undertakings in this connection, which bear specified interest and are CPI-linked. It was agreed that if, on the maturity date of each of the aforementioned loans, it becomes clear that the linkage differentials and the interest accrued exceed the yield accumulated in an agreed provident fund, they would be reduced accordingly. The tax effects, if any, related to this reduction will devolve on the Bank. When such a difference is created, an appropriate provision is made. At the balance sheet date, the balances of these loans amount to NIS 22 million.

17) The Bank has undertaken vis-à-vis the trustee of the debentures and subordinated notes issued by Tefahot Issue Company from the United Mizrahi Bank Group Ltd., to fulfill the payment terms, as stated in the debentures and subordinated notes. For further details, see Note 11.

Note 19 - Contingent Liabilities and Special Commitments (continued)

18) The Bank has committed to borrowers in certain savings plans who would borrow from the Bank, to the following fixed terms:

	December 31,	
	2012	2011
90% of the interest rate prevailing at the time the loan was issued [(1)]	1,216	1,350
0.25% less than the interest prevailing at the time the loan was issued [(1)]	253	489
	1,469	**1,839**

(1) The commitment may be utilized only if certain conditions stipulated in the savings plans are met. Granting of credit is subject at all times to the Bank's exclusive discretion, in accordance with procedures determined by the Bank, with due consideration to client attributes and subject to review of the actual client application for credit to be granted by the Bank.

19) As from July 1, 2004, a new two-year agreement went into effect between Bank Tefahot, at that time, and the Government, whereby the collection commission rate determined by the tender held by the Ministry of Finance, with the participation of the mortgage banks will apply to loans to eligible borrowers issued on or after July 1, 2004, which are significantly lower than the commission rate on loans issued until June 30, 2004. This agreement has been continuously extended each year, most recently through June 30, 2013.

In May 2008, a new agreement between the Ministry of Finance and the banks became effective (the agreement is expected to be renewed annually, unless any one of the parties announced their wish to terminate the agreement), whereby loans to eligible borrowers with low point rating are provided out of Bank funds and at Bank risk. The interest on these loans is determined based on interest for special assistance loans out of Ministry of Finance funds. Loan terms have been specified to be 25, 20, 15 or up to 10 years, at the customer's choice, but no longer than the term of assistance out of Ministry of Finance funds. The remainder of the conditions would be in line with generally acceptable conditions for assistance out of Ministry of Finance funds, including a waiver of early repayment commission.

For loans granted to certain eligible borrowers, the Ministry of Finance pays the banks which grant loans out of Bank funds the difference between the actual interest rate charged and the average interest rate published by the Bank of Israel, plus spread. Concurrently with loan origination

as stated above, the banks may continue to grant loans out of Ministry of Finance funds to low-rated eligible borrowers, under terms of the previous agreement (dated 2004) and subject to total loans for the group of low-rated eligible borrowers not exceeding 8% of total Bank loans to this group (out of Bank funds and out of budgeted funds).

The agreement for provision of assistance to eligible borrowers out of Bank funds, signed in 2008, has been extended through June 30, 2012.

Bank management estimates that impact of the new tender would moderate, in coming years, the decline in revenues from new loans in the eligible borrowers' credit portfolio, due to previous Ministry of Finance tenders. The share of this credit portfolio for which the Bank is responsible would increase at the same time.

Group revenues from all loans to eligible borrowers under State responsibility in 2012 amounted to NIS 66 million, compared to NIS 73 million in 2011.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

E. Financial derivatives activity – volume, credit risk and maturity

a) Activity on consolidated basis

						2012
	Interest contracts					
	NIS - CPI	Other	Currency contracts	Contracts for shares	Commodity contracts and others	Total
1. **Stated amounts of financial derivatives**						
A. Hedging derivatives (1)						
Forward contracts	100	-	-	-	-	100
Swaps	-	2,457	-	-	-	2,457
Total	**100**	**2,457**	**-**	**-**	**-**	**2,557**
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	-	2,449	-	-	-	2,449
B. ALM derivatives (1)(2)						
Forward contracts	10,481	1,550	54,712	-	38	66,781
Option contracts traded on stock exchange:						
Options written	-	-	1,640	2,900	-	4,540
Options purchased	-	-	2,372	2,939	-	5,311
Other option contracts:						
Options written	-	-	8,245	-	-	8,245
Options purchased	-	-	8,505	-	-	8,505
Swaps	2,042	38,153	12,625	-	-	52,820
Total	**12,523**	**39,703**	**88,099**	**5,839**	**38**	**146,202**
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	1,493	21,717	-	-	-	23,210
C. Other derivatives (1)						
Forward contracts	-	-	342	-	-	342
Option contracts traded on stock exchange:						
Options written	-	-	3,872	9,836	-	13,708
Options purchased	-	-	3,872	9,836	-	13,708
Other option contracts:						
Options written	-	161	148	809	1	1,119
Options purchased	-	72	174	787	1	1,034
Swaps	-	-	-	3,957	-	3,957
Total	**-**	**233**	**8,408**	**25,225**	**2**	**33,868**

(1) Except for credit derivatives and spot contracts for foreign currency swaps.

(2) Derivatives which constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

E. Financial derivatives activity – volume, credit risk and maturity (continued)

a) Activity on consolidated basis (continued)

						2012
	Interest contracts		contractual Foreign currency	contracts with respect to shares	Commodity contracts and others	Total
	NIS - CPI	Other				
D. Credit derivatives and spot contracts for foreign currency swaps						
Credit derivatives in which the Bank is guarantor	-	-	-	-	177	177
Foreign currency spot swap contracts	-	-	2,331	-	-	2,331
Total	**-**	**-**	**2,331**	**-**	**177**	**2,508**
Total stated amounts of derivatives	**12,623**	**42,393**	**98,838**	**31,064**	**217**	**185,135**
2. **Fair value, gross, of financial derivatives**						
A. Hedging derivatives (1)						
Positive fair value, gross	1	-	-	-	-	1
Negative fair value, gross	-	316	-	-	-	316
B. ALM derivatives (1)(2)						
Positive fair value, gross	245	1,280	1,451	282	1	3,259
Negative fair value, gross	215	1,490	1,377	131	1	3,214
C. Other derivatives (1)						
Positive fair value, gross	-	2	79	177	-	258
Negative fair value, gross	-	1	79	166	-	246
D. Credit derivatives						
Credit derivatives in which the Bank is guarantor						
Negative fair value, gross	-	-	-	-	1	1
Total positive fair value, gross	**246**	**1,282**	**1,530**	**459**	**1**	**3,518**
Total negative fair value, gross (3)	**215**	**1,807**	**1,456**	**297**	**2**	**3,777**

(1) Except for credit derivatives and spot contracts for foreign currency swaps.

(2) Derivatives which constitute part of the Bank's asset and liability management system, which were not intended as hedges.

(3) Includes negative fair value, gross, of embedded financial derivatives amounting to NIS 4 million.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

E. Financial derivatives activity – volume, credit risk and maturity (continued)

a) Activity on consolidated basis (continued)

						2011
	Interest contracts				Commodity	
			Currency	Contracts	contracts	
	NIS - CPI	Other	contracts	for shares	and others	Total
1. **Stated amounts of financial derivatives**						
A. Hedging derivatives [(1)]						
Forward contracts	670	-	-	-	-	670
Swaps	-	2,211	-	-	-	2,211
Total	**670**	**2,211**	**-**	**-**	**-**	**2,881**
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	-	2,211	-	-	-	2,211
B. ALM derivatives [(1)(2)]						
Forward contracts	9,721	3,509	58,780	119	15	72,144
Option contracts traded on stock exchange:						
Options written	-	-	2,436	338	-	2,774
Options purchased	-	-	[(3)] 3,317	763	-	4,080
Other option contracts:						
Options written	-	-	11,396	803	12	12,211
Options purchased	-	-	10,559	366	12	10,937
Swaps	1,279	40,068	10,541			51,888
Total	**11,000**	**43,577**	**97,029**	**2,389**	**39**	**154,034**
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	779	24,983	-	-	-	25,762
C. Other derivatives [(1)]						
Forward contracts	-	-	427	-	-	427
Option contracts traded on stock exchange:						
Options written	-	-	5,096	9,120	2	14,218
Options purchased	-	-	5,096	9,120	2	14,218
Other option contracts:						
Options written	-	1,016	7	649	-	1,672
Options purchased	-	1,019	26	591	-	1,636
Swaps	-	-	-	3,863	-	3,863
Total	**-**	**2,035**	**10,652**	**23,343**	**4**	**36,034**

(1) Except for credit derivatives and spot contracts for foreign currency swaps.
(2) Derivatives which constitute part of the Bank's asset and liability management system, which were not intended as hedges.
(3) Reclassified.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

E. Financial derivatives activity – volume, credit risk and maturity (continued)

a) Activity on consolidated basis (continued)

						2011
	Interest contracts		Foreign currency contractual	contracts with respect to shares	Commodity contracts and others	
	NIS - CPI	Other	currency	shares	and others	Total
D. Credit derivatives and spot contracts for foreign currency swaps						
Credit derivatives in which the Bank is guarantor	-	-	-	-	535	535
Credit derivatives in which the Bank is beneficiary	-	-	-	-	28	28
Foreign currency spot swap contracts	-	-	2,364	-	-	2,364
Total	**-**	**-**	**2,364**	**-**	**563**	**2,927**
Total stated amounts of derivatives	**11,670**	**47,823**	**110,045**	**25,732**	**606**	**195,876**
2. **Fair value, gross, of financial derivatives**						
A. Hedging derivatives (1)						
Positive fair value, gross	5	-	-	-	-	5
Negative fair value, gross	-	292	-	-	-	292
B. ALM derivatives (1)(2)						
Positive fair value, gross	209	995	(3) 1,541	(3) 30	1	2,776
Negative fair value, gross	144	1,287	1,918	(3) 5	1	3,355
C. Other derivatives (1)						
Positive fair value, gross	-	3	81	(3) 250	-	334
Negative fair value, gross	-	3	78	(3) 244	-	325
D. Credit derivatives						
Credit derivatives in which the Bank is guarantor						
Negative fair value, gross	-	-	-	-	9	9
Total positive fair value, gross	**214**	**998**	**1,622**	**280**	**1**	**3,115**
Total negative fair value, gross (4)	**144**	**1,582**	**1,996**	**249**	**10**	**3,981**

(1) Except for credit derivatives and spot contracts for foreign currency swaps.
(2) Derivatives which constitute part of the Bank's asset and liability management system, which were not intended as hedges.
(3) Reclassified.
(4) Includes negative fair value, gross, of embedded derivatives amounting to NIS 17 million.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

E. Financial derivatives activity – volume, credit risk and maturity (continued)

b) Credit risk on financial derivatives according to counter-party to the contract on consolidated basis

						2012
	Stock exchanges	Banks	Dealers/ Brokers	Governments and central banks	Others	Total
Balance sheet balances of underlying assets [(1)]	470	2,358	23	-	667	3,518
Off-balance sheet credit risk on financial derivatives [(2)]	-	1,255	433	-	2,214	3,902
Total credit risk on financial derivatives	**470**	**3,613**	**456**	**-**	**2,881**	**7,420**

						2011
	Stock exchanges	Banks	Dealers/ Brokers	Governments and central banks	Others	Total
Balance sheet balances of underlying assets [(1)]	[(3)] 291	2,002	21	-	801	3,115
Off-balance sheet credit risk on financial derivatives [(2)]	[(3)] 71	[(3)] 2,681	[(3)] 126	-	[(3)] 2,130	5,008
Total credit risk on financial derivatives	**362**	**4,683**	**147**	**-**	**2,931**	**8,123**

(1) Includes positive fair value, gross, of embedded derivatives amounting to NIS 0 million.

(2) Off-balance sheet credit risk for financial derivatives (including those with negative fair value) as calculated for the purposes of the per-borrower limitation in Regulation 313.

(3) Reclassified.

Note 19 - Contingent Liabilities and Special Commitments (continued)

As of December 31

Reported amounts (NIS in millions)

E. Financial derivatives activity – volume, credit risk and maturity (continued)

c) Maturity dates – stated amounts: year-end balances - Consolidated

					2012
	Up to three months	3 months to 1 year	1-5 years	Over 5 years	Total
Interest contracts:					
NIS-CPI	1,528	5,702	3,122	2,271	12,623
Other	2,989	11,061	13,475	14,868	42,393
Currency contracts	52,778	32,715	5,549	7,796	98,838
Contracts for shares	28,114	2,340	610	-	31,064
Commodities and other contracts	34	6	40	137	217
Total	**85,443**	**51,824**	**22,796**	**25,072**	**185,135**

					2011
	Up to three months	3 months to 1 year	1-5 years	Over 5 years	Total
Interest contracts:					
NIS-CPI	3,135	4,159	3,125	1,251	11,670
Other	6,155	13,896	12,706	15,066	47,823
Currency contracts	(1) 67,072	32,756	4,630	5,587	110,045
Contracts for shares	22,158	3,304	270	-	25,732
Commodities and other contracts	35	332	200	39	606
Total	**98,555**	**54,447**	**20,931**	**21,943**	**195,876**

(1) Reclassified.

Note 19 - Contingent Liabilities and Special Commitments (continued)

E. Financial derivatives activity – volume, credit risk and maturity (continued)

d) Description of derivative instruments and the risks inherent in such activity

1) General

The Bank's activities in derivative instruments, such as futures contracts and forward trades, options and financial swaps, are executed both as broker for its customers and on its own account, as part of the management of its assets and liabilities and in order to minimize as much as possible the Bank's exposure to market risks.

2) Types and description of activity in derivative instruments

The activities in derivative instruments include currency contracts, interest rate contracts and other contracts, and contracts for customers in the MAOF market, on different indices and assets, as outlined below:

- Forward transactions and futures contracts:
  A contract between two parties to buy or sell a specified quantity of commodities, currencies, interest or other financial instruments ("underlying asset"), to be executed on a future date and at a price specified in advance.

- Swaps:
  Contracts to exchange a specified quantity of underlying assets on the transaction date, with a reciprocal obligation to re-exchange the items that had been exchanged on a future date.

- Options:
  Contracts that confer, in return for the payment of a premium, the right to purchase (call) or sell (put) the underlying assets at a pre-determined fixed price, quantity and time.

- Credit derivatives:
  Contracts that confer, in return for the payment of a one-time or periodic premium, the right to receive payment in the event of a change in credit rating, the inability to honor obligations or any other credit event, relating to the State or the company, as stipulated in the contract.

- Spot trades (transactions for immediate delivery):
  Exchanges of two currencies, based on an exchange rate agreed in advance, to be executed within two business days.

Note 19 - Contingent Liabilities and Special Commitments (continued)

3) Risks inherent in derivative instrument activities:
The Bank's activities in derivative instruments expose it to credit risks and to market risks that include interest risks, basis risks and liquidity risks, as detailed below:

A. Credit exposure in derivative instruments, which is defined by the Supervisor of Banks as "present credit exposure", quantifies the maximum possible loss that the Bank will sustain if the other party does not fulfill the terms of the transaction, after deducting enforceable set-off agreements, and without taking collateral into account. In the credit derivatives written by the Bank, the credit exposure is expressed in the amount that the Bank will be obliged to pay if the event stipulated in the contract occurs. To manage the credit extent of the exposure inherent in derivative instruments over the life of the transaction, the exposure is estimated at the price of the commitment in the reverse transaction for the remaining life of the transaction. Collateral requirements are determined according to the type of customer, and sometimes, at a fixed percentage of the credit facility determined for a given customer. In other cases, exposure is determined according to scenarios based on the Black and Scholes Model. The collateral required by the Bank usually includes liquid collateral such as securities, deposits, etc., and is valued as collateral in accordance with the various collateral coefficients used by the Bank.

B. The market risks in derivative instruments with which the Bank contends result from their various sensitivities to unexpected fluctuations in interest rates, the inflation rate, exchange rates and other financial indices. The Bank manages the market risks involved in financial derivatives by including these instruments within the management of exposure to market risks of the entire range of the Bank's operations.

C. Liquidity risk from transactions in derivative financial instruments stems from the inability to quickly close the exposure by cash payment or by creating reverse exposure. The derivative instruments and their effect on liquidity needs are an integral part of the management of the Bank's liquidity risk in accordance with Proper Banking Conduct Regulation 342.

D. The operational risk in derivative instruments is due to the risk of erroneous execution of transactions, beginning from the date they are entered into until they are settled, due to human error or to mechanical error.

Note 20 – Balances and Estimates of Fair Value of Financial Instruments

1) Fair value of financial instruments

For most of the Bank's financial instruments, a "market price" cannot be quoted, because there is no active market in which they are traded. Therefore, the fair value is estimated using acceptable pricing models, such as present value of future cash flows, discounted at an interest rate that reflects the level of risk inherent in the instrument.

The estimate of fair value using future cash flows and determination of a discount rate are subjective. Therefore, for most financial instruments, the estimation of fair value is not necessarily an indication of the realization value of the financial instrument on the balance sheet date. The fair value valuation uses interest rates prevailing at the balance sheet date, and does not take into account fluctuations in interest rates. The assumption of different interest rates will result in fair values that could be substantially different. Essentially, this relates to financial instruments that bear fixed interest or are interest-free, or to CPI-linked financial instruments with shorter maturities than those in which similar transactions are actually effected. In addition, in determining the fair value, the commissions to be received or paid as a result of the business activity are not taken into account, nor does it include the tax effect. Moreover, the difference between the carrying value and the fair value balances may not be realized, because, in most cases, the Bank will hold the financial instrument to maturity. Consequently, it should be emphasized that the data included in this note do not indicate the value of the Bank as a going concern. In addition, because of the broad range of valuation techniques and the possible estimates to be applied during the valuation of the fair value, one must be cautious when comparing the fair values between different banks.

2) The principal methods and assumptions for estimating fair value of financial instruments:

A. Fair value was calculated by the managements in the Bank Group, taking into account the possibility of early repayment based on empirical analysis.
The early repayment assumptions in mortgages are based on empirical testing of the early repayment rate out of all mortgages, on annual basis. These assumptions are tested from time to time against actual early repayments for each linkage segment and for each interest type individually.
The Bank has deposits and savings accounts with exit points (bearing fixed or variable interest, linked or non-linked to the CPI) for which interest terms are known in advance. Assumptions concerning exit at these points are based on empirical analysis and are reviewed and updated from time to time. The early repayment assumptions resulted in a NIS 385 million decrease in total fair value of assets, and in a NIS 60 million decrease in total fair value of liabilities.

B. Deposits from the public, deposits with banks and loans to Governments, as well as debentures and subordinated notes – the discounting of future cash flows using interest rates at which, in the estimation of the managements in the Bank Group, similar transactions could have been executed on the balance sheet date. For transactions which bear variable interest, the difference between the spread over the variable interest base for the transaction, and the spread for similar transactions upon the reporting date is separated. In calculating fair value, this difference is treated as a fixed interest component.

Note 20 – Balances and Estimates of Fair Value of Financial Instruments

C. Securities, including asset-backed securities, see Note 1.I.

D. Investments in corporations for which a market value cannot be quoted are not included in this Note at their fair value but rather at cost, (net of impairment provisions) which, in the estimation of management, is not lower than the fair value of the investment.

E. Loans to the public – The fair value of loans to the public is estimated by the present value of cash flows method, using an appropriate discount rate. For loans which bear variable interest, the difference between the spread over the variable interest base for the transaction, and the spread for similar loans upon the reporting date is separated. In calculating fair value, this difference is treated as a fixed interest component. The balance of the loans was broken down according to the risk level of the individual borrower at the balance sheet date, and as to mortgages, according to homogeneous categories, for which the flows of future receipts (principal and interest) were calculated.

These receipts were discounted at the interest rate at which the Bank estimates it will be possible to execute similar transactions on the balance sheet date, and which reflects the risk level inherent in the loans to a customer at a similar risk level, and as to mortgages, according to homogeneous categories.

In certain loans granted by the Bank and a subsidiary at variable interest that changes at a frequency of up to three months, namely housing loans, the carrying value approximates fair value.

F. The fair value of problem debt is calculated using a discount rate that reflects the level of credit risk inherent in them. In no case were these discount rates lower than the highest interest rate used by the members of the Bank Group in providing loans on the balance sheet date. The future cash flows of problematic debt were calculated after deducting the provisions for credit loss.

A decrease of 1% in the discount rate affects the fair value of the problematic debts of the Group by NIS 23 million.

G. Off-balance sheet financial instruments in which the balance represents credit risk and contingent liabilities and special commitments – the balance in the financial statements as of the balance sheet date approximates the fair value.

H. Financial derivatives – Financial derivatives that have an active market were valued at market value. Financial derivatives not traded on an active market have been valued using internal models and have been validated by a professional appointed by the Bank to this end.

Note 20 – Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

3. Information on the fair value of financial instruments is presented below:

A. Fair value balances

					Consolidated
					December 31, 2012
	Carrying				Fair value
	amount	Level 1[(1)]	Level 2[(1)]	Level 3[(1)]	Total
Financial assets					
Cash and deposits with banks	16,671	2,259	11,930	2,495	16,684
Securities[(3)]	9,041	5,783	3,001	260	9,044
Securities loaned or sold in repurchase agreements	207	207	-	-	207
Loans to the public, net	128,651	-	10,463	119,690	130,153
Loans to Governments	317	-	-	317	317
Investments in associates	33	-	-	33	33
Assets with respect to derivatives	3,518	484	2,182	[(2)] 852	3,518
Other financial assets	1,926	-	-	1,926	1,926
Total financial assets	[(4)] **160,364**	**8,733**	**27,576**	**125,573**	**161,882**
Financial liabilities					
Deposits from the public	128,499	-	32,232	98,369	130,601
Deposits from banks	1,694	-	71	1,669	1,740
Deposits from the Government	107	-	-	120	120
Debentures and subordinated notes	14,039	13,259	-	2,203	15,462
Liabilities with respect to derivatives	3,773	351	2,270	[(2)] 1,152	3,773
Other financial liabilities	3,657	-	2,889	768	3,657
Total financial liabilities	[(4)] **151,769**	**13,610**	**37,462**	**104,281**	**155,353**

(1) Level 1 - Fair value measurement using quoted prices on an active market. Level 2 - Fair value measurement using other significant observed data. Level 3 - Fair value measurement using significant non-observed data.
(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.
(3) For more details of the carrying amount and fair value of securities, see Note 3.
(4) Includes assets and liabilities amounting to NIS 36,578 million and NIS 29,564 million, respectively, whose carrying amount equals their fair value (instruments presented at fair value on the balance sheet). For more information on instruments measured at fair value on recurring basis and on non-recurring basis, see Note b. blow.

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

A. Fair value balances - continued:

					Consolidated
					As of December 31, 2011 (unaudited)
	Carrying				Fair value
	amount	Level 1(1)	Level 2(1)	Level 3(1)	Total
Financial assets					
Cash and deposits with banks	15,972	4,259	8,360	3,364	15,983
Securities(3)	8,432	5,531	2,578	318	8,427
Securities loaned or sold in repurchase agreements	136	136	-	-	136
Loans to the public, net	(5) 119,293	-	9,304	(5) 111,609	120,913
Loans to Governments	196	-	-	196	196
Investments in associates	31	-	-	31	31
Assets with respect to derivatives	(5) 3,115	(5) 76	2,001	(2) 1,038	3,115
Other financial assets	(5) 1,249	-	-	1,249	1,249
Total financial assets	(4) **148,424**	**10,002**	**22,243**	**117,805**	**150,050**
Financial liabilities					
Deposits from the public	119,236	-	10,336	110,509	120,845
Deposits from banks	2,007	-	47	2,007	2,054
Deposits from the Government	152	-	-	166	166
Debentures and subordinated notes	12,202	(5) 10,445	-	(5) 2,671	13,116
Liabilities with respect to derivatives	3,964	122	2,577	(2) 1,265	3,964
Other financial liabilities	3,241	-	2,736	505	3,241
Total financial liabilities	(4) **140,802**	**10,567**	**15,696**	**117,123**	**143,386**

(1) Level 1 - Fair value measurement using quoted prices on an active market. Level 2 - Fair value measurement using other significant observed data. Level 3 - Fair value measurement using significant non-observed data.
(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.
(3) For more details of the carrying amount and fair value of securities, see Note 3.
(4) Includes assets and liabilities amounting to NIS 35,675 million and NIS 28,205 million, respectively, whose carrying amount equals their fair value (instruments presented at fair value on the balance sheet). For more information on instruments measured at fair value on recurring basis and on non-recurring basis, see Note b. blow
(5) Reclassified.

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

B. Items measured at fair value:

1. On recurring basis

					Consolidated
					For the year ended December 31, 2012
	Prices quoted on active market (level 1)	Other significant observed data (level 2)	Non-observed significant data (level 3)	Total fair value	Carrying amount
Assets					
Securities available for sale					
Debentures and bonds					
Of Government of Israel	2,106	2,594	-	4,700	4,700
Of foreign governments	95	-	-	95	95
Of banks and financial institutions in Israel	123	-	-	123	123
Of banks and financial institutions overseas	-	165	229	394	394
Of others in Israel	25	-	-	25	25
Of others overseas	10	127	31	168	168
Shares	4	-	-	4	4
Securities held for trading:					
Debentures of the Government of Israel	2,291	-	-	2,291	2,291
Of banks and financial institutions overseas	3	-	-	3	3
Credit with respect to loans to clients	393	-	-	393	393
Assets with respect to derivatives (1)					
Interest contracts:					
NIS / CPI	-	145	101	246	246
Other	-	1,109	173	1,282	1,282
Currency contracts	109	928	493	1,530	1,530
Contracts for shares	375	-	84	459	459
Commodities and other contracts	-	-	1	1	1
Total assets	**5,534**	**5,068**	**1,112**	**11,714**	**11,714**
Liabilities					
Deposits with respect to borrowing from clients	393	-	-	393	393
Liabilities with respect to derivatives (1)					
Interest contracts:					
NIS / CPI	-	167	48	215	215
Other	-	1,482	325	1,807	1,807
Currency contracts	126	621	709	1,456	1,456
Contracts for shares	225	-	68	293	293
Commodities and other contracts	-	-	2	2	2
Other	-	-	4	4	4
Total liabilities	**744**	**2,270**	**1,156**	**4,170**	**4,170**

(1) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

B. Items measured at fair value - continued:

1. On recurring basis

					Consolidated
					For the year ended December 31, 2011
	Prices quoted on active market (level 1)	Other significant observed data (level 2)	Non-observed significant data (level 3)	Total fair value	Carrying amount
Assets					
Securities available for sale					
Debentures and bonds					
Of Government of Israel	3,227	2,297	-	5,524	5,524
Of foreign governments	86	-	-	86	86
Of banks and financial institutions in Israel	159	-	-	159	159
Of banks and financial institutions overseas	-	192	220	412	412
Asset-backed	-	-	61	61	61
Of others in Israel	81	-	-	81	81
Of others overseas	9	89	37	135	135
Shares	6	-	-	6	6
Securities held for trading:					
Debentures of the Government of Israel	1,183	-	-	1,183	1,183
Of banks and financial institutions overseas	3	-	-	3	3
Securities loaned or sold in repurchase agreements	136	-	-	136	136
Credit with respect to loans to clients	231	-	-	231	231
Assets with respect to derivatives (1) (2)					
Interest contracts:					
NIS / CPI	-	86	128	214	214
Other	-	879	119	998	998
Currency contracts	76	782	682	1,540	1,540
Contracts for shares	-	254	108	362	362
Commodities and other contracts	-	-	1	1	1
Total assets	**5,197**	**4,579**	**1,356**	**11,132**	**11,132**
Liabilities					
Deposits with respect to borrowing from clients	231	-	-	231	231
Liabilities with respect to derivatives (1) (2)					
Interest contracts:					
NIS / CPI	-	116	28	144	144
Other	-	1,273	309	1,582	1,582
Currency contracts	122	1,081	793	1,996	1,996
Contracts for shares	-	107	125	232	232
Commodities and other contracts	-	-	10	10	10
Other	-	11	6	17	17
Total liabilities	**353**	**2,588**	**1,271**	**4,212**	**4,212**

(1) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

(2) Reclassified.

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

B. Items measured at fair value:

2. On non-recurring basis - Continued

					For the year ended
				December 31, 2012	December 31, 2012
					(audited)
	Prices quoted on active market (level 1)	Other significant observed data (level 2)	Non-observed significant data (level 3)	Total fair value	Loss
Impaired credit whose collection is contingent on collateral	-	-	145	145	72

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

C. Change in items measured at fair value on recurrent basis, included in level 3 - continued:

									Consolidated
									For the year ended December 31, 2012
		Realized / unrealized gain (loss), net [(1)] included							
	Fair value as of January 01, 2012	On statement of profit and loss	On statement of other compre-hensive income under Equity	Acquisi-tions	Sales	Disposi-tions	Transfer to level 3	Fair value as of December 31, 2012	Unrealized gain (loss) with respect to instruments held as of December 31, 2012
Assets									
Securities available for sale									
Debentures and bonds:									
Of banks and financial institutions overseas	220	9	-	-	-	-	-	229	9
Asset-backed	61	(11)	(1)	-	(49)	-	-	-	(1)
Of others overseas	37	2	-	-	-	(8)	-	31	2
Assets with respect to derivatives [(2) (3)]									
Interest contracts:									
NIS / CPI	128	8	-	48	-	(106)	23	101	111
Other	119	19	-	40	-	(5)	-	173	125
Currency contracts	682	94	-	300	-	(583)	-	493	91
Contracts for shares	108	-	-	63	-	(87)	-	84	-
Commodities and other contracts	1	-	-	1	-	(1)	-	1	-
Total assets	**1,356**	**121**	**(1)**	**452**	**(49)**	**(790)**	**23**	**1,112**	**337**
Liabilities									
Liabilities with respect to derivatives [(2) (3)]									
Interest contracts:									
NIS / CPI	28	2	-	45	-	(30)	3	48	(6)
Other	309	(67)	-	90	-	(7)	-	325	(100)
Currency contracts	793	73	-	413	-	(570)	-	709	(10)
Contracts for shares	125	-	-	68	-	(125)	-	68	-
Commodities and other contracts	10	-	-	1	-	(9)	-	2	-
Other [(3)]	6	(1)	-	-	-	(1)	-	4	(1)
Total liabilities	**1,271**	**7**	**-**	**617**	**-**	**(742)**	**3**	**1,156**	**(117)**

(1) Realized gain (loss) included on the statement of profit and loss under "Non-interest financing revenues". Unrealized gain and loss included in equity under Adjustments for Presentation of Available-for-Sale Securities at Fair Value.

(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties. Standard 157 applies as from January 1, 2011. Level 3 classifications with respect to credit risk are included under column "Transfer to level 3".

(3) Included on statement of profit and loss under "Non-interest financing revenues".

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

C. Change in items measured at fair value on recurrent basis, included in level 3 - Continued:

	Consolidated								
	For the year ended December 31, 2011								
		Realized / unrealized gain (loss), net [(1)] included							
	Fair value as of January 01, 2011	On statement of profit and loss	On statement of other comprehensive income under Equity	Acquisitions	Sales	Dispositions	Transfer to level 3	Fair value as of December 31, 2011	Unrealized gain (loss) with respect to instruments held as of December 31, 2011
Assets									
Securities available for sale									
Debentures and bonds:									
Of banks and financial institutions overseas	221	-	(1)	-	-	-	-	220	(1)
Asset-backed	60	-	1	-	-	-	-	61	1
Of others overseas	45	2	(3)	-	-	(7)	-	37	(1)
Assets with respect to derivatives [(2) (3) (4)]									
Interest contracts:									
NIS / CPI	8	2	-	-	(10)	-	128	128	2
Other	4	(1)	-	-	-	-	116	119	(1)
Currency contracts	-	-	-	-	-	-	682	682	-
Contracts for shares	17	11	-	2	-	-	78	108	3
Commodities and other contracts	-	-	-	-	-	-	1	1	-
Total assets	**355**	**14**	**(3)**	**2**	**(10)**	**(7)**	**1,005**	**1,356**	**3**
Liabilities									
Liabilities with respect to derivatives [(2) (3) (4)]									
Interest contracts:									
NIS / CPI	62	(1)	-	-	(61)	-	28	28	(1)
Other	4	(1)	-	-	-	-	306	309	(1)
Currency contracts	-	-	-	-	-	-	793	793	-
Contracts for shares	-	8	-	-	-	-	117	125	8
Commodities and other contracts	-	-	-	-	-	-	10	10	-
Other [(3)]	3	-	-	3	-	-	-	6	-
Total liabilities	**69**	**6**	**-**	**3**	**(61)**	**-**	**1,254**	**1,271**	**6**

(1) Realized gain (loss) included on the statement of profit and loss under "Non-interest financing revenues". Unrealized gain and loss included in equity under Adjustments for Presentation of Available-for-Sale Securities at Fair Value.
(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties. Standard 157 applies as from January 1, 2011. Level 3 classifications with respect to credit risk are included under column "Transfer to level 3".
(3) Included on statement of profit and loss under "Non-interest financing revenues".
(3) Reclassified.

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

D. Additional information about non-observed significant data and valuation techniques used in fair value measurement of items classified at Level 3:

	Fair value as of December 31, 2012	Valuation technique	Non-observed data	Range	Weighted average (unaudited)
Securities available for sale:					
Debentures of foreign banks and financial institutions	5	Estimated recouperation rate	Recouperation rate	5.00%	5.00%
Debentures of foreign banks and financial institutions	40	Cash flow discounting	Discount rate	1.06%-1.59%	1.54%
CLN	184	Cash flow discounting	Probability of default	0.65%-1.25%	1.17%
Asset-backed debentures	31	Cash flow discounting	Discount rate	5.97% -6.18%	6.11%
Debentures of foreign others		Estimated recouperation rate	Recouperation rate		
Assets with respect to derivatives:					
Interest contracts - NIS CPI	48	Cash flow discounting	Inflation expectations	(0.30%)-1.90%	1.00%
Contracts for shares	6	Options pricing model	Standard deviation for securities	29.50%-57.80%	30.40%
Other	798	Cash flow discounting	Counterparty credit quality	1.10%-3.60%	1.92%
Liabilities with respect to derivatives:					
Interest contracts - NIS CPI	4	Cash flow discounting	Inflation expectations	(0.30%)-1.90%	1.70%
Other	1,148	Cash flow discounting	Counterparty credit quality	1.10%-3.10%	1.92%

E. Transfers between Levels 1 and 2 of the fair value hierarchy

There were no transfers from Level 2 to Level 1 during the reported period.

F. Election of fair value alternative

Due to election of the fair value alternative, the Bank treats investments in certain debentures at fair value, charging the changes to profit and loss and classified the under the portfolio held for trading - even though they had not been purchased for this purpose.

Election of the fair value alternative was made for under the following circumstances:

1. Reduce volatility in profit and loss resulting from changes between the original measurement basis of financial instruments designated at the fair value alternative, and the measurement basis of financial derivatives used to manage risk with respect to such investments.
2. Complexity of implementing hedge accounting.
3. More accurate economic presentation of assets managed on fair value basis.

Note 20 - Balances and Estimates of Fair Value of Financial Instruments (continued)

Reported amounts (NIS in millions)

The following table lists the fair value of items measured at fair value due to election of the fair value alternative:

	Fair value as of December 31, 2012	Profit with respect to change in fair value for the year ended December 31, 2012
Securities available for sale	1,106	21

	Fair value as of December 31, 2011	Profit with respect to change in fair value for the year ended December 31, 2011
Securities available for sale	531	5

Note 21 - Interested and Related Parties - Consolidated

Reported amounts (NIS in millions)

A. Balances

	As of December 31, 2012									
							Interested parties		Related parties owned by the banking corporation	
	Controlling shareholders		Key executives [5]		Othets[6]		Was interested party during the transaction		Jointly-owned affiliates or investees	
	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]
Assets										
Loans to the public	4	4	4	6	473	647	-	1	8	20
Investments in affiliates	-	-	-	-	-	-	-	-	60	60
Liabilities										
Deposits from the public	9	11	34	44	134	1,069	-	-	1	7
Shares (included in shareholders' equity) [3]	4,164	4,164	-	39	-	-	-	-	-	-
Credit risk in off-balance sheet financial instruments [4]	1	1	5	5	162	173	-	-	-	-

(1) Reclassified.
(2) Based on balances at the end of each month.
(3) The share of interested and related parties in the Bank's capital.
(4) Credit risk in off-balance sheet financial instruments, as calculated for the purposes of per-borrower limitations.
(5) Key executives of the banking corporation or its parent company, including Board members and CEOs, along with their relatives.
(6) Any corporation in which a person or corporation included in one of these interested party groups has a controlling interest, jointly owns, has significant influence or owns 25% or more of their issued share capital or voting rights there of, or may appoint 25% or more of their Board members.

	As of December 31, 2011									
							Interested parties[1]		Related parties owned by the banking corporation	
	Controlling shareholders		Key executives [5]		Othets[6]		Was interested party during the transaction		Jointly-owned affiliates or investees	
	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]	Balance as of balance sheet date	Highest balance during the year [2]
	5	5	5	6	388	519	-	-	16	27
	-	-	-	-	-	-	-	-	17	17
	8	10	23	30	72	853	-	-	1	10
	3,659	3,659	43	46	-	-	-	-	-	-
	-	-	1	1	375	451	-	-	8	10

Note 21 - Interested and Related Parties – Consolidated - (continued)

Reported amounts (NIS in millions)

B. Summary of business results with interested and related parties

	For the year ended December 31,			
	2012			
	Interested parties			Related parties owned by the banking corporation
	Controlling shareholders	Key executives (2)	Others(3)	Jointly-owned affiliates or investees
Interest revenues with respect to loans to the public	-	-	20	1
Interests expenses with respect to deposits from the public	-	-	(2)	-
Total net, incomes (expenses)	**-**	**-**	**18**	**1**
Non-interest, financing revenues	-	-	2	-
Operating and other expenses	-	(42)	(3)	-
Total	**-**	**(42)**	**17**	**1**

C. Remuneration and other benefits payable to interested parties (by the banking corporation and its investees)

	For the year ended December 31,			
	2012			
	Key executives(2)		Others(3)	
	Total benefits	Total number of benefits recipients	Total benefits	Total number of benefits recipients
Interested party employed by or on behalf of the corporation	(4) 34	14	-	-
Board member not employed by or on behalf of the corporation	8	14	-	-
Other interested party not employed by or on behalf of the corporation	-	-	3	3

(1) Reclassified.

(2) Key executives in the Bank corporation or its parent company, including board members and executive management with their close relatives.

(3) Any corporation in which a person or corporation included in one of these interested party groups has a controlling interest, jointly owns, has significant influence or owns 25% or more of their issued share capital or voting rights there of, or may appoint 25% or more of their Board members.

(4) Includes: short-term employee benefits: NIS 23(2011-26,2010-23) million; post-emplyments benefits: NIS 1(2011-5, 2010-0) million; share-based payment: NIS 10(2011-18,2010-29) million.

2011				2010			
Interested parties(1)			Related parties owned by the banking corporation	Interested parties(1)			Related parties owned by the banking corporation
Controlling shareholders	Key executives (2)	Others(3)	Jointly-owned affiliates or investees	Controlling shareholders	Key executives (2)	Others(3)	Jointly-owned affiliates or investees
-	-	16	1	-	-	-	1
-	-	(1)	-	-	-	(4)	-
-	**-**	**15**	**1**	**-**	**-**	**(4)**	**1**
-	**-**	2	**-**	**-**	**-**	**-**	**-**
-	(55)	(2)	-	-	(57)	(3)	-
-	**(55)**	**15**	**1**	**-**	**(57)**	**(7)**	**1**

(1) 2011				(1) 2010			
Key executives(2)		Others((3)		Key executives(2)		Others((3)	
Total benefits	Total number of benefits recipients	Total benefits	Total number of benefits recipients	Total benefits	Total number of benefits recipients	Total benefits	Total number of benefits recipients
(4) 49	15	-	-	(4) 52	15	-	-
6	12	-	-	5	12	-	-
-	-	2	4	-	-	3	4

Note 22 - Interest revenues and expenses

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011(1)	2010(1)	2012	2011(1)	2010(1)
A. Interest revenues (2)						
From loans to the public	6,146	6,364	5,210	5,814	6,046	4,960
From loans to Governments	7	4	8	7	4	21
From deposits with the Bank of Israel and from cash	189	276	39	153	225	13
From deposits with banks	26	68	48	16	10	17
From securities loaned or sold in repurchase agreements	4	4	4	4	4	4
From debentures	219	124	200	164	54	159
Total interest revenues	**6,591**	**6,840**	**5,509**	**6,158**	**6,343**	**5,174**
B. Interest expenses						
On deposits from the public	2,594	3,004	1,906	2,823	3,115	1,931
On deposits from governments	5	11	11	5	11	11
On deposits from banks	68	15	146	252	133	298
For debentures	710	711	558	275	347	323
Total interest expenses	**3,377**	**3,741**	**2,621**	**3,355**	**3,606**	**2,563**
Total interest revenues, net	**3,214**	**3,099**	**2,888**	**2,803**	**2,737**	**2,611**
C. Details of net effect of hedging financial derivatives on interest revenues	**(73)**	**(78)**	**(36)**	**(73)**	**(78)**	**(36)**
D. Details of interest revenues (expenses) on accrual basis from debentures						
Held to maturity	26	5	-	-	-	-
Available for sale	176	120	210	147	55	169
Held for trade	17	(1)	(10)	17	(1)	(10)
Total included under interest revenues	**219**	**124**	**200**	**164**	**54**	**159**

(1) Reclassified upon initial application of the Supervisor of Banks' directives concerning format of statement of profit and loss for banking corporations. For details see Note 1.D.1.

(2) Includes the effective element in the hedging ratios.

Note 23 - Non-interest financing revenues

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011[1]	2010[1]	2012	2011[1]	2010[1]
A. Non-interest financing revenues with respect to non-trade operations						
1. From activity in derivatives						
Non-effective element of hedging ratios [2]	(2)	(2)	-	(2)	(2)	-
Net revenues (expenses) with respect to ALM derivatives [3]	(100)	369	(293)	(100)	369	(295)
Total from activity in derivatives	**(102)**	**367**	**(293)**	**(102)**	**367**	**(295)**
2. **From investment in debentures**						
Gain on sale of debentures available for sale	118	11	30	113	11	28
Loss on sale of debentures available for sale	(5)	(2)	-	(4)	(2)	-
Provision for impairment of debentures available for sale	(8)	(10)	(2)	(8)	(10)	(2)
Total from investment in debentures	**105**	**(1)**	**28**	**101**	**(1)**	**26**
3. **Exchange rate differences, net**	**(21)**	**(409)**	**174**	**(30)**	**(442)**	**178**
4. **Gain (loss) from investment in shares**						
Gains on sale of available-for-sale shares	5	5	3	5	5	3
Provision for impairment of available-for-sale shares	-	-	(5)	-	-	(5)
Dividends from available-for-sale shares	24	1	1	24	1	1
Total from investment in shares	**29**	**6**	**(1)**	**29**	**6**	**(1)**
5. Net gain with respect to loans sold	**-**	**6**	**-**	**-**	**6**	**-**
Total non-interest financing revenues (expenses) with respect to non-trade operations	**11**	**(31)**	**(92)**	**(2)**	**(64)**	**(92)**

(1) Reclassified upon initial application of the Supervisor of Banks' directives concerning format t of statement of profit and loss for banking corporations. For details see Note 1.D.1.

(2) Excludes the effective element in the hedging ratios.

(3) Derivatives which constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 23 - Non-interest financing revenues - Continued

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011(1)	2010(1)	2012	2011(1)	2010(1)
B. Non-interest financing revenues with respect to trade operations (2)						
Net revenues with respect to other derivatives	40	30	58	40	30	58
Realized gain (loss) from adjustment to fair value of debentures held for trade, net	32	11	5	32	11	5
Unrealized gain (loss) from adjustment to fair value of debentures held for trade, net	12	8	4	12	8	4
Total from trade operations (3)	**84**	**49**	**67**	**84**	**49**	**67**
Details of non-interest financing revenues with respect to trade operations, by risk exposure						
Risk exposure	-	3	-	-	3	-
Foreign currency exposure	22	21	(14)	22	21	(14)
Exposure to shares	(3)	6	41	(3)	6	41
Exposure to commodities and others	65	19	40	65	19	40
Total	**84**	**49**	**67**	**84**	**49**	**67**

(1) Reclassified upon initial application of the Supervisor of Banks' directives concerning format of statement of profit and loss for banking corporations. For details see Note 1.D.1.
(2) Includes exchange rate differentials resulting from trading operations.
(3) For interest revenues from investment in debentures held for trading, see Note 22.

Note 24 - Commissions

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
Account management [1]	294	296	292	273	275	273
Translation differences	129	127	116	117	119	109
Credit cards	142	141	132	98	100	95
Handling credit	161	135	119	150	127	113
Foreign trade activity	34	43	38	34	39	36
Activity in securities and certain derivatives	215	265	303	169	212	232
Net revenues from credit portfolio service	77	88	95	75	86	92
Mutual fund distribution commissions	35	39	39	27	31	32
Home insurance distribution commissions	26	33	33	-	-	-
Life insurance distribution commissions	103	92	86	34	30	40
Commissions from financing transactions	153	131	95	152	127	92
Provident fund operations	47	53	53	26	31	29
Other commissions	36	31	31	25	23	22
Total operating commissions	**1,452**	**1,474**	**1,432**	**1,180**	**1,200**	**1,165**

(1) In Israeli and foreign currency

Note 25 - Other Income

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
Gain from sale of buildings and equipment	-	-	4	-	-	4
Capital loss from sale of buildings and equipment	-	(2)	(2)	-	(2)	(2)
Management fees from subsidiaries	-	-	-	-	1	1
Revenues from security services	6	6	6	6	6	6
Trustee fees	6	7	8	-	-	-
Other	14	6	[1] 17	14	7	12
Total other income	**26**	**17**	**33**	**20**	**12**	**21**

(1) Reclassified.

Note 26 - Salaries and Related Expenses

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	[(1)]2011	[(1)]2010	2012	[(1)]2011	[(1)]2010
Salaries (including bonuses)	1,108	1,057	1,038	951	907	899
Expense arising from share-based payment transactions [(2)]	31	24	25	28	22	23
Severance pay, provident and pension, continuing education fund and vacation	202	188	152	188	174	131
National Insurance and VAT on salaries	322	302	284	288	271	254
Other related expenses	24	26	25	17	18	18
Supplement to provisions for related expenses, due to changes in salaries during the current year	14	18	5	2	2	2
Total salaries and related expenses	**1,701**	**1,615**	**1,529**	**1,474**	**1,394**	**1,327**
Includes: salaries and related expenses overseas	49	44	47	35	30	33

(1) Reclassified.

(2) See Note 16.A.

Note 27 - Other Expenses

For the year ended December 31,

Reported amounts (NIS in millions)

	Consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
Marketing and advertising	65	72	56	50	58	45
Communications	43	44	45	32	33	35
Computer	72	77	66	12	13	13
Office expenses	34	30	27	27	23	20
Insurance	12	11	19	11	11	17
Professional services	74	74	77	64	62	64
Board members' fees	9	8	7	7	6	6
Training and continuing education	8	9	9	5	6	6
Commissions	23	28	47	23	29	31
Cars and travel	42	39	41	41	39	41
Sundry	51	52	44	46	52	46
Total other expenses	**433**	**444**	**438**	**318**	**332**	**324**

Note 28 - Provision for Taxes on Profit

For the year ended December 31,

Reported amounts (NIS in millions)

A. Composition

	Consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
Current taxes -						
For the current year	591	526	449	511	437	403
For prior years	1	-	(51)	-	-	(47)
Total current taxes	**592**	**526**	**398**	**511**	**437**	**356**
Changes in deferred taxes -						
For the current year	7	(4)	31	5	14	28
For prior years	-	-	(1) 40	-	-	(1) 40
Total deferred taxes	**7**	**(4)**	**71**	**5**	**14**	**68**
Total provision for taxes on income	**599**	**522**	**469**	**516**	**451**	**424**
Includes provision for taxes overseas	18	7	22	16	4	17

(1) Retroactively adjusted as per directives of the Supervisor of Banks with regard to employee rights. See Note 1.Q.2.

Note 28 - Provision for Taxes on Profit (continued)

For the year ended December 31,

Reported amounts (NIS in millions)

B. Reconciliation between the theoretical tax amount that would be applicable had the profit been taxable at the statutory tax rate applicable to Banking Corporation in Israel, and between the provision for taxes on profit as included in the statement of profit and loss:

			Consolidated			The Bank
	2012	2011	2010	2012	2011	2010
Statutory tax rate applicable to a bank in Israel	35.53%	34.48%	35.35%	35.53%	34.48%	35.35%
Tax amount based on statutory tax rate	613	553	456	519	464	399
Tax (tax saving) from:						
Subsidiaries' income:						
In Israel [(1)(2)]	(16)	(16)	(10)	(6)	(7)	(3)
Overseas	(2)	(8)	(1)	-	-	-
Special and supplementary provision for doubtful debts	4	-	1	4	-	1
Exempt income	(2)	(1)	1	(2)	(1)	1
Adjustment differences on depreciation, amortization and capital gains	(1)	(1)	(2)	(1)	(1)	(2)
Other non-deductible expenses	9	12	4	8	10	3
Temporary differences and losses for which [(1)] deferred taxes have not been recorded	(14)	11	(1)	(14)	11	(1)
Taxes for prior years	1	-	[(3)] 5	-	-	[(3)] 4
Change in deferred tax balances due to change in tax rates	(12)	[(1)] (29)	12	(11)	[(1)] (25)	18
Adjustment differences on monetary assets and other differences, net	19	1	[(1)] 4	19	-	[(1)] 4
Total provision for taxes on income	**599**	**522**	**469**	**516**	**451**	**424**

(1) Reclassified.

(2) In the Bank -auxiliary corporations

(3) Retroactively adjusted as per directives of the Supervisor of Banks with regard to employee rights. See Note 1.Q.2.

Note 28 - Provision for Taxes on Profit (continued)

For the year ended December 31,

Reported amounts (NIS in millions)

C. On August 30, 2012, the VAT Ordinance (VAT Rate for Non-Profits and Financial Institutions) (Interim Provision), 2009 was published, and an amendment to said Ordinance was published on December 31, 2009, with a further amendment to said Ordinance published on February 13, 2011. According to the amended ordinance, which updates the profit tax rate, in each of 2009 and 2012, the VAT with respect to payroll tax and profit tax would be updated from an average rate of 16% to an average rate of 17% as from September 1, 2012. Moreover, the payroll tax rate applicable to financial institutions would increase to 17% for payrolls payable with respect to work as from September 2012, compared to 16% for 2012 and 15.5% for 2013 and there after.

On December 5, 2011, the Knesset passed the Taxation Burden Revision Act (Legislative Amendments), 2011. According to the amendment, the gradual decrease in corporate tax rate, doen to 18% in 2006, was rescinded, and the corporate tax rate from 2012 onwards would be 25%.

Following the aforementioned amendments, the statutory tax rates applicable to banking corporations have been amended as follows:

Tax year	Statutory tax rate
2011	34.48%
2012	35.53%
2013 and later	35.90%

D. The Bank has finalized tax assessments, or tax assessments deemed to be final, through the 2007 tax year. The former Bank Adanim has finalized tax assessments through 2006. Bank Yahav has finalized tax assessments through 2002.

E. In conjunction with the merger of Adanim Mortgage Bank Ltd. on February 23, 2009, certification was received from the Income Tax Authority on February 01, 2009, on fulfillment of the conditions of the merger. It should be noted that, as aforesaid in Par. D., the Bank has no final tax assessments for the year 2009.

Note 28 - Provision for Taxes on Profit (continued)

For the year ended December 31,

Reported amounts (NIS in millions)

F. Deferred tax assets and provision for deferred taxes

	Consolidated				The Bank			
	December 31,				December 31,			
	Balances		Average tax rate in %		Balances		Average tax rate in %	
	2012	2011	2012	2011	2012	2011	2012	2011
Deferred taxes for:								
Provision for credit loss[(1)]	372	389	35.9	35.1	342	351	35.9	35.1
Provision for vacation pay, long-service bonuses and employee rights [(1)]	102	91	35.9	35.0	90	73	35.9	35.0
Excess provision for employee rights on retirement, net [(1)]	239	236	35.9	35.1	233	229	35.9	35.1
Other securities [(1)(3)]	4	7	35.9	35.1	4	7	35.9	35.1
Adjustment of depreciable non-monetary assets[(2)]	(22)	(15)	35.9	35.1	(23)	(17)	35.9	35.1
Other - from monetary assets [(1)(2)(4)]	15	9	35.9	35.1	15	9	35.9	35.1
Other - from non-monetary assets, net [(1)(2)]	28	31	35.9	35.1	26	30	35.9	35.1
Total deferred taxes	738	748	35.9	35.1	687	682	35.9	35.1
Deferred taxes include:								
(1) Deferred tax assets included in "other assets"	772	776	35.9	35.1	721	710	35.9	35.1
(2) Deferred taxes payable included in "other liabilities"	(34)	(28)	35.9	35.1	(34)	(28)	35.9	35.1
Deferred taxes, net	**738**	**748**	**35.9**	**35.1**	**687**	**682**	**35.9**	**35.1**

(3) Changes in this item amounting to NIS 24 million due to adjustment of fair value of securities available for sale (last year – NIS 18 million) were charged to a separate item in shareholders' equity.

(4) Changes in this item amounting to NIS 7 million due to net gain from cash flow hedges (last year – NIS 4 million) were charged to a separate item in shareholders' equity.

Note 29 - Earnings per Ordinary Share

For the year ended December 31,

			Consolidated
			For the year ended December 31,
			Reported amounts (NIS in millions)
	2012	2011	2010 [(1)]
Net profit used to calculate earnings per share:			
Basic earnings			
Total net profit attributable to holders of ordinary shares of the banking corporation	1,076	1,044	801
Diluted earnings			
Total net profit attributable to holders of ordinary shares of the banking corporation	1,076	1,044	801
Earnings per share:			
Basic earnings			
Total net profit attributable to holders of ordinary shares of the banking corporation	4.77	4.65	3.63
Diluted earnings			
Total net profit attributable to holders of ordinary shares of the banking corporation	4.74	4.57	3.58

(1) Retroactively adjusted for application of the Supervisor of Banks' directives with regard to employee rights. Note 1.Q(2) below.

	2012	2011	2010
Weighted average number of shares [(1)]			
Weighted average number of ordinary shares used to calculate basic earnings	225,483,132	224,737,921	220,640,534
Weighted average number of ordinary shares used to calculate diluted earnings	226,997,469	228,446,525	223,896,184

(1) Excludes 2,500,000 shares bought back by the Bank. For details see Note 13.D.

Note 30 - Operating Segments and Geographic Regions - Consolidated

Bank Group operating segments

The Bank manages its operations in six major operating segments, which are distinguished by client characteristics and type of banking services required, as well as by the organizational unit responsible for servicing each segment. Operating segment definition is based on the Bank's organizational structure, as described below. The operations in the six operating segments include all areas of banking operations including classic banking activity (loans and deposits), securities activity for clients and activity in derivative instruments. Operations of the various segments are conducted via Bank branches, trading room, Business Centers, Bank HQ departments and subsidiaries in Israel and overseas.

The Bank's operating segments are:

Household segment - under responsibility of the Retail Division, This segment includes small household clients and mortgage operations. The division provides appropriate banking services and financial products to segment clients, including in the field of mortgages.

Small business segment – under responsibility of the Retail Division, which also serves small business clients, having an indebtedness level of less than NIS 6 million, sales of less than NIS 30 million and liquid asset balance of less than NIS 10 million. Banking services and financial products, including commercial banking services as required, are provided to segment clients.

Private banking – private banking is under responsibility of the Private Banking and International Operations sector of the Financial Division. Private banking sector clients are individual clients with liquid assets (primarily short-term deposits and security investments) over NIS 1 million. Clients of this segment have high financial wealth, to whom the Bank offers access to unique products and services in capital management activity, advisory service and investment management.

Commercial banking – clients of this segment are private and public companies of medium size (middle market) and medium level of indebtedness, and are served by the Business Banking Division, primarily by the Business sector, which operates via six business centers located throughout Israel. Business customers are assigned to the Business sector primarily using the following criteria: total indebtedness of NIS 6-25 million, sales of NIS 30-120 million or liquid assets of NIS 10-40 million. Segment clients operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

Business banking - the Major Corporations sector in the Business Division is responsible for the Business Banking segment, which is the focal point for handling the largest business clients. Criteria by which clients are assigned to the Corporate sector include: total indebtedness over NIS 25 million, sales over NIS 120 million or liquid assets over NIS 40 million. This segment provides a range of banking and financial services to the largest companies in the economy, in an array of industries, at relatively high levels of indebtedness. Segment clients operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

Financial management - operations in this segment include, inter alia, management of assets and liabilities, management of exposure to market risk, management of the nostro portfolio and liquidity management as well as trading room operations in the financial and capital markets. The segment is under responsibility of the Finance Division, except for investments in non-banking corporations, which are under the responsibility of the business division.

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

The main products offered by the Bank's different operating segments are:

- **Banking and finance** – an array of banking services offered to private and corporate clients, including management of checking account, provision of a current loan account, different kinds of credit and guarantees, receiving deposits, foreign trade activities (imports, exports, documentary credit, etc.), trading in derivative instruments, including trading in currencies and interest rates, etc.
- **Capital market** – security transactions for clients on stock exchanges in Israel and overseas, provident fund operating services and mutual fund distribution (management of provident funds and mutual funds until sold) which are among investment tracks available to Bank clients.
- **Credit cards** – A set of financial products and banking services given in conjunction with credit cards issued to Bank clients by credit card companies in Israel.
- **Mortgages** – Housing loans secured by charges on a residence, out of the Bank's funds and within the framework of government aid programs.
- **Construction and real estate** – banking operations vis-à-vis companies in the real estate sector, as well as unique banking services for the real estate sector, including the financing of real estate products by the closed financing method.

The principles used in assigning balances, income and expenses to clients in the system are as follows:

- Credit interest revenues and deposit interest expenses are directly attributed to the client. For credit, an expense set at cost of capital raised is attributed to clients, against an inter-segment credit to the Financial Management segment. For deposits, revenue set at cost of capital raised is attributed to clients, against an intersegment debit to the Financial Management segment. Each of the segments is credited for capital attributed to operations there of, against a debit to the Financial Management segment. Capital consumption is measured by the average risk-free assets managed by the segment.
- For derivative instrument operations, profits are attributed to the client at the spread incorporated in the price of the derivative instrument quoted to the client. Profit arising from changes to fair value of derivatives is attributed to Financial Management.
- Profit and loss from Bank investment in securities and from strategic positions are attributed to Financial Management.
- Expenses with respect to credit loss are directly attributed to clients on behalf of whom they were made.
- Commission and other revenues are specifically attributed to clients.
- Payroll, building maintenance and other expenses attributed specifically to branches, are loaded on branch clients.
- Payroll expenses of headquarters staff, maintenance and other expenses not specifically related to branches, are loaded on clients based on appropriate load bases.
- Expenses attributed directly to Bank branches, including salary and benefits, rent and maintenance are attributed to different segments as inter-segment expenses, based on segment affiliation of clients services by the branches.

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

- Provision for tax on operating profit is attributed to clients, pro-rated in accordance with the effective tax rate and accounting for tax impact referring to specific segments and not to all Bank operations.
- Return on equity is calculated as the ratio of net profit to attributed equity. Equity is attributed based on average client risk assets.
- Balance sheet and assets-under-management balances are specifically attributed to clients.
- Fixed assets are attributed based on appropriate ratios.

In order to analyze results of Bank operations by relevant criteria, clients have been assigned to the organizational units in charge of servicing them. Information presented below by operating segment is based on the Bank's organizational structure on client assignment to various departments and then to operating segments, and on attribution of results and balances to clients and segments in the profitability measurement system.

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

For the year ended December 31, 2012

Reported amounts (NIS in millions)

B. Information on operating segments

	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net:							
From outside operating segments	3,265	(12)	316	198	331	(884)	3,214
Inter-segment	(1,543)	85	133	(27)	324	1,028	-
Total interest revenues, net	**1,722**	**73**	**449**	**171**	**655**	**144**	**3,214**
Non-interest financing revenues	7	1	1	1	76	9	95
Commissions and other revenues	778	55	238	60	216	131	1,478
Total income	**2,507**	**129**	**688**	**232**	**947**	**284**	**4,787**
Expenses with respect to credit loss	65	(12)	36	8	178	1	276
Operating and other expenses							
From outside operating segments	1,717	78	459	66	217	249	2,786
Inter-segment	(119)	5	(53)	68	86	13	-
Other operating expenses - total	**1,598**	**83**	**406**	**134**	**303**	**262**	**2,786**
Pre-tax profit	844	58	246	90	466	21	1,725
Provision for taxes on profit	294	20	86	31	161	7	599
After-tax profit	**550**	**38**	**160**	**59**	**305**	**14**	**1,126**
Share in net profits of affiliates, after tax	-	-	-	-	-	-	-
Net profit:							
Before attribution to non-controlling interest	550	38	160	59	305	14	1,126
Attributable to non-controlling interest	(50)	-	-	-	-	-	(50)
Attributable to equity holders of the banking corporation	**500**	**38**	**160**	**59**	**305**	**14**	**1,076**
Return on equity (percentage of net profit attributed to equity holders of the banking corporation out of average equity)	**12.8%**	**39.9%**	**38.8%**	**14.3%**	**10.5%**	**2.6%**	**13.1%**
Average balance of assets	85,857	2,274	7,179	4,704	26,919	28,110	155,043
Includes: Investments in associates	-	-	-	-	-	60	60
Average balance of liabilities	58,446	6,958	8,280	3,545	31,702	35,811	144,742
Average balance of risk assets(1)	51,763	1,191	5,160	5,172	36,323	5,476	105,085
Average balance of provident and mutual fund assets	-	-	-	-	-	73,821	73,821
Average balance of securities	26,895	7,767	5,606	3,633	59,957	42,271	146,129
Loans to the public, net (end balance)	93,013	1,178	6,860	4,679	22,921	-	128,651
Deposits from the public (end balance)	58,645	7,077	8,159	3,358	33,934	17,326	128,499
Average balance of other assets managed	20,206	2	191	224	261	-	20,884

(1) Risk weighted assets - as calculated for capital adequacy (Proper Conduct of Banking Business Regulation No. 201).

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

For the year ended December 31, 2012

Reported amounts (NIS in millions)

C. Information on profit from interest revenues before expenses with respect to credit loss

	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Margin from credit granting operations	1,131	31	344	144	552	-	2,202
Margin from receiving deposits	524	41	80	24	70	-	739
Other	67	1	25	3	33	144	273
Total interest revenues, net	**1,722**	**73**	**449**	**171**	**655**	**144**	**3,214**

D. Information on geographic regions [(1)]

	Revenues for the year ended December 31, 2012(2)	Net profit for the year ended December 31, 2012	Total assets as of December 31, 2012
Israel	4,672	1,054	155,010
Outside of Israel	115	22	7,232
Total consolidated	**4,787**	**1,076**	**162,242**

(1) Profit and assets according to geographic regions were allocated on the basis of the location of the Group's offices.

(2) Includes operating profit from financing operations before expenses with respect to credit loss and other operating revenues.

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

For the year ended December 31, 2011

Reported amounts (NIS in millions)

B. Information regarding operating segments (2)(3)

	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net:							
From outside operating segments	3,600	10	413	240	216	(1,380)	3,099
Inter-segment	(2,000)	79	26	(67)	304	1,658	-
Total interest revenues, net	**1,600**	**89**	**439**	**173**	**520**	**278**	**3,099**
Non-interest financing revenues	11	1	3	2	44	(43)	18
Commissions and other revenues	808	56	236	65	196	130	1,491
Total income	**2,419**	**146**	**678**	**240**	**760**	**365**	**4,608**
Expenses with respect to credit loss	68	(5)	84	6	164	21	338
Operating and other expenses							
From outside operating segments	1,635	74	441	65	223	229	2,667
Inter-segment	(116)	5	(50)	66	84	11	-
Other operating expenses - total	**1,519**	**79**	**391**	**131**	**307**	**240**	**2,667**
Pre-tax profit	832	72	203	103	289	104	1,603
Provision for taxes on profit	271	26	66	34	91	34	522
After-tax profit	**561**	**46**	**137**	**69**	**198**	**70**	**1,081**
Share in net profits of affiliates, after tax	-	-	-	-	-	1	1
Net profit:							
Before attribution to non-controlling interest	561	46	137	69	198	71	1,082
Attributable to non-controlling interest	(38)	-	-	-	-	-	(38)
Attributable to equity holders of the banking corporation	**523**	**46**	**137**	**69**	**198**	**71**	**1,044**
Return on equity (percentage of net profit attributed to equity holders of the banking corporation out of average equity)	**15.4%**	**41.0%**	**34.9%**	**17.2%**	**7.7%**	**24.9%**	**14.6%**
Average balance of assets	77,528	2,533	6,545	4,888	25,222	24,802	141,518
Includes: Investments in associates	-	-	-	-	-	52	52
Average balance of liabilities	51,460	6,352	7,164	3,189	30,213	35,562	133,940
Average balance of risk assets(1)	46,260	1,201	5,046	5,176	33,362	4,960	96,005
Average balance of provident and mutual fund assets	-	-	-	-	-	77,626	77,626
Average balance of securities	23,927	9,672	6,980	3,212	60,730	32,886	137,407
Loans to the public, net (end balance)	83,768	1,191	6,428	4,778	23,128	-	119,293
Deposits from the public (end balance)	54,091	5,831	7,773	3,471	32,524	15,546	119,236
Average balance of other assets managed	21,150	-	223	154	86	-	21,613

(1) Risk weighted assets - as calculated for capital adequacy (Proper Conduct of Banking Business Regulation No. 201).

(2) Reclassified.

(3) Reclassified upofn initial application of the Supervisor of Banks' directives concerning format of statement of profit and loss for banking corporations. For details see Note 1.D.1.

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

For the year ended December 31, 2011

Reported amounts (NIS in millions)

C. Information on profit from interest revenues before expenses with respect to credit lossed

	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Margin from credit granting operations	1,001	35	323	144	402	-	1,905
Margin from receiving deposits	527	52	83	22	71	-	755
Other	72	2	33	7	47	278	439
Total interest revenues, net	**1,600**	**89**	**439**	**173**	**520**	**278**	**3,099**

D. Information on geographic regions [(1)]

	Revenues for the year ended December 31, 2011(2)	Net profit for the year ended December 31, 2011	Total assets as of December 31, 2011
Israel	4,476	1,010	142,365
Outside of Israel	132	34	7,881
Total consolidated	**4,608**	**1,044**	**150,246**

(1) Profit and assets according to geographic regions were allocated on the basis of the location of the Group's offices.

(2) Includes operating profit from financing operations before expenses with respect to credit loss and other operating revenues.

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

For the year ended December 31, 2010

Reported amounts (NIS in millions)

B. Information regarding operating segments [(2)(3)]

	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net:							
From outside operating segments	2,780	(5)	358	220	504	(969)	2,888
Inter-segment	(1,401)	58	(15)	(63)	53	1,368	-
Total interest revenues, net	**1,379**	**53**	**343**	**157**	**557**	**399**	2,888
Non-interest financing revenues	(8)	1	6	3	36	(63)	(25)
Commissions and other revenues	815	58	219	65	153	155	1,465
Total income	**2,186**	**112**	**568**	**225**	**746**	**491**	**4,328**
Expenses with respect to credit loss	83	-	45	2	343	-	473
Operating and other expenses							
From outside operating segments	1,574	63	414	69	210	(4) 236	2,566
Inter-segment	(112)	(2)	(47)	70	79	12	-
Other operating expenses - total	**1,462**	**61**	**367**	**139**	**289**	**248**	**2,566**
Pre-tax profit	641	51	156	84	114	243	1,289
Provision for taxes on profit	233	19	56	30	41	90	469
After-tax profit	408	32	100	54	73	153	820
Share in net profits of affiliates, after tax	-	-	-	-	-	-	-
Net profit:							
Before attribution to non-controlling interest	408	32	100	54	73	153	820
Attributable to non-controlling interest	(18)	-	-	-	-	(1)	(19)
Attributable to equity holders of the banking corporation	**390**	**32**	**100**	**54**	**73**	**152**	**801**
Return on equity (percentage of net profit attributed to equity holders of the banking corporation out of average equity)	**12.7%**	**52.2%**	**27.6%**	**13.6%**	**2.8%**	**48.5%**	**11.8%**
Average balance of assets	68,097	2,040	5,292	4,590	24,821	18,290	123,130
Includes: Investments in associates	-	-	-	-	-	52	52
Average balance of liabilities	45,392	5,724	6,383	2,970	21,098	34,362	115,929
Average balance of risk assets[(1)]	40,863	765	4,518	4,945	32,475	4,242	87,808
Average balance of provident and mutual fund assets	-	-	-	-	-	77,130	77,130
Average balance of securities	27,045	7,315	7,840	4,059	66,264	35,081	147,604
Loans to the public, net (end balance)	73,869	962	5,771	4,717	21,721	-	107,040
Deposits from the public (end balance)	46,864	4,946	6,413	3,631	24,072	20,065	105,991
Average balance of other assets managed	22,655	-	369	3	156	-	23,183

(1) Risk weighted assets - as calculated for capital adequacy (Proper Conduct of Banking Business Regulation No. 201).

(2) Reclassified.

(3) Reclassified upon initial application of the Supervisor of Banks' directives concerning format of statement of profit and loss for banking corporations. For details see Note 1.D.1.

(4) Retroactively adjusted as per directives of the Supervisor of Banks with regard to employee rights. See Note 1.Q(3).

Note 30 - Operating Segments and Geographic Regions - Consolidated (continued)

For the year ended December 31, 2010

Reported amounts (in NIS millions)

C. Information on profit from interest revenues before expenses with respect to credit losses

	Households	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Margin from credit granting operations	836	19	258	134	405	-	1,652
Margin from receiving deposits	424	35	57	16	48	-	580
Other	119	(1)	28	7	104	399	656
Total	**1,379**	**53**	**343**	**157**	**557**	**399**	**2,888**

D. Information on geographic regions [(1)]

	Revenues for the year ended As of December 31, 2010 [(2)]	Net profit for the year ended As of December 31, 2010 [(3)]	Total assets As of December 31, 2010 [(3)]
Israel	4,167	756	125,246
Outside of Israel	161	45	8,058
Total consolidated	**4,328**	**801**	**133,304**

(1) Revenues and assets by geographic regions were allocated based on Group office locations.
(2) Includes operating profit from financing operations before expenses with respect to credit loss and other commission revenues.
(3) Retroactively adjusted as per directives of the Supervisor of Banks with regard to employee rights. See Note 1.Q(3).

Note 32 - Information Based on Nominal Data - the Bank

(NIS in millions)

	As of December 31	
	2012	2011
Total assets	151,659	139,933
Total liabilities	143,029	132,455
Total shareholders' equity	**8,630**	**7,478**

	For the year ended December 31,		
	2012	2011	2010
Nominal net profit	1,083	1,070	820

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