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And a Description of the Bank Group's Business

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

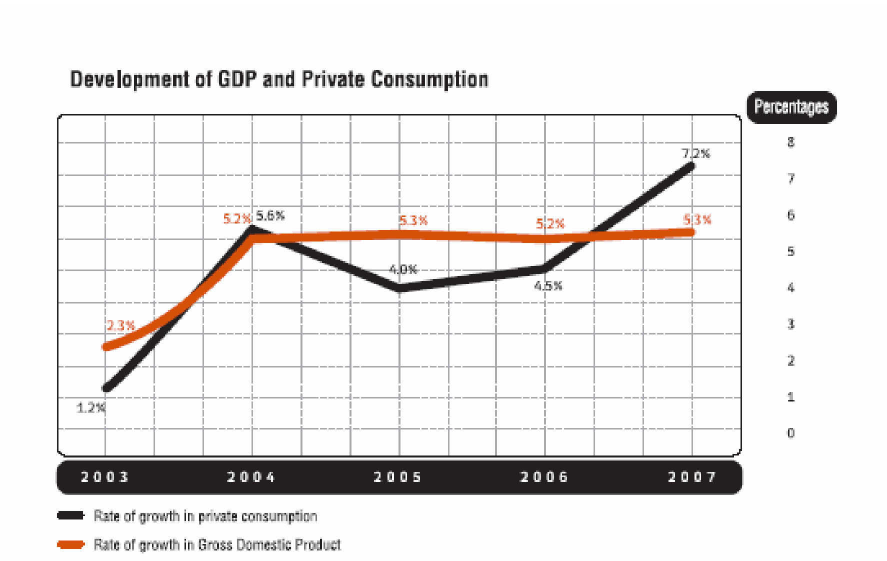
At the meeting of the Board of Directors held on March 24, 2008, 17 Adar B 5768, it was resolved to approve and publish the consolidated financial statements of Mizrahi Tefahot Bank Ltd. and its investees as at December 31, 2007.
The financial statements were prepared in accordance with the directives and guidelines issued by the Supervisor of Banks.

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

Developments in Israel's Economy in 2007

Real Developments

In 2007, rapid growth of the economy, which started in the second half of 2003, continued. According to prelimiary estimates by the Central Bureau of Statistics with regard to national accounts for 2007, GDP grew by 5.3% in 2007, following growth of 5.2% in 2006. Per capita GDP grew by 3.5% in 2007, following growth of 3.4% in 2006, and domestic business product grew by 6.3% following growth by 6.5% in 2006. Imports of goods and services grew by 12.8% in 2007, compared to 3.3% in the previous year.



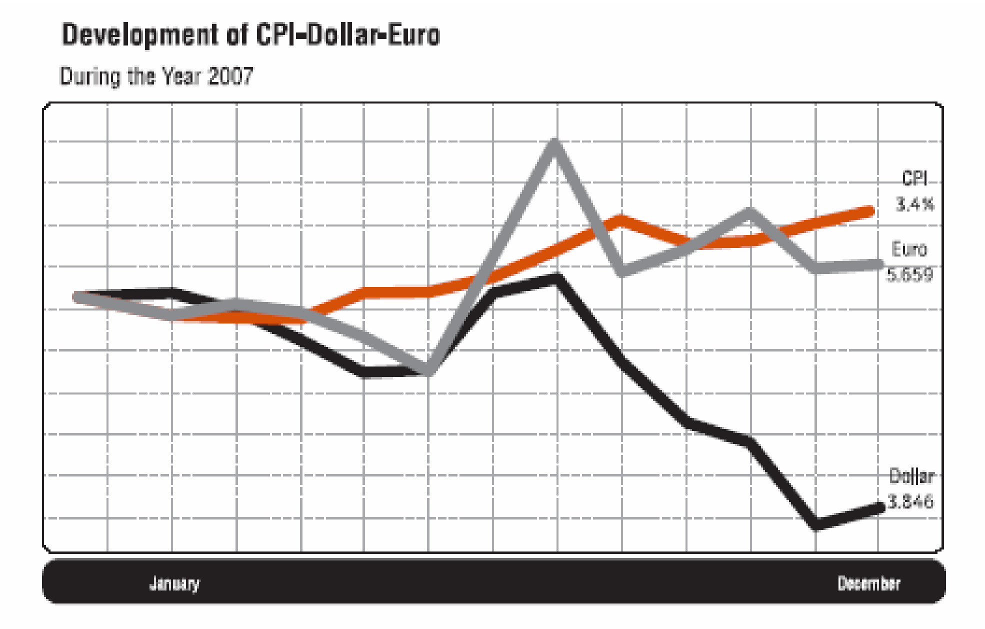
On the use side, 2007 saw sharp growth in private consumption by 7.2% in 2007 (in 2006 - 4.5%), which reflects 5.3% growth (in 2006 - 2.7%) in per capita private consumption. Growth rate for export of goods and services was 8.6% (in 2006 - 5.9%); capital investments grew by 13.6% (in 2006 - 10.1%); and public consumption grew by 2.6% (in 2006 - 2.3%).

In 2007, the decline in unemployment rate continued, down to 7.4% on average (temporary data), vs. 8.4% in 2006, accompanied by growh in the civilian work force.

Inflation and exchange rates

In 2007, the Consumer Price Index rose by 3.4%, higher than the government's target range of 1%-3% annually. This compares to a 0.1% decline in 2006. The factors which led to accelerated inflation were primarily: prices of food, fruits and vegetables as well as housing maintenance, whereas the revaluation of the NIS vs. the USD moderated the increase in the CPI.

In 2007, the NIS was revaluated by 9.0% vs. the USD, and was devaluated by 1.7% vs. the Euro. At December 31, 2007, the exchange rate reached NIS 3.846 to the dollar, compared with NIS 4.225 to the dollar on December 31, 2006. The NIS exchange rate to the Euro at December 31, 2007 was NIS 5.659 per Euro, compared with NIS 5.564 per Euro at the end of 2006. In early 2008 the NIS continued to be revaluated vs. the USD, as well as vs. the Euro, with exchange rates as of March 17, 2008 being NIS 3.426 to 1 USD and NIS 5.401 to 1 Euro.



Monetary and fiscal policy

In the first half of 2007, the Bank of Israel lowered interest rates for its sources 5 times, totaling 1.5 percentage points, down to a nominal 3.5% par annum. In the second half of 2007, in view of increased indications of accelerated inflation, the Bank of Israel twice raised interest rates by 0.25% each time, so interest rate for December 2007 was at 4.00%. In late December the interest (for January 2008) was raised to 4.25%. At end of February 2008, the Bank of Israel announced a 0.5% decrease in interest rate (for March 2008) – to 3.75%.

Total deficit in the government 2007 budget (excluding credit) amounted to NIS 0.1 billion, a very low 0.02% of GDP, compared to a target of 2.9% of GDP.

The government's domestic budget (including credit) recorded a surplus of NIS 9.5 billion. The low deficit is primarily due to revenue receipts, which were higher than planned by NIS 14.5 billion.

Residential construction and the mortgage market

The limited volume of activity in the residential construction industry continued in 2007 as well. According to estimated by the Central Bureau of Statistics for 2007, investment in residential constructing in 2007 was similar to that in 2006, following the slow-down in the industry in recent years (except for a 6% growth in 2006, mainly due to repairs of damage caused by the war in Lebanon). The first 10 months of 2007 saw a decline in housing starts - by 6% over the same period in 2006, mainly in public sector construction and mainly in the periphery. Annualized housing starts in the first 10 months of 2007 amounted to less than 30,000 units.

In 2007, growth in demand for housing accelerated, and the number of residential unit transactions grew by 11% in the first 10 months of 2007 over the same period in the previous year, amounting to an annualized rate of 93,000 transactions.

Unsold new unit inventory at end of October 2007 was 16% lower than at end of 2006, standing at 16,500 units. Decreased inventory applied to private construction housing as well as to public construction housing.

Concurrently with the growth in number of transactions, and in view of the lower mortgage interest, 2007 saw an increase in mortgage origination (excluding refinancing), in terms of number of loans as well as amounts, compared to 2006, where mortgage origination decreased. The average credit amount for the average loan continued to grow in 2007. The refinancing rate out of total mortgages was similar to the previous year, relatively low compared to 2005 - the record year in refinancing. In 2007, the level of arrears improved relative to the balance of housing loans, with a decline in weight of arrears in banks' housing credit portfolio. This came about after stabilization of the level of arrears in 2005-2006.

In early August 2007, a motion was filed with the Court to suspend proceedings concerning the Heftziba construction group. After the hearing, the Court appointed a Special Administrator on its behalf to review facts with regard to the financial status of group companies and to present a program aimed at limiting damage due to collapse of Heftziba group companies; the Court ordered proceedings to be suspended for a set time period. On November 5, 2007, the Court extended the suspension of proceedings until further notice. Recently most banks, including Bank Mizrahi-Tefahot Ltd., reached agreements in principle with the Special Administrator, to allow the projects pledged to the banks to be exempted from the suspension of proceedings. The Court has yet to approve the agreement with Bank Mizrahi-Tefahot Ltd.

Capital market

The local capital market continued in 2007 the positive trend of recent years. This trend was supported by positive macro-economic data, in particular continued rapid growth of the economy - mainly of the business sector, decrease in national debt, low monetary interest and moderate inflationary environment.

On the stock exchange, the Tel Aviv 25 Index and the Tel Aviv 100 Index rose in 2007 by 31% and 25%, respectively. The Real Estate 15 Index finished 2007 with a 1% increase. Average daily trading volume in equity and convertible securities grew by 45% over 2006, amounting to NIS 2 billion. Issuance of equity and convertible securities in 2007 amounted to NIS 21 billion, an 80% growth over the previous year.

Note that the domestic stock market benefited in 2007 from a foreign capital inflow amounting to $800 million.

In early 2008, due to impact of declines in capital markets world wide, primarily resulting from concerns with regard to a slow-down in global economy and the outcome of the sub-prime crisis in the USA – major stock indices have declined. From January 1, 2008 to March 17, 2008 the Tel Aviv 25 Index declined by 21%, with the Tel Aviv 100 Index declining by 23%. This was accompanied by growth in the average daily trading volume in equity and convertibles, to NIS 2.4 billion.

On the bond market, the business sector raised in 2007 NIS 87 billion from the public and from institutional investors, an 85% growth over the previous year. Note that reduction in government debt raising in the first half of the year and the pension fund reform supported this trend. Average daily trading volume in bonds grew 90% in 2007, and amounted to NIS 3.3 billion.

The Bond Index rose 4% in 2007, with the Non-Linked Bond Index rising 2.5% and the CPI-Linked Bond Index rising 6%.

From January 1, 2008 to March 17, 2008 the Bond Index, the Non-linked Bond Index and the Linked Bond Index rose by 1.9%, 3.0% and 1.4%, respectively. Average daily trading volume in bonds grew to NIS 4.2 billion.

Global economy

According to an estimate by the International Monetary Fund, the global growth rate in 2007 was 5%, similar to the previous year. Growth rates in the USA, Euro-land and Japan slowed in 2007, ranging from 2%-2.5%. China and India, whose weight in global production has been increasing in recent years, saw continued rapid growth of 11% and 9%, respectively.

The slow-down in the real estate market and the sub-prime crisis in the USA led to decreased willingness to extend credit and to a liquidity crunch, which caused a decline in demand and slower growth in the USA. Against this backdrop, the US Federal Bank lowered interest rates in the second half of 2007 by a total of 1 percentage point (in January-March 2008 the US Federal Bank further reduced interest rates by a cumulative 2.0 percentage points).

Following the rise in oil and commodity prices, inflation rose in 2007 in the USA, Euro-land and in other countries.

In view of the sub-prime crisis and slower growth in the USA, increase in price of oil and commodities and the concern with regard to their impact on the global economy, global capital markets were unstable in the second half of 2007. The growth trend in major equity indices in most markets in the first half of 2007 was reversed, with declines in most indices. The Dow Jones Industrials and S&P 500 declined in the second half of 2007 by 1.1% and 2.3%, respectively – compared to increase by 7.6% and 6.0%, respectively, in the first half of the year; the Dj EuroSTOXX, CAC and FTSE 100 indices declined in the second half of 2007 by 2.0%, 7.3% and 2.3%, respectively – compared to increase by 9.0%, 9.3% and 6.2%, respectively, in the first half of the year; the German DAX index which rose in the first half of 2007 by 21.4%, only rose by 0.7% in the second half of the year; the Nikkei index declined in the second half of 2007 by 15.6%, compared to an increase by 5.3% in the first half of the year.

Instability in capital markets worsened in early months of 2008, with significant declines in major indices along with continued devaluation of the USD vs. most major currencies.

In the period from January 1, 2008 to March 17, 2008, the Dow Jones Industrials and S&P 500 indices declined by 9.9% and 12.3%, respectively; the Dj EuroSTOXX, CAC and FTSE 100 declined by 18.9%, 18.2% and 12.8%, respectively; the DAX and Nikkei indices declined by 20.0%.

Bank Group Operations and Description of its Businesses Development

Prospective 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 (“the Law”).

The actual results of the Bank could be significantly different from those included in the forward-looking information, or all that is implied therefrom. Prospective 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/prospective information and expressions involve risk and lack of certainty, because they are based on management's assessments of future events that include many factors, including as a result of 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 matters.

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 126 branches and business centers. Furthermore, business customers are supported by business centers and professional departments at Bank headquarters, which specialize by sector. The Bank's overseas operations are conducted via 3 subsidiaries, 3 branches and 3 representative offices in Europe, USA 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 activity, customer portfolio management, trust services, underwriting and issuance, mutual fund distribution and provident fund operation (until June 8, 2006 – also mutual fund management; until June 28, 2007 - also provident fund management). In conjunction with implementation of the provisions of the legislative reform in the capital markets, the Bank sold its mutual fund and provident fund operations. See Note 6.E.2) to the financial statements for information on sale of provident fund operations. The Bank continues to provide distribution and operation services to mutual funds as well as operation services to provident funds. Upon conclusion of sale by the Bank of its mutual fund and provident fund operations, the Bank was granted a license to provide retirement advisory services to salaried employees and to self-employed - and has started operations in this area as well.

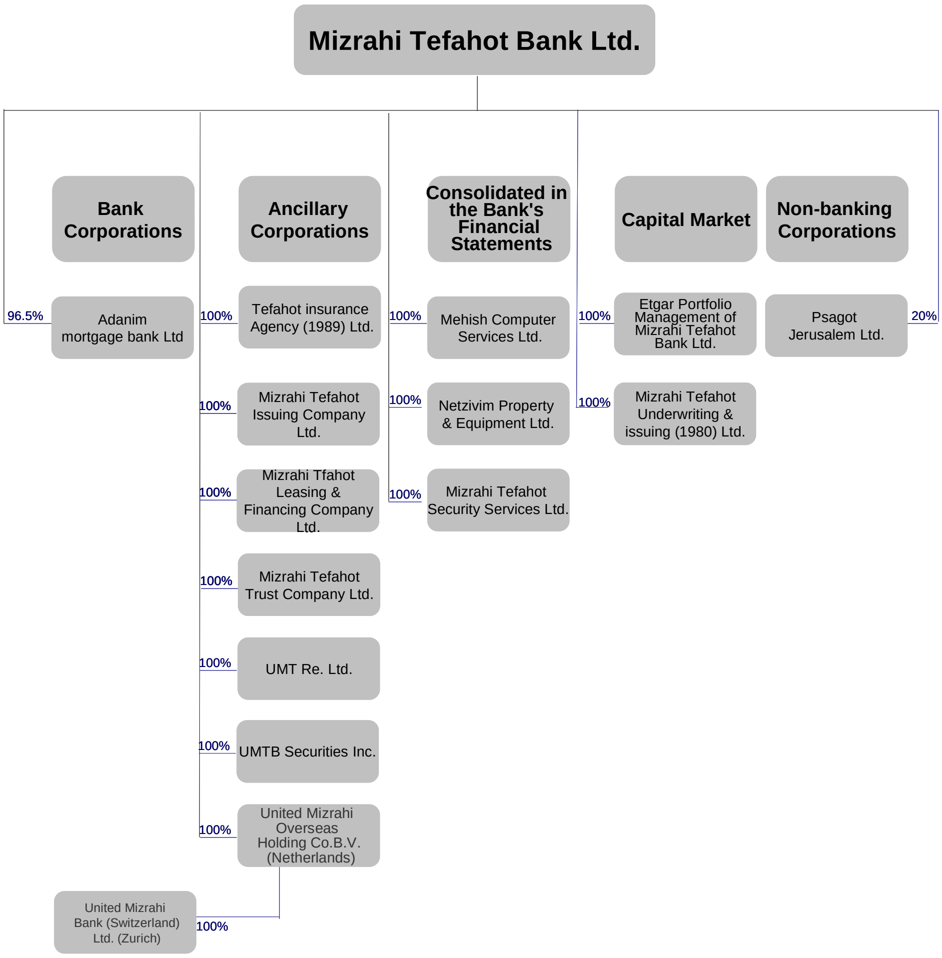
During 2007, several significant changes were made to the Bank Group:

Sale of Bank Group's provident fund operations - On June 28, 2007, the Bank Group completed sale of its provident fund operations (including operations via Netivot – Management Company Ltd., whereas the Bank holds 60% of its shares), after completing in 2006 the sale of mutual fund operations under its management. This was in conjunction with Group preparations for implementation of the "Bachar Reform" in the capital market. For details of sale of operations by the Bank, see Note 6.E.2) to the financial statements.

Acquisition of controlling stake in Bank Yahav - On March 27, 2007, the Bank signed a memorandum of understandings, whereby the Bank would acquire 50% of issued capital of Bank Yahav for Government Employees Ltd. ("Yahav"), including associated rights. See Note 6.E.4 to the financial statements for additional details.

Agreement with Isracard - On November 13, 2007, the Bank signed a memorandum of understandings with Isracard Ltd. and Europay (Eurocard) Israel Ltd. (“Isracard" and “Europay”, respectively), whereby the parties would enter into accelerated negotiations to replace their current agreed arrangements with a new agreement which would include, *inter alia*, issuance of Mizrahi-Tefahot branded credit cards. See Note 6.E.5) to the financial statements for information.

Holding Structure - Major Companies[1]:



(1) The bank has other additional investments which are deemed immaterial to the banking activity

See Note 6 to the financial statements for additional information on the structural changes in the Group.

Control of the Bank Group

To the best of the knowledge of the Bank and the Board of Directors, the holding of the interested parties in the shares of the Bank, as of December 31, 2007, are as follows:

	Holder	No. of shares	%of capital and voting rights
	M.W.Z. (Holdings) Ltd.(1)	15,585,785	7.02%
Wertheim Group	F & W (Registered Partnership) (2)	28,825,102	13.00%
	Total Wertheim Group	44,410,887	20.02%
	C.A.B.M. Ltd. (3)	7,066,264	3.19%
	L.A.B.M. (Holdings) Ltd.(4)	12,862,041	5.80%
	E.A.B.M. Ltd.(5)	15,175,631	6.84%
	Ofer Brothers Properties (1957) Ltd. (6)	14,591,953	6.58%
	Ofer Brothers Investments Ltd.(7)	7,477,642	3.37%
Ofer Group	Total Ofer Group	57,173,531	25.78%
	Total holdings – controlling shareholders	101,584,418	45.80%
Others	Eliezer Yones (8)	1,940,771	0.87%
	Abraham Natan (9)	1,300	-
	Total holdings – interested parties	103,526,489	46.67%
	Public	118,286,062	53.33%
	Total	221,812,551	100.00%

(1) 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%).
(2) A registered partnership held by Mr. Moshe Wertheim (1%) and by M.W.Z. (Holdings) Ltd. (99%).
(3) A private company wholly-owned and controlled by Ofer Development and Investments Ltd., a private company, the shares of which are held by Ofer Brothers Investments 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., a private company wholly-owned and controlled by Ofer Brothers Properties (1957) Ltd.
(4) A private company wholly-owned and controlled by L.I.N. (Holdings) Ltd., a private company wholly-owned and controlled by Mr. Eyal Ofer (95%) and a foreign company (5%).
(5) A private company wholly-owned and controlled by Ofer Brothers Holdings Properties Ltd., a private company wholly-owned and controlled by Ofer Brothers Properties (1957) Ltd.
(6) A private company, the shares of which are held by Leora Ofer (15%), Doron Ofer (15%), Yehuda (Yuli) Ofer (36.67%), L.I.N. (Holdings) Ltd. (33.33%) (as aforesaid, a private company wholly-owned and controlled by Mr. Eyal Ofer (95%) and a foreign company (5%)).
(7) A private company wholly-owned and controlled by Ofer Brothers Properties (1957) Ltd.
(8) Of which 1,938,771 shares via the Bank Mizrahi-Tefahot Recording Company Ltd. and Zeev Feldman, CPA - holding the shares in trust for Mr. Eliezer Yones. In addition, Mr. Eliezer Yones, the Bank's President, holds 2,185,778 non-negotiable options exercisable into 2,185,778 ordinary shares, NIS 0.1 par value each.
(9) Mr. Avraham Natan serves as an outside director in the Bank.

Shareholder agreements

An agreement was signed on October 6, 1994 between E.A.B.M. Ltd., C.A.B.M. Ltd. and L.A.B.M. (Holdings) Ltd., as one party (“Ofer Group corporations”) and between Feinberg-Wertheim (Registered Partnership) (1) as the other party ("Wertheim Group corporations") for cooperation in exercising rights associated with Bank shares ("voting agreement"). The voting agreement sets forth, *inter alia*, rules for joint voting of controlling shareholders at General Meetings, for each party's right of refusal upon sale of shares by the other parties, for rights to appoint Board members and rights to appoint the Chairman of the Board of Directors.

Concurrently with signing of the voting agreement a cooperation agreement was signed between the corporations that are the controlling shareholders of the companies comprising the Ofer Group, i.e. between E.A.B.M. Ltd., C.A.B.M. Ltd, Ofer Brothers Properties (1957) Ltd. and Ofer Brothers Investments Ltd. ("Ofer Properties") as one party, and between L.A.B.M. (Holdings) Ltd., which is wholly-owned by L.I.N. (Holdings) Ltd. ("L.A.B.M.") as the other party, whereby in all matters relating to holdings of Bank shares, its control and management rights, the parties will divide equally. Therefore, the Ofer corporations' quota of directors (as structured above) will be divided equally between Ofer Properties and L.A.B.M. According to terms of the agreement, decisions will not be made by the Ofer Group corporations, on any matter related to the Bank, including in votes at the Bank's General Meetings, unless Ofer Properties and L.A.B.M. have given their consent.

Permits and Arrangements with Regard to Control of the Bank

To the best of the Bank's knowledge, after a NIS 90 million capital infusion into Ofer Brothers Properties (1957) Ltd., the Supervisor of Banks informed the representative of Ofer Properties in a letter dated March 6, 2008, that in view of efforts by Ofer Group to permanently resolve the issue of holding of means of control, the Bank of Israel intends to allow continued negotiations aimed at regulating Ofer Group holding of means of control in the Bank, to the satisfaction of the Supervisor of Banks, through December 31, 2009, provided that after said date, if said holdings have yet to be regulated, Ofer Brothers Properties (1957) Ltd. would maintain a ratio of capital to sources of 40% or higher, in accordance with generally accepted accounting practices.

Investments in Bank Capital and Transactions in Bank Shares

- On April 19, 2007, the Bank allocated to Mr. Eliezer Yones, Bank President, via trustee 1,938,771 ordinary Bank shares of NIS 0.1 par value each. This is subsequent to exercise of 3,278,664 options allocated to the trustee on December 23, 2004 pursuant to provisions of the stock option plan in accordance with a private offer to the Bank President, approved by the Board of Directors on October 25, 2004 which is part of terms of employment of the President.

  On May 2, 2007 the aforementioned shares were transferred for registration with the Bank Mizrahi-Tefahot Recording Company Ltd. For further details see Note 16.D. to the financial statements.
- On January 8, 2008 the Bank was informed that the group of companies consisting of David Lubinski Ltd., Clal Holdings Insurance Business Ltd. and Epsilon Investments Ltd., indirectly controlled by the same controlling shareholders, own Bank shares totaling more than 5% of the Bank's issued share capital (on the announcement date - 5.325%). The Bank was further informed that the date of the transaction which caused the aforementioned group to become an interested party in the Bank was January 1, 2008, due to combination of holdings by Bank Hapoalim provident funds acquired by Clal Holdings Insurance Business Ltd.

  On March 4, 2008 the Bank was informed that following sale of Bank shares on the stock exchange, the aforementioned group was no longer an interested party in the Bank.

Board of Directors' decision with regard to capital adequacy ratio

On May 14, 2007 the Board of Directors passed a resolution, instructing Bank management to act so as to have capital adequacy ratios (including upper tier II capital) of no less than 11.2% starting with financial statements for the second quarter of 2007.

On February 25, 2008, the Bank's Board of Directors resolved to instruct Bank management to act so as to have the capital adequacy ratio (including upper tier II capital) be no less than 12.0% by end of 2009, without change to the Bank's dividend distribution policy (see below).

These resolutions are in conjunction with the resolution by the Bank's Board of Directors from April 2006, stipulating that the Tier I and Tier II capital adequacy ratio, excluding upper tier II capital, shall be no less than 10%. Said resolutions were made in view of the custom among banks globally to maintain capital adequacy rates higher than the minimum requirements imposed by regulators, in order to reflect to investors and depositors the conservative approach and international standards which the Bank wishes to adopt, as well as in view of the intent of the Supervisor of Banks to adopt Basel II regulations and to have capital allocated for operating risk as well. The ratio of capital to risk components as of December 31, 2007 was 11.33%. The ratio of capital to risk components excluding upper Tier II capital was 10.16%.

Raising of capital sources

In 2007, the Bank raised by private placement to institutional investors NIS 490 million by issuing complex capital notes, deemed to be Upper Tier II capital. These capital notes along with capital notes amounting to NIS 451 million raised in late 2006, were listed for trading on the stock exchange under a prospectus published in May 2007.

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 said objectives on total risk assets for the Bank, and hence 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 as set forth above.

According to Bank Management assessment, the Bank would raise, by end of 2009, additional capital sources for its current operations, while meeting the minimum capital ratio requirements. The amount that the Bank intends to raise is estimated at NIS 700 million, which will be raised as Upper Tier II capital through complex capital notes, subject to market conditions prevailing at that time. In addition, the Bank would raise subordinated capital notes considered Tier II capital amounting to an estimated NIS 500 million per year.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, 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.

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%, a dividend 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.

In addition to the aforesaid, the distribution of a dividend by the Bank is subject to the provisions of law and additional limitations, as provided in Notes 13 and 14 to the financial statements.

Distributed Dividends

Below are details of dividends distributed by the Bank since 2006 through the publication date of these financial statements (in reported amounts):

Payment date	Dividend per share (in Agorot)	Total dividend paid (NIS millions)
September 13, 2006	57.00	125
December 19, 2006	91.41	200
June 13, 2007	90.49	200
September 19, 2007	56.46	125
December 19, 2007	33.82	75
February 19, 2008	33.80	75

CHART 3

Profit and Profitability

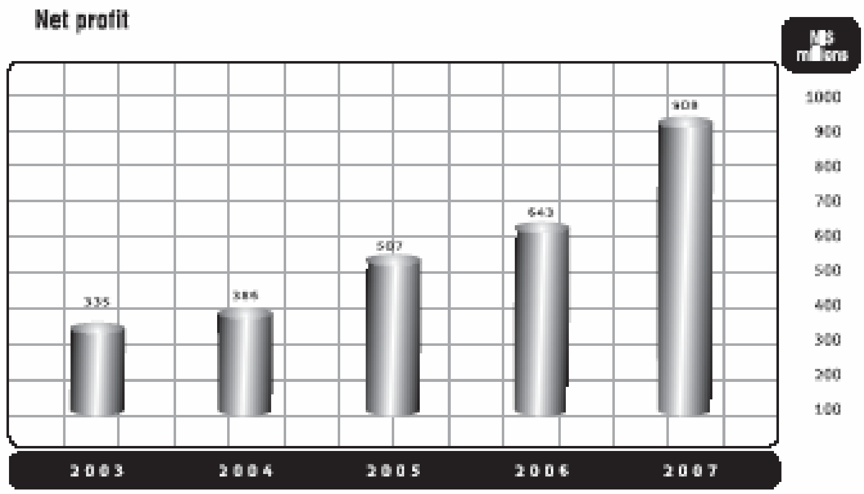
Group net profit in 2007 amounted to NIS 908 million, compared to NIS 643 million in 2006, a 41.2% growth.

Return on equity in 2007 was 17.2%, compared to 13.0% in 2006.

Group net profit excluding non-recurring items set forth below, amounted in 2007 to NIS 681 million, compared to NIS 607 million in 2006 - a 12.2% growth. This profit reflects return on equity of 12.9%, compared with 12.3% in 2006.

In Q4 of 2007, Group net profit amounted to NIS 147 million, compared to NIS 141 million in the same quarter in the previous year - a 4.3% growth.

Result for the fourth quarter of 2007 include most of the impact of provision for impairment of investment in asset-backed securities (NIS 90 million out of a total of NIS 114 million for all of 2007).



Below is an analysis of impact of non-recurring items on net profit (NIS in millions):

	For the Year Ended December 31		
	2007	2006	2005
Reported net profit	908	643	507
Provision for pension and severance pay for early retirement plan	-	233	-
Implementation Bank of Israel guidelines on manner of calculation of provision for doubtful debt for mortgages	-	54	-
Tax impact	-	(109)	-
After-tax capital gains from sale of provident fund operations (2007) and from sale of mutual fund operations and holdings of Excellence shares (2006)	(218)	(214)	-
Net profit (loss) from realized real estate and other investments	(9)	-	2
Cumulative impact of change in accounting policy	-	-	4
Net profit excluding non-recurring items	**681**	**607**	**513**
Return on equity excluding non-recurring items	**12.9%**	**12.3%**	**11.7%**

The main factors contributing to the increase in Group profits in 2007, compared with 2006:

- NIS 153 million increase in profit from financing operations before provision for doubtful debt, excluding provision for impairment of investments in securities.
- NIS 43 million increase in revenues from operating commissions.

The main factors which mitigated growth in Group profits in 2007, compared with 2006:

- Growth by NIS 37 million in provision for doubtful debt and other credit instruments. This growth resulted primarily from provision for impairment of Bank investment in instruments exposed, directly or indirectly, to the US mortgage market or to any leveraged funds, amounting to NIS 114 million (of which NIS 24 million in the third quarter of 2007 and NIS 90 million in the fourth quarter of 2007). These investments as of December 31, 2007 amounted to NIS 22 million ($5 million) out of an original investment of NIS 157 million ($35 million). See Note 3 to the financial statements for additional information. On the other hand, current provision for doubtful debt decreased by NIS 77 million.
- Decline by NIS 83 million in other revenues, primarily due to sale of the provident fund management and mutual fund management operations.
- NIS 54 million increase in operating expenses, excluding provision for pension and severance pay last year due to an early retirement plan.

Development of income and expenses

Group profit from financing operations before provision for doubtful debt amounted to NIS 2,026 million in 2007, compared with NIS 1,987 million in 2006, an increase of -2.0%.

Below is an analysis of development of major items for profit from financing operations in 2007 (NIS in millions):

	2007	2006	Rate of change
Current operations	**1,969**	**1,819**	**8.2%**
Income from interest on problem loans	171	111	54.1%
Profit (loss) from realization and impairment of debentures held for sale and debentures held for trading, net	(90)	5	-
Effect of accounting treatment of derivatives at fair value	(24)	52	-
Total	**2,026**	**1,987**	**2.0%**

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

In the fourth quarter of the year, profit from financing operations before provision for doubtful debt amounted to NIS 507 million, compared with NIS 552 million in the same period last year, a decrease of 8.2%, due primarily to provision for impairment of investment in asset-backed securities of NIS 90 million, recorded in the fourth quarter of 2007. Excluding this provision, profit from financing operations in the fourth quarter of 2007 grew by 8.2%.

Below are details of financing profit by major operating segments of the Group (NIS in millions)(1):

Results presented for 2007 are not comparable to results for 2006. See Note 30 to the financial statements for details.

Operating segment	2007
Household	
Mortgages	339
Other	577
Private banking	49
Small business	277
Commercial banking	115
Business banking	462
International operations	(2)(9)
Financial management	216
Total	2,026

(1) For definition of operating segments, see below the chapter on "Bank Group Operating Segments".

(2) Includes provision for impairment of asset-backed securities, amounting to NIS 114 million.

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

Linkage segment - financial assets	2007	2006	Change in %
Israeli currency - non-linked	62,137	47,495	30.8%
Israeli currency - linked to the CPI	39,950	36,570	9.2%
Foreign currency (2)	60,896	54,679	11.4%
Total	162,983	138,744	17.5%

(1) Reclassified.

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

The increase in the average balance of financial assets in the non-linked shekel segment is explained mainly by the significant growth in activity volume in derivative instruments, and from increase in credit extended to the public in the Bank's normal course of business. The increase in the average balance of financial assets in the CPI- and foreign currency linked segments is mostly explained by increase in activity volume in derivative instruments.

Interest margins (difference between the rate of income on assets and the rate of expenses on liabilities) in the various linkage segments (including the effect of derivatives, in percent) are as follows:

Linkage segment	2007	2006
Israeli currency - non-linked	1.50	(1) 1.66
Israeli currency - linked to the CPI	0.54	0.52
Foreign currency (1)	0.08	0.81
Total	0.77	(1) 1.10

(1) Reclassified.

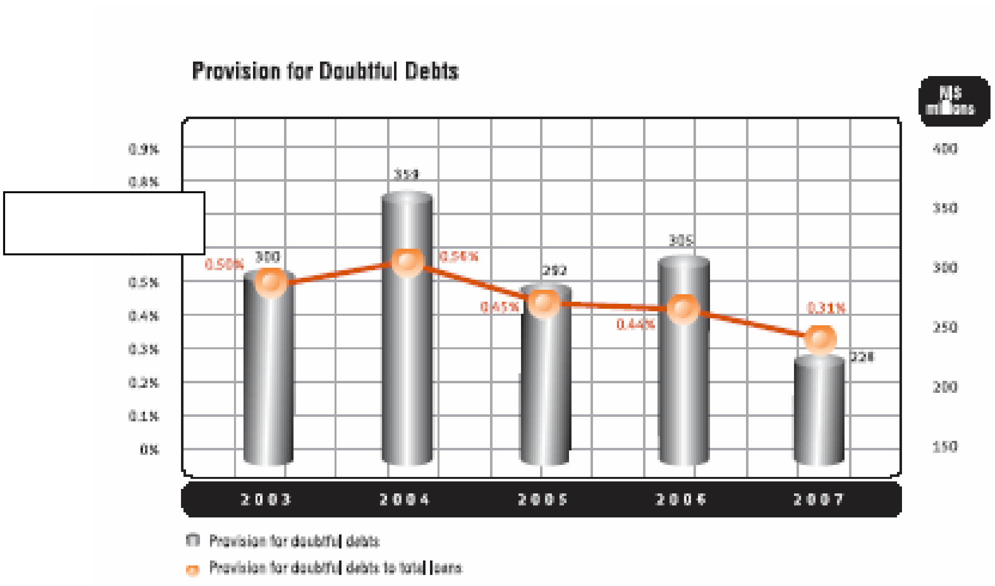
(2) Local activity and overseas affiliates (includes foreign currency-linked Israeli currency).

The decrease in interest spreads, mainly in the foreign currency sector, is due to increased activity in derivatives, where spreads are relatively lower, and to the fact that impact of option activity, from which NIS 345 million in revenues was recorded in 2007 (NIS 1 million in 2006) is not included under asset and liability management, hence is not included in the interest margin.

Provision for doubtful debt for the Group in 2007 amounted to NIS 228 million, compared with NIS 305 million in 2006, a decrease of 25.2%, primarily due to extraordinary provision of NIS 54 million in Q1 of 2006, for implementation of the guidelines prescribed in the circular of the Bank of Israel regarding the manner in which the provision for doubtful debt is to be calculated for housing loans (mortgages). Excluding the extraordinary provision in Q1 of 2006, provision for doubtful debt decreased in 2007 by 9.2% compared to 2006.

In the fourth quarter of 2007, provision for doubtful debt amounted to NIS 50 million, compared with NIS 64 million in the same period last year, a decrease of 21.9%.

Total provision for doubtful debt and other credit instruments increased by approximately NIS 37 million, mainly due to provision of NIS 114 million (of which NIS 24 million in the third quarter of 2007 and NIS 90 million in the fourth quarter of that year) for impairment of Bank investments in instruments directly or indirectly exposed to the US mortgage market or to any type of leveraged funds.



Development of provision for doubtful debt (NIS in millions) is as follows:

	For the Year Ended December 31	
	2007	2006
Specific provision:		
By extent of arrears	30	77
Other	218	194
Total specific provision	248	271
General and additional provision	(20)	(20)
Total excluding non-recurring effects	228	251
Application of Bank of Israel directives on calculation of provision for doubtful debt by extent of arrears	-	54
Total	228	305
Rate of provision for doubtful debt to total credit to the public	0.31%	(1) 0.44%

(1) Provision for doubtful debt in 2006, excluding impact of implementation of the Bank of Israel circular of NIS 54 million, was 0.36% of total credit portfolio to the public.

Details of provision for doubtful debt by major Group operating (NIS in millions) is as follows:

Results presented for 2007 are not comparable to results for 2006. See Note 30 to the financial statements for details.

Operating segment	2007
Household	
Mortgages	41
Other	26
Small business	74
Commercial banking	7
Business banking	77
International operations	3
Total	228

The balance of the general and supplementary provision for doubtful debt in the Group's balance sheet amounted to NIS 172 million as of December 31, 2007, compared with NIS 192 million as of December 31, 2006.

Profit from financing operations after provision for doubtful debt amounted to NIS 1,798 million in 2007, compared with NIS 1,682 million in 2006, a 6.9% growth.

Total operating and other income for the Group in 2007 amounted to NIS 1,190 million, compared to NIS 1,215 million in 2006, a 2.1% decline.

Income from operating commissions for the Group was NIS 1,034 million in 2007, compared with NIS 991 million in 2006, a 4.3% growth. The increase is primarily due to increase in commission income from customer operations in the capital market and from credit card commissions. In the fourth quarter of the year, income from operating commissions amounted to NIS 265 million, compared to NIS 254 million in the same period last year, a 4.3% growth.

Profit from equity investments, net amounted in 2007 to NIS 65 million, compared to NIS 50 million in 2006, a 30.0% growth. The majority of profits in 2007, as in the same period last year, arise from dividends received from investment in stocks. In the fourth quarter of the year, profit from investment in stocks amounted to NIS 20 million, compared to NIS 18 million in the same period last year, an 11.1% increase.

Other income for the Group totaled NIS 91 million in 2007, compared with NIS 174 million in 2006, a decrease of 47.7% In the fourth quarter of the year, operating and other expenses amounted to NIS 18 million, compared to NIS 44 million in the same period last year, a 59.1% decrease. The decrease is primarily due to decline in management fee income from mutual funds and from provident funds, due to sold operations.

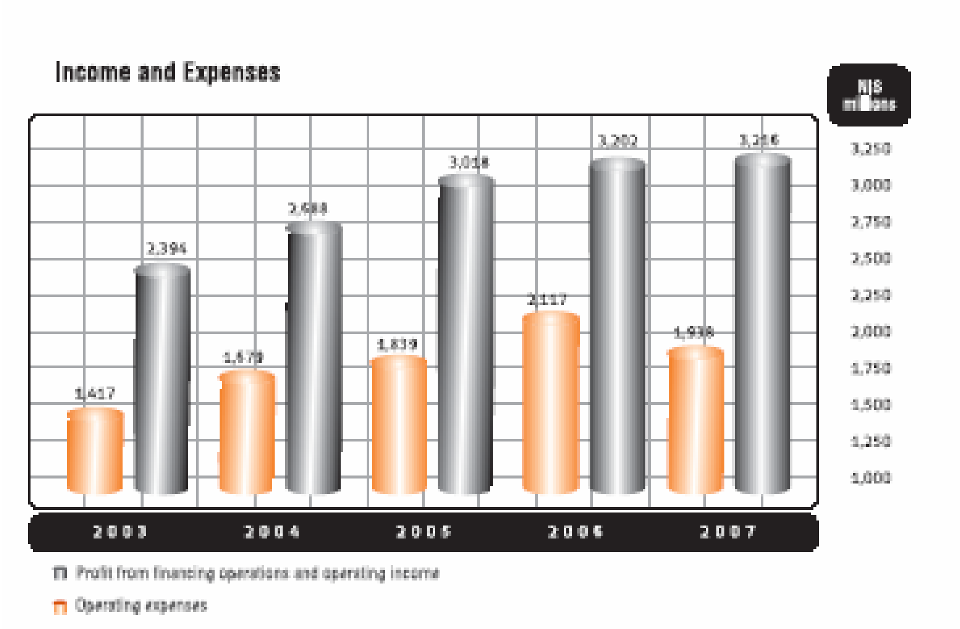
Operating and other expenses for the Group totaled NIS 1,938 million in 2007, compared with NIS 2,117 million in 2006, a decrease of 8.5%. Excluding provision for pension and severance pay, as set forth below, increase in operating and other expenses over 2006 was 2.9%. In the fourth quarter of the year, operating and other expenses amounted to NIS 511 million, compared to NIS 508 million in the same period last year, a 0.6% increase.

Operating and other expenses for the Group totaled NIS 1,169 million in 2007, compared with NIS 1,395 million in 2006, a decrease of 16.2%. The decrease is primarily due to provision for pension and severance pay amounting to NIS 233 million in 2006, due to the retirement plan included under the terms of the labor agreement signed with the employee representatives. Excluding the aforementioned provision, increase in salary expenses over 2006 was 0.6%. In the fourth quarter of the year, salary expenses amounted to NIS 291 million, compared to NIS 310 million in the same period last year, a 6.1% decrease due to provision for pension and severance pay as set forth above, NIS 25 million of which was recorded in the same period last year.

Maintenance and depreciation of buildings and equipment expenses in 2007 amounted to NIS 421 million, compared to NIS 385 million in 2006, a 9.4% increase; this is primarily due to increase in expenses for computer software and equipment maintenance, as well as to increase in depreciation due to increased investment in previous years, primarily in computers and software. In the fourth quarter of the year, Maintenance and depreciation of buildings and equipment expenses amounted to NIS 110 million, compared to NIS 106 million in the same period last year, a 3.8% increase.

Other operating expenses for the Group was NIS 348 million in 2007, compared with NIS 337 million in 2006, a 3.3% growth.

In the fourth quarter of the year, other operating expenses amounted to NIS 110 million, compared to NIS 92 million in the same period last year, a 19.6% increase.



As a result of developments in income and expenses, there were changes in the financial ratios, as follows:

	For the Year Ended December 31	
	2007	2006
Operational Coverage Ratio (1)	61.4%	57.4%
Cost-Income Ratio(2)	60.3%	66.1%
Excluding extraordinary changes in income and expenses(3):		
Operational Coverage Ratio (1)	57.6%	56.7%
Cost-Income Ratio(2)	59.5%	61.6%

(1) Total operating and other income to total operating and other expenses.

(2) Total operating and other expenses to total operating and financing income before provision for doubtful debt.

(3) In 2006 – provident fund management fees, mutual fund management fees, distribution commission for mutual funds and provision for pension and severance pay due to retirement plan.
In 2007 – provision for impairment of investment in securities and mutual fund distribution commissions.

Group pre-tax operating profit in 2007 amounted to NIS 1,050 million, compared to NIS 780 million in 2006, a 34.6% growth.

Provision for taxes on operating profit amounted to NIS 368 million in 2007, compared with NIS 349 million in 2006, an increase of 5.4%. In the fourth quarter of the year, provision for taxes on operating profit amounted to NIS 95 million, compared to NIS 158 million in the same period last year, a 39.9% decrease. The decrease in the fourth quarter was primarily due to impact of the Adjustment Law due to the negative CPI in the last quarter of 2006, as well as to a decrease in operating profit before taxes, as set forth above.
For details on rescinding of the Adjustment Law, see below in the chapter on Legislation.

Net operating profit of the Group reached NIS 681 million in 2007, an increase of 59.5% compared with the NIS 427 million posted in 2006. Excluding impact of provision for pension and severance pay for labor agreements, and excluding impact of implementation of guidelines set forth in the Bank of Israel circular on calculation of provision for doubtful debt for housing loans (mortgages) as set forth above, Group net operating profit grew in 2007 by 12.6% over 2006.In the fourth quarter of the year, net operating profit after provision for taxes amounted to NIS 153 million, compared to NIS 138 million in the same period last year, a 10.9% increase.

Group after-tax profit from extraordinary items amounted in 2007 to NIS 227 million, compared to NIS 216 million in 2006. Profit from extraordinary items in 2006 was due to sale of the Group's mutual fund operations and to realization of its holdings in Excellence. Profit from extraordinary items this year was primarily due to sale of the Group's provident fund operations.

Return on equity

In May 2007, the Supervisor of Banks issued an amendment to the Public Reporting Regulations, which modifies the way return on equity is calculated. According to regulations, return on equity should be calculated as the ratio of net profit (less dividends on preferred shares) to average shareholders' equity. Average shareholders' equity would include "total capital resources", as presented in the reporting of income and expense rates, less average balance of minority interest and less/plus the average balance of unrealized profit/loss from adjustment to fair value of debentures held for trading as well as profit/loss from debentures held for sale, which are included in shareholders' equity under "Total other profit". "Total capital resources" mentioned above, is calculated as the difference between average asset balance to average liability balance.

Return(1) on Group profit and its development relative to shareholders' equity (in %):

	2007	2006	2005
In accordance with reporting regulations for 2007 and thereafter(2)			
From current operations	12.9	8.6	11.7
Net profit	17.2	13.0	11.6
In accordance with reporting regulations prior to amendment			
From current operations	13.5	9.1	12.4
Net profit	17.9	13.8	12.3

(1) Annualized return.

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

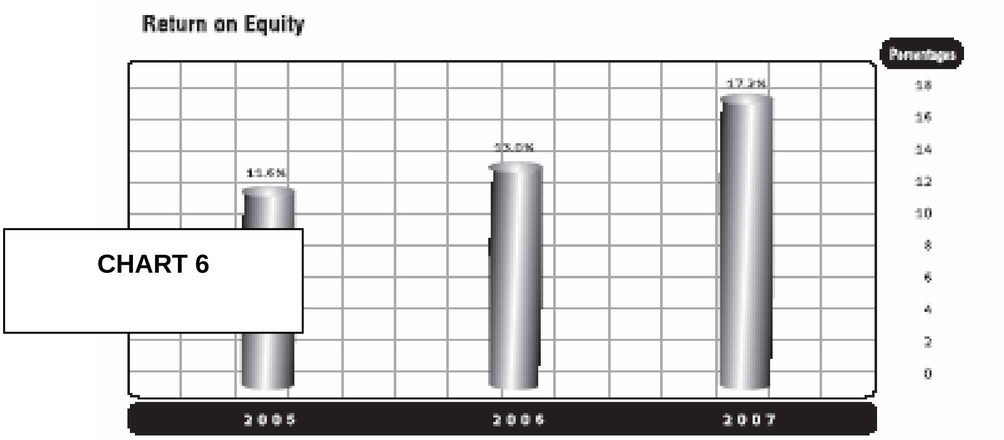


CHART 6

Earnings per share

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

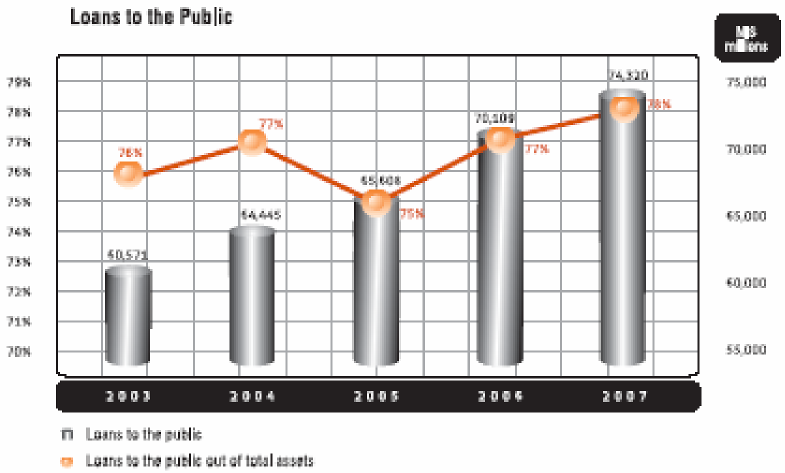
	2007	2006	2005
Basic earnings per share:			
From current operations	3.08	1.95	2.35
From net profit	4.11	2.94	2.32
Diluted earnings per share:			
From current operations	3.03	1.91	2.33
From net profit	4.04	2.88	2.30

Development of balance sheet items

Development in loans to the public according to main operating segments (NIS in millions):

	December 31		Rate of change
	2007	2006	In %
Balance sheet total	95,317	90,711	5.1%
Credit to the public	74,320	70,109	6.0%
Deposits from the public	75,290	73,234	2.8%
Securities	6,145	5,979	2.8%
Shareholders' equity	5,557	5,061	9.8%

Loans to the public in the consolidated balance sheet at December 31, 2007 accounted for 78% of total assets, compared with 77% at the end of 2006. The Group's loans to the public increased in 2007 by NIS 4.2 billion, a 6.0% increase.



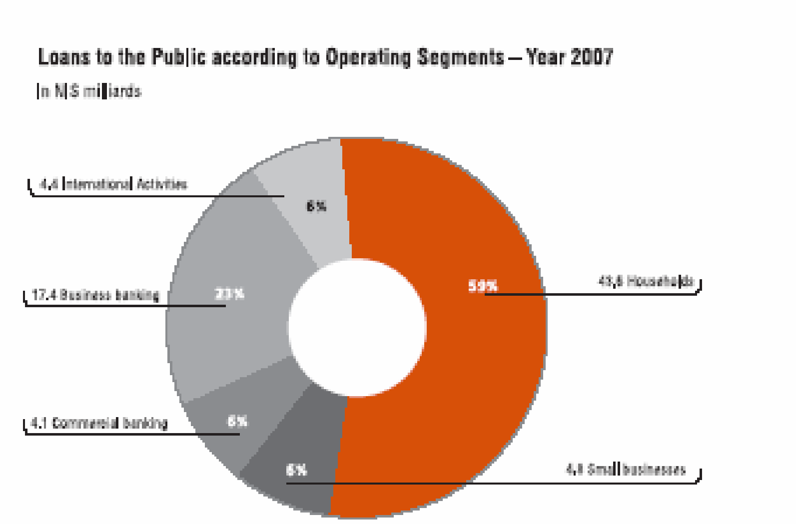
Credit to the public by linkage segments (NIS in millions) is as follows:

Linkage segment	Balance as of December 31			Segment share of total credit to the public as of December 31	
	2007	2006	Change in %	2007	2006
Israeli currency					
Non-linked	27,911	24,399	14.4%	37.5%	34.8%
CPI- linked	33,586	33,044	1.7%	45.2%	47.1%
Foreign currency and foreign currency linked	12,823	12,666	1.2%	17.3%	18.1%
Total	74,320	70,109	6.0%	100%	100%

Credit to the public by operating segments (NIS in millions) is as follows:

Results presented for 2007 are not comparable to results for 2006. See Note 30 to the financial statements for details.

Operating segment	Balance as of December 31
	2007
Household	
Mortgages	37,665
Other	5,938
Private banking	-
Small business	4,806
Commercial banking	4,087
Business banking	17,412
International operations	4,412
Total	74,320



Credit risk for credit 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 credit 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.

Total Group credit risk as of December 31, 2007 amounted to NIS 98.6 billion, compared to NIS 95.0 billion in 2006 - an increase of 3.7% primarily due to increase in housing loans.

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

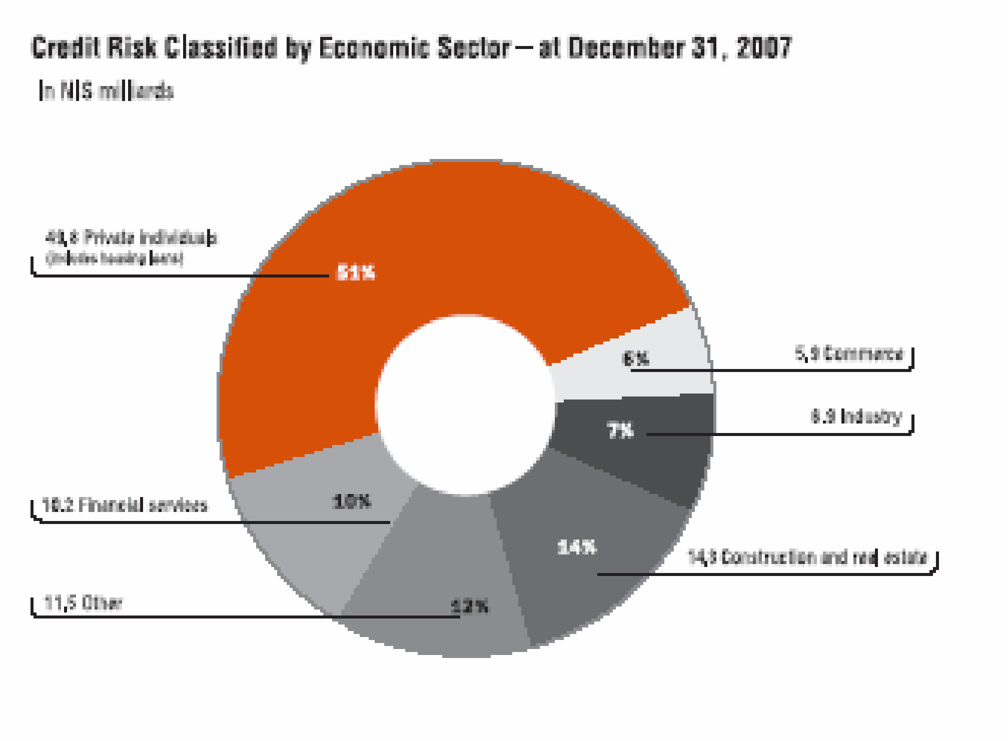
	2007		2006	
Borrower credit risk (NIS in thousands)	Share of total Group credit risk	Share of total Group number of borrowers	Share of total Group credit risk	Share of total Group number of borrowers
Up to 150	15.6%	78.4%	16.8%	78.6%
150-600	29.7%	18.8%	29.0%	18.9%
600-2,000	11.6%	2.3%	9.9%	2.0%
Above 2,000	43.1%	0.5%	44.3%	0.5%

Credit Risk According to major industrial sectors (1) (in NIS millions)

	2007		2006		
Sector	Total credit risk of the public	% of total credit risk	Total credit risk of the public	% of total credit risk	% change
Private individuals (includes housing loans)	49,800	50.5%	46,529	49.5%	7.0%
Construction and real estate	14,262	14.5%	15,135	16.1%	(5.8%)
Financial services	10,207	10.4%	10,705	11.4%	(4.7%)
Industry	6,943	7.0%	6,487	6.9%	7.0%
Commerce	5,869	6.0%	4,570	4.9%	28.4%

(1) Includes loans to the public, the public's investments in debentures and the off-balance sheet credit risk.

Of the total credit risk in the construction and real estate sector, the off-balance sheet credit risk at December 31, 2007 totals NIS 7,653 million, compared with NIS 8,595 million at December 31, 2006, a decrease of 10.9%. The off-balance sheet credit risk to this industry constitutes 33.0% of the Group's off-balance sheet credit on December 31, 2007, compared with 37.2% on December 31, 2006.



Total Group credit risk for problem loans at December 31 - (in million NIS)

	2007	(1) 2006
Non-accrual debt	934	1,003
Rescheduled debt	185	172
Debt designated for rescheduling	2	15
Debt in temporary arrears	1,027	1,475
Includes: for housing loans	615	644
Debt under special supervision	912	835
Includes: Debt for which there is a specific provision	120	146
Housing loans for which there is a provision based on length of arrears	670	732
Total balance sheet credit to problem borrowers	3,730	4,232
Off-balance sheet credit to problem borrowers	616	494
Total credit risk for problem borrowers	4,346	4,726

(1) Restated.

Securities – balance of investment in securities increased in 2007 by 2.8%.

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

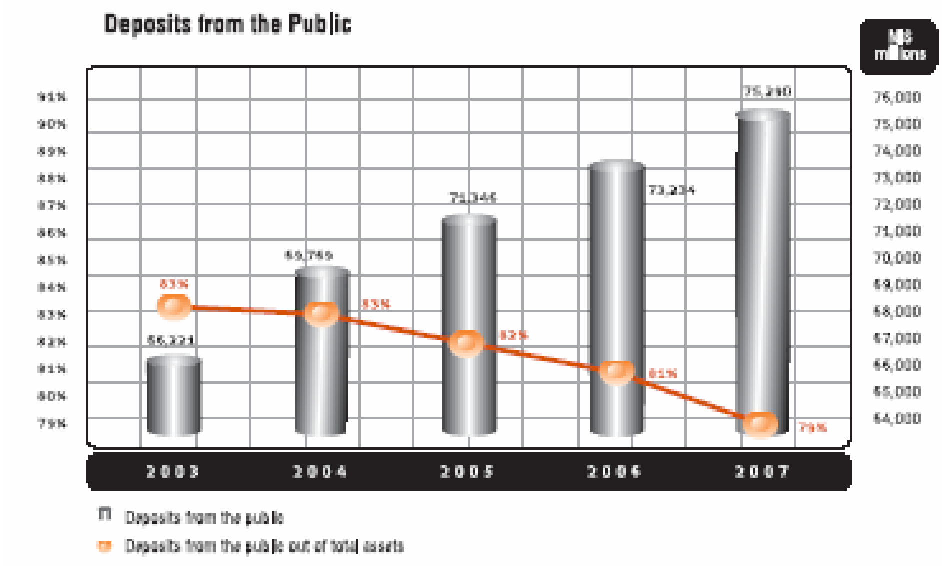
	Balance as of December 31		Change in %
Linkage segment	2007	2006	
Israeli currency			
CPI- linked	1,207	398	-
Non-linked	1,742	1,823	(4.4%)
Foreign currency and foreign currency linked	2,797	3,354	(16.6%)
Non-monetary items	399	404	(1.2%)
Total	6,145	5,979	2.8%

Distribution of balance of Group investment in securities by issuer type (NIS in millions) is as follows:

	Amortized cost	Unrealized gains	Unrealized loss	Fair value (book value)
Securities held for sale:				
Debentures of the Government of Israel	4,026	5	21	4,010
Foreign government debentures	69	-	-	69
Bank debentures	1,241	-	14	1,227
Corporate debentures	205	-	4	201
Asset-backed debentures	182	-	23	159
Other stocks	295	104	-	399
Total securities held for sale	6,018	109	62	6,065
Securities held for trading:				
Government of Israel debentures	80	-	-	80
Total securities	6,098	109	62	6,145

Deposits from the public - these account for 79.0% of total consolidated balance sheet as of December 31, 2007, compared with 81% at the end of 2006.

In 2007, deposits from the public in the Bank Group increased by NIS 2.1 billion, an increase of 2.8%.



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

Linkage segment	Balance as of December 31		Rate of change	Share of total deposits from the public as of December 31	
	2007	2006	(%)	2007	2006
Israeli currency					
Non-linked	36,125	34,187	5.7%	48.0%	46.7%
CPI- linked	20,020	20,986	4.6%	26.6%	28.6%
Foreign currency and foreign currency linked	19,145	18,061	6.0%	25.4%	24.7%
Total	75,290	73,234	2.8%	100.0%	100.0%

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

Results presented for 2007 are not comparable to results for 2006. See Note 30 to the financial statements for details.

Operating segment	Balance at December 31, 2007
Household	30,731
Private banking	2,204
Small business	11,106
Commercial banking	2,432
Business banking	10,753
International operations	2,570
Financial management	15,494
Total	75,290

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

Shareholders' equity

According to the measurement principles prescribed by the Supervisor of Banks with respect to securities held for sale, the adjustment of these securities to their fair value is recorded directly to shareholders' equity. The change in the capital reserve in 2007, net of the related tax, was a decrease of NIS 38 million. Shareholders' equity as of December 31, 2007 includes a positive capital reserve of NIS 27 million, due to adjustment of securities held for sale to fair value, after applicable taxes.

Group ratio of shareholders' equity to balance sheet total as of December 31, 2007 amounted to 5.83%, compared with 5.58% at the end of 2006.

Ratio of capital to risk components

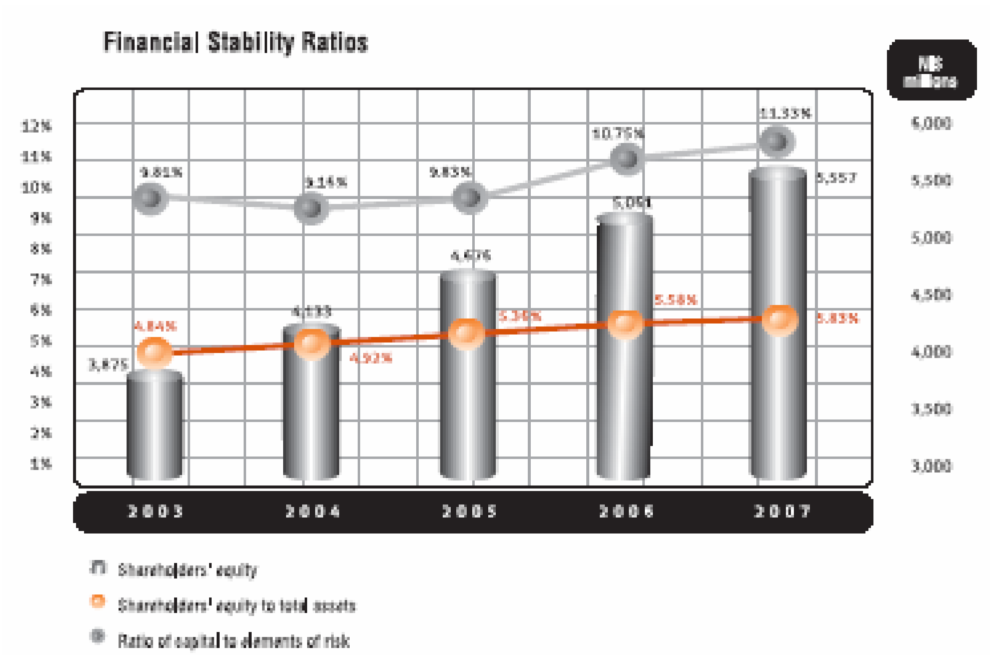
As per instructions of the Supervisor of Banks, any banking corporation is required to maintain a total minimum capital ratio of no less than 9% of weighted total of risk components of its balance sheet assets and off-balance-sheet items, and said instructions set forth the manner of calculation of total capital and total risk components.

Development of Group ratio of capital to risk components is as follows:

	December 31, 2007	December 31, 2006
Ratio of Tier I capital to elements of risk	6.69%	6.67%
Ratio of total capital to elements of risk	11.33%	10.75%
Minimum capital ratio required by the directives of the Supervisor of Banks	9.00%	9.00%

The ratio of capital to risk components as of December 31, 2007 also accounts for the capital adequacy requirement due to market risk, in accordance with Directive 341 – Adequacy of Capital in Respect of Market Risk, the effect of which on the capital ratio, as of December 31, 2007, is 0.26%. In 2007, subordinated notes amounting to NIS 450 million and complex capital notes amounting to NIS 490 million were raised, compared to raising of complex capital notes amounting to NIS 451 million last year.

The balance of complex capital notes and subordinated notes for Group capital adequacy, as of December 31, 2007, amounts to NIS 3,710 million, compared to NIS 2,936 million at the end of 2006. These amounts include complex capital notes listed for trading amounting to NIS 961 million. See Notes 11 and 14 to the financial statements for further details.



Main Investees

The contribution of investees to net operating profit was NIS 69 million in 2007, compared with NIS 76 million last year. Most of the decline is due to sale of the Group's provident fund and mutual fund operations.

Bank Adanim Mortgages & Loans Ltd. ("Bank Adanim")

Bank Adanim operates via 10 independent branches.

On February 9, 2007 the Bank acquired the balance of public holdings in Bank Adanim, and as of that date Bank Adanim became a private company, wholly owned by the Bank. On February 18, 2007, Bank Adanim allocated to the Bank 6,212 ordinary NIS 1 par value shares, in exchange for NIS 72 million paid to Bank Adanim in May 2006 in conjunction with a contract between the Bank and Bank Adanim, aimed at providing to Bank Adanim the equity required for its current business operations. See Note 6.E.1 to the financial statements for additional details.

Bank Adanim's contribution to Group net profit in 2007 amounted to NIS 22 million, similar to its contribution in 2006.

Net profit return on equity (average equity, as defined in the Supervisor of Banks' Public Reporting Regulations) amounted in 2007 to 10.2%, compared to a 10.1% return in 2006.

Bank Adanim's balance sheet total on December 31, 2007 amounted to NIS 4,038 million, compared to NIS 3,757 million on December 31, 2006. The balance of credit to the public as of December 31, 2007 amounted to NIS 3,933 million, compared to NIS 3,696 million at end of 2006.

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 customers obtaining mortgages from the Bank.

Tefahot Insurance's contribution to group net profit in 2007 amounted to NIS 42 million, compared to NIS 30 million in 2006, a 40% growth. Growth in profit is primarily due to a non-recurring provision recorded in 2006.

Net return on equity amounted to 14.4% in 2007, compared to 11.9% in 2006.

See Note 19.D.14)b. to the financial statements for information on the institution of a new arrangement for marketing insurance incidental to mortgages.

Other investees operating in Israel

Other investees operating in Israel, most of which are under the full control of the Bank and are supported by its infrastructure, contributed NIS 8 million to the Bank's profits in 2007, net, compared with NIS 13 million, net, in 2006.

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.

Net profit of Mizrahi Bank Switzerland in 2007 amounted to CHF 2.7 million, compared to CHF 2.0 million in 2006.

Balance sheet total for Mizrahi Bank Switzerland as of December 31, 2007 amounted to CHF 141 million, compared with CHF 155 million at the end of 2006, a decrease of 9.5%.

Total credit to the public as of December 31, 2007 amounted to CHF 86 million, compared to CHF 108 million at end of 2006; total deposits at banks as of December 31, 2007 amounted to CHF 35 million, compared to CHF 27 million at end of 2006. Total credit to the public as of December 31, 2007 amounted to CHF 35 million, compared to CHF 19 million at end of 2006; total deposits at banks as of December 31, 2007 amounted to CHF 59 million, compared to CHF 94 million at end of 2006. These data exclude off-balance-sheet items, such as fiduciary deposits and customer 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 Mizrahi Bank Switzerland, to Group net profit Group in 2007, was NIS 1.6 million, compared with NIS 0.2 million in 2006.

Investment in non-banking corporations

The Bank has a department tasked with monitoring nostro investments made in non-banking corporations in the past, and reviewing the value of these investments on an ongoing basis. About 84% of these investments are negotiable and presented at their market value. Other investments are presented at cost. In case of impairment of a non-temporary nature, a provision for impairment is made by the Bank.

Bank investments in non-banking corporations amounted to NIS 410 million at December 31, 2007, as follows:

A. NIS 345 million is invested in marketable securities included in the portfolio of securities available for sale; this sum includes NIS 322 million, constituting the market value of securities pledged for debt of a certain customer, which were classified as securities in accordance with the letter from the Supervisor of Banks.

B. NIS 25 million is invested in participation units in various equity funds.

C. NIS 11 million constitutes the balance of the Bank's investment in Psagot Jerusalem Ltd., a private company that had purchased land in Jerusalem for its development for residential construction, including an investment in capital notes that totaled NIS 24 million as of December 31, 2007. In addition, the Bank provided credit to Psagot Jerusalem Ltd., which as of December 31, 2007 amounted to NIS 33 million.

D. Investments in multiple other corporations, which are stated at cost, the balance of the investment in which totaled NIS 29 million as of December 31, 2007.

During 2007 the Bank sold all its holdings in Mofet Israel Technology Fund Ltd. ("Mofet"), which comprised 20% of capital and voting rights in Mofet, in exchange for NIS 23 million. The Bank recorded, for this sale, net profit from extraordinary operations amounting to NIS 8 million.

Bank net revenue from dividends and capital gains from non-banking corporations in 2007 amounted to NIS 65 million, compared to NIS 50 million in 2006.

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, 2007, is 90 thousand square meters, as provided in the table below:

Type of property (1)	Gross sqm. as of December 31, 2007		
	Owned	**Leased**	**Total area**
Branches throughout Israel	29.8	18.0	47.8
Offices and warehouses	26.4	8.5	34.9
Properties not in use, but have potential future use (2)	2.5	4.8	7.3
Disused property offered for sale or to be vacated	0.1	-	0.1
Total	58.8	31.3	90.1

(1) The Bank a lot for future use encompassing a total of 1.3 thousand square meters, gross. The Bank also owns 4.8 thousand square meters of covered and uncovered parking areas that are not included in the table.

(2) Of which 0.9 thousand square meters leased to others and 4.0 thousand square meters under refurbishment.

It is the Bank's policy to hold only those properties the Bank actually needs or expects to need 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.

On October 6, 2006, the Bank signed agreements for sale of real estate properties in Tel-Aviv (lots with total area of 1,800 square meters and buildings with total gross area of 4,500 square meters). As part of this transaction, the Bank leases from the buyer part of the buildings with total gross area of 3,354 square meters for an interim period until an alternative property is located and adapted for use by Bank departments located in these buildings.

During 2007 the Bank started adapting an alternative property with an area of 4,000 square meters. Adaptation should be concluded in the first half of 2008, and upon its conclusion the alternative property will be populated and the lease period would end. The alternative property is reflected in the above table under "Disused property with potential future use".

The net book value of the Bank's buildings and land at December 31, 2007 is NIS 677 million.

Intangible assets

The Bank Group has data base entries for customers, suppliers and employees.

The Bank owns rights to the following trademarks: "Mizrahi-Tefahot", "Tefahot - Number 1 in Mortgages" and "Pension portfolio based on Nobel prize winning model", as well as rights to trademarks associated with the Bank name in Switzerland and in the European Union. Applications were also filed for registration of trademarks related to the Bank name in the USA and in Canada.

Information Technology and Operations in the Bank

General

The Bank's IT services are provided by a wholly-owned subsidiary of the Bank - Mehish Computer Services Ltd. ("Mehish"). Mehish works to develop sophisticated IT systems and to continuously improve the level of the Bank's technology equipment. Following the merger of Bank Tefahot and Mizrahi Bank, the IT Unit of the former Bank Tefahot is being merged into Mehish. During 2006, a physical merger was performed of telecom networks and most of the IT equipment. In 2007, the merfer of deposit systems into a single system was concluded, and action started on merger of other systems. The merger of the remaining systems will continue in coming years.

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 Mehish systems (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 customers, scanners and check readers.

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 several hundred 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 policies are based on building the main systems in a backup site within a time frame of not more than 8 hours. To this end, a disaster recovery plan (DRP) was built, based on an agreement with IBM, 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. The data at the DRP site is updated in real time by the "hot backup" method. Several open systems, which were defined as having a low critical level, are not included at the backup site at this time. These systems use a "cold backup". In 2008, site expansion will continue and systems will be added, according to priorities set by the Bank. In order to ensure reliability of backup using the DRP site, and the ability to recover from disaster, drills are conducted semi-annually. In addition to the backup system, other means provide physical equipment security, in both the main site and the backup site: identification of leaks, identification of flooding, preventing electrical surges, etc.

Information security

The Bank Group has a function for managing the security of applications and the network, which is responsible for data security, 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 data security event.
- 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 infrastructure and management of data security projects.
- Information security policy for overseas branches.

ISO certification on information security issues for direct banking – the Bank is the first bank in Israel to be certified on this issue.

See the chapter on Risk Management below for Bank policy on information security.

Vendors

Mehish has a number of significant suppliers:

- 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.

Projects

The Bank Group, via Mehish, is pursuing multiple projects requiring major IT investment, which are in various development and deployment stages. These projects may be grouped as follows:

a. Business support - IT systems which reflect innovation and creativity allow the Group to offer its customers advanced products and services, some of which are unique:

- Customer relations systems – CRM. Mizrahi-Tefahot Bank is the first bank to operate such system in branches and customer centers, other than mortgage branches.
- Pension advisory service – based on the CRM system and constitutes part of the Bank's preparations for providing pension consultancy for salaried employees and for the self-employed.
- New mortgage-management system – replacement of the old mortgage-management system with a modern technology system, which enables, *inter alia*, the shift to online activity and processing, balance processing on a daily basis, and flexibility in specifications and day-to-day operation of various mortgage products.

  All Bank branches involved in mortgage processing have started using the new system.
- New branch system – using ".Net" technology to replace the old OS/2-based system.
- A new site was established and launched for web-based operations using ".Net" technology.
- New profitability system – a system that enables measurement of profitability, from the level of a single transaction, through the various hierarchal levels in the organizational structure up to the level of the organization as a whole. The system was launched in 2007.
- Data warehouse – a new system, launched in 2007, for collecting business and marketing data on a daily basis and enables analysis of a large number of dimensions, for the Bank's relevant business issues.
- International operations – a system supporting the Bank's international operations.
- Provident fund operation for members - a system developed using ".NET" technology, enabling a significant upgrade of provident fund operations and complete compliance with statutory instructions.

- Financial advisory service - a system to enable provision of advanced advisory services to customers by Bank investment advisors.
- HOVAV - a new system for problem loan management.
- Insurance agency - a system for management of insurance incidental to providing a mortgage, via the Group's insurance agency.

b. Regulation - the Group, via Mehish, develops new systems and adapts existing ones to changing regulatory requirements. A major, significant project in this category is the Basel II Project - a Bank-wide project for implementation of IT systems to enable Group compliane with Basel II provisions.

c. IT infrastructure development - investment in infrastructure development forms an important basis, allowing the bank to meet expansion of its business as well as 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.

Total investment in hardware and software (including capitalized salary cost) in 2007 and 2006 amounted to NIS 163 million and NIS 153 million, respectively.

Off-balance sheet activity

Provident funds - the Group provides operating services to provident funds, after concluding, in 2007, sale of provident fund operations under its management.

The value of fund assets for which the Group provides operating services amounted to NIS -30.1 billion as of December 31, 2007, compared with NIS 26.3 billion as of December 31, 2006 - an increase of -14.4%.

Said fund assets for which the Group provides operating services include assets sold by the Group in 2007, worth NIS -12.3 billion (including all assets of Netivot funds, of which the Bank had owned only 60% of operations).

See Note 6.E.2) to the financial statements for information on sale of provident fund operations.

Customer activity in securities – The value of the securities portfolios in the custody of the Bank, held by customers, reached NIS 95.6 billion at the end of the year, compared with NIS 76.1 billion at the end of 2006, an annual increase of 25.6%.

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, 2007 amounted to NIS 16.9 billion, compared to NIS 17.0 billion at end of 2006. These amounts exclude standing loans and government deposits extended for them. See Note 19.B to the financial statements for additional information.

Description of Businesses of the Bank Group by Operating Segment

Bank Group operating segments

The Bank manages its operations in seven major operating segments, which are distinguished by customer 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 set forth below. The operations in the seven operating segments include all areas of banking operations including classic banking activity (loans and deposits), securities activity for customers 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.

In view of changes in presentation of operating segments in line with changes in Bank organizational structure, and with operation of the new measuring system, as set forth below, the results presented for 2007 are not comparable to results presented for 2006.

In recent years the Bank has been reorganized, including renewed determination of the operating segments and customer types for the various units. The following principles apply to operating segment assignment to organizational units, with description of major changes:

- The Business Banking division was re-organized to concentrate handling of major customers in specialized units at Bank headquarters or at specially designated centers. The Major Corporations sector in Bank HQ is responsible for the Business Banking segment, which is the focal point for handling the largest business customers. Criteria by which customers 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. Other mid- to large business customers are handled by the Business sector (commercial banking sector), using six business centers 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.
- In 2007, private banking was transferred to the Retail division. Private banking customers are individual customers with liquid assets (primarily short-term deposits and security investments) over NIS 2.5 million, and corporations with liquid assets in excess of NIS 8 million.

- The Retail division is also in charge of the Household segment, which includes smaller individual customers and the Mortgage sector, as well as the Small Business segment, which includes small corporate customers. Most of the business customers in the retail division have indebtedness level of less then NIS 6 million, sales of less than NIS 30 million and liquid asset balance of less than NIS 10 million.
- International operations, including Bank branches overseas and operations of banking centers for tourists in Israel, have been placed under the Financial division. The Financial division is also in charge of financial management, including management of assets and liabilities, liquidity, security portfolio investments and trading room operations in the money- and capital markets.

The Bank's operating segments are:

Household segment - under responsibility of the Retail Division, which provides segment household customers with appropriate banking services and financial products, including mortgages;

Small business segment - under responsibility of the Retail Division, which provides segment customers - small businesses - with banking services and financial products, including commercial banking services appropriate for their needs;

Private banking - under responsibility of the Retail Division. This segment includes customers with 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 – under responsibility of the Business Banking Division, including the business sector, the construction and real estate sector and the corporate sector, which divide among themselves the servicing of business customers, depending on the amount of their debt, turnover and nature of their activities; The commercial banking segment includes mainly operations vis-à-vis medium-sized private and public companies (middle market), which are characterized by medium-sized indebtedness, highly scattered among different economic sectors.

Business banking - with this segment, the Business Division provides a range of banking and financial services to the largest corporations, in a range of sectors, having relatively high indebtedness. This segment also includes the banking services group for major customers in the construction and real estate sector.

International operations – operations in this segment include international operations in the Bank's overseas branches as well as operations vis-à-vis foreign resident customers at tourist banking centers in Jerusalem and Tel Aviv.

Financial management - operations in this segment include, *inter alia*, management of the nostro portfolio, management of exposure to market risk 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.

Along with re-organization, changes have also been made to internal product composition of the segments. The capital market attributes have been redefined to include income and expenses from customer transactions in securities both in Israel and overseas, in addition to the management and operation of provident funds and mutual funds – which were part of this segment in the past. The definition of the credit card sector was also updated to include, in addition to operating income and expenses, also the profit from credit card financing operations.

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 customers, including a checking account, a current loan account, different kinds of credit and guarantees, 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 customers on stock exchanges in Israel and overseas, provident fund operating services (management of provident funds and mutual funds until sold) which are among investment tracks available to Bank customers.
- **Credit cards –** A set of financial products and banking services given in conjunction with credit cards issued to Bank customers 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.

During 2007 the Bank launched a new system for profitability measurement, which measures results of Bank operations and provides a break-down of asset and liability balances from the individual transaction level through the organizational structure hierarchy up to the enterprise-wide level. Bank management uses the new system to analyze operating results by organizational criteria and by product offered by the Bank to customers. Profit is assigned in the system to customers and to products, which are presented in accordance with the Bank's organizational structure.

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

- Credit interest income and deposit interest expenses are directly attributed to the customer. For credit, an expense set at cost of capital raised is attributed to customers, against an inter-segment credit to the Financial Management segment. For deposits, a revenue set at cost of capital raised is attributed to customers, against an inter-segment debit to the Financial Management segment.
- For derivative instrument operations, profits are attributed to the customer at the spread incorporated in the price of the derivative instrument quoted to the customer. 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.
- Provision for doubtful debt is directly attributed to customers for whom it is made.
- Commission and other income is specifically attributed to customers.
- Salary expense is attributed to customers assigned to specific contact persons. In addition, salary expenses of managers and staff of headquarter departments not referring to specific customers, are assigned to customers.
- Maintenance and other expenses are assigned to customers using the appropriate ratios.
- 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 customers services by the branches.
- Provision for tax on operating profit is attributed to customers, 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 customers.
- Fixed assets are attributed based on appropriate ratios.

In order to analyze results of Bank operations by relevant criteria, customers have been assigned in the system to the organizational units in charge of servicing them. Information presented below by operating segment is based on the Bank's organizational structure, including recent changes, on customer assignment to various departments and hence to operating segments, and on attribution of results and balances to customers and segments in the new system.

Financial Information on Operating Segments

The Bank is one of the five largest banking groups, with its share of the five largest groups in terms credit to the public reaching 12%. Since uniform rules have not been prescribed to allocate the customers 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: Due to restructuring at the Bank resulting in changes in expenses due to operations by segment, comparison of 2007 data by operating segment to previous years' data is not possible. See Note 30 to the financial statements for details.

CHART 11

Profitability

Segment	2007		
	Net operating profit	Net profit	Return on equity (in percentages)
Household			
Mortgages	230	230	12.7%
Other	87	208	44.1%
Private banking	38	90	-
Small business	26	65	21.6%
Commercial banking	23	24	9.2%
Business banking	226	231	13.0%
International operations	(56)	(56)	(24.0%)
Financial management	107	116	26.3%
Total	681	908	17.2%

Balance sheet balances

Segment	As of December 31, 2007	
	Credit to the public	Deposits from the public
Household		
Mortgages	36,646	-
Other	6,957	30,731
Private banking	-	2,204
Small business	4,806	11,106
Commercial banking	4,087	2,432
Business banking	17,412	10,753
International operations	4,412	2,570
Financial management	-	15,494
Total	74,320	75,290

Household segment

General information on the operating segment

The household segment typically includes individual customers with low levels of indebtedness and relatively limited financial transactions, which do not warrant inclusion in the business segment or the private banking segment. Segment customers include customers with individual accounts, joint accounts for couples etc. The segment also includes mortgage borrowers. The segment is highly scattered. Following the merger with Bank Tefahot at the beginning of 2005, the Bank set up a Retail Division, which is responsible for areas including the household segment. Since that time, the Retail Division deals with the retail activities of households and mortgage activities. In 2007 the division was also put in charge of the private banking segment (see below).

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 customer’s needs, the level of his income and the judgment of the Bank based on factors including economic models. Pursuant to provisions of Proper Conduct of Banking Business Regulation No. 325, whose main provisions became effective in 2006, the pre-set limits may not be exceeded. See the chapter on Legislation for an elaboration on the Supervisor’s directives.
- **Investments –** providing investment-related services to customers, such as: Various deposits for different terms.
- **Loans for different purposes –** includes loans that are not for the purpose of purchasing a home against a charge on the residence, and other loans for various periods and at different terms.
- **Assistance in financing the purchase of vehicles –** In recent years, activity in the area of loans to purchase autos from the importer, and it constitutes an important element of the segment’s activities. Within this framework, the Bank works together with several auto importers, while offering joint campaigns for financing the vehicle purchases by the customers.

Mortgages

The main services in the mortgages sector are loans from the Bank's funds; additionally, the Bank is engaged in the mortgages 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.

The volume of mortgages issued in the Households Segment (banking and finance; mortgages):

	Loans issued (in NIS millions)			Rate of change	
	2007	2005(1)	2006(1)	2005 to 2006	2006 to 2007
Mortgages issued (for housing and any purpose)					
From the Bank's funds	7,465	5,539	5,572	34.8%	(0.6%)
From the Treasury's funds					
Directed loans	773	802	849	(3.6%)	(5.5%)
Standing loans and grants	166	223	248	(25.6%)	(10.1%)
Management for others	66	92	166	(28.3%)	(44.6%)
Total new loans	8,470	6,656	6,835	27.3%	(2.6%)
Recycled loans	1,124	757	3,358	48.5%	(77.5%)
Total loans issued	9,594	7,413	10,193	29.4%	(27.3%)
Number of borrowers (includes recycled loans)	35,938	26,805	36,836	34.1%	(27.2%)

(1) Reclassified.

A description of the main mortgage services is provided below:

Loans out of Bank funds - loans out of Bank funds and at its risk, which it grants 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, considering the kind of loan and repayment ability of the borrower.

The Bank issues credit in different linkage segments and uses a "combined mortgage" – a loan composition that combines the following elements or a part thereof: CPI-linked element at fixed or variable interest, non-linked shekel element and a dollar-linked element. The combined mortgage enables the Bank to maintain profitability and spread risk to the customer.

Against the backdrop of the low inflation and interest rates, 2007 was characterized by borrowers' growing preference for fixed-rate CPI-linked mortgages and a consistent increase in loans taken in the non-linked shekel segment. 2007 also saw continued decline in performance of the dollar-linked segment.

- **Services within the Ministry of Housing's 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, as provided below:

  a. **Loans -** Within this framework, the Bank provides and manages loans given out of State funds and at its risk, with the Bank serving mainly as a conduit to transfer the money to the eligible borrower and handle collections. In return, the State pays the Bank a commission. An agreement between the Bank (1) and the State of Israel signed July 1, 2004 and extended until June 30, 2008, stipulated that the commissions on State-assisted loans given as from July 1, 2004 will be determined by tender held by the Ministry of Finance with the participation of the mortgage banks, at a significantly lower rate than the commissions on loans issued until June 30, 2004. In February 2008, the Ministry of Finance issued a tender for a new contract to provide loans to eligible borrowers, to be effective from April 2008 for 1 year. At the end of the year, the agreement would be renewed for 1 more year, unless one of the parties informs the other of its wish to terminate the agreement; however, in any case, the agreement would expire after 5 years. Pursuant to terms of the new agreement, as specified in the tender, loans will be granted to eligible borrowers with low point rating out of Bank funds, under terms commonly used in the past for loans out of Ministry of Finance funds, with the Ministry of Finance paying the lending banks interest differentials and margins based on the loan-to-value ratio, geographic location and tender bids.
  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 loan restrictions. For other eligible borrowers terms are unchanged.

Following the new tender, in continuation of the trend started by previous Ministry of Finance tenders, the gradual decline of revenue rates for new loans in the eligible borrower loan portfolio is expected to continue in coming years, leading to gradual decline in Bank revenues from these operations. See Note 19.D.20 to the financial statements for further information.

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 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 in property insurance.

  The borrowers so interested may join an insurance arrangement with one of the insurers with which the insurance agency owned by the Bank has an undertaking, or, alternatively, to make suitable insurance arrangements independently, provided that the policy is assigned to the Bank. It was practice of the vast majority of borrowers to take out property and life insurance, which are conditions for receiving the loans, within the framework of the Bank's arrangement through the Bank, and effective December 1, 2005, through an agency wholly-owned and controlled by the Bank, as provided below.

Marketing of insurance

On February 17, 2005, the Superintendent of Insurance and the Supervisor of Banks informed the banks of their policy on the matter of “marketing life and property insurance ancillary to a housing loan by a banking corporation".

Pursuant to these instructions, starting on December 1, 2005, the Bank's insurance is marketed by a wholly-owned insurance agency of the Bank (Tefahot Insurance Agency (1989) Ltd.), the activities of which are separate from the activities of the Bank and are limited solely to property insurance, including water damage, and life insurance incidental to the loan given 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 customer purchases life insurance and property insurance independently and produces the insurance forms necessary for taking out the loan.

The new arrangement increases competition in the marketing of insurance incidental to the purchase of a home, and therefore, could cause a gradual reduction in the Bank's income from insurance. The Bank is prepared to contend with the strong competition in the industry. Thus for example, a shift occurs from uniform tariffs to differential tariffs, which enable the Bank to offer attractive tariffs to groups of borrowers – especially young borrowers. Since the arrangement only applies to new loans beginning December 1, 2005, the decrease in income, as of the date of the financial statements, is not expected to be significant, and in the estimation of the Bank, will not be significant in the upcoming years.

In August 2003, the Superintendent of Insurance informed the insurance companies that he intends to approve the insurance tariffs for the insurance brokerage activities of mortgage banks, directly or through subsidiaries, for housing insurance related to the issuance of mortgages, so that the rate of damages (see the explanation below) that will be allowed for property insurance through mortgage banks, which was 57% in 2003, will rise gradually, beginning in 2004, up to the rate of 70% in 2008 and thereafter. The rate of the damages, means that part of the premium paid to the sub-insurer, after deducting the commissions paid to the insurance companies and banks (directly or through insurance agencies), so that an increase in the rate of damages reduces the part of the premium that constitutes the commission of the Bank and of the insurance companies for the insurance. Until the date of the financial statements, this change in the damages rate did not have a material effect on the Bank's income from the sale of insurance. The Bank does not expect the said change to have a material effect on its income in the future.

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

	2007	2006
Property insurance	42	45
Life insurance	72	73

As from January 1, 2007, the policies issued to customers through Bank-owned insurance agencies no longer include third party liability insurance coverage.
The aforementioned Bank estimates regarding impact of the above on Bank income from sale of life and property insurance to borrowes is forward-looking information. This estimate is based on a custome-made model which accounts for various assumptions on net premium paid to insurers, size of insured credit portfolio, share of insurance purchase by the Bank Group out of total new mortgages issued etc. The Bank estimate may eventually differ from actual decline in income, should the assumptions underlying the model fail to materialize or should they partially materialize.

See Note 19.D.13)a. and b. to the financial statements for class actions against the Bank related to the Group's insurance activities.

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 distribution and operation services for mutual funds and provident funds, as well as management services prior to their sale.
See Note 6.E.2) to the financial statements for information on sale of provident fund operations.

Credit cards

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

"Tefahot Credit Card" - marketing of this product started in 2006, aimed at assisting mortgage sales as well as opening of current accounts. The product enables the allocation of a credit facility, based on the customer's repayment ability and the asset already pledged to the Bank, through which the customer can finance additional expenses involved in purchasing a home (furniture, renovations, etc.), or for any other reason. To this end, the customer 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.

"Free Student" credit card - in September 2007 the Bank launched its "Free Student" credit card. The card provides students with credit for various uses. Credit using 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). Customers may repay early, in full or partial payment, with no fees or charges.

As of the date of these financial statements, the Bank is in process of establishing a custom branded card for the Bank, and is reviewing options for launching and promotion of the branded card. For the memorandum of understandings with Isracard and Europay, regarding allocation of their shares to the Bank and regarding issue of a branded card, see Note 6.E.5) to the financial statements.

Unique Bank services

Under the household segment, the Bank offers its customers services which express the advantages of the combination of products described above. Within this structure, the Bank offers various benefits in current accounts and credit of customers who take out mortgages, in order to encourage the mortgage customers to maintain their current account in the Bank. The Bank also offers mortgage-related benefits to customers with current accounts in the Bank, in order to encourage these customers to take out mortgages through the Bank.

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

Executive Account – in 2007 the Bank launched a unique brand – the “Executive Account” - in order to enable a preferred segment of individuals to make the most of managing their current account with Mizrahi-Tefahot. The brand emphasizes service, account management, bank value propositions, financial benefits and non-banking services provided to Executive Account customers. Customers 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.

Benefits to mortgage holders - In March 2005, the Bank launched a campaign in which it offered unique benefits to certain groups of customers with an account in the Bank who had a mortgage. 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 customer's meeting other prescribed conditions during that month.

Pension consultancy - the Bank is the first bank in Israel to provide pension consultancy to its own and other banks' customers, both salaried employees and the self-employed. This is based on the computer-supported advisory model created by the Bank. This advisory service is provided by qualified pension advisers, providing an objective advisory service. For details of the pension advisory service, see chapter "Events Outside Bank Group Normal Course of Business".

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

Legislation

A description of the normative framework applicable to the Bank is presented in the chapter on legislation. A description of some of these legislative arrangements, which were recently published and which have clear impact on the activities of the Households Segment, is provided below:

Transfer barriers - On July 14, 2005, the update of the Proper Conduct of Banking Business Regulations No. 432, "Transfer of Activity and Closing of Account of a Customer" was published, with the objective of simplifying the transfer of customers between banks, while also increasing competition among the banks for the activity of this segment's customers. Consequently, the Regulation could also support the Bank's efforts to develop additional baking activity with mortgage customers.

Credit facilities – On February 8, 2005, the Supervisor of Banks published Proper Conduct of Banking Business Regulations No. 325 ("Management of Credit Facility in Current Account"), whereby an overall credit limit will be determined in the current account of a customer, as will be approved by the Bank, and the Bank will not approve a deviation from this limit, subject to the conditions prescribed in the directive (see the chapter on Legislation for details).

Provision for doubtful debt (mortgages) – On January 1, 2006, the Bank of Israel published a circular on the manner in which the provision for doubtful debt is to be computed for housing loans (mortgages). For details of rules for reduction in provision for doubtful debt by depth of arrears, as published in the circular by the Supervisor of Banks, see Note 1.P.3) to the financial statements.

Uniform commission lists and supervision of commissions - Starting on December 1, 2005 the Bank implements commission tracks for customer account activity, as established in accordance with guidelines from the Supervisor of Banks.
On January 8, 2008 the Banking Regulations (Customer Service) (Commissions), 2008 were issued, including publication of a comprehensive list and summary lists of bank commissions. The objective of these lists is to reduce the number of commissions charged by banks and to achieve uniformity of commission names so as to allow customers to review commissions charged and to compare commissions charged by different banks. The regulations apply as of July 1, 2008 and the Bank is preparing to implement them. For further details, see chapter on Legislation and Supervision of Bank Group Operations.
Furthermore, various proposed laws are in different stages of legislation, intended to enhance supervision and regulation of bank-customer relations, especially for household segment customers, concerned primarily with supervision of increased commissions, prohibition of commission charging for certain services etc. Nevertheless, as of the date of these financial statements, these proposals are in different stages of legislation, may be modified, and there is no certainty as to when they would become effective

legislation, hence it is not possible to assess the impact of these various provisions, if and when they should become effective, on Bank operating results in general, and those of the retail sector in particular.

Technological changes

See the chapter on Marketing and Distribution below for technological changes that occurred in the marketing and distribution areas.

Critical success factors in the Household Segment

As a result of the merger between Mizrahi Bank and Tefahot in early 2005, the Bank was exposed to hundreds of thousands of mortgage-holding customers and customers in the deposit sector (customers of the former Bank Tefahot), which constitute a natural target population for marketing of additional Bank products. Expansion of the customer base and broadening the array of services to customers in the Households Segment, while exploiting the reservoir of the customers of the former Bank Tefahot represents a critical factor for the success of this segment.

Furthermore, with the Bank's acquisition of 50% of issued capital of Bank Yahav, Bank Yahav customers may join the retail sector operations, and would be exposed to potential additional activities within the Group, e.g. in mortgages.

Customers

The activities of the households segment are characterized by broad dispersal of the 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 customer or another does not have a material effect on the overall activity of the segment.

However, it should be noted that a considerable part of the active mortgage loans were given to Ministry of Construction and Housing eligible borrowers, half of which are young couples, and the rest, in similar proportions, to new immigrants and other eligible borrowers. In recent years, as a result of the ongoing reduction of assistance on the part of the State, the population of Housing Ministry eligible borrowers has decreased, so that in 2007 more than 80% of the loans were given to customers who are not Ministry of Housing eligible borrowers, compared with 75% in 2006.

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 the direct banking system (Internet and call center).

Bank branches - includes 126 business centers, branches and affiliates, including 10 branches of Bank Adanim. 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 banking - the direct banking network includes call centers, the Bank's website, deployment of self-service terminals and provision of information via cellular phones.

- **Call Centers** - in the second half of 2007, the Bank began to divert telephone calls from the branches to the “Mizrahi Tefahot Call Center”. This is due to Bank policy to increase the sales capacity of the branches, expand business hours and improve the quality and speed of service through the Call Center. The Bank currently operates call centers at two sites, in Tel Aviv and in Jerusalem.
- **Website -** in the first half of 2007, the Bank launched a new website for obtaining information and transacting a wide range of banking transactions online, while improving system user interface and execution speed, while achieving high availability. During 2008 further improvements are planned for the website transaction section, including replacement of the underlying platform for operation of the website's marketing section.
- 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

With respect to this array of products, the number of competitors in the households 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 sector has seen intense competition among banks, which creates barriers to customer moves. 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 customers.

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 customers, 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 merger and Yahav acquisition hold potential for expanding activities in the household segment, based on on-going activities vis-à-vis customers.

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 mortgages sector, in terms of the volume of loans issued and the balance of the loans portfolio. Based on Bank of Israel data, the Bank's share in the housing loans issued out of Bank funds and out of State funds (excluding Bank Adanim) reached 30% in 2007 (due to increased competition in this sector, primarily in the third quarter of 2007), and its cumulative share (loans portfolio), reached 34% of the total banking system. The Bank's share of credit granted as of early 2008 is 32%. The Bank's major competitors are Leumi Mortgage Bank, Bank Hapoalim and Discount Mortgage Bank. Note that 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 mortgages sector is investing resources in constant improvement of its professional standard and the service it provides to customers.

The main entry barriers in this segment are:

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

Cooperation agreements

Several years ago, the Bank entered into 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 customers, 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.

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 customers.

The agreements prescribe mechanisms for calculating the amounts to which the Bank is entitled for the activities of its customers in the cards issued, including based on the volume of usage by the Bank's customers 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 on the Memorandum of Understandings with Isracard Ltd. and Europay (Eurocard) Ltd. on formulating a new agreement for issuance of Bank branded credit cards, see Note 6.E.5) to the financial statements.

Business goals and strategy

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

- Increasing market share by broadening the customer base, mainly among the customers of the former Bank Tefahot and those of Bank Yahav, as a platform for achieving growth in market share and income.
- Expanding activity in the branch network and converting all the branches into sales units in the households segment, for traditional banking activity and mortgage activity, and for cross-selling to customers.
- Retaining Bank share of the mortgages market and expanding it, while focusing on areas with high profitability, by providing valuable proposals to customers, based on the synergy between the mortgage, commercial and financial activities.
- The CRM system (Customer Relations Management), aimed at presenting all relevant information to the banker in order to offer appropriate products to the customer and improve customer relations. During the second half of 2007, the CRM system was deployed in all the Bank's commercial branches.
- The Bank is conducting a project to upgrade its IT system supporting the process of mortgage issuing and management. The new system enables, *inter alia*, use of online transaction processing and daily balance updates. The system would also enable flexible specification and day-to-day operation of the different mortgage products, would facilitate development of new, flexible products and would improve the Bank's competitiveness and capacity to quickly react to changes in the business environment. All Bank branches involved in mortgage processing have started using the new system.
- Over the past two years the Bank has been upgrading its branch computer system, starting to use ".NET" technology. In 2008, the Bank is preparing to deploy and launch the new system. This system positions the bank in the top tier in terms of operations and service to customers and employees.

- Continued development of products aimed at focused population groups, in order to increase volumes of activity.
- Making available different relationships with the customer and nurturing cultivating the customer as an objective of the households segment.
- 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 customers.
- Improving the logistical cooperation with Bank Adanim, while focusing on the development of relative advantages.

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 customers). Additionally, the segment’s results are affected by the entry of credit card companies into retail financing (see the chapter on competition above for information).

As indicated above, the merger between the Bank and Bank Tefahot as well as the acquisition of Bank Yahav holdings constitute an opportunity to broaden the Bank’s customer base and expand its operations in the household segment.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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 Households Segment

Results presented for 2007 are not comparable to results for 2006 as set forth below.

	For the Year Ended December 31, 2007					For the Year Ended December 31, 2006				
	Banking and finance	Credit cards	Capital market	Mortgages	Total	Banking and finance	Credit cards	Capital market	Mortgages(1)	Total
	In NIS millions					In NIS millions				
Profit (loss) from financing operations before provision for doubtful debt										
From outside operating segments	(412)	13	21	2,200	1,822	(127)	-	-	941	814
Inter-segment	964	(10)	-	(1,860)	(906)	445	-	-	(427)	18
Profit from financing operations before provision for doubtful debt	552	3	21	340	916	318	-	-	514	832
Operating and other revenues	167	63	97	262	589	172	52	80	306	610
Total income	719	66	118	602	1,505	490	52	80	820	1,442
Provision for doubtful debt	26	-	-	41	67	38	-	-	136	174
Operating and other expenses										
From outside operating segments	724	41	40	207	1,012	1,485	25	57	282	1,849
Inter-segment	(59)	(3)	-	-	(62)	(922)	-	-	-	(922)
Total operating and other expenses	665	38	40	207	950	563	25	57	282	927
Operating profit (loss) Before taxes	28	28	78	354	488	(111)	27	23	402	341
Provision for taxes on operating profit (loss)	9	10	28	124	171	(36)	12	10	174	160
Operating profit (loss) after taxes	19	18	50	230	317	(75)	15	13	228	181
Net after-tax profit from extraordinary items			121	-	121	-	-	72	-	72
Net profit (loss)	**19**	**18**	**171**	**230**	**438**	**(75)**	**15**	**85**	**228**	**253**
Return on equity					**19.2%**					**12.4%**
Average balance of assets	6,647	848	-	34,935	42,430	4,602	-	-	33,835	38,437
Average balance of liabilities	33,219	-	-	-	33,219	10,828	-	-	20,433	31,261
Average balance of risk assets	7,056	-	-	26,943	33,999	4,300	-	-	26,271	30,571
Average balance of provident and mutual fund assets	-	-	-	-	-	6,044	-	-	1,395	7,439
Average balance of securities	-	-	19,565	-	19,565	-	-	1,956	-	1,956
Credit to the public (end balance)	6,477	1,331	-	35,795	43,603	-	-	-	-	-
Deposits from the public (end balance)	30,731	-	-	-	30,731	-	-	-	-	-
Average balance of assets under management	176	-	-	16,934	17,110	60	-	-	17,382	17,442
Components of profit from financing operations before provision for doubtful debt:										
Margin from credit granting operations	148	3	-	340	491	136	-	-	489	625
Margin from receiving deposits	360	-	-	-	360	169	-	-	12	181
Other	44	-	21	-	65	13	-	-	13	26
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**552**	**3**	**21**	**340**	**916**	**318**	**-**	**-**	**514**	**832**

(1) Reclassified.

Results presented for the household segment for 2007 are not comparable to results presented for 2006 due to changes in presentation of operating segments in line with restructuring of the Bank and the launch of a new measuring method using a dedicated system. The change in the household segment is focused on two areas:

Private banking customers, serviced by senior financial advisors in branches, were previously assigned to the private banking segment. These customers are now assigned to banking and finance under household, hence financing profit, revenues, expenses, balances of deposits and securities which were previously under the private banking segment have been moved to the household segment.

Another change is due to use of a computer system which assigns profitability to customers at the individual transaction level, including assigning the cost of sources under inter-segment profit from financing operations against the financial management segment.

Material impact on the household segment in 2007 primarily include implications of the sale of the Bank Group's provident fund and mutual fund operations, which led to a significant drop in operating revenues in the capital market along with profit from extraordinary items from the actual sale. Segment profitability was impacted by overall growth in profit from current financing operations, including growth in credit – mostly for mortgages – and growth in total deposits.

Private Banking Segment

General information on the operating segment

Private banking is the concept of unique banking services geared to customers with high financial wealth, with a considerable part of their activity executed in the management of financial assets. Private banking customers at the bank are individual customers with liquid assets and security investments over NIS 2.5 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 customers of the segments who have signed consulting agreements. A response is also provided for other financial needs of these customers, 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 growing volume of financial assets of customers belonging to the high socio-economic classes and the potential of the diverse business relationship embedded in the activities of these customers.
- Growing demand by customers 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, as alternatives to traditional products (savings accounts, securities etc.)

During 2007, private banking was placed under responsibility of the retail division, as part of the concept of serving all individual customers under a single division.

Products

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

- **Banking and finance –** A wide range of banking and finance products are offered to this segment's customers, while formulating an investment strategy suitable for each customer, tailored for his characterization and special needs, as well as an array of advanced investment products including deposits and structured products.

- **Credit cards** - The Bank offers the customers of the segment an array of credit cards issued by credit cards issued in Israel.
- **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 distribution and operation services for mutual funds and provident funds, as well as management services prior to their sale. See Note 6.E.2) to the financial statements for information on sale of provident fund operations.

Legislation

A description of the normative framework applicable to the Bank is presented in the chapter on legislation. In addition, the Securities Authority published a guideline in January 2007 in connection with the clarification of the needs of customers (individuals).

According to the guideline, the Bank is required, within the scope of the consulting services it provides to customers, to question the customer on the basis of a list of questions that constitutes part of the guideline. This is done, in order to learn the preferences and needs of the customer. The Bank is prepared to meet the requirements of the guidelines through the broadening and preparation of documents and forms suitable for clarifying the required details. Regarding new customers, the guidelines will apply as from November 2007, and as to customers who have signed consulting agreements prior to the said date, the guidelines will take effect as from July 2008.

Technological changes

See the chapter on IT Systems and Computers below for the technological changes, including with respect to operation of provident funds and pension advisory service.

Critical factors for success

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

Customers

This segment serves customers with high financial wealth, mainly individual customers with liquid deposits and security investments exceeding NIS 2.5 million and business customers with such liquid balances in excess of NIS 8 million. See Note 30 to the financial statements for details.

The customer group served by this segment is heterogeneous, there are no material dependencies or relations between customers, hence the private banking segment is not dependent on any specific group of customers 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 the direct banking system, conferences are conducted for customers in this segment, according to select population segments and inquiries through direct mail in a special format.

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 the total system.

In addition, 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 the 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 customer, in the organization of professional conferences for the segment's select customers, in the intensive introduction of specialized and unique products to the segment's customers, and in efforts to identify and attract new customers on a regular basis.

The segment’s main entry barriers 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 intends to upgrade, bolster and strengthen the organizational structure of the private banking segment, in preparation for the intake and support of additional customers in the coming years.

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

The economic growth constitutes an opportunity to expand the activities of this segment, mainly in the investments area. In this connection, we cite the activities of foreign banks and non-banking entities as one of the threats to the Bank's activities in the investments area.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, customers’ 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

Results presented for 2007 are not comparable to results for 2006 as set forth below.

	For the Year Ended December 31, 2007			For the Year Ended December 31, 2006			
	Banking and finance	Capital market	Total	Banking and finance	Credit cards	Capital market	Total
	In NIS millions			In NIS millions			
Profit from financing operations before provision for doubtful debt							
From outside operating segments	(101)	1	(100)	(562)	-	-	(562)
Inter-segment	148	1	149	751	-	-	751
Profit from financing operations before provision for doubtful debt	47	2	49	189	-	-	189
Operating and other revenues	3	18	21	94	9	37	140
Total income	50	20	70	283	9	37	329
Operating and other expenses							
From outside operating segments	11	-	11	43	9	20	72
Inter-segment	1	-	1	206	-	-	206
Total operating and other expenses	12	-	12	249	9	20	278
Pre-tax operating profit	38	20	58	34	-	17	51
Provision for taxes on operating profit	13	7	20	11	-	8	19
Operating profit after taxes	25	13	38	23	-	9	32
Net after-tax profit from extraordinary items	-	52	52	-	-	33	33
Net profit	**25**	**65**	**90**	**23**	**-**	**42**	**65**
Return on equity			-				76.7%
Average balance of assets	-	-	-	2,498	-	-	2,498
Average balance of liabilities	2,210	-	2,210	17,115	-	-	17,115
Average balance of risk assets	-	-	-	1,272	-	-	1,272
Average balance of provident and mutual fund assets	-	-	-	3,490	-	-	3,490
Average balance of securities	-	4,731	4,731	-	-	7,392	7,392
Credit to the public (end balance)	-	-	-				
Deposits from the public (end balance)	2,204	-	2,204				
Average balance of other assets managed	-	-	-	12	-	-	12
Components of profit from financing operations before provision for doubtful debt:							
Margin from credit granting operations	-	-	-	54	-	-	54
Margin from receiving deposits	47	-	47	118	-	-	118
Other	-	2	2	17	-	-	17
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**47**	**2**	**49**	**189**	**-**	**-**	**189**

Results presented for the private banking segment for 2007 are not comparable to results presented for 2006 due to changes in presentation of operating segments in line with restructuring of the Bank and the launch of a new measuring method using a dedicated system. The change in the private banking segment is mainly transfer of private banking customers, served by senior financial advisers in the branches. These customers were previously assigned to the private banking segment, and are now assigned to banking and finance under the household segment. Therefore, financing profit, revenues, expenses and balances of deposits and securities have been diverted from private banking to household. Furthermore, private banking customers in the Bank's overseas branches, previously included under this segment, are now assigned to the international operations segment.
Another change is due to use of a computer system which assigns profitability to customers at the individual transaction level, including assigning the cost of sources under inter-segment profit from financing operations against the financial management segment.
Material impact on the private banking segment in 2007 primarily include implications of the sale of the Bank Group's provident fund and mutual fund operations, which led to a significant drop in operating revenues in the capital market along with profit from extraordinary items from the actual sale.

Small Businesses Segment

General information on the operating segment

The small business segment operates within the retail division, and mainly serves family-owned businesses and small business customers with relatively low turnover and total indebtedness of up to NIS 6 million. Service of segment customers, under responsibility of the Bank's retail division, is characterized by a large variance among customers. In view of the fact that the availability of data and their reliability regarding the customers of this segment is relatively low, there is a need for professional service and appropriate means of control, in order to assess the quality of the customer for the purpose of issuing credit. Additionally, this segment is characterized by a high required-collateral percentage from the customers to ensure credit repayment.

Products

Banking and finance

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

- Loans for various purposes – loans against the discounting of checking/credit cards, business loans, etc.
- Import/export activities – foreign currency operations, adaptation of credit facilities to the nature of the customer's activities using technological means, such as: EDI on the Internet.
- 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 customer's needs, turnover and judgment of the Bank. According to the directives of the Supervisor of Banks, there will be no exceeding the approved facilities. See the chapter on legislation for information.
- **Credit cards -** The Bank offers the customers of the segment an array of credit cards issued by credit cards issued in Israel.
- **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 distribution and operation services for mutual funds and provident funds, as well as management services prior to their sale. See Note 6.E.2) to the financial statements for information on sale of provident fund operations.

See below for information on alternatives to these products.

Legislation

A description of the normative framework applicable to the Bank is presented in the chapter on legislation. A description of some of these legislative arrangements, which were recently published and which have clear impact on the activities of the Private Banking Segment, is provided below:

Credit facilities – On February 8, 2005, the Supervisor of Banks published Proper Conduct of Banking Business Regulations No. 325 ("Management of Credit Facility in Current Account"), whereby an overall credit limit will be determined in the current account of a customer, as will be approved by the Bank, and the Bank will not approve a deviation from this limit, subject to the conditions prescribed in the directive (see the chapter on Legislation for details).
For changes in legislation and regulation intended to regulate bank-customer relations, including commission pricelist, see above under Household Segment and under the Legislation chapter.

Technological changes

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

Critical factors for success

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

Customers

In the small businesses segment there is no dependence on a specific customer or a limited number of customers.

Marketing and distribution

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

Competition

The existing competition in this operating segment is mainly within the banking system. Furthermore, activity of non-banking credit providers (insurance companies, non-bank credit cards and various financing companies) is increasing. The Bank's principal methods for dealing with the competition are active marketing, personal ties with the customer, providing personal service and comprehensive professional solutions for the full range of customer financial needs. The objective is to increase market share.

The main entry barriers in this segment are:

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

Business goals and strategy

Bank strategy emphasizes expansion of operations in the small business segment.
Below are the key goals in the small business segment and the business strategy deriving from these goals:

- Increasing marketing activity opposite customers, while segmenting the customers by occupation, size of operation and individual needs.
- Maximize potential profitability for each customer by adopting a comprehensive view of customer activity, creating a comprehensive relationship based on credit products and marketing of other products – depending on customer attributes.
- Expand geographic deployment of services provided to segment customers.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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

Results presented for 2007 are not comparable to results for 2006 as set forth below.

	For the Year Ended December 31, 2007				For the Year Ended December 31, 2006			
	Banking and finance	Credit cards	Capital market	Total	Banking and finance	Credit cards	Capital market	Total
	In NIS millions				In NIS millions			
Profit from financing operations before provision for doubtful debt								
From outside operating segments	(314)	3	2	(309)	452	-	-	452
Inter-segment	588	(2)	-	586	(16)	-	-	(16)
Profit from financing operations before provision for doubtful debt	274	1	2	277	436	-	-	436
Operating and other revenues	147	9	17	173	269	18	42	329
Total income	421	10	19	450	705	18	42	765
Provision for doubtful debt	74	-	-	74	65	-	-	65
Operating and other expenses								
From outside operating segments	353	2	6	361	7	15	31	53
Inter-segment	(26)	-	-	(26)	553	-	-	553
Total operating and other expenses	327	2	6	335	560	15	31	606
Pre-tax operating profit	20	8	13	41	80	3	11	94
Provision for taxes on operating profit	7	3	5	15	32	1	5	38
Operating profit after taxes	13	5	8	26	48	2	6	56
Net after-tax profit from extraordinary items	-	-	39	39	-	-	23	23
Net profit	**13**	**5**	**47**	**65**	**48**	**2**	**29**	**79**
Return on equity				**21.6%**				**13.3%**
Average balance of assets	4,938	-	-	4,938	7,018	-	-	7,018
Average balance of liabilities	9,796	-	-	9,796	14,919	-	-	14,919
Average balance of risk assets	4,561	-	-	4,561	8,880	-	-	8,880
Average balance of provident and mutual fund assets	-	-	-	-	2,361	-	-	2,361
Average balance of securities	-	-	21,091	21,091	-	-	43,106	43,106
Credit to the public (end balance)	4,806	-	-	4,806				
Deposits from the public (end balance)	11,106	-	-	11,106				
Average balance of other assets managed	158	-	-	158	138	-	-	138
Components of profit from financing operations before provision for doubtful debt:								
Margin from credit granting operations	168	-	-	168	275	-	-	275
Margin from receiving deposits	86	-	-	86	118	-	-	118
Other	20	1	2	23	43	-	-	43
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**274**	**1**	**2**	**277**	**436**	**-**	**-**	**436**

Results presented for the small business segment for 2007 are not comparable to results presented for 2006 due to changes in presentation of operating segments in line with restructuring of the Bank and the launch of a new measuring method using a dedicated system.
The small business segment is presented, starting with these financial statements, based on a computer system which assigns profitability to customers at the individual transaction level, including assigning the cost of sources under inter-segment profit from financing operations against the financial management segment.
The change in definition of the population included in this segment is due to the fact that it is not based on customer segmentation by attributes, but rather by their organizational assignment.

Commercial Banking Segment

General information on the operating segment

The commercial banking segment includes primarily activity vis-à-vis medium-sized private and public companies (Middle Market) with medium turnover of NIS 30-120 million and total indebtedness from NIS 6-25 million. This includes extensive distribution over different economic sectors. Segment customers are served under the Bank's business division.

The customers of this segment are characterized by the range of banking services they consume and the collateral percentage, which is generally higher than for customers of the business banking segment.

In 2005–2007, due to the improved state of the economy and the business atmosphere, which were expressed by the increased growth and in investments, some recovery was evident in this segment, which was reflected in the increased consumption of bank financing for the expansion of the different kinds of activity.

Products

Customers of the segment are offered services, mainly in the area of banking and finance. 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, as well as investment in deposits and in securities.

Legislation

A description of the normative framework applicable to the Bank is presented in the chapter on legislation.

Technological changes

See the chapter below on IT systems and computerization below for technological changes and projects being conducted in the computerization area.

Critical factors for success

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

Customers

Segment customers 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 customer.

Marketing and distribution

The main marketing and distribution parties in this segment are the six business centers that are the responsibility of the Business Division, business centers and branches spread throughout the country. There is no dependence on outside marketing channels.

Competition

The existing competition in this operating segment is mainly within the banking system. The activities of non-banking financing entities are marginal, but there are signs of an awakening in this area.

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

The major barriers facing a customer in moving to and from the Bank, derive mainly from the fact that there is some difficulty in transferring security from one bank to another; a factor that is significant in this sector, which is characterized by a relatively large volume of security. In order to increase the market share in the segment, while dealing with the difficulties created by the barriers the segment on taking in new customers, the Bank is working toward formulating solutions based mainly on improving the standard of service, professionalism and rapid response to 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 effective mainly regarding the small banks in the Israeli banking system.
- Minimum capital requirements – requirements as a percentage of 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 customers and their needs. The service provider must provide high quality, rapid service, while providing optimal solutions.
- Construction and maintenance of physical infrastructure (such as branches) and technological infrastructure (IT systems).
- Customer habits – with emphasis on maintaining current relationships and reputation of banking institutions

Business goals and strategy

The Bank's business strategy emphasizes the expansion of the customer 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 customers and expanding banking services to current and secondary customers. This is based on the range of products offered to segment customers, as described above.

The Bank would continue to operate, under the business banking division, dedicated departments for customers of the different segments, aided by business centers throughout the country.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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 issues of human resources.

Results of the Commercial Banking Segment

Results presented for 2007 are not comparable to results for 2006 as set forth below.

	For the Year Ended December 31, 2007				For the Year Ended December 31, 2006	
	Banking and finance	Credit cards	Capital market	Total	Banking and finance (1)	Total
	In NIS millions				In NIS millions	
Profit from financing operations before provision for doubtful debt						
From outside operating segments	183	-	2	185	211	211
Inter-segment	(70)	-	-	(70)	(139)	(139)
Profit from financing operations before provision for doubtful debt	113	-	2	115	72	72
Operating and other revenues	34	2	6	42	24	24
Total income	147	2	8	157	96	96
Provision for doubtful debt	7		-	7	6	6
Operating and other expenses						
From outside operating segments	121	-	3	124	3	3
Inter-segment	(9)	-	-	(9)	53	53
Total operating and other expenses	112	-	3	115	56	56
Pre-tax operating profit	28	2	5	35	34	34
Provision for taxes on operating profit	9	1	2	12	14	14
Operating profit after taxes	20	1	3	23	20	20
Net after-tax profit from extraordinary items	1	-	-	1	-	-
Net profit	**21**	**1**	**3**	**24**	**20**	**20**
Return on equity				**9.2%**		**11.1%**
Average balance of assets	4,349	-	-	4,349	2,916	2,916
Average balance of liabilities	2,167	-	-	2,167	914	914
Average balance of risk assets	3,801	-	-	3,801	2,700	2,700
Average balance of provident and mutual fund assets	-	-	-	-	41	41
Average balance of securities	-	-	2,149	2,149	4,797	4,797
Credit to the public (end balance)	4,087	-	-	4,087		
Deposits from the public (end balance)	2,432	-	-	2,432		
Average balance of other assets managed	50	-	-	50	137	137
Components of profit from financing operations before provision for doubtful debt:						
Margin from credit granting operations	80	-	-	80	61	61
Margin from receiving deposits	18	-	-	18	5	5
Other	15	-	2	17	6	6
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**113**	**-**	**2**	**115**	**72**	**72**

(1) Includes operating results for credit cards and the capital market, in immaterial amounts.

Results presented for the commercial banking segment for 2007 are not comparable to results presented for 2006 due to changes in presentation of operating segments in line with restructuring of the Bank and the launch of a new measuring method using a dedicated system. The commercial banking segment is presented, starting with these financial statements, based on a computer system which assigns profitability to customers at the individual transaction level, including assigning the cost of sources under inter-segment profit from financing operations against the financial management segment.
The change in definition of the population included in this segment is due to the fact that it is not based on customer segmentation by attributes, but rather by their organizational assignment, based on the new structure and operating principles of customer assignment under the business banking division. This change causes activity to be shifted between the commercial banking segment and the business banking segment.
Furthermore, commercial banking customers in the Bank's overseas branches, previously included under this segment, are now assigned to the international operations segment.

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 customer and turnover in excess of NIS 120 million. This segment also includes the banking services 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 customers 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.

The ongoing economic growth and the entry of parties interested in non-banking investments in the Israeli economy could contribute to increased interest in this segment. Investment funds operating in the economy could generate acquisition and hi-tech activity.

Products

Banking and finance

In this segment, the Bank offers customers a diverse range of banking and financial service 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 customers of the real estate sector are:

Construction credit - In this area, the Bank provides different kinds of credit, particularly short and intermediate-term loans, intended to finance the purchase of land and the investment in construction, as well as different kinds of bank guarantees.

Construction project financing - The financing of construction projects is a unique service, provided by the Bank to a group of customers in this industry alone. Within this framework, the customer is allocated a package of financial and banking services, suited to the specific needs of each project and based on its characteristics. This includes credit facilities to purchase land, construction loans, monetary guarantees, performance guarantees, and guarantees to the buyers of units in a project. 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.

Legislation

A description of the normative framework applicable to the Bank is presented in the chapter on legislation. A description of some of these legislative arrangements, which were recently published and which have clear impact on the activities of the Business Banking Segment, is provided below:

Transactions with related persons – In accordance with Proper Banking Conduct Regulation No. 312 ("Transactions of Banking Corporation with Related Persons"), a limitation has been imposed on the Bank, whereby the Bank is permitted to grant credit to the category of "related persons" of the Bank, as defined in regulation, not to exceed 10% of the Bank's capital. Due to this limitation, the Bank stipulated in some of the agreements with these persons that the credit may be utilized, in full or part, only if it does not cause deviation in the said limitation.

Financing an 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 limitation – The provisions of Proper Banking Conduct Regulation No. 315 ("Supplementary Provision for Doubtful Debt") stipulate that when all the debt ("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 exceeds 20% of the total debt 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 debt. This limit is evaluated on an unconsolidated basis. This limitation is not effective with respect to the Bank's activity as of the date of the financial statements.

Limitations on debt of a borrower and a group of borrowers – In accordance with Proper Banking Conduct Regulation No. 313 ("Limitations on Debt 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 regulation, after certain amounts provided in the regulation were deducted from the debt, not to exceed 15% or 30% of the Bank's capital, respectively. The Regulation also prescribes that total indebtedness of the six largest borrowers and borrower groups in any bank will not exceed 135% of its capital. Due to this limitation, the Bank stipulated in some of the agreements with these persons that the credit may be utilized, in full or part, only if it does not cause deviation in the limitations per-borrower or per-borrower groups.

Securing home buyers – the Sale Law (Apartments) (Securing the Investments of Home Buyers), 1974 (in this paragraph – ("the Sale Law" or "the Law") prohibits the apartment seller ("seller" and "apartment" as defined in the Law) to receive proceeds exceeding 15% of the price, unless the buyer is secured through one of the alternatives provided in the Law. One of the alternatives provided in the Law to secure apartment buyers is the furnishing of a bank guarantee under the Sale Law. 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 – On February 4, 2008, the Supervisor of Banks published Proper Conduct of Banking Business Regulations No. 326 ("Financial Assistance"). This regulation is aimed at securing monies of apartment buyers on projects financed using financial assistance, and ensuring that sources designated for project construction, in particular proceeds from sale of apartments, are concentrated in the designated project account. This is achieved by implementing payment vouchers. The regulation stipulates that a banking corporation may only provide financial assistance to a construction project if a booklet of payment vouchers is produced and handed to the developer for each apartment to be sold in the project. 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 sets forth 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 would apply to financial assistance agreements signed June 1, 2008 onwards. The Bank is preparing to implement these regulations.

Basel II – In conjunction with preparations for application of the Basel II principles by banking corporations in Israel, the Supervisor of Banks announced his intention to apply the Basel II regulations starting in 2009. The Business Division, which is responsible for the business banking segment, is preparing to implement these provisions within the scope of the Bank's general preparations on this issue. The Business Division deals mainly with the credit aspects deriving from the provisions of Basel II and the related provisions. For details on Bank preparations for application of these regulations, see below under the Legislation chapter.

Technological changes

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

Critical factors for success

Critical factors for success in the Business Banking segment include a strong ability to analyze the customer's needs and their financial condition, including the identification of risk deriving from activity opposite customers, including as a result of expected changes in the economy and the industry in which he is engaged, and on providing professional, fast and effective service that offers a comprehensive and appropriate solution to the customer's needs in all banking areas. This is done while offering diverse and innovative products while controlling risk due to any activity.

Customers

Segment customers include large business customers with sales in excess of NIS 120 million or total indebtedness in excess of NIS 25 million. Furthermore, in accordance with the approach of the Bank's Executive Management regarding the segment allocation of the real estate activities, and in accordance with the manner in which these customers are serviced and the Bank's organizational structure, the Business Banking segment includes the customers who receive banking services in the construction and real estate segments, even if the volume of their debt is mid-sized. In this segment, there is no dependence on a major individual customer.

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 customer needs, the servicing of the business banking customers in this segment was placed under the Corporate Sector in the Head Office, divided into departments and teams having specific industry specialization. The teams consult with the Bank’s specialists in the fields of foreign trade, capital market, trading in derivatives, etc., with the goal of providing a comprehensive solution for the customer’s needs. Real estate customers are serviced by the construction and real estate sector, which also constitutes part of the Business Division and operates, *inter alia*, through four regional business departments located in the main activity centers and 12 branches that specialize in financial support.

Competition

Most of the competition in the Business Banking Segment is opposite the large and mid-sized banks in Israel, and for some services – the entire capital market. The entry of foreign banks and non-banking entities, mainly insurance companies, is concentrated in long-term credit. Note that along with growth of credit balances of the entire business sector in Israel in recent years, the share of banks in financing this sector has significantly declined.

The alternatives for the products and services offered by the segment are the raising of 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 customer'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. The segment has placed emphasis on the best possible personal service to the business customer and adapting it to the customer's needs according to his unique characteristics, while focusing on industry expertise and providing specific professional advice in specialty areas.

There are almost no barriers to customer movement between banks in banking activity of this operating segment. This is due to the fact that customers in this segment are mostly customers of multiple banks.

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 entered into activities with the goal of financing projects in the industry. 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, usually by joint transactions with banks which are not among the five major banking groups. The independent activity of the small banks in the real estate industry is limited, mainly due to the limitations on borrowings of an individual borrower or group of borrowers.

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 customers' needs, readily available and fast service, and maintaining close and personal ties with customers. This is done particularly through the specialized business departments specializing in the building and real estate industry, dispersed among the principal business centers of Israel.

The main entry barriers in this segment are:

- Regulatory limitations on banking corporations – including per-borrower and per-group of borrower limitations, as a result of the high volume of credit required as part of the activities of the 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 customers in this industry.
- Minimum capital requirements – requirements as a percentage of 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 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 infrastructure (such as branches) and technological infrastructure (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 customer, leveraging credit products and offering other products to establish a comprehensive customer relationship.

- Segment business customers by size, sector of operation and other attributes in order to optimally specify their business needs and to provide an appropriate, professional solution.
- Putting emphasis on profitability and yield of the uses, and a gradual shift to the measurement of return and risk by the principles included in the Basel II recommendations for the management of credit risk and operational risk.
- The sale of loans or long-term securitization of credit that does not maximize the profitability potential relative to the Bank capital made available for it and in order to enable greater flexibility in managing the credit of these customers with respect to regulatory limitations (mainly as relates to per-borrower limits).

The risk in realizing the strategy set forth above is mainly a reduction in the volume of activity with certain customers, from which the Bank's profit is relatively low. In contrast, the overall profitability of the Bank could rise, as it focuses on profitable customers and expansion of activity opposite them, while utilizing the Bank's capital resources.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, customers' 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 issues of human resources.

Results of the Business Banking Segment

Results presented for 2007 are not comparable to results for 2006 as set forth below.

	For the Year Ended December 31, 2007					For the Year Ended December 31, 2006		
	Banking and finance	Credit cards	Capital market	Real estate and construction	Total	Banking and finance (1)	Real estate and construction	Total
	In NIS millions					In NIS millions		
Profit from financing operations before provision for doubtful debt								
From outside operating segments	238	-	31	388	657	389	494	883
Inter-segment	15	-	-	(210)	(195)	(124)	(269)	(393)
Profit from financing operations before provision for doubtful debt	253	-	31	178	462	265	225	490
Operating and other revenues	131	1	23	8	163	52	27	79
Total income	384	1	54	186	625	317	252	569
Provision for doubtful debt	24	-	-	53	77	4	56	60
Operating and other expenses								
From outside operating segments	99	-	1	33	133	78	34	112
Inter-segment	57	-	-	11	68	81	29	110
Total operating and other expenses	156	-	1	44	201	159	63	222
Pre-tax operating profit	204	1	53	89	347	154	133	287
Provision for taxes on operating profit	72	-	18	31	121	76	55	131
Operating profit after taxes	132	1	35	58	226	78	78	156
Net after-tax profit from extraordinary items	-	-	5	-	5	2	1	3
Net profit	**132**	**1**	**40**	**58**	**231**	**80**	**79**	**159**
Return on equity					**13.0%**			**10.0%**
Average balance of assets	12,217	-	-	5,282	17,499	9,264	6,529	15,793
Average balance of liabilities	11,379	-	-	861	12,240	6,247	1,437	7,684
Average balance of risk assets	13,830	-	-	12,468	26,298	13,141	10,633	23,774
Average balance of provident and mutual fund assets	-	-	-	-	-	260	81	341
Average balance of securities	-	-	37,711	-	37,711	14,281	-	14,281
Credit to the public (end balance)	11,201	-	-	6,211	17,412			
Deposits from the public (end balance)	9,800	-	-	953	10,753			
Average balance of other assets managed	20	-	-	93	113	82	134	216
Components of profit from financing operations before provision for doubtful debt:								
Margin from credit granting operations	134	-	-	178	312	163	162	325
Margin from receiving deposits	72	-	-	-	72	24	18	42
Other	47	-	31	-	78	78	45	123
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**253**	**-**	**31**	**178**	**462**	**265**	**225**	**490**

(1) Includes operating results for credit cards and the capital market, in immaterial amounts.

Results presented for the business banking segment for 2007 are not comparable to results presented for 2006 due to changes in presentation of operating segments in line with restructuring of the Bank and the launch of a new measuring method using a dedicated system. The business banking segment is presented, starting with these financial statements, based on a computer system which assigns profitability to customers at the individual transaction level, including assigning the cost of sources under inter-segment profit from financing operations against the financial management segment.

The change in definition of the population included in this segment is due to the fact that it is not based on customer segmentation by attributes, but rather by their organizational assignment, based on the new structure and operating principles of customer assignment under the business banking division. This change causes activity to be shifted between the commercial banking segment and the business banking segment.

Furthermore, business banking customers in the Bank's overseas branches, previously included under this segment, are now assigned to the international operations segment.

International Operations segment

General information on the operating segment

The international operations segment in 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 set forth below. The international operations segment, in Israel and overseas, is under responsibility of the Bank's financial division.

Deployment, products and customers

These are the different affiliates, their 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 holding company of the Bank registered in Holland – UMOHC B.V. ("the holding company"). The Swiss subsidiary is subject to the regulatory laws in Switzerland.

USA subsidiary – UMTB Securities Inc., a wholly-owned subsidiary of the Bank incorporated in the State of Delaware in the USA. Provides broker-dealer services for Bank customers for transactions in securities traded on the USA capital markets. The Bank received a permit from the Bank of Israel to hold a subsidiary, as aforesaid. On April 4, 2007, the company obtained a license from the Securities and Exchange Commission (SEC) to transact in securities traded on USA capital markets, and became a member of the National Association of Security Dealers (NASD).

Bank's overseas branches – Overseas branches offer their customers 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 engaged mainly in commercial banking, private banking and foreign trade. Deposits with this branch are insured by the Federal Deposit Insurance Corporation(FDIC). Most of the branch customers are US residents.

- **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 customers are local, Israeli and international customers.
- **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.

International banking branches in Israel: The Bank operates two special branches, located in Jerusalem and Tel Aviv, serving foreign resident customers. These branches provide full banking services to their customers, primarily private banking. The branches are under Israeli supervision and report to the International Operations sector.

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 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 below:

Subsidiary in Switzerland - The EBK – Eidgenossische Bankenkommission, the federal regulatory authority of Switzerland.

Subsidiary, UMTB Securities Inc. – the American Securities and Exchange Commission (SEC) and National Association of Securities Dealers (NASD).

Los Angeles branch - The State of California Financial Institution Department, the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve Bank. In accordance with the regulations of the Federal Deposit Insurance Corporation (FDIC), the Los Angeles Branch must hold "eligible assets", as defined in the regulations, at a rate of 106% of total liabilities. According to these regulations, a deposit in a bank that did not waive the set off agreement opposite 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.

On November 19, 2007, the FDIC conducted an audit at the Los Angeles branch concerned, *inter alia*, with implementation of the compliance program with banking confidentiality laws and prohibition of money laundering. On February 7, 2008, a meeting

was held between Bank and FDIC representatives, and an exchange of letters ensued between the Bank and FDIC with regard to audit findings and their treatment.
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.

Technological changes

The international operations segment operates within the Bank Group to constantly align systems and day-to-day operations. Each affiliate has a local IT department, serving the affiliate's specific nees. During the year, systems have been reviewed and upgraded at each affiliate separately, and the affiliates have been aligned among themselves and with Bank Group operations in Israel.

Critical success factors

Critical success factors for the international operations segment are based on providing a global high-quality service to different global markets, primarily to Bank customers. Service provided to customers is based on understanding their personal needs and providing individual solutions based on intensive local knowledge of local markets in order to find the appropriate range of products.

Marketing and distribution

Each affiliate in the international operations segment has a unique target audience. Marketing is conducted by segment headquarters in Israel, based on requirements of each affiliate and in full cooperation with them.

Competition

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 customers.
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 segment is also focused on providing high-quality service and maintaining strong customer relationships, organizing professional events for select segment customers, intensive launching of custom products for segment customers and efforts to locate and recruit new customers on a day-to-day basis.

The main entry barriers in this segment are:

- Regulatory limitations
- Minimum capital requirements
- Recruiting professional staff, with various language skills
- Install and maintain physical infrastructure
- A supply of unique financial products.

Business goals and strategy

The segment emphasizes world-wide business development, including expanding operations at existing affiliates and reviewing creation of additional operating centers.

The segment strives to create strategic alliances with leading financial institutions in international banking and jointly working with them. The segment 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 is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, customers' 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 issues of human resources.

International Operations segment results

	For the Year Ended December 31, 2007		
	Banking and finance	Capital market	Total
Profit from financing operations before provision for doubtful debt			
From outside operating segments	(105)	-	(105)
Inter-segment	96	-	96
Profit from financing operations before provision for doubtful debt	(9)	-	(9)
Operating and other revenues	53	3	56
Total income	44	3	47
Provision for doubtful debt	3	-	3
Operating and other expenses			
From outside operating segments	130	-	130
Inter-segment	-	-	-
Total operating and other expenses	130	-	130
Pre-tax operating profit	(89)	3	(86)
Provision for taxes on operating profit	(31)	1	(30)
Operating profit after taxes	(58)	2	(56)
Net after-tax profit from extraordinary items	-	-	-
Net profit (loss)	**(58)**	**2**	**(56)**
Return on equity			**(24.0%)**
Average balance of assets	5,873	-	5,873
Average balance of liabilities	5,999	-	5,999
Average balance of risk assets	3,456	-	3,456
Average balance of provident and mutual fund assets	-	-	-
Average balance of securities	-	766	766
Credit to the public (end balance)	4,412	-	4,412
Deposits from the public (end balance)	2,570	-	2,570
Average balance of other assets managed	-	-	-
Components of profit from financing operations before provision for doubtful debt:			
Margin from credit granting operations	88	-	88
Margin from receiving deposits	17	-	17
Other	(114)	-	(114)
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**(9)**	**-**	**(9)**

International operations are presented as a segment for the first time in 2007, following a change in management concept of its place and organizational affiliation with the financial division. In recent years, results of international operations were included under other segments.

The loss presented for the segment is primarily due to provision for impairment of non-temporary nature of investment in asset-backed securities, amounting to NIS 114 million in 2007. Excluding the aforementioned provision, the segment would have presented net profit of NIS 15 million.

Financial Management Segment

The activities in the financial management segment are concentrated in several key areas: Management of all assets and liabilities, management of the nostro 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 equity investments in non-banking corporations. This is in line with management view of how these operations should be managed.

The sources of the activity in the nostro 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 risk (see the chapter on risk management for details on the liquidity model and limitations of management and the board of directors). The activities in this segment are intended to maximize the yield on the investment of these surpluses, while maintaining the volume of activity and the level of exposure to market risk that were limited by the management and the board of directors. Limit criteria were also prescribed for nostro activity, based on the credit risk inherent in the portfolio's activity, to disperse investments and their liquidity. The activity in the nostro account is subject to meeting the credit limits prescribed in the Bank for countries, banks and companies. The financial management segment strives to expand nostro investments in Israel and overseas, and to enter new investment areas, including complex instruments, subject to Bank risk management policy.

In management of exposure to market risk, the Bank adopts an active policy of opening and closing positions, with the objective of creating profits, within a specified risk level.
The volume of activity and risk must meet the market risk exposure limits prescribed by the board of directors and management. For details of the model for management of the held-for-sale portfolio and of risk limitation and management of exposure to market risk, as well as implementation of a new, advanced system for risk management and current management of exposure, see below the Risk Management chapter.
The Bank's activities in the financial management segment require that the Bank allot capital. The capital requirement is computed according to Proper Banking Conduct Regulation No. 341 ("Allotment of Capital due to Exposure to Market Risk). The Bank regulates the capital needs required for this activity by computing the exposure to market

risk inherent in the trading portfolio of the Bank, as defined in the provisions of Regulation No. 341.

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 computed 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 opposite 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. The various segments are charged by the financial management segment for the sources made available to them from capital raised outside the Bank.

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 Issue Company Ltd., as provided below in the chapter on issuing subordinated notes and debentures to the public.
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 customers trading in securities in Israel and overseas.

In December 2005, the Bank was appointed chief market maker for "Shahar" bonds by the Ministry of Finance, in accordance with the Government Loans Law, 1979. The Bank started making a market pursuant to this appointment on September 4, 2006.

Business goals and strategy
The segment includes management of the nostro portfolio, management of exposure to market risk and liquidity management. Segment objectives in these areas include active management of exposure and nostro portfolio in order to maximize gains while maintaining controlled exposure to market risk and appropriate liquidity, pursuant to limitations specified in Board and management directives.

The segment would also act 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 the Bank's trading room operations in financial and capital markets. The Bank intends to expand its operations in this area by expanding the customer base and intensifying business activity and customer 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. Also, professional staff engaged in this area and technological systems to support the different activities.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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 financial markets and capital markets in Israel and world-wide, other factors that impact the exposure to financial risk, price and availability of financial assets, customers' financial robustness, the public's preferences, legislation, directives of regulatory entities, the behavior of competitors, technological developments and issues of human resources.

Financial Management Segment results

Results presented for 2007 are not comparable to results for 2006 as set forth below.

	For the Year Ended December 31, 2007			For the year ended December 31, 2006
	Banking and finance	Capital market	Total	Banking and finance (1)
	In NIS millions			In NIS millions
Profit from financing operations before provision for doubtful debt				
From outside operating segments	(131)	7	(124)	189
Inter-segment	341	(1)	340	(221)
Profit from financing operations before provision for doubtful debt	210	6	216	(32)
Operating and other revenues	114	32	146	33
Total income	324	38	362	1
Operating and other expenses				
From outside operating segments	153	14	167	28
Inter-segment	28	-	28	-
Total operating and other expenses	181	14	195	28
Pre-tax operating profit	143	24	167	(27)
Provision for taxes on operating profit	50	9	59	(13)
Operating profit after taxes	93	15	108	(14)
Share in net after-tax operating profits (losses) of affiliates	(1)	-	(1)	(4)
Net after-tax profit from extraordinary items	9	-	9	85
Net profit	**101**	**15**	**116**	**67**
Return on equity			**26.3%**	**14.7%**
Average balance of assets	18,955	-	18,955	21,482
Average balance of liabilities	23,082	-	23,082	11,306
Average balance of risk assets	8,681	-	8,681	6,828
Average balance of provident and mutual fund assets	45,472	-	45,472	66
Average balance of securities	-	6,790	6,790	-
Credit to the public (end balance)	-	-	-	
Deposits from the public (end balance)	15,494	-	15,494	
Average balance of other assets managed	-	-	-	74
Components of profit from financing operations before provision for doubtful debt:				
Margin from credit granting operations	-	-	-	-
Margin from receiving deposits	-	-	-	-
Other	210	6	216	(32)
Total profit from financing operations from outside of operating segments and inter-segment before provision for doubtful debt	**210**	**6**	**216**	**(32)**

(1) Reclassified.

Results presented for the financial management segment for 2007 are not comparable to results presented for 2006 due to changes in presentation of operating segments in line with restructuring of the Bank and the launch of a new measuring method using a dedicated system. The financial management segment is presented, starting with these financial statements, based on a computer system which assigns profitability to customers at the individual transaction level, including assigning the cost of sources under inter-segment profit from financing operations against the financial management segment.

The financial management segment previously also included results of international operations. In 2007, the segment presents operating results of trading rooms on financial and capital markets, as well as management of Bank assets and liabilities.

Marketing Operations

The Bank's marketing activities and its marketing strategy are derived from the Bank's strategic plan. The Bank's marketing channels, which form the basis of the strategic plan, include branches throughout Israel, business centers, professional departments at Bank headquarters as well as direct banking channels.

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:

- 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.
- Expansion of customer activities with the Bank, along with increase in average revenue per customer, focusing on mortgage customers (former Bank Tefahot), household customers, private banking customers and customers with potential future profitability, such as military staff and students.
- Maintain Group market share in mortgages, and maintain the Group's positioning as leader in this area.

In order to achieve these objectives of the marketing plan, the Bank operates based on the following principles and means:

- Intensive customer awareness and communicating the existing benefit in the combination of retail banking and mortgage banking to customers, 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 to customers.
- 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: Pension advisory service, investments, credit cards and mortgage.
- Offer innovative products and services based on customer needs, by applying professional analysis of needs and price-performance considerations with regard to the customer.

- To strengthen and set apart the Group's brand (Mizrahi-Tefahot), and to build an outstanding competitive position that stands apart, and is intended to give the Bank a leading position in the existing and future competitive environment. The brand-related activities include, *inter alia*, the use of mass communication, intended to create an image effect, to raise the public's awareness of the merged bank and to solidify the new position of the Bank and its values.
- Establish marketing strategy for major Group brands, primarily "Mizrahi-Tefahot" and "Tefahot", centered on the move to double-headed operations in the retail segment, in accordance with customer profile.
- 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 existing retail and business customers, increasing the percentage of customers using direct banking, formulating unique offers with value and developing a service policy that supports the positioning and needs of the customer.
- Development of appropriate infrastructure, in order to enable the required marketing activity, centered on approaching each customer with the suitable value proposition, at the right time, using the right channel and message for the customer. Development of the infrastructure will be carried out mainly through the development of educational tools, management and control tools, development of technological systems, expansion and improvement of online banking.
- Expand service availability for customers, by opening new branches, by adapting and adding activity areas to existing customers. The Bank also expands its direct distribution channels, aimed at enabling the customer to choose the contact time and channel convenient for the customer, combining a physical branch location and direct channels.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, financial markets and capital markets, public preferences, legislation, directives of regulatory entities, the behavior of competitors (including banking

corporations and non-banking competitors), aspects related to the Bank's image, technological development, developments in availability, purchase and rental prices of properties and issues of human resources.

Branch deployment

Group branches are primarily aimed at providing professional, high-quality service to customers 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 customer activities and offer to customers 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 created a combined nation-wide branch network which includes, as of the date of these financial statements, 126 business centers, branches and affiliates, including 10 Bank Adanim branches.

In 2007, efforts continued to make optimal use of the merged branch network, adapting the branches, their nature and location to the Bank's busines plan, based on a comprehensive review of branch deployment conducted by the Bank in 2005 - following which it set forth 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. Since the merger and through 2007, in conjunction with this plan, 21 mortgage points of sale were added, bringing the total to 66. In 2008 the Bank plans launching new points of sale, including 8 new commercial ones.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, customers' 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 issues of human resources.

Direct banking

In 2007, there was a continuation of the gradual, shift of some customer banking activities to direct banking channels (telephone, Internet and cellphones). 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.

The service provided through the Internet, as well as the Call Center, 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 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, cellular phones).
- To expand customers’ usage of the direct banking systems, in order to improve service.
- To develop the call center (“Mizrahi Direct”) as the major channel for diverting day-to-day activities in the branches.
- To use the direct banking system as a tool for building an advantage for the Bank and for attracting new preferred customers.

The direct banking services offered to the Bank’s customers are:

Telephone service - the Bank's call center. This may be used to transact most banking business. Mizrahi Direct makes it possible for its subscribers to also receive telephone services by voice mail, either by computer or a banker at the center;

Tefahot Direct - a center which allows customers to transact a range of mortgage-related transactions. These include: application for a housing loan, obtaining information on existing loans and making payments.

Web service - in the first half of 2007, the Bank launched a new website for obtaining information and transacting a wide range of banking transactions online, while improving system user interface and execution speed, while achieving high availability. The Bank intends to continue improving the user interface and expand the range of transactions available on the website in 2008.

Cellular Mizrahi – a system to distribute banking and financial information through cellular telephones, e-mail, fax and the Internet;

Mizrahi PC – a system parallel to "Mizrahi on the Internet", enabling direct connection to the Bank's computer, not through the Internet, and consequently – faster execution of transactions;

E-mail services – a system to distribute details on transactions executed in an account through e-mail, direct to the customer's e-mail address;

Service Stations – enable the receipt of information in the commercial and mortgages sectors and execution of a limited number of transactions in the account; in some branches it is possible to use the self-service equipment to deposit and issue checks;

ATMs – the Bank has 94 ATMs for cash withdrawals, some of which also enable the withdrawal of foreign currency (dollar, euro). In the first quarter of 2007, the Bank integrated 20 ATM's for the deposit of checks.

Fax service – makes it possible to receive current banking information on a variety of subjects, at the frequency specified by the customer.

Human Resources

Staff – general information

Provided below is information on the number of employees, in terms of full-time positions in the Bank and in subsidiaries. The number Bank workers provided below also includes employees who are not employed by the Bank but by companies related to the Bank, including employees of Mehish Computer Services Ltd. and Mizrahi Security Services Ltd. – service companies that provide computerization, security and protection services to the Bank:

2007	At the Bank	Overseas branches	Bank Total	Israeli subsidiary	Overseas subsidiary	Group Total
Number of full-time employees as of December 31, 2007 (1)(2)	3,956	64	4,023	177	27	4,227
Number of full-time employees (1) based on monthly average	3,777	64	3,841	173	23	4,037

2006	At the Bank	Overseas branches	Bank Total	Israeli subsidiary	Overseas subsidiary	Group Total
Number of full-time employees (1) at December 31, 2006 (3)	3,705	64	3,769	169	18	3,956
Number of full-time employees (1) based on monthly average (2)	3,607	64	3,671	163	18	3,852

(1) Includes impact of overtime.

(2) The number of full-time equivalent employees as of end of 2007 includes 30 positions for overtime exceeding the annual average.

(3) Restated.

Below is a breakdown of the number of jobs in the Group by operating segments (1):

	As of December 31	
	2007	2006
Household	2,298	1,668
Private banking	33	647
Small business	791	1,258
Commercial banking	250	126
Business banking	405	216
Financial management	299	41
International operations (2)	151	-
Total	4,227	3,956

(1) Includes Head Office employees that are allocated ratably over the various segments.

(2) First presented in 2007.

Human resources management

Bank management regards all Bank staff and managers as a primary foundation to achieving growth targets in operations and profitability. In 2007 the Human Resources and Training Division was re-organized, to better adapt it to the Bank's changing needs and the increasing competition in the banking system. 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 Human Resource Development and Training department, in conjunction with development of the Bank's human resources in all aspects.

Human Resources division - the division coordinates the planning of manpower needs, recruitment, absorption, preservation and promotion of employees, in accordance with the Bank's work plan, and manages the Bank's payroll and compensation systems.

As part of nurturing human resources, the division created an enterprise well-being department.

In recent years the Bank made a material change to its community relations area, such that Bank employees became partners in a diverse range of social involvement activities.

In 2007 this area came under the responsibility of the Human Resources division. For details, see the chapter on community involvement and charitable donation below.

Human resource development and training - the Bank invests in development of its human resources and in constant improvement of professional and personal skills of its staff and managers, by establishing promotion tracks and a range of enhancement programs offered by the Bank's training center.
The training center is in charge of establishing efficient and effective processes for employees, old and new, entering a new position, of professional and managerial training in accordance with needs of the various positions and of knowledge refreshing via workshops. Based on the training needs resulting from the gaps between knowledge necessary for an employee to perform his functions and the actual knowledge, the training center prepares a curriculum that covers the gaps in knowledge in the different banking subjects, managerial skills and in familiarity with Bank systems. Significant emphasis is placed on managerial training as part of the personal development of managers. In addition, the Bank encourages achievement and expansion of academic education of its employees, as well as broadening their horizons via external workshops.
In 2007, 3,400 Bank employees attended 14,500 training days at a cost of NIS 9.2 million.
The training budget for 2008 is NIS 8.9 million, based on a plan that calls for 12,250 training days to be delivered to 3,650 employees.

The plan to increase the number of employees trained while reducing the number of training days, takes into consideration improved efficiencies of the learning processes, given that each year sees an increase in the number of courses and training sessions delivered by eLearning (with no classroom training). In 2007 some 5,700 eLearning events took place (remote execution of learning tasks by employees) and another 8 courses and eLearning course-wares were developed, to be used for training in 2008.

Labor relations

The labor relations in the Bank are collective (except for a limited group of senior employees, as provided below, and employees of Bank Adanim (1)), which are expressed in two employee organizations:

A. **The Employees' Association of United Mizrahi Bank Ltd**. is a longstanding organization, which by virtue of the inter-organization agreement with the Histadrut Poalei Hamizrahi is empowered, by the said Histadrut, to act as the representative organization of the Bank's employees for the purpose of entering into collective agreements and representing the Bank's employees ("**Employees' Association**").

However, the Employee Association is empowered to declare a general strike at the Bank only for a period of time not exceeding 4 hours, or a strike at a majority of the Bank's branches for a period of time not exceeding 24 hours. For any longer strike, it requires the consent of the Histradrut Hapoalei Hamizrahi.

B. **The Council of Managers and Authorized Signatories of United Mizrahi Bank Ltd.** was established by the managers in 2005 ("Manager Council"). On September 19, 2005, a pact was signed between the Bank and the Manager Council ("the pact"), in which the Bank recognized the managers as a "collective bargaining unit" for the purpose of negotiations and signing of agreements. Under the terms of the special collective agreement dated April 11, 2006 between the Bank and the Employee Association, The Employee Association also recognized the separate representation for managers as a separate collective bargaining unit. See below for information on the agreements signed.

C. **Mehish' Employees' Committee –** The representative organization authorized to sign on behalf of Mehish employees on collective agreements applying to the Company's employees (except for Mehish employees employed under personal agreements).

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 wage agreement was signed for the years 2002-2004, which was in effect until December 31, 2004. This agreement applied to all of the Bank's employees except for those among them that on December 31, 2004 were former Bank Tefahot employees, which was merged with and into the Bank on January 1, 2005.

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

On December 21, 2005 and January 23, 2006, agreements were signed regarding the conversion of the salaries of those who had been employees of Tefahot to the salary method at Mizrahi, and imposition of the labor constitution on those employees ("salary conversion agreements").

For the years 2007-2005, a wage agreement has not yet been signed (except for those who were employees of Bank Tefahot, and for which a wage agreement was signed for the period through March 31, 2005).

Salary update method

The salaries of most of the Bank's employees (except for a limited number of employees employed under personal contracts that were signed between them and the Bank, see the chapter on personal employment agreements below) are updated, in addition to the cost of living updates in the economy, based on three main elements of the update:

A. The elements that are updated regularly at rates and in the manner prescribed from time to time, in negotiations on labor agreements (the main element of which is base salary), as well as other increments deriving from the base salary, namely seniority increment, which is updated at the start of every year at a rate that grows as the seniority of the employee gets higher, reaching up to 4% (of base salary) for every year of an employee with seniority in the Bank over 26 years of service;
B. Components updated based on the Consumer Price Index;
C. Elements that are linked to changes in non-bank tariffs.

All of the elements listed above 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 Employees' Association. The updating of part of the salary based on criteria that are not linked to the CPI, as well as granting automatic seniority increments, as above, create a situation in which the increase in the real salary in the Bank is higher as the inflation rate falls. In a reality of low single-digit, or even negative 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 ("long-service bonuses"). The Bank's financial statements include a provision for these obligations, according to an actuarial computation that is based on past experience and the probability that on the date of record, the employee will still be employed by the Bank.

There are also 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 advancement is generally based on rank promotion, with respect to which the Bank's Executive Management makes decisions annually, as well as a bonus element. Decisions relating to the extent of the personal advancement and bonus or grant are not derived from provisions of labor agreements, but are influenced by the individual assessment of the employee's performance and the condition of the Bank and its profitability in the relevant period.

Pension and benefit arrangements

A. Those who were employees of Mizrahi Bank on the eve of the merger are covered by the Bank's obligation to pay pension and severance pay through regular deposits in the employees' names to pension, benefit and severance pay funds. These deposits, as well as future amounts and a one-time amount deposited in the past, release the Bank from its obligation under the law to pay severance pay to those employees (see Note 16 to the financial statements for details).

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. The loan agreements stipulated that the loan amounts are linked to the CPI plus real interest at the rate stipulated. It was also stipulated that if it became clear, on the repayment date of all of these loans, that the linkage and interest differences on the loans during the loan period exceeds the yield in a certain provident fund agreed upon – the employee will not be charged an amount exceeding the loan amount revalued according to this yield. If necessary, the Bank makes suitable provisions for these differences between the interest on the said loan and the yield of the provident fund, and for the tax implications, if any, on the reduction in the loans. The balance of the loans given to employees in this framework stood at NIS 41 million on December 31, 2007.

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. In respect of its obligation until February 1, 2006, the bank paid all the amounts required to cover the obligation, through a deposit in pension and provident funds (see Note 16 to the financial statements for details).

   See Note 16.J-H to the financial statements for information on the special obligations 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"). This agreement stipulated that the provisions of the special collective bargaining agreement would be in effect until December 31, 2010 ("term of the special collective bargaining agreement"). 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 special collective agreement prescribed a mechanism for integrating the Bank's employees in their new positions within the scope of the merger, and the Bank has undertaken that throughout the special collective loan period it will not take any dismissal measures against permanent employees of the Bank because of financial needs. However, the Bank may terminate permanent employees due to regulatory needs or disciplinary problems ("individual termination"). The parties also agreed that during the term of the special collective bargaining agreement, the Bank could terminate up to 50 permanent employees due to incompatibility, in accordance with the special collective bargaining agreement. Moreover, the parties agreed on a voluntary retirement plan for up to 200 employees during the term of the collective bargaining agreement, all as provided in the special collective bargaining agreement.

In 2006 the Bank made a provision of NIS 208 million, based on management estimates of the cost of the voluntary retirement program.

It was also stipulated that contrary to the situation that prevailed before the agreement, the Bank's employees will be able to choose whether or not to belong to the Employees' Association (it is clarified 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 special 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 new collective bargaining unit for managers, as defined therein, alongside the collective bargining unit for all Bank employees (regarding the agreement between the Manager Council and the Bank, see below).

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

A. On April 10, 2006, the Managers' Council and the Bank signed a special collective agreement ("the agreement"), in which the Bank and the Managers' Council ratified the pact (which together with the agreement, and previous agreements between the parties shall be called in this paragraph – "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.

B. By virtue of the pact and the collective agreement to ratify the pact signed between the Bank and the Managers Council (see below), the collective agreements signed between the Bank and the Employees 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 Managers Council from September 19, 2005 and thereafter.

C. In December 2005, an agreement was signed between the Bank and the Managers Council regarding the conversion of the salary of those who had been managers in Bank Tefahot and had become managers in the Bank, to the salary method practiced in the Bank, while retaining the value of their terms.

D. 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 set forth 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 set forth in the employee retirement program.

Pension and benefit arrangements

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

B. Managers who were employees of Bank Tefahot on the eve of the 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 obligation until January 1, 2006, the Bank paid all the amounts necessary to cover these debt through deposits with pension and provident funds.

Employment terms for Mehish employees

The employment terms for employees of Mehish are arranged in the labor constitution that was signed in 1989 and in a series of agreements signed between the Employees Council of Mehish and the Company over the years, the key points of which are provided below:

A. Salary updates for Mehish 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, Mehish 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 Mehish employees.

B. The labor constitution prescribes the maximum quota for contracted employees, pursuant to the undertaking between Mehish and outside vendors, which make workers available to Mehish, and under the professional management of Mehish. In this connection, it should be noted that disputes have arisen in the past between the Company's management and the Employees Council regarding the quota of contracted employees and the outsourcing of projects. On December 29, 2003, a labor dispute was announced in the company. On March 31, 2004, the parties signed an agreement to end the labor dispute, in which certain conditions were stipulated with regard to the company'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 Mehish 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 in the name of the employees to pension, provident 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 Mehish and the Employees Council which contains a voluntary retirement plan. 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 Mehish.
In 2006 the Bank made a provision of NIS 25 million, based on management estimates of the cost of the voluntary retirement program.

E. On March 8, 2007, the Employee Association, Manager Council, Mehish Workers 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 Mehish. 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 Mehish. Pursuant to this agreement, the collective bargaining agreements applicable to Mehish employees, including the infrastructure agreement in Mehish from 1989, as well as any new collective bargaining agreement to be signed, will apply to the Tefahot employees who have been integrated.

Stock Options

On February 27, 2005, the Bank's board of directors resolved to adopt an option plan for employees and officers of the Bank and its subsidiaries, pursuant to which will be allotted 12,000,000 options, exercisable for 12,000,000 ordinary shares, NIS 0.1 par value each, of the Bank. The options were allocated on a differential basis, in accordance to a "quality ranking", by which each manager was evaluated. See Note 16.A.2 to the financial statements for details.

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 personal employment contracts with senior employees, as defined in the agreements, and several personal employment contracts with certain officials. 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 full provisions for the severance bonuses accrued through the balance sheet date. See Note 16.E-G to the financial statements.

See below regarding information on the employment terms of the Chairman of the Board of Directors and President of the Bank.

Labor relations at Bank Adanim

Labor relations at Bank Adanim are based on a set of procedures that summarize the rights and obligations of Bank Adanim employees, as approved by the Bank Adanim Board of Directors. The salary and compensation system is based on the employee's position, function and contribution to the activities of Bank Adanim. Since 2007, Bank Adanim has started using individual employment contracts signed by new employees.

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. The division includes the retail sector, which is responsible mainly for the activity of the household segment and the small business segment; the mortgage sector, which is responsible for the activities of the mortgage segment; and the direct banking sector, which is responsible for distribution through the different direct banking channels; and the private banking sector, which is responsible for private banking operations with select customers, and which was placed under responsibility of the division during 2007. The Bank's branches and business centers operate in this division, in six geographic regions and a direct banking region, which also includes the call centers.

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. The division also includes other units providing specialized services for customers in specific sectors: the construction and real estate sector, the international finance and trade sector, the special customers and settlement sector and the diamonds business center.

Financial Division – This division includes the financial management sector, which is responsible for management of the Bank’s financial assets and liabilities, as well as the international operations sector, which is responsible for international operations, *inter alia*, via overseas affiliates and subsidiaries. The division includes the financial and 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 & Customer Service Sector which supports all financial market operations, providing back-office services.

Customer Asset Management & Technology Division - the division includes the provident fund sector and the departments in charge of the pension advisory service and financial advisory service offered to customers. 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 Issue Company (1980) Ltd., and Mizrahi-Tefahot Trust Company Ltd. The division is also in charge of information technology, including pursuant to requirements of Proper Banking Conduct Regulation 357, via Mehish Computer Services Ltd., a wholly-owned subsidiary of the Bank.

Comptrollership, Planning & Operations Division - This division consolidates control over all the different risk elements of the Bank; the Process Engineering division, in charge, *inter alia*, of back-office banking operations and the Planning & Economics Division,, in charge of supervision and control of subsidiaries. The division is also responsible for banking insurance (including: banking insurance as well as officer and director insurance), insurance incidental to mortgages and information security at the Bank, as required under Proper Banking Conduct Regulation 357.

Human Resources and Administration Division – This division consolidates the management of human resources, training, logistics, administration and efficiency (includes properties and construction), protection and security.

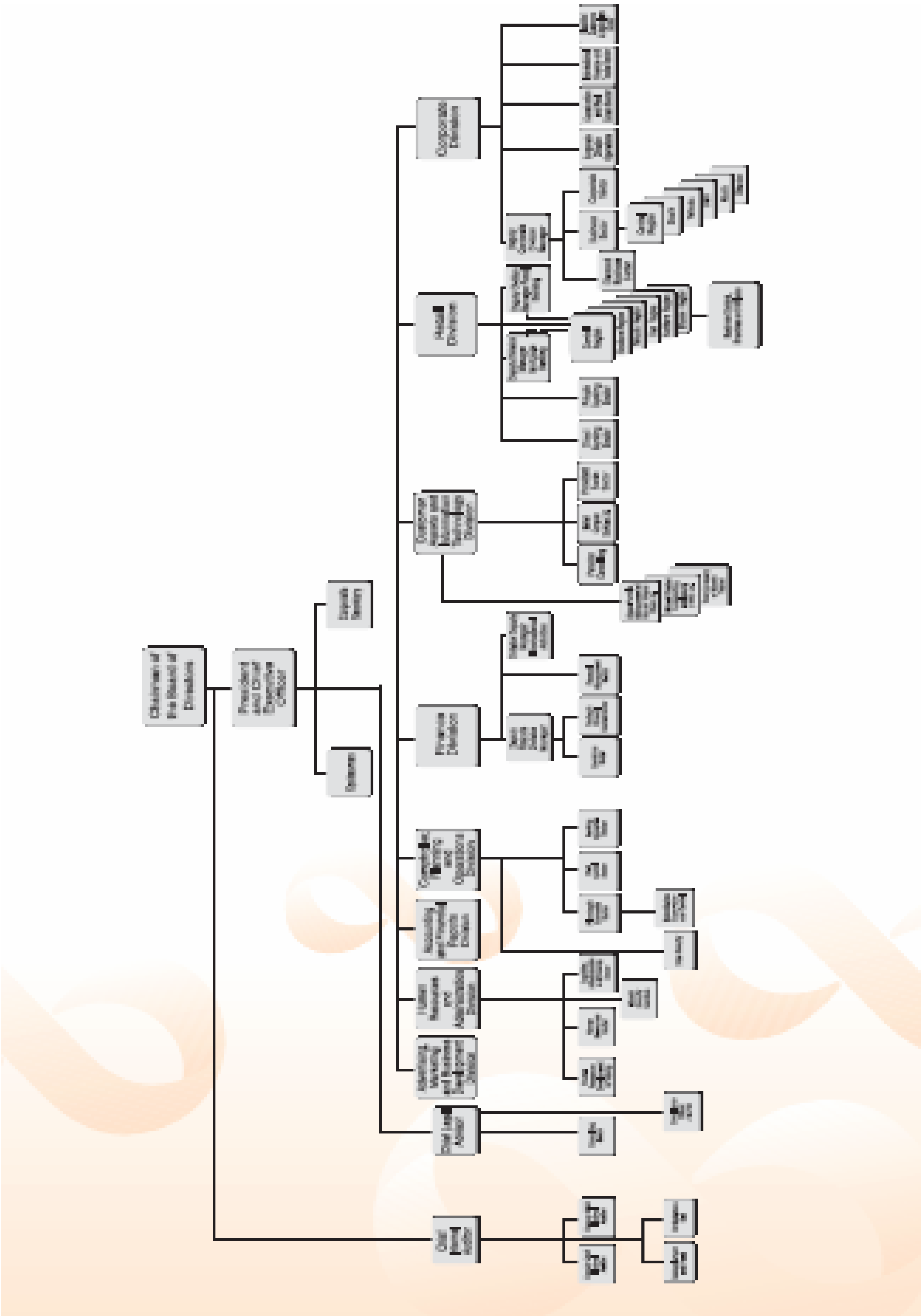
Marketing, Advertising and Business Development Division – This division consolidates activities relating to advertising, marketing, and development of financial products and other services which the Bank markets to customers.

Accounting & Financial Reporting Division - in charge of compiling the Bank's public financial statements, reporting to statutory authorities and to management, taxation, implementation of Sarbanes-Oxley at the Bank, main ledger, accounting and treasury.

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 (including the compliance officer who was also appointed for the money laundering prohibition) and to handle claims against the Bank.

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

Bank organizational chart



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. For details of the amendment to the Inflationary Adjustment Act, see below in this chapter.

Corporate tax and profit tax

The overall tax rate for corporate tax and profit tax applicable to the Bank's income is expected to decrease in the coming years, as follows:

Year	Total tax (corporate tax and profit tax in %)
2007	38.53%
2008	36.80%
2009	35.93%
2010 and later	35.06%

Profit tax accounts for 15.5% of salary expenses paid by the Bank, including the amounts that represent social provisions. Payroll tax constitutes an expense for the purpose of calculating corporate tax, but is not recognized, until 2007, as an expense in calculating profit tax.

Tax assessments

The Bank has finalized tax assessments for the tax years through 2003, inclusive. The former Bank Tefahot has tax assessments that are finalized or deemed finalized through 2004. Bank Adanim has finalized tax assessments through 2006.

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 set forth in the tax authority approval over a 10 year term, starting in 2004.

- Tax authorities approved in August 2007 the merger, as of December 31, 2006, of Mashabim Issuance Company Ltd. into Netzivim Properties and Equipment Ltd., pursuant to provisions of section 103a of the Income Tax Ordinance.

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 a dividend distribution to the Bank is exempt from tax in Israel.
- Arrangement for implementing the recommendations of the Givoli Committee regarding the reversal of provisions for doubtful debt – According to this arrangement, when the Bank reverses provisions for doubtful debt that it had recorded in its books during the five years preceding the reversal, the Bank is taxed as though the provisions had never been made, plus 50% of the interest stipulated in the Income Tax Ordinance, from the date the provision was made until the date of reversal.

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 explained below.

Amendments to the Income Tax Act (Adjustments for Inflation) and to the Value Added Tax Act

On February 26, 2008, the Tax Act (Adjustments for Inflation) (Amendment no. 20) (Restriction of Applicable Period), 2008 was enacted ("the amendment"), whereby the Inflationary Adjustment Act would be rescinded in the 2007 tax year, and starting in the 2008 tax year, provisions of the Act shall no longer apply, other than interim provisions aimed at avoiding distortions in tax calculations. The amendment also made changes to the VAT Act which impact calculation of the profit tax and payroll tax paid by financial institutions.

The impact of discontinuation of the Inflationary Adjustments Act, as of December 31, 2007, is estimated at lowering net profit by NIS 15 million for each 1% in annual rise of the CPI.

Amendments to the VAT Act, based on salary expenses in 2007, are expected to increase the Bank's net profit by NIS 5 million in 2008, and by NIS 10 million in 2009 and later. For details, see Note 28.D. to the financial statements.

Legislation and Regulation of Bank Group Operations

The Law for Arrangement of Engagement in Investment Consultancy, Investment Marketing and Management of Portfolios – 1995 ("Consultancy Law")

The Consultancy Law prescribes the rules for engaging in investment consultancy, in marketing investments and in managing investment portfolios, and arranges, *inter alia*, the engagement of banking corporations in investment consultancy. The Consultancy Law defined and prescribed the obligations of trust and prudence of investment consultants toward their customers, as well as the obligation of proper disclosure of significant matters for the consultation given and the transactions proposed by the consultants, the obligation of confidentiality toward the customers and the obligation to compile a consultancy agreement. Furthermore, the Law prohibits acting under conflicts of interest or receiving any benefits in association with investment consultancy, other than wages and expense reimbursement, from the customer.

The Law also empowers the Securities Authority to oversee investment consultants, including banking corporations, and to impose civil financial penalties on them when they do not fulfill the Law's requirements.

The Law also specifies what financial assets and securities are subject to it. It was further stipulated that violation of the provisions of the Law, which constitutes a disciplinary violation, will also apply to banking corporations and not only to consultants that they employ. A similar provision was stipulated for the violation of the Law's provisions for which legal liability applies.

Other material amendments were made to the Consultancy Law following the Bachar Reform. See Note 19.D.22) to the financial statements for further information.

Prohibition on Money Laundering Law, 2000 ("Prohibition on Money Laundering Law")

The Prohibition on Money Laundering Law prohibits, *inter alia*, certain actions defined in the law, in assets that originate, directly or indirectly, in a crime, in property used to perpetrate a crime or property that enabled the perpetration of a crime.

In February 2002, the Money Laundering Prohibition Ordinance (Obligations Concerning Identification, Reporting and Record Keeping by Banking Corporations), 2001 (“the ordinance”) became effective. The Ordinance was issued by the Bank of Israel

Supervisor, with approval of the Knesset's Constitution, Statute and Justice Committee, by his authority as set forth in the Money Laundering Prohibition Ordinance. The ordinance stipulates, *inter alia*, identification, verification, reporting and record-keeping requirements imposed on banking corporations and auxiliary corporations, as defined by law. Concurrent with the issuance of the Ordinance, limiting Ordinances were issued that imposed similar requirements on providers of financial services other than banks. The provisions of the Law and the said Ordinance, supplement the amendment to the provisions of Proper Conduct of Banking Business Regulations No. 411 on preventing money laundering and the financing of terror, on the identification of customers and record-keeping. This ordinance contains complementary instructions and further obligations for preventing money laundering and terrorism, primarily concerning "know the customer", account monitoring, definition of high-risk customers, correspondent banking etc.

On December 12, 2006, the Ordinance was materially amended, partially effective upon publication and partially to become effective gradually by February 12, 2008. These amendments set forth, *inter alia*, easements for identification and authentication of Israeli couriers and incidental customers, the added obligation to check customers and parties to transactions against lists of terror organizations and activists, and extended obligation to report activities in accounts on that list. The Supervisor of Banks was also authorized to specify special means of authentication, minor amendments were added concerning beneficiary declarations and opening correspondent accounts, and a section was added on obligation to identify by credit card companies. Furthermore, the reporting threshold for transactions vis-à-vis countries and territories included on the high-risk country list was lowered to NIS 5,000.

During 2007, the Supervisor of Banks issued further clarifications with regard to implementation of the Ordinance. The Bank is prepared and applies the amended provisions of the Ordinance, *inter alia* based on clarifications of the Supervisor of Banks.

On January 15, 2008, amendments were published to Proper Banking Conduct Regulation No. 411, which allow the Supervisor of Banks to impose financial sanctions on a banking corporation for being in breach of said regulation.

See the Chapter on Risk Management for information on the official responsible for fulfilling the Bank's obligations in accordance with the Prohibition on Money Laundering Law and the provisions of Proper Conduct of Banking Business Regulations No. 411, and the Bank's actions to apply the regulations.

Credit Data Service Law, 2002 ("Credit Data Law")

The Credit Data Law took effect in August 2004. The Law constitutes the legal infrastructure for operating a credit-data service and a data service about dealers (who sell an asset or provide service through engagement, including a producer), by licensed parties. The services include the gathering, administration and maintenance of various data, as detailed in the Credit Data Law, for the purpose of providing it to another party.

The Credit Data Law stipulates, *inter alia*, that the holder of a credit-data service provider license is permitted to gather information on a customer, even without the customer's consent (such as information on the non-payment of debt by a customer). Among the sources for providing such information are banks and credit card issuers. Under the Credit Data Law, credit providers approved Credit Data Service Regulations, 2004, were approved, with the purpose of prescribing the arrangements necessary to implement the provisions of the Credit Data Law. The regulations prescribe, *inter alia*, the manner in which the data is to be transferred from banking corporations to license-holders, their content and the payments to be paid to the banking corporations for delivering the information to the license-holders.

Amendment 3 to the Law, enacted on July 25, 2007, waives the instruction requiring an "authorized source", as defined by the Law, not to transfer information regarding customer debt to any holder of credit data service provider license before 90 days or more have elapsed since the due repayment date of the unpaid debt. Furthermore, multiple restrictions on providing information in the credit report by a credit data service license holder were eliminated.

The amendment further stipulates that when an information source becomes aware of an error in the information they have provided to the license holder, the information source should inform any license holder to whom they have previously provided information about the customer of the error, correction or change, and the license holder shall have to amend the information, inform the customer, and provide an amended report to anyone who received a report on said customer from them within the preceding six months. The law also specified several amendments on imposing financial sanctions by the credit data service registrar on anyone acting in contradiction to provisions of the law.

Subject to publication of appropriate regulations, the amendment will become effective 9 months after publication. The Bank provides information to a credit data service license holder pursuant to provisions of the law, and is preparing to apply provisions of Amendment 3 as set forth above.

Prohibition on Financing Terrorism Law, 2005 ("Terrorism Financing Prohibition Law")

In January 2005, the Prohibition on Financing Terrorism Law, 2005, was published, stipulating the offenses related to the financing of terrorist acts and organizations. The Terrorism Financing Prohibition Law prohibits, *inter alia*, executing transactions in property with the objective of promoting, enabling, or financing terror activities. Within the framework of this law, amendments were also made to the Prohibition on Money Laundering Law, which were intended to make the struggle against money laundering and against the financing of terrorism more effective.

In February 2005, the Proper Conduct of Banking Business Regulations No. 411 was amended, which to that date included provisions associated with the Money Laundering Prohibition Law, so as to impose various duties on banking corporations in conjunction with the Terrorism Financing Prohibition Law. Furthermore, the Supervisor of Banks issued several circulars concerning reporting of activity in accounts of customer suspected of terrorism, proclamation of terror organizations and illegal associations etc.
Legislation of the law and amendment of the regulation place fighting against money laundering and against terrorism financing on equal footing.

Holocaust Victim Assets Law (Restitution to Heirs and Dedication to Assistance and Commemoration), 2006

On January 3, 2006, the Holocaust Victim Assets Law (Restitution to Heirs and Dedication to Assistance and Commemoration), 2006, was published. The objective of the Law is to increase activity for identification of assets located in Israel, for which there is a basis to assume their owners perished in the Holocaust. Within the scope of this law, a government company was established, to work toward identification of such assets, will become its property and will be transferred to those holding rights therein, if located. In accordance with the Law's provisions, any person holding or managing the asset of a Holocaust victim must file a report with the government company within 30 days of the date the company publishes an announcement thereon, or from the date he became aware that the asset is in his possession.
For details on the company’s appeal to the Bank, see under Legal Proceedings chapter.

Securities Act (Amendment 32), 2007

The Securities Act, 1968 prohibits use of inside information regarding company securities. The amendment to said Act, enacted on May 15, 2007, expands the prohibition to also cover derivative financial instruments.

The Act sets a penalty of fine or 5 years' imprisonment for any offense concerning use of inside information and fraud in derivative financial instruments by any inside person within a company.

Furthermore, the provisions of section 52e were extended also to use of inside information for company securities. These provisions stipulate that when a key company insider acquired or sold securities or options within three months from the date on which securities were acquired or sold by the company, they would be deemed to have used inside information.

Banking Act (Customer Service) (Amendment 12), 2007

On June 26, 2007, the amendment to the Banking Act (Customer Service) (Amendment 12), 2007 was enacted. The amendment is aimed at increasing competition among banks, and sets forth arrangements concerning supervision of commission prices and increased transparency of banking service prices, such that customers may practically compare prices of banking services.

For details on the amendment to the Act and its impact on Bank operating results, see Note 19.D.15) to the financial statements.

Payment System Act, 2008

On February 3, 2008, the Payment System Act, 2008 was ratified. Following recommendations of the International Monetary Fund and the World Bank, which set international standards for payment systems, the Bank of Israel Governor decided, in December 2002, on a reform of the payment system in Israel so as to have domestic payment systems comply with said standards. In conjunction with this reform, a new system was mandated for payment and clearing of Israeli currency, with banks as participants, to large payments in real time (Real Time Gross Settlement - RTGS). In August 2007 the Bank of Israel launched the RTGS system. This system allows customers to transfer in real time NIS-denominated amounts between bank accounts in the same bank or between banks. Settlement is immediate and final.

The Act is aimed at setting regulations required to minimize risk involved with transfer of such real time payments, and to confer legal certainty in order to ensure the payment systems' stability. The Act applies to payment system operators' obligations aimed at ensuring the stability and proper functioning of such systems in order to reduce the system risk which may arise from their improper operation. In view of the importance of the payment systems, they were placed under Bank of Israel control, and the Bank of Israel Governor would be appropriately authorized, *inter alia*, to instruct the system operator and to obtain information. Furthermore, the Bank of Israel would be authorized to provide, against collateral, intra-day credit to participants in said system, in order to secure efficient functioning of the system.

Arrangements in the State Economy (Amended Legislation to Achieve Budgetary Targets and Economic Policies in Fiscal Year 2008), 2008

The Arrangements Act, published on January 1, 2008, includes, *inter alia*, an amendment to the Financial Services Supervision Law (Engagement in Pension Consulting and Marketing), 2005. The amendment stipulates that banking corporations whose shareholders' equity does not exceed NIS 10 billion, would be permitted, starting January 1, 2009, and subject to obtaining an appropriate license from the Supervisor of Capital Market, Insurance and Savings in the Ministry of Finance, to consult, in conjunction with pension consulting services they provide, also on pension products with an insurance component, including: Pension insurance, life insurance with a savings component and disability insurance – provided it is part of a pension insurance or life insurance policy. Banking corporations whose shareholders' equity is higher than NIS 10 billion would be allowed to provide pension consulting, including on insurance-related pension products, at later dates.

The Bank acts in the field of pension consultancy in accordance with a license from the Supervisor of Capital Market, Insurance and Savings. For details of possible impact of the amendment to the Act on consultancy operations, see the chapter Anticipated Developments.

Financial Services Supervision Law (Provident Funds) (Amendment 3), 2008

The amendment enacted on January 23, 2008 includes amendments to the Financial Services Supervision Law (Provident Funds) and complementary amendments to the Financial Services Supervision Law (Insurance) and to the Financial Services Supervision Law (Engagement in Pension Consulting and Marketing).

The amendment objective is to divert pension savings to a minimum pension track and to postpone the decision on how funds are withdrawn (as lump sum or pension) to retirement age.

Therefore, a minimum amount was specified, out of funds accumulated by the member, which may only be withdrawn as monthly pension payments upon retirement. Over and above said amount, the member may choose to withdraw the balance as a lump sum or to increase the monthly pension payment over the set minimum.

All provident fund licenses granted to date by the Supervisor of Capital Market, Insurance and Savings in the Ministry of Finance to capital-based provident fund shall remain valid, and there would be no changes to rules applicable to amounts deposited through 2007. However, starting on January 1, 2008 funds would be deposited to a “non pension paying provident fund”, and may only be withdrawn upon retirement by transfer to a “pension paying provident fund” in order to receive monthly payments of no less than the minimum pension set by law. These restrictions shall not apply to severance pay.

The amendment to the law eliminates central severance pay provident funds registered on behalf of the employer. However, active funds which received employer deposits in December 2007 would be allowed to continue receiving deposits through 2010, but only for employees for whom deposits were made in December 2007.

The amendment also increases the deductible rate for purchase of disability insurance and sets the same tax benefits for comprehensive-pension plans and non-comprehensive-pension plans.

For details of pension arrangements of Group employees, see the Human Resources chapter.

Extension Ordinance for Comprehensive Pension Insurance

On December 30, 2007 the Extension Ordinance for Comprehensive Pension Insurance was published, to be effective starting January 1, 2008. The Ordinance stipulates that employers are required to provide appropriate amounts for pension insurance for employees with 9 months of service or more, subject to terms set forth in the Ordinance.

Provisions of the ordinance stipulate that pension provisions replace severance pay in accordance with provision rates. Provisions would be at 2.5% of salary in the first year, of which 1.667% by the employer and 0.833% by the employee, and would be updated as per provisions of the Ordinance.

The Bank is in compliance with provisions of the Ordinance. For details of pension arrangements of Group employees, see the Human Resources chapter.

Tax Act (Adjustments for Inflation) (Amendment no. 20) (Restriction of Applicable Period), 2008

For information on the amendment to the Adjustment Act ratified on February 26, 2008, and on Bank estimated impact of application of the Act on bank profits in 2008 and later, see Note 28.D to the financial statements.

Proper Conduct of Banking Business Regulation No. 325

The Regulation deals with the prohibition on exceeding approved credit facilities in current accounts and debitory accounts (together – "current account") except in exceptional cases, as provided in the Regulation, and with anchoring the credit facilities in the current account in an agreement between the bank and the customer. The bank is required, *inter alia*, to have all customers to whom the bank is willing to enable a debit balance in their current account, to sign a facility agreement with respect to the credit facility in their account.

Most of the provisions in the regulation became effective in 2006. Commencing January 1, 2007, the above Regulation also applies to foreign currency accounts. Through July 1, 2007, the Bank was allowed to provide a credit facility unilaterally to customer who had no facility agreement in place.

The Bank acts, with regard to credit facilities, in compliance with the regulation and based on credit facilities adapted to customer needs.

The impact of application of this regulation on Bank operating results is not material.

Measuring and disclosure of impaired debt, credit risk and provision for credit loss

On December 31, 2007, the Supervisor of Banks published his directive in a circular concerning: “Measuring and disclosure of impaired debt, credit risk and provision for credit loss (“the regulation”). This directive is based, *inter alia*, on USA Accounting Standards 5, 114 and 118 as well as on regulatory directives by banking supervision bodies and by the USA Securities and Exchange Commission. The guiding principles on which the directive is based introduce a material change over current directives on classification of problem debt and measuring of provisions for credit losses in conjunction with such debt.

The directive requires the banking corporation to make appropriate provision for credit loss in order to cover anticipated credit loss arising from its credit portfolio, including provision for anticipated credit loss associated with off-balance-sheet credit instruments.

As instructed by the Supervisor, this directive will be applied in financial statements of banking corporations starting on January 1, 2010, with no retroactive application to financial statements for previous periods.

In preparation for application of the directive, as of the publication date of these financial statements, the bank has completed specification of the processes and computer systems required for applying the directive, and has started the process to select a software vendor to make required development and changes to systems. At this stage in preparation for application of the directives, it is not possible to estimate the impact of application of the directives on the Bank's shareholders' equity, since the models for calculating provisions for credit losses have yet to be finalized. Completion of the methodology and initial estimated of impact of said application are anticipated in mid-2008. For details, see Note 1.X. to the financial statements.

Public Reporting Regulation 645 ("Sarbanes Oxley Act 302")

In accordance with Public Reporting Regulation 645, published in November 2004 and amended in May 2007, which is based on Section 302 of the American Sarbanes Oxley Act ("SOX Act"), beginning from the financial statements published as of June 30, 2005, the President and the Chief Accountant of the Bank have each separately signed a Certification attached to the financial statements on the effectiveness of "Disclosure Controls and Procedures".

Sarbanes Oxley Act 404

In a circular dated December 5, 2005, the Supervisor of Banks instructed that banking corporations will implement the requirements of Section 404 of the Sarbanes Oxley Act, as well as the SEC regulation promulgated there under. These guidelines prescribe, *inter alia*, that the corporation's management will declare its responsibility for setting up and maintaining a system of proper internal controls on financial reporting, and will give an assessment, as of the end of the corporation's last fiscal year, of the effectiveness of the corporation's internal control system and procedures for financial reporting. Implementation of the Supervisor's demands requires a thorough examination of the infrastructure systems for internal controls in banking corporations, and the upgrade and/or building of such a system in accordance with the findings of the examination. The Supervisor's instructions prescribe that management's certification of its responsibility for control and its assessment of the control system will be provided initially for the financial statements as of December 31, 2008.

Upon publication of the Regulation, the Bank began preparations for its implementation, with the assistance of an outside consultant. As part of the preparations, the Bank acquired a specialized computer system for management of controls during the first quarter of 2007. As of the publication date of these financial statements, the Bank is in advanced preparation stage for application of this regulation.

Other regulations

In addition, banking corporations are required to file immediate reports with the Supervisor (*inter alia*, on 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 accountant, ratio of capital to elements of risk, etc.).

Details of other legislation, including directives of the Supervisor of Banks, whose impact is mainly focused on operations of an individual operating segment, are presented under the Legislation section which is part of the operating segment’s description in the chapter on Description of Bank Group Business by Operating Segments.

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

General

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 regulations is intended to improve measuring and management of different risk factors facing the financial institution, and to ensure 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 set forth below.

The first layer of Basel II includes minimum capital allocation due to market risk and credit risk, as well as due to operating risk (capital allocation not required by Basel I). The new guidelines improve capital allocation for credit risk by enabling calculation of the minimum capital using a standard model, essentially similar to that of Basel I, but relying on external debt rating by rating agencies recognized by the regulator, used a larger number of exposure groups while adapting risk coefficients to the various groups, and recognizes other financial collateral which may be offset against the exposure. The regulations also 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 regulating authority (in Israel: The Bank of Israel), which may only be granted after extensive validation of the model. Furthermore, the first layer recognizes more extensive credit reduction methods (CRM) compared to those supported by Basel I.

In order to use the advanced models, banks are required to build a two-dimensional credit rating system (probability of default – PD and percentage of loss given default – LGD), based on processes of quantification and validity of the calculations. As part of the process, the bank is required to choose the rating philosophy: a rating system with the range of a point in time, which calculates on in the economic situation prevailing at the present time, or a rating system that has a cyclical reference, which takes a full business cycle into account. Additionally, the bank is required to build a control and management mechanism for the process of issuing credit and managing risk. This mechanism must meet the standards of independence, transparency, responsibility and professionalism by those engaged in the rating, the control and audit and responsibility of management and the board of directors

In the area of operational risk, the guidelines propose three alternative approaches for computing 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 profit; 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 (SRP) 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 regulations 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, internal capital allocation, specification of authority etc.

In addition, the second layer is aimed at 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 over time. Therefore, stress tests are an important tool in estimating the capital required of banks, and these feature prominently in the second layer of the regulation.

The third layer of Basel II regulation involves reporting and disclosure to the regulating authority and to the public. This requires the financial institution to disclose its risk level and its risk management processes. This requires more extensive, detailed and intensive disclosure, compared to previous regulations.

Application of the Basel Committee recommendations by the Israeli banking system

Application of the Basel II principles in Israel has started, and the Supervisor of Banks announced his intention of applying Basel II provisions starting in 2009.

In early July 2007, the Bank of Israel published a translated draft of the Basel II Committee recommendations. Furthermore, the Bank of Israel established teams to formulate requirements vis-à-vis banking corporations. Work of these teams was accompanied by publication of a range of guiding documents which specify, in detail, the desired manner of implementation of the Basel Committee recommendations by Israeli banking corporations. The Bank of Israel instructed the banking groups to act to apply the Basel Committee recommendations, including layers 2 and 3, subject to a comprehensive multi-annual work plan which would refer to all aspects impacted by application of the recommendations, based on results of meticulous and detailed results of gap analysis reviews.

In August 2007, the Supervisor of Banks mandated that a "quantitative impact review" be carried out, in which banks were required to review and calculate the impact of applying the standard approach to calculation of minimum capital according to Basel II provisions on the required capital allocation for each bank.

The Supervisor of Banks also instructed, in a temporary directive dated December 2007, that several instructions relating to disclosure in financial statements be applied, which are application of part of the Basel II layer 3, based on information available to the bank prior to application of the Basel II recommendations.

Bank preparation for applying the recommendations

Bank Mizrahi-Tefahot started preparations for application of the Basel II instructions prior to publication of the Bank of Israel instructions on this matter. The Bank sees application of the regulation as a challenge, due to the importance it attached to risk management processes, risk control and corporate governance in the Bank Group. Furthermore, the Basel II regulation recognizes the fact that retail and mortgage business, which are primary lines of business in Bank operations, are exposed to relatively low risk, hence capital requirements for these operations are lower compared to capital requirements under Basel I.

The Bank launched its Basel II project in 2006, established a steering committee headed by a Bank executive, established the required teams and started mapping gaps and technology required for application of this regulation. The project is conducted at Group level, based on a detailed work plan which includes all regulation components.
The Bank Board of Directors has approved the multi-annual work plan prepared for compliance in full with the Basel Committee regulations. Based on this plan, a large-scale project is under way at the Bank, with participants from all divisions and departments and with assistance from external consultants in order to apply the standard approach and to put in place the advanced models. The work plan also includes a dedicated chapter on operating risk management, as per Basel II requirements, and as is customary for leading banks around the world.

As of December 31, 2007, the Bank Group is in advanced application stages of the regulation, and has started entering data required for capital calculation as per Basel II requirements, into the “Algorithmics” system, selected to be the Bank’s integrative risk management system for management of market risk, assets and liabilities, credit risk, liquidity management and capital calculations in accordance with Basel II. The Group has completed capital calculations using the standard model which were required of Bank Adanim.

The Bank has started preparing for application of layers 2 and 3 of the regulation, as per instructions on this matter from the Bank of Israel. As of December 31, 2007, the Bank has completed several gap reviews associated with level 2 of the regulation, some of which were conducted by renowned overseas consultants: liquidity risk, credit risk and interest risk in the banking portfolio. The remaining required reviews are expected to be completed by end of the first quarter of 2008. The Bank has started processing gaps arising from the completed reviews.

In addition, the Bank has completed the gap review concerning operating risk, and has started processing the gaps in accordance with a detailed work plan approved by its Board of Directors. The Bank has established a supporting organizational structure for treating operating risk, and is in advanced stages of upgrading Bank policy for treating operating risk. The Bank has completed operating risk reviews throughout the Group, as part of the methodology to identify operating risk, as is customary for leading banks around the world.

For further information on Bank preparations for application of Basel II regulations, see the Risk Management chapter.

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. As of the date of the financial statements, there are several bills in various stages of legislation, including bills regarding interest on credit balances in current accounts and regarding commissions collected by the banks. These bills were intended to increase the supervision and arrangement of bank-customer relations, especially customers from the household segment, principally limiting the ability to increase commissions, limiting the total commissions income, prohibition on collecting commissions on certain services, etc. 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.

Significant Agreements

A. Agreements for sale of provident fund operations and agreements on operation and distribution, as the case may be, signed following the sale of fund operations. See Note 6.E.2) to the financial statements for information.

B. Deed of trust dated November 16, 2006 in connection with the complex capital notes that were issued. Pursuant to the deed of trust, the Bank may, without requiring consent of the trustee and/or capital note holders, issue additional capital notes in the same series up to NIS 2 billion par value, subject to Bank of Israel approval. The Bank may also issue other series of subordinated notes and/or debentures and/or subordinated capital notes and/or other obligatory notes to be ranked higher or lower or equal to the subordinated capital notes. See Note 11 to the financial statements for details.

C. Employment agreements signed with the Employee Council, the Manager and Authorized Signatory Association, and the Mehish Employee Committee. For details, see the Human Resources chapter above.

D. Letters of indemnification. See Note 19.D.6) through 19.D.11) to the financial statements for details.

E. Agreement to acquire 50% of issued capital of Bank Yahav for Government Employees Ltd. ("Bank Yahav") inclusive of all rights associated therewith. See Note 6.E.4) to the financial statements for information.

F. Memorandum of Understandings with Isracard Ltd. and Europay (Eurocard) Ltd. on formulating a new agreement for issuance of Bank branded credit cards and allocation to the Bank of 3.6% of shares of these companies. See Note 6.E.5) to the financial statements for information.

Legal Proceedings

See Note 19.D.12) and 13) to the financial statements for material legal proceedings to which the Bank is a party.

Parliamentary investigative Committee on the Location and Restitution of Assets of Holocaust Victims ("the Investigative Committee")

In April 2001, a document of principles was signed between the Bank and other banks and between the Investigative Committee regarding an arrangement for an independent investigation of the accounts of Holocaust victims in banks in Israel. In its wake, independent investigators were appointed to assist the Parliamentary Investigative Committee in locating the bank accounts of Holocaust victims.

In January 2005, a report was published by the Investigative Committee summarizing the investigation of banks in Israel of the assets of Holocaust victims (“the Committee’s Report”). According to the Committee’s Report, the Bank’s alleged obligations range between NIS 1.8 million and NIS 12.9 million at various interest and linkage terms.

The Bank disputes the findings in the Committee’s Report, and, in its opinion, based on documents it received from the Investigative Committee that served as the basis for the report, and supported by a legal opinion based on these documents, it has significant defense arguments, both factual and legal, in its defense against the findings of the Investigative Committee and its conclusions. In the estimation of the Bank’s management, based on the opinion of its legal counsel, the level of legal exposure to the Bank as a result of the findings and conclusions of the Investigative Committee is low.

On May 3, 2007, the Corporation for Location and Restitution of Holocaust Victim Assets Ltd., established pursuant to the law (“the company”) contacted the Bank, demanding that the Bank conduct a review for assets belonging to Holocaust victims (including assets which the Bank disputes the fact that they belong to Holocaust victims). After conducting said review, the Bank was required to transfer such funds, plus interest and linkage differences, to the company. On May 8, 2007, the Bank responded to the company, reiterating its position that it holds no assets of Holocaust victims, as reflected in the investigative committee’s report.

On June 4, 2007, the Bank agreed for the Knesset to submit to the Corporation for Location and Restitution of Holocaust Victim Assets Ltd. all information and findings available to it with regard to assets of Holocaust victims which were collected during work of the investigative committee, and the Bank consented to cooperate with the company in this matter. Following said date, additional letters were exchanged by the company and/or its representatives and the Bank and/or its representatives, following which the Bank provided further documents to the company. As of the date of these financial statements, no further demands or demanded liability have been received from the company.

Also see the highlights of the Holocaust Victim Assets Law (Restitution to Heirs and Dedication to Assistance and Commemoration), 2006, in the chapter on Legislation and Regulation of Bank Group Operations above.

Arrest 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 was 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 annual financial statements.

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 weeks. The Bank has started providing such documents.

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 review conducted by the Bank, it has not committed any offence in Israel nor in the USA, and if any offences have been committed by the Bank employee as the indictment alleges, he did so in contrast to Bank procedures and to his obligations to the Bank.

The Bank has informed the Supervisor of Banks of the aforementioned events and developments.

Letter from the Restrictive Trade Practices Authority

On March 19, 2008, a letter was received from the Restrictive Trade Practices Authority indicating that in view of findings of Authority investigations in November 2004, the Supervisor of Restrictive Trade Practices is considering exercising her statutory authority to determine that 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.

Prior to the Supervisor making her decision as to exercising her statutory authority, the Bank was given the opportunity to provide its arguments in writing to the Supervisor, no later than May 5, 2008.

The Bank will review the material relevant to the hearing and would present its arguments to the Supervisor. The Bank is unable, at this stage, to estimate the impact of the Supervisor exercising her statutory authority, should she decide to do so.

Events outside the Normal Course of Bank Group Business

Presented below is information on significant events in the Bank's businesses, which deviate from its normal course of business:

A. Sale of provident funds and mutual funds

As part of the Bank's preparations to implement the Bachar Reforms, the Bank's Board of Directors resolved on November 13, 2005 to sell the provident and mutual funds operations under Bank management, as follows:

- **Sale of provident funds -** On March 5, 2007, after obtaining all required regulatory approvals, the transaction to sell the Bank's provident fund management operations was concluded in exchange for NIS 343 million, after adjustments that were agreed by the parties to the transaction. The proceeds were calculated at 3.63% of total provident fund assets under Bank management as of February 28, 2007, amounting to NIS 9.4 billion.

  Pursuant to the agreement, the Bank will remain guarantor for 5 years from March 5, 2007, three of those years without consideration, for the nominal value of the deposits of members that are members of several provident funds included in the transaction, according to their provisions and bylaws. The guaranteed amount is NIS 143 million, which are considered risk assets according to the Bank of Israel directives, against actual assets of NIS 3.1 billion.

  As part of the transaction, in addition to the sales agreement, an operating agreement, distribution agreement and special services agreement were signed between the parties,

  For this transaction, the Bank recorded in its statement of profit and loss for the first quarter of 2007, net profit from extraordinary operations in the amount of NIS 199 million.

- **Sale of Bank holdings (60%) in Netivot Management Company Ltd.** - On June 28, 2007, the transaction for sale of provident fund operations managed by Netivot was completed, in exchange for NIS 51.8 million, which is 2.7% of average total assets under management by Netivot in the 3 months preceding completion of this transaction. The transaction was completed after obtaining all required regulatory approvals.

Netivot’s profit from completion of this transaction amounted to NIS 32 million after tax. For this transaction, the Bank recorded in its statement of profit and loss for the second quarter of 2007, net profit from extraordinary operations in the amount of NIS 19 million (60% - equal to Bank share in holdings in Netivot).

In conjunction with this transaction, and in addition to the sale agreement, the parties signed other agreements, including an agreement for provident fund operation by the Bank and agreement on provision of services to provident fund members by the Bank in 2007.

- **Sale of mutual funds** – On April 10, 2006, the Bank and Emda Mutual Fund Management Ltd. ("Emda"), a wholly-controlled subsidiary of the Bank, signed an agreement for the sale of mutual fund management operations of Emda.

Under the terms of the undertaking for the sale of the funds, agreements were signed to distribute the funds as well as agreements to provide other services to the funds by the Bank. Distribution agreements dated April 10, 2006 and June 7, 2006 stipulated, *inter alia*, that the Bank would distribute units in the mutual funds managed by the buyer (including the sold Emda funds) to its customers and will enable them to purchase and hold the units through the Bank, in return for a distribution commission at the rate set forth in the agreements.

With respect to the Emda funds, the distribution agreement will remain in effect for a 10-year period to begin on the closing date. At the end of this period, the agreement will be extended automatically for additional periods of one year each, subject to providing notice of cancellation by one of the parties, 90 days in advance. With respect to the other funds – the distribution agreement will be in effect as from the date the distribution regulations take effect, and any party will be allowed to cancel it, at any time, after serving notice 90 days in advance.

It was further stipulated between the parties that the buyers will work to replace the trustee (as defined in the Mutual Funds Law) in the acquired funds, replacing him with the Bank's Trust Company, on the earliest possible dates according to any law or agreement, for a period of five years from the start of the period that the Bank's Trust Company begins its tenure as each funds' trustee. Pursuant to provisions of circular dated November 15, 2006, issued by the Securities Authority to mutual fund managers and to trustees "on matters related to independence of the trustee and his tenure", replacement of the trustee in the acquired funds was delayed, such that the replacement is expected to be made gradually (for each fund separately) in 2008-2009.

The Bank and Emda are liable, pursuant to the agreement, for any representations made to the buyers in the agreement, for a three-year period from the closing date, subject to certain exceptions. The parties' liability pursuant to the agreement does not apply to indirect and/or future and/or income-expense damages, expected or unexpected, including damage to reputation that the parties will sustain, but rather direct damages alone.

On June 8, 2006, the sale was closed, and in consideration, Emda received NIS 213 million from the buyers and the Bank recorded capital gains of NIS 130 million after tax. The proceeds is subject to a one-time adjustment (increase or decrease of proceeds), *inter alia*, for factors including a change that occurs, if it occurs, during the three-year period from the closing date, at the rate of the distribution commissions that can be collected according to the distribution commission regulations, on the basis of the prescribed formula. As of the date of the financial statements, the distribution commission regulations were not changed.

The sale of the provident and mutual funds managed by the Bank is a function of the Bank's preparations for implementing the provisions of the Capital Market Reform, in which, according to the resultant legislative amendments, a banking corporation was prohibited from holding any means of control in a provident fund management company, in a provident fund, or in a mutual fund management company. It was also stipulated that a banking corporation with equity of not more than NIS 10 billion (like the Bank) will be permitted to receive a pension consultancy license and to sell pension products, subject to certain limitations, once the sale of its holdings in provident and mutual funds it controls has closed. For pension consultancy license granted to the Bank, see below.

As a result of the implementation of the Bachar Reform, and with the closing of the sale of all the mutual and provident funds, as aforesaid, Bank revenues from management fees on provident and mutual funds that were held in the Bank Group have ceased. However, the Bank may collect distribution commissions, in accordance with the provisions of the Regulations enacted under the Provident Fund Law and the Mutual Fund Investments Law, respectively. As of the date of the financial statements, the Bank entered into distribution agreements with most of the mutual fund managers to distribute units of the mutual funds they manage, in consideration for distribution fees at the rates permitted by the distribution commission regulations. Furthermore, the Bank has started providing pension consultancy and has entered into distribution and consulting agreements with producers of pension products and in pension consulting agreements with customers, as set forth below.

Therefore, despite the decline in Group revenues in the immediate future, it is not possible to estimate the overall impact on total Group revenues in the future, after maximizing potential operations of mutual fund distribution and pension consultancy.

Below are details relating to the Bank's income from Provident Funds and Mutual Funds (in NIS millions):

	2007	2006
Provident fund management fees	-	102
Mutual fund management fees	-	33
Mutual fund distribution fees	28	11

B. Grant of Pension Consultancy Permit – pursuant to sale of mutual fund and provident fund assets under management by the Bank or its subsidiaries, the Bank was granted a Corporate Pension Consultancy Permit on August 7, 2007 by the Supervisor of Capital Market, Insurance and Savings in the Ministry of Finance. Furthermore, in conjunction with grant of said permit, the controlling shareholders of the Bank were granted a Pension Consultancy Control Permit.

Upon receiving the aforementioned permit, the Bank launched pension consultancy operations to salaried employees and to the self-employed. Consultancy is provided by licensed pension consultants at Bank branches around Israel.

Consulting with regard to the pension mix appropriate for the customer is provided based on a computer system which analyzes pension product data and customer preferences, using a custom model for maximizing expected return on the pension portfolio at the risk level appropriate for the customer.

Pursuant to provisions of the Financial Services Supervision Law (Engagement in Pension Consulting and Marketing), 2005 and subsequent regulations, the Bank may charge pension product providers distribution commissions at variable rates based, *inter alia*, on product type and control of said product prior to enactment of the Law on August 10, 2005 (“the effective date”) as follows:

- Pension funds (which were not controlled by banks) and non-bank provident funds (which were not controlled by banks on the effective date) – a commission of up to 0.25% per annum for amounts deposited in the fund since January 1, 2006. For amounts deposited in the fund prior to this date, the commission charged would be 0.1% per annum.

- Bank provident funds (which were controlled by banks on the effective date) – a commission of up to 0.25% per annum for all amounts deposited, even if deposited prior to January 1, 2006.
- Bank provident funds, jointly owned on the effective date by banks and others – a distribution commission of up to 0.25% per annum, based on the holding percentage of the relevant bank of the fund.

The Bank may charge a distribution commission for pension products of a customer who has signed a consulting agreement with the bank, after the bank has signed distribution agreements with the pension product providers.

As of the date of publication of these financial statements, 35 distribution agreements have been signed with companies which produce and manage pension products, which together have an 85% share of the relevant market.

C. **Acquisition of controlling stake in Bank Yahav -** On March 27, 2007, the Bank signed a memorandum of understandings, whereby the Bank would acquire 50% of the issued capital of Bank Yahav for Government Employees Ltd. ("Bank Yahav") inclusive of all rights associated therewith ("the acquired shares"). In exchange for the acquired shares, the Bank would pay proceeds as follows, based on Bank Yahav's required shareholders' equity for maintaining a minimum capital ratio of 10% ("required shareholders' equity"). It was agreed that Bank Yahav would continue to obtain computer services from Bank Hapoalim, under terms currently in place between Bank Hapoalim and Bank Yahav, for a 3-year period from the transaction completion date. On September 9, 2007, a detailed agreement was signed for sale of the acquired shares based on principles set forth in the memorandum of understandings dated March 27, 2007.

On November 13, 2007 an addendum to the agreement was signed by the parties, whereby, *inter alia*, the date for completion of the transaction was set to March 27, 2008; however, if by that date, sale of provident funds owned or controlled by Bank Yahav ("the funds") would not be completed - the completion date would be postponed to June 27, 2008. Furthermore, arrangements were agreed, subject to the statute, with regard to Bank Yahav's preparations in conjunction with competition in the sector in which it operates. The parties also agreed on the final proceeds to be paid by the Bank for Bank Yahav shares owned by Bank Hapoalim, in accordance with principles for such calculation set forth in the agreement, at NIS 371 million, such that the proceeds would no longer be adjusted to changed in Bank Yahav's capital or results through the completion date (other than potential adjustment due to dividend distribution). Furthermore, Bank Hapoalim would be entitled to receive 50% of the additional shareholders' equity expected at Bank Yahav from sale of the funds.

Completion of this transaction is contingent on multiple suspensive conditions, including obtaining approval of the Commissioner of Restrictive Business Practices; obtaining a permit from the Bank of Israel Governor for sale and holding of the shares sold and for control of Bank Yahav by the Bank; completion of sale of the funds; transfer of the founding share at Bank Yahav (which is part of the acquired shares), in accordance with provisions of the "Share Capital" chapter of Bank Yahav's articles of incorporation.

D. Agreement with Isracard - On November 13, 2007, the Bank signed a memorandum of understandings with Isracard Ltd. and Europay (Eurocard) Israel Ltd. ("Isracard" and "Europay", respectively), whose highlights are set forth below. Isracard, Europay and the Bank would enter into accelerated negotiations (aiming to conclude them by April 3, 2008, pursuant to the addendum to the MOU signed on March 4, 2008) to replace their current agreed arrangements with a new agreement (for a 10-year term) aimed at issuing Mizrahi-Tefahot branded credit cards and agreeing on arrangements for operation and servicing by Isracard and/or Europay of debit cards to be issued by them and to be distributed by the Bank to its customers ("the new agreement").

The new agreement shall be signed no later than April 3, 2008 (as per the aforementioned addendum to the MOU), and in return the Bank would be eligible to receive allocation, at no further consideration, of 3.6% of Isracard and Europay ordinary shares in exchange for the new agreement and its provisions.

Should the new agreement not be signed by April 3, 2008, the Bank would be eligible to receive allocation of 1.8% of Isracard and Europay ordinary shares in exchange for continuing the current agreements in place for a 10-year term from the date of signing the MOU. In this case the Bank may distribute its branded card through any party of its choice. In December 2007, the Bank received allocation of 1.8% of the aforementioned shares.

Note that the maximum total shares to be allocated to the Bank in exchange for the aforementioned agreements, would be 3.6% of Isracard and Europay shares. The shares would be allocated subject to customary first-right-of-refusal to Bank Hapoalim Ltd. upon transfer of the shares by Mizrahi-Tefahot to any third party, and subject to a blocking period, whereby Mizrahi-Tefahot may not transfer the shares to any third party (other than Bank Hapoalim) during a 1-year period (the aforementioned right-of-first-refusal and blocking period shall be in effect for as long as Isracard and/or Europay shares are not listed for trading on the stock exchange).

The MOU is subject to all regulatory requirements required by statute, if any.

E. Listing for trading of complex capital notes – On May 21, 2007, a prospectus was published for listing for trading in early June 2007 of complex capital notes amounting to NIS 460 million par value, issued by the Bank in November 2006, which consist of upper Tier II capital for maintaining a minimum capital ratio. In June the Bank issued and listed for trading additional capital notes in the same series, amounting to NIS 500 million par value. See Note 11A to the financial statements for details.

F. Signing of collective agreement with representatives of managers

On March 22, 2007, the Manager Council and the Bank signed a salary agreement for 2005-2007, whereby the parties agreed, *inter alia*, on compensation for managers, the effective date for the Manager Constitution with regard to limitations on termination of managers and institution of voluntary retirement plan for managers. For details, see the Human Resources chapter.

Business Strategy

On December 24, 2007 the Bank's Board of Directors approved a new strategic plan for 2008-2012, based on the following principles:

- The objective is to achieve in 2012 return on equity from current operations of 18% on average.
- During the strategic plan, the Bank would maintain a capital adequacy ratio (including complex capital notes) at no less than 11.2% and a capital adequacy ratio (excluding complex capital notes) at no less than 10%, as per the previous Board of Directors decision dated May 2007. This is in view of the custom among banks globally to maintain capital adequacy rates higher than the minimum requirements imposed by regulators, in order to reflect to investors and depositors the conservative approach and international standards which the Bank wishes to adopt, as well as in view of the intent of the Supervisor of Banks to adopt Basel II regulations and to have capital allocated for operating risk as well. On February 25, 2008, the Bank's Board of Directors resolved to instruct Bank management to act so as to have the capital adequacy ratio (including subordinated notes) be no less than 12% by end of 2009.
- During this strategic plan, the dividend distribution policy adopted by the Bank would be maintained, whereby, subject to the Bank's ratio of capita to risk components being no less than 10%, the Bank would distribute annually dividends equal to 40% of net operating profit and 80% of net profit from extraordinary items.

Forecasts and Assessments with Regard to Bank Group Business

The Bank bases its future growth plan on several major efforts in the following areas:

- Continued growth of Bank market share of the household segment;
- Maintaining Bank position as a leader in the mortgage market;
- Upgrading trading and execution infrastructure (trading rooms) and continued leadership position in this area;
- Expansion of international operations, with emphasis on private banking and trading infrastructure;
- Expansion of the business customer base and establishing unique value propositions, mainly for small-to-medium businesses.

The growth engines are aimed to grow Bank revenues at an average annual rate of over 8% (though not in linear fashion), while maintaining expenses at a moderate annual growth rate of 4% (also not in linear fashion). We emphasize that these rates include the cost associated with acquisition of control of Bank Yahav and establishing the Group from a multi-brand viewpoint.

The Bank has based the new strategic, multi-annual plan, *inter alia*, on implementation of acquisition of the controlling stake in Bank Yahav; on potential benefits to the Bank from implementation of Basel II recommendations; pension consultancy and insurance; continued organic growth; expense containment and continued improvement in efficiency with introduction of ever growing variable, performance-based compensation; and continued expansion of the back-office operation division while transferring logistics operations from branches to this division – a process launched by the Bank in early 2007.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's Board of Directors, as described below. This information may not materialize due to changes which may occur in various factors outside of the Bank’s control. 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 issues of human resources.

Anticipated developments

Insurance consulting

Pursuant to legislation changes included in the Arrangements in the State Economy Law, enacted in conjunction with approval of the 2008 budget, the Bank, starting in January 2009, and subject to obtaining a permit from the Capital Market, Insurance and Savings Division of the Ministry of Finance, provide in conjunction with pension consultancy it provides, may also provide consulting for pension insurance products, life insurance including savings and disability insurance, provided it is part of a pension insurance or life insurance policy. Providing insurance consulting would allow for expansion of the Bank's pension consultancy operations. For details of the aforementioned amended legislation, see the chapter on Legislation and Supervision of Bank Group Operations.

The Bank would be entitled to receive a distribution commission from insurance companies, similar to agreements concerning other pension products, i.e. pension funds and provident funds. For details of the distribution commissions, see chapter "Events outside the Normal Course of Bank Group Business".

As part of preparations for providing insurance consulting, the Bank would update the consulting model to include insurance products in addition to pension funds and provident funds included therein, and would sign distribution agreements with insurance companies who wish to do so.

Acquisition of holdings in Bank Yahav

On March 27, 2007, the Bank signed a memorandum of understandings, whereby the Bank would acquire 50% of issued capital of Bank Yahav for Government Employees Ltd. ("Yahav"), including associated rights. On September 9, 2007, a detailed agreement was signed with regard to acquisition of said shares and rights based on principles set forth in the memorandum of understandings. On November 13, 2007, an addendum to the agreement was signed which set forth, *inter alia*, the proceeds to be paid by the Bank and the date for completion of this transaction. Completion of this transaction is contingent on several suspensive conditions set forth in the agreement. Acquisition of holdings in Bank Yahav is aligned with Bank business strategy which emphasizes, *inter alia*, development of Group retail operations. For further information on acquisition of holdings in Bank Yahav, see Note 6.E.4) to the financial statements.

Acquisition of holdings in Isracard

On November 13, 2007, the Bank signed a memorandum of understandings with Isracard Ltd. and Europay (Eurocard) Israel Ltd. ("Isracard" and "Europay", respectively), whereby the parties would enter into accelerated negotiations to replace their current agreed arrangements with a new agreement which would include, *inter alia*, issuance of Mizrahi-Tefahot branded credit cards, and the Bank's entitlement to allocation of 3.6% of ordinary Isracard and Europay shares, as set forth in the MOU and agreed in the new agreement. The allocation of Isracard and Europay shares would allow the Bank to expand and intensify its presence and involvement in the retail sector, especially in the credit card segment. See Note 6.E.5) to the financial statements for additional details of the MOU.

This information is a kind of forward-looking information, which is based on various assumptions and forecasts presented to the Bank's 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, other factors that impact the exposure to financial risk, the public's preferences, legislation, government directives, regulations of regulatory entities, the behavior of competitors, aspects related to the Bank's image, technological developments and issues of human resources.

Sources and financing

Group financing sources include deposits, obligatory notes and debentures of various types, as well as 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 examines the degree of concentration of the depositors, and within this framework, management imposes a limitation on the holding of liquid resources against large depositors. This limitation is part of the management of liquidity risk.

For composition of deposits by type of depositor, see financial statements for December 31, 2007 and Notes 9 and 10 thereof.

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. Banks may borrow or lend money with the Bank of Israel at a price range of 1% over or above the Bank of Israel interest rate. 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

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.

Deposits in the Bank of Israel to absorb surplus liquidity

When there is surplus 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 period of 1 or 7 days, and the maximum interest in these tenders is the Bank of Israel interest it declares. Moreover, there is a window for depositing daily deposits in the Bank of Israel, unlimited in amount, at interest that is 1% lower than the Bank of Israel interest rate. At the end of 2006, the Bank of Israel announced completion of the process of replacing the main monetary tool of the Bank of Israel, intended to absorb surplus liquidity in the economy – from deposits in tenders to banks to MAKAM issued to the general public in ordinary tenders. This activity of the Bank of Israel brought the banking system to a situation in which there is a need for monetary loans throughout every month of activity.

Loans from the Bank of Israel to reduce the liquidity shortage

On days when there are liquidity deficits in 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 1% 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. In the fourth quarter of 2006, the Bank of Israel started issuing REPO tenders for repurchase of debentures and MAKAM (ultra short-term bonds). This tool is also intended to inject liquidity into the banking system.

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. See the chapter on risk management for information on the management of liquidity risk by the Bank.

Short-term loans (MAKAM)

Another financial instrument used to absorb surplus shekel liquidity is the short-term loan (MAKAM), through regular issuances to the public and the activity of the Bank of Israel in the secondary market.

RTGS real-time settlement systems

In August 2007, the Bank of Israel launched the Real Time Gross Settlement framework (RTGS). This system allows customers to transfer in real time NIS-denominated amounts between bank accounts in the same bank or in different banks. Settlement is immediate and final. The Bank is prepared computer and management-wise for this significant change in the manner of transferring monies in Israel. As part of its preparations, the Bank acquired a computer system for management of daily liquidity and has developed internal interfaces to enable NIS transfers to be made in real time.

Issuing notes and debentures to the public

The Bank is working toward raising long-term sources through issuances. Mizrahi Tefahot Issue Company ("Tefahot Issue Company"), a company wholly-owned and controlled by the Bank, has been engaged since its founding in the issuance of obligatory notes and depositing the proceeds in the Bank. Over the years, Tefahot Issue Company issued to the public subordinated notes under issued prospectuses.

Under the terms of a shelf registration published by the Company for the public on November 28, 2006 and effective for a 2-year term, Mizrahi Tefahot Issue Company is permitted to issue to the public additional obligatory notes with par value of NIS 5 billion.

Within this framework, the Company issued through December 31, 2007 obligatory notes amounting to NIS 750 million, of which NIS 450 millions in subordinated notes.

As of the date of these financial statements, the company issued to the public obligatory notes (Series 25-30) with total par value of NIS 1,974 million. The revaluated balance as of December 31, 2007 of these obligatory notes in circulation amounted to NIS 2,093 million.

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 complex capital 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 notes were listed for trading in early June 2007. In June 2007, the Bank raised a further NIS 490 million (NIS 500 million par value) by private placement with institutional investors, by expansion of capital notes (Series A). These notes were listed for trading upon issuance. The revaluated balance of the complex capital notes as of December 31, 2007 amounted to NIS 972 million. See Note 11 to the financial statements for details.

Rating of Bank obligations

The Bank's obligations are rated regularly by Ma'alot Israel Securities Rating Company Ltd. ("Ma'alot") at AA+. See Note 11.A for information on the subordinated notes that were issued by the Bank.

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 Bank of Israel Governor on a change in the monetary interest.

In the CPI-linked sector, most variable-interest loans are mortgages. The rate adjustment mechanism is based on the average cost of raising sources for the mortgage banking system. The frequency of the change in interest rate on CPI-linked mortgage loans is diverse, depending on loan type: 1 year, 2.5 years, 5 years, 7 years and 10 years. In view of the decline in recent years of funds raised directly by mortgage banks (mostly due to merger of the large mortgage banks with their parent companies), the Bank reviews, in cooperation with the Bank of Israel, replacement of the “Source Anchor” with an alternative base, while maintaining the same margin.

In the foreign currency 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. Mortgages also have an additional variable interest track, at a frequency of 3 months, 6 months and one year, in which the mechanism for updating the interest is determined according to the lower of a certain margin above mobilization costs and between a certain margin above the LIBOR interest rate.

Risk Management

Day-to-day activities in a variety of balance sheet and off-balance-sheet financial instruments expose the Group to financial and other risk, mainly – market and liquidity risk, credit risk, and operational risk. The risk management policies in the various areas are intended to support the achievement of the Group's business goals while limiting the associated risk.

The Group manages its risk on a day-to-day basis, in accordance with the Bank of Israel's Proper Conduct of Banking Business Directive no. 339. Within this framework, the Group has appointed risk managers, and the Bank has established a Risk Management Department. Bank management regards the Bank's risk control and management system as one of its core competencies, hence it is Bank policy to constantly strive to improve the risk control and management system, Specifically, the Bank is in advanced stages of application of the Basel II regulations, and successful application of these regulations is a key component in the concept used by Bank management and its Board of Directors for empowering a culture of risk control and management within the Bank.

Bank management believes that risk control and management must be an integrative process. As part of this approach, the Bank purchased a new risk management system (the Algorithmics system) that enables management and control under a single platform of the market risk and liquidity risk of the Bank, and in the future, also the various credit risk components, including implementation of Basel II regulations for calculating regulatory and economic capital. The Bank began implementation of an advanced module of the system, enabling it to manage and control exposure of its customers in the capital market, using the infrastructure it uses to manage market, liquidity and credit risk. During 2007 the Bank completed a move to enable use of advanced models for management of customer exposure to the foreign currency segment of the capital market. This effort would be expanded in 2008, aiming to include customers operating in other trading arenas. Furthermore, as of end of 2007, the system started receiving input files for calculation of required regulatory capital in accordance with Basel II guidelines (layer 1 – standard method).

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 both the level of the individual borrower and the level of economic sectors. As mentioned earlier, the Bank is in advanced stages of applying the Basel II guidelines. Quantitative aspects of the regulation, and not less important – its qualitative components, have a strong impact on how credit risk is managed by the Bank. In early 2008, the Bank completed a gap review with regard to Basel II requirements for credit risk management, and is in the process of studying these gaps in order to have them eliminated.

The Division Manager, Business Banking is in charge of credit risk management at the Bank. 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 customer, based on their level of indebtedness. Any findings requiring action are reported to the entity in charge of the relevant credit. The Bank has a Tracking and Control Department, which used computer systems to discover and alert to unusual accounts and customers, including based on information external to the Bank. In addition, the Bank operates a Credit Control Unit under the Risk Management Division (see below in this chapter), which reports its findings directly to the President.

Procedures for handling credit and collateral, as well as the relevant IT systems, are constantly reviewed and updated, in order to adapt them on a regular basis to the changing business environment, while learning the lessons of previous events. As part of Bank policy, the Bank's credit staff participate in all Bank committees related to risk management, since there is a strong link between credit risk management by the Bank and management of its liquidity risk, operating risk and market risk.

In an ongoing effort to improve the professionalism of employees dealing with credit, professional training activities and seminars are conducted at all the levels, while focusing on professional improvement with respect to specific matters. At the same time, substantial resources are invested in improving and raising the level of sophistication of the control tools and IT systems available to the decision makers in the credit area, for the purpose of properly estimating the business risk of borrowers, while emphasizing an assessment of their repayment ability and overseeing their business activities.

Risk distribution - The Bank's credit policies are based on the dispersal of risk and their controlled management. Risk dispersal is characterized by several aspects:

- Dispersal of the loan portfolio among the different economic sectors, including limiting exposure in certain sectors.
- Dispersal over sized groups of customers.
- Dispersal over linkage segments.
- Geographic dispersal where relevant (construction industry, mortgages).

Industrial 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, agriculture, construction, local authorities, 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 customers: The Bank provides credit to large customers through the Corporate sector, which operates teams with sector expertise. Occasionally the Bank limits its share of credit to a major customer relative to total extent of credit to that customer 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 maintains compliance with limitations on indebtedness of borrowers and borrower groups, as well as total indebtedness of the six largest borrowers, according to provisions of Proper Banking Conduct Regulation 313.

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 dispersal: In providing credit to the construction industry, and in some cases in mortgages, the Bank insists on geographic distribution, in order to reduce the excessive geographic concentration in the providing credit.

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.
For further details, see the chapter describing the household segment.

Considerations in extending credit – The considerations involved in granting credit are based mainly on the quality of the customer, his reliability, financial strength, liquidity, repayment ability, seniority in the industry, length of time with the Bank, behavior in the account, etc. and on the quality of the collateral, as described below. Likewise, the Bank works to match credit type and terms to customer 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.

Authority to issue 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 a 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.

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: Liens on real estate, vehicles, deposits, securities, 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, promptness of realization and legal status, in addition to assessing the repayment ability of a customer 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 and its legal status. 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. 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. Collateral which are negotiable securities is constantly updated as per its market value; deposits and bank guarantees are updated on an ongoing basis according to their terms. For real estate serving as collateral, the procedure specifies the date for valuation by a licensed assessor, by 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.

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 debt 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 customers, when securities form a significant element of their collateral.

Credit in the construction and real estate industry - 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 in which the construction is being carried out, and based 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. The balance of financial loans to the real estate sector by the construction financial support method represented 37% of the total financial credit to the real estate industry at December 31, 2007, compared with 42% of the total financial credit to sector as of December 31, 2006.

Monitoring and controls – The Bank's IT 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 customer-account development and management.

Borrowers' 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.
This system is used for most of the Bank's business loans. The goal of this system is to improve the management of credit risk and the decision-making process. The system determines the rating of a borrower as a function of the quality of the customer, the collateral furnished and the amount of credit received. The credit rating also constitutes a basis for pricing the relevant credit.

Credit exposure in customer trading in financial derivatives – Rules and procedures were prescribed for determining the amount of collateral required for the Bank's customer trades in financial derivatives, as well as rules for closing the exposure created due to these trades. The means of monitoring and controlling the activity and exposure in derivatives are constantly being improved. The Bank has a dedicated department specialized in control of exposure due to capital market operations.

Handling of problem loans and collection of debt – The handling of problem loans requires special focus and professionalism, with segregation from the level that approved or processed the credit extended and collateral received. Therefore, the handling of these customers is concentrated in a separate sector in the business banking division.

Provision for doubtful debt – The Bank uses a system of computer reports for identifying accounts, customers and transactions with higher than usual credit risk. Decisions on making provisions for doubtful debt are based on scanning the entire credit portfolio, assisted by the aforementioned reports, using a structured procedure which determines, *inter alia*, the authority to review and decide on such provisions. In making the decision, considerations are made with regard to the nature of the transaction, the financial status of borrower and guarantors, and the size and quality of collateral provided to the Bank. In addition, a valuation of the impact of changes in the business environment on the borrower and their business is carried out.

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, such that changes in market conditions may lead to changes in the fair value of the different financial instruments. The principal market risk to which the Bank is exposed are interest risk, basis risk and liquidity risk.

Market risk management is intended to maximize Bank profit at the prescribed risk level.

Exposure to market risk (basis, interest, and liquidity) 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 VAR model and stress tests (see the explanation of these models below) became the principal management tools for managing market risk. Since 2005, the Bank operates within the Board of Directors' restrictions for 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, in the highest of several calculation methods, will not exceed 6% of shareholders' equity, and that the maximum loss in stress tests, in the highest of several calculation methods, will not exceed 15% of equity. The Risk Control Division conducts back testing to ascertain

adequacy of the VAR model on an annual basis, using advanced models in this field.
The Bank regularly monitors and controls exposure to the subsidiaries' exposure to the different market risk.

The procedure for market risk exposure, approved by the Bank's Board of Directors in 2005, prescribes, *inter alia*, the ranking of authorities and frequency of discussions and reporting of exposure status at 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 Financial Division Manager must immediately report to the Bank President any deviation from management restrictions, in excess of the deviation permitted by the Bank's Risk Manager. Any exercise of authority by the Risk Manager to authorize deviation is to be reported at the following meeting of the Management Committee on Asset and Liability Management.

When exceptional events occur in the money and capital markets, 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 changes.
The Bank regularly operates a "risk monitoring forum" which convenes monthly, with the objective of setting the Bank's extreme scenarios, discuss and prescribe the methodology for managing and controlling risk. The Forum is headed by the Manager of the Controllership, Planning and Operations Division. Also members are representatives of the Finance Division and of the Controllership, Planning and Operations Division.

The Bank also 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 different Bank units with the liquidity "providers" and liquidity managers.

The regular activities of the abovementioned forums enables the existence of day-to-day communications regarding the management of different risk among all the divisions in the Bank that take part in the process of managing and controlling risk.

The Bank's Board of Directors receives an update once every six weeks on the status of the management of assets and liabilities in the various linkage segments. The Board of Directors also holds a quarterly discussion on the “Exposure Report”, as defined in Proper Conduct of Banking Businesses Regulation No. 339.

Examination and control of the various market risk 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 Controllership, Planning and Operations Division. The mechanisms for quantifying the exposures and controlling the compliance within the approved activity frameworks are anchored in internal work procedures.

The internal estimate of VAR of the Bank Group presents the risk of a loss during a month, with the probability of it occurrence not exceeding 1%. Below is the maximum VAR (according to the historic method) of the Bank Group (in NIS millions):

	2007	2006
As of December 31	126	128
Maximum value during year	169 (in Aug.)	168 (in Nov.)
Minimum value during year	104 (in Jan.)	110 (in Feb.)

In order to compute capital adequacy for the purposes of market risk, in accordance with the directives of the Bank of Israel, the Bank prescribed policies and procedures for defining the Bank's marketable portfolio. The Bank calculates its required capital adequacy according to the standard model on a consolidated basis, as mandated by the Bank of Israel's Proper Conduct of Banking Business Directive no. 341.

As part of its preparations for application of the Basel II regulations, the Bank reviews guidelines on capital requirements for market risk, including re-characterization of the negotiable portfolio.

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 dispersal of the risk. In addition to measuring the total risk value, the Bank measures and manages the mix of risk elements.

In 2007, the Bank created a model to calculate the efficient front of the portfolio of securities held for sale. In the second half of 2007, the model started to be used as a tool in management of the Bank’s held-for-sale portfolio. The portfolio management methodology, under the efficient front model, is based on managing the expected return relative to the risk level desired by the Bank.

Basis risk

Linkage-basis risk relates to 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.

Below is an analysis of the sensitivity of the Group's profit to changes in the main exchange rates and in the CPI as of December 31, 2007:

Profit (loss) in NIS millions

	Scenarios				Extreme historical scenario (1)	
	10% increase	5% increase	5% decrease	10% decrease	Maximum increase	Maximum decrease
CPI	252	126	(126)	(252)	76	(23)
Dollar	11	(1)	20	(62)	(1)	8
Pound Sterling	-	-	2	5	-	1
Yen	1	1	-	3	2	-
Euro	5	1	12	43	2	15
Swiss Franc	7	4	(3)	(7)	7	(4)

(1) Extreme scenarios were calculated based on daily changes in the exchange rate and monthly changes in the CPI, in the last 10 years.

Interest risk

Interest risk is 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.

Below is a description of the sensitivity of Bank positions, as of December 31, 2007, to corresponding shifts of 1% and 2% of interest rate curves (NIS in millions):

	1% corresponding shift in curve		2% corresponding shift in curve	
	upwards	downwards	upwards	downwards
CPI-linked shekel	(105)	106	(208)	212
non-linked shekel	(19)	19	(37)	37
In foreign currency	(9)	10	(18)	23
All sectors	(133)	135	(263)	272

Interest risk in the Bank's banking portfolio is monitored on a weekly basis, both in managing interest risk for the overall portfolio in VAR terms, and individually 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. Interest risk measuring using this model started in the fourth quarter of 2007, and is in the process of application, study and deployment.

In compiling the mortgage repayment forecast for the Bank, assumptions with regard to pre-payment are taken into account. The pre-payment rates are determined by linkage type and interest type, and based on statistical analysis of past pre-payment events.

The VAR model (Value At Risk)

As required according to the directives of the Bank of Israel, the Bank computes the VAR values and the stress-test values on a monthly basis. The VAR is calculated by each of the three calculation methods commonly used: the analytic method (parameters), the Monte Carlo simulation method, and the historical simulation method.

A summary of the models used by the Bank in computing 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 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 set up a managerial and technical infrastructure to compute the VAR model and the stress tests under different alternatives. The results of the models, including an analysis of the results, are reported on an ongoing basis to the Bank's Market Risk Manager and to the President, and quarterly to the Board of Directors.

Some of the VAR calculations are based on historical data. Accordingly, the Bank examines the quality of the market data that it uses in the VAR calculations, including through back testing, in order to improve the forecasting ability of the models that it uses.

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. It also works to expand the use of these models 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 expand use of these models, *inter alia*, in order to review some of its investment decisions. This was achieved by reviewing the potential gain from the investment alternative and reviewing its inherent risk, expressed by the change in VAR from execution of the new transaction (incremental VAR).

The Bank has acquired a new risk management system, whose different modules are gradually deployed at the Bank. As of the end of 2007, the Bank is in final stages of moving the system to production in all matters related to VAR Calculations, stress tests, liquidity risk management and other calculations, as required by Asset and Liability Management.

Financial capital and linkage position

Financial capital – As of December 31, 2007, the Bank’s capital exceeded its non-monetary items by NIS 4,028 million. The Group's free capital, which includes financial capital, plus loans that were classified as an investment in shares, in accordance with the guidelines of the Supervisor of Banks, and plus the general and supplementary provision for doubtful debt, financed in 2007 primarily used in the non-linked NIS-denominated segment and in the CPI-linked segment, based on the current asset and liability management policy at all times.

Liquidity risk

Liquidity risk result 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 No. 342 “Management of Liquidity Risk".

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’s Board of Directors approved, in late 2004, a policy document containing a ranking of authority levels, procedures, limitations and emergency plan in the event of a liquidity crisis. The Board of Directors prescribed a minimum ratio of 1 between the liquid resources and the financing needs, during the ordinary life and in various scenarios.

Moreover, the Bank's Executive Management set limitations on the following matters:

- The ratio of liquid resources for financing purposes exceeding 1, to be used as a "safety cushion".
- The optimal composition of liquid resources to cover the "safety cushion" and the financing needs.
- Allocating liquid resources against the balances of large depositors.

In 2007 there were no recorded deviations from the Board of Directors' limitations.

The Bank has significant surplus liquid means over financing requirements for 1-month term in both NIS and foreign currency. The surplus liquidity in NIS is invested mainly in Bank of Israel deposits of up to 1-week term and in government bonds. The surplus foreign currency liquidity is invested in short-term deposits in overseas banks, in local banks and in the Bank of Israel, and in debentures that are realizable quickly.

Quantitative analysis of market risk

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:

Linkage status – Details on the assets and liabilities in the various linkage segments at December 31, 2006 and 2005 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 because of differences in the treatment of capital items, in certain problem loans, in investments in investees and the remaining non-monetary items, between the accounting approach and the economic approach (as explained below).

In order to reflect the Bank's economic exposures, the Bank classifies certain problem debt as loans in the non-linked NIS sector, instead of the original loan sectors. A customer's loan that is classified as securities, in accordance with the directives of the Supervisor of Banks, is classified for asset and liability management purposes as non-linked NIS loans, as is the practice for all problem debt.

Surplus CPI-linked assets of the Group, which include balance sheet and off-balance-sheet items as of December 31, 2007 as presented in Note 17 to the financial statements, amounting to NIS 1.8 billion. After allocation of the general and supplementary provision for doubtful debt to free capital and the classification of certain problem loans to the non-linked NIS sector, the position in the CPI-linked sector as of December 31, 2007 is surplus uses of NIS 1.7 billion. As of December 31, 2006, the surplus uses amounted to NIS 1.3 billion.

Surplus foreign currency liabilities of the Group, which include balance sheet and off-balance-sheet assets and liabilities as of December 31, 2007, as presented in Note 17 to the financial statements, amount to NIS 207 billion. Foreign currency liabilities include foreign currency deposits of NIS 258 million used to finance investments in overseas subsidiaries, of which NIS 250 million are stated in the balance sheet as non-monetary items. The allocation of foreign currency deposits to finance the overseas investments correspondingly reduces the liabilities in the foreign currency sector. After the allocation of the general and supplementary provision for doubtful debt to free capital, and the reclassification of certain problem loans to the non-linked NIS-denominated sector, the Bank has surplus foreign currency sources as of December 31, 2007 of NIS 296 million, compared with surplus uses of NIS 135 million as of December 31, 2006.

The position in the non-linked NIS sector, after allocation of the free capital and reclassification of certain problem loans, balances the open economic positions in the CPI-linked and foreign currency sectors.
In Appendix D to Management Review, the Group's exposure to interest on a consolidated basis is presented in terms of average effective duration. The cash flows for computing the exposure are based on assumptions on the percentage of withdrawals at exit points in savings plans of the Group and of the percentage of early discharge of mortgages. The percentage of withdrawals is based on empirical data.

In the non-linked NIS sector, the duration gap of liabilities to assets is just 0.04 of a year, due to the fact that most of the activity in the non-linked NIS sector is at variable interest, linked to the prime rate, and the resultant interest risk is minimal. The 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.

The duration to maturity of liabilities in the CPI-linked sector is 0.10 of a year, compared with 0.31 of a year in 2006. The computation of duration to maturity is based on assumptions of the prepayment of savings and loans. Without these assumptions, the duration to maturity of assets exceeds that of liabilities by 1.02 of a year. Without the assumption of prepayment, the difference in the IRR decreases from 0.36% to 0.24%.

In the foreign currency sector, the duration to maturity of assets exceeds that of liabilities by 0.11 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.

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 both the sources side and the uses side, is concentrated in terms of up to one year. As of December 31, 2007, 97% of total liabilities are for this term (compared to 93% as of December 31, 2006), and 81% are for terms of up to 1 month (compared to 75% as of December 31, 2006).

In the CPI-linked sector, the main activity on the sources side was soliciting deposits. Most of the deposits are for ten-year periods, with the possibility of withdrawal at the end of two years. The Bank anticipates that these deposits will be withdrawn before the end of the period, although, according to the accounting guidelines, these balances are presented in the note based on the maximum period. The percentage of liabilities for terms above two years out of total liabilities rose from 68% at the end of 2006 to 69% at the end of 2007. The Bank recycled in 2007 some 85% of withdrawals of CPI-linked deposits into new deposits in a range of deposit available at the Bank, compared with 95% in 2006.

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 2007, there was an increase in the Bank’s balance of deposits from the public. The balance of deposits from the public rose from NIS 73.2 billion on December 31, 2006 to NIS 75.3 billion on December 31, 2007, an increase of 2.8%.

The increase was in the non-linked NIS-denominated sector. The volume of public deposits in these sectors reached NIS 36 billion in the non-linked NIS sector and NIS 19 billion in the foreign currency sector, increases of 5.7% and 6%, respectively, compared with 2006. In the CPI-linked sector, there was a 4.6% decrease. In 2007, there were no limits on the possibility of soliciting different types of deposits in the Bank.

Financial derivatives

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 customers 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 dealing 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.N to the accompanying financial statements.

The Bank operates in credit derivatives in its nostro 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, 2007 amounted to NIS 692 million.

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. VAR limits on the options portfolio of the Bank is computed daily.

In 2007, the Bank launched as part of its risk management system an advanced module for review of 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, intra-day. The Bank intends to extend use of this module to all its derivative operations in 2008.

The volume of transactions in financial derivatives according to the different categories is detailed in Note 19.E to the accompanying financial statements.

Operational risk

Basel I guidelines referred to operating risk as residual risk, and in fact defined it as risk which is not market risk nor credit risk. Basel II guidelines explicitly define operating risk, and indicate the major factors which create operating risk (internal processes, people, systems and external events). Furthermore, the Basel II first layer includes capital requirements for operating risk.

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 or credit risk.
c. A significant share of operating failures has very low probability but relatively large damage potential.

In conjunction with Bank preparations for application of the Basel II regulations, and in accordance with Bank of Israel directives on this issue, the Bank completed in 2007 a gap review with regard to operating risk. The Bank has started taking action to eliminate the gaps identified.

To this end, the Bank has established a department at Bank headquarters which would collect and identify operating risk components from all Bank departments. In addition to this department, as an additional layer, the Bank operates the Operating Risk Control Department, focused on actions taken to reduce operating risk and on capital calculations required as per Basel II guidelines. Understanding that operating risk requires an integrative viewpoint, both these departments report to the Bank's Operating Risk Manager. Another layer in the area of operating risk is that of internal audit, which acts independently. The Bank approach is that responsibility for operating risk management lies primarily with managers and staff of the different lines of business.

In 2007, the Bank completed operating reviews which mapped these risk elements for most Bank departments. These reviews are one of the major tools used in identifying operating risk.

Findings of these operating risk reviews, as well as reports of relevant events, are discussed by the Steering Committee on Operating Risk and Information Security, headed by a member of the Executive Management. The Bank is taking action to eliminate gaps as they are identified, and to improve control 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.

Bank policy on operating risk stipulates that this is an organizational and cultural process. Hence, the Bank started carrying out preliminary reviews in several Bank departments in order to set clear standards for collection of failure events, reporting by contact persons for operating risk, operation of computer systems for locating and identifying operating risk etc. These pilot implementations are intended to aid the Bank in increasing awareness and fostering an organizational culture of dealing with operating risk.

As of end of 2007, the Bank is undergoing a process to upgrade Bank policy on operating risk and to adapt existing policy to requirements of Basel II and of Bank of Israel. Furthermore, the Bank is upgrading its business continuity policy and adapting it to Basel II requirements.

Information security

In accordance with Proper Conduct of Banking Businesses Regulation 357, the Bank appointed a Information Security Director, who reports to the Director of the Controllership, Planning and Operations Division. The information security unit, headed by the Information Security Director, is responsible for prescribing the Bank's information security policy, for developing information security software, and to follow-up its implementation in the Bank, examining the effectiveness of the information security system and dealing with exceptional information security events. Information security policy at the Bank is implemented, *inter alia*, by the Information Security Department of Mehish Computer Services Ltd., a wholly-owned subsidiary of the Bank. See also under chapter on IT above.

Legal risk

Proper Conduct of Banking Businesses Regulation 339 prescribes, *inter alia*, that banking corporations must take action to reduce the legal risk resulting from their various operations. According to the regulation, the legal risk is "the risk of a loss resulting from not having the possibility of legally enforcing an agreement".

Within the scope of the Bank's preparations to manage legal risk and comply with the regulation, a Legal Risk Manager was appointed, with the function of managing this risk and taking action to reduce them. As part of the risk management plan, the Bank analyzed the elements of the legal risk in its operations (such as: absence/existence of an agreement and possibility of its enforcement), the ranges of risk (type of agreement, identification of the other party, creation of security, etc.) and the specific risk characteristics of the different risk ranges, while examining the level of risk and exposure.

The Bank prescribed procedures that facilitate the minimizing of legal risk in operations and in the different units of the Bank. The procedures prescribe, *inter alia*, the interfaces between the legal counsel system of the Bank and its various units; specify the kinds of agreements that the Bank is permitted to sign and the procedures for their drafting; determining the manner in which the other side to an agreement is evaluated, including his authority to act on behalf whoever is acting on behalf of others; and define the manner in which the collateral is to be obtained and recorded. Also specified was the share of the legal system in preparation of the Bank's internal procedures and in preparing the resultant documents and forms.

The legal system of the Bank regularly monitors developments in legislation, regulation and rulings, which could have implications for the day-to-day activities of the Bank's units. The Bank acts to minimize the risk based on these developments and according to their implications. Likewise, the legal system prepares, as needed, the updates needed in uniform agreements used by the Bank, for all the framework agreements to which the Bank is a party and in legal opinions that constitute a basis for the undertakings.

The Bank's IT systems support the management of legal risk, *inter alia*, through the production of computerized standard legal documents and following-up on the receipt of collateral. Likewise, the Bank uses specialized IT systems to monitor the statutory registration of certain collateral.

The principles of procedures binding on Bank departments in Israel with regard to legal engagements, are also binding on Bank branches overseas, with these branches making use of services of local external attorneys vetted by the Legal department in Israel. In addition, the Bank set specific guidelines for each branch which are in line with the unique terms and risk facing that branch.

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 the regulations applicable to a banking corporation.

Proper Conduct of Banking Business Regulations No. 308, published on January 17, 2002, requires banking corporations to appoint a Compliance Officer as part of actions taken by them to comply with consumer directives which apply to bank relationships with its customers and to compliance with provisions of the Money Laundering Prohibition Act, and as part of risk management by the Bank. This is done in order to reduce the probability of violation of laws and regulations and lead to early discovery of such violations, and to reduce the Bank's exposure to claims, damage to its reputation and damages that it could sustain as a result of these.

According to the regulation, the Bank conducted in 2002 a survey of infrastructures, in which the consumer regulations were mapped, procedures, IT and control systems suitable for the Bank's different work processes, risk of deviating from the regulations were identified and the controls and requirements for closing the gaps identified were specified. Also, subsequently to completion of the aforementioned mapping, the Bank closely monitors new legislation, including Bank of Israel directives and court verdicts published from time to time, to review Bank compliance with applicable provisions.

Within the scope of the Group's preparations for compliance with the Proper Conduct of Banking Businesses Regulation 308, a Compliance Unit commenced operation in 2002, led by a Compliance Officer who is also responsible for implementing the Prohibition on Money Laundering Law 2000 and the Prohibition on Financing Terrorism Law, 2005, as discussed below. Additionally, a committee was appointed to assist the Compliance Unit in fulfilling its obligations.

The Compliance Unit updates, as needed, the requirements for eliminating gaps, if any, in accordance with current law and monitors processing of these requirements, including procedure adaptation and training delivered to integrate the instructions and changes in the IT systems. The objective being to ensure Bank compliance with current provisions.
Within this framework, the Bank launched in December 2007 new courseware, “The Bank and the Consumer – Consumer Regulations”, with the objective of increasing employee awareness and expanding their knowledge in this area. All branch and business-center employees at the Bank are required to undergo a test as part of this courseware.

Prohibition on money laundering and financing of terrorism

The Prohibition on Money Laundering Law 2000 and the Prohibition on Financing Terrorism Law, 2005, and the laws promulgated there under impose obligations on banks to identify customers, record their particulars and report on certain activities carried out through the banking corporation. For further details, see chapter on Legislation and Supervision of Bank Group Operations.

As part of the Bank's preparations to implement the provisions of Proper Conduct of Banking Business Regulation 411 – Preventing Money Laundering, Financing of Terrorism and Identification of Customers, the Bank's Executive Management and Board of Directors approved the Bank's policy regarding customers at risk. Within this framework, the basic list included in the regulation was expanded, and additional tests were added for accounts at risk, which will be subject to special oversight.

During 2007, the Bank continued the activities required to apply the legislative provisions regarding the prohibition on money laundering, including: the update and integration of procedures in the different units and preparation of improvements in the IT systems. In this framework, the Bank launched a new computer system to assist in collecting the subjective reports required pursuant to the Money Laundering Prohibition Act, in collecting required information for them and in control and monitoring of processing of these reports.

Moreover, employees were given training and the educational material related to the prohibition on money laundering and the related tests. The actions taken led to increased awareness of the subject and consequently – to an increase in the number of reports sent to those responsible for implementing the Law in the Bank.

Control of Risk

Until 2006, the control of risk was carried out by several units. During 2006, the Bank established a Risk Control Unit, which constitutes part of the Controllership, Planning and Operations Division. The Unit consolidates all of the units responsible for controls in the different areas of activity in the Bank will be consolidated in the Department, with clear segregation between the units engaged in the business activities.

Credit risk is controlled via ongoing evaluation of the risk level of Bank customers (loan review) in order to estimate credit quality and in accordance with Proper Banking Conduct Regulation No. 319. Control also takes place for credit at overseas branches. Control activities are gradually being adapted to Basel II requirements.

Market risk and liquidity risk are controlled *inter alia*, through the examination and evaluation of the models used to measure the risk, the data base used in these models and the extent to which the actual activities conform to the exposure principles and limitations approved by the Board of Directors and Executive Management. The Risk Monitoring Forum, headed by the Director of the Controllership Division, meets monthly to discuss issues related to the control of risk and the methodologies for measuring risk. Control includes back testing of models used to calculate exposure.

Operating risk management and control is taking action to implement Bank policy concerning operating risk, in accordance with guidelines of Basel II and Bank of Israel.

Day-to-day control is used for exposure from customer trading in the capital markets, on the customers' compliance with the facilities and limitations prescribed for their activities in the Bank.

The dealing room operations are also controlled, including testing of compliance with various limitations prescribed by the Board of Directors and Executive Management and testing of exceptional trades.

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	Low
Interest risk	Low
Inflation risk	Low
Exchange rate risk	Low
Share price risk	Low
Liquidity risk	Low
Operating risk	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.

Management's assessments were made, *inter alia*, based on the assumption that credit risk and operational risk are always considered more significant than market risk, from a statistical standpoint.

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's Executive Management believes that giving of itself in this manner, not only contributes to the community, but expresses the spirit and character of the Bank, contributes to creating an atmosphere of commitment, "pride in the unit" and identification among the workers and managers, and eventually also makes its mark on the business accomplishments.

Since 2005, the Bank has concentrated on 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. In 2006 the Bank shifted from a situation of response to initiation and focus, similar to other business organizations, which have adopted a defined and clear policy of social involvement.

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.

In order to emphasize the importance that the Bank attributes to this strategic process, a new social brand was launched, containing the logo and name “**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 dispersal of activities, while utilizing the Bank's dispersal, the existence of extensive partnerships with communal organizations throughout the country, and intensified intra-organizational and extra-organizational community involvement.

As a result of the strategic processes carried out in this area, the budget allocated for community activities was increased substantially, and concurrent with the focus on a defined social area, a structured, ongoing process of participation by all of the Bank's employees in the extensive community activities was initiated by the Bank. In the spirit of the values of the Bank's brand – initiative, reciprocity and extra – the employees were called upon to be partners in the community projects supported by the Bank. Consequently, 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.

Within the scope of the Bank's community program, activities are conducted at every location where the Bank has a business presence, while maintaining a broad partnership with local social and communal organizations.

More than 100 of the Bank's branches have forged ties with 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.

The range of "**Mizrahi Tefahot in the Community"** activities includes projects on Jewish holidays and assistance provided to underprivileged populations routinely, as well as in times of crisis.

Additionally, during 2006 and 2007, unique ventures – various lateral projects were carried out related to conveying life-skills to children and youth, in order to assist them in making a future for themselves and establishing a better life, and in assisting the population of special-needs children.

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. Furthermore, a program to support the Ethiopian immigrant community in Sderot was formulated, in partnership with local social organizations, a unique informational guide "Added Value" was produced containing products that are produced by social organizations through people with special needs aimed at assisting the population treated by these organizations in gaining exposure for and sales of their products. The bank is promoting an organizational culture which encourages purchasing of gift items from the “Added Value” catalog for various Bank-managed events.

In order to expand the range of partners in these activities as much as possible, the Bank initiates projects to add additional stakeholders - employees and their families – via projects like “Children for Children” and “This Child is You”; customers – continuation of a project to include Bank customers in the designation of charitable donations to social organizations focused on helping children and youth, to whom the Bank provides support for social ventures.

The activities of **"Mizrahi-Tefahot in the Community"** are succeeding in significantly advancing many social segments and areas, while enabling the Bank's employees a broad cushion for self expression and emotional empowerment.

The Bank intends to significantly expand during 2008 its activity in the field via branches and Head Office units that have not yet forged ties with suitable organizations in the community, and to intensify activities with organizations already adopted by the Bank.

Several new ventures will be carried out in cooperation with different social organizations, such as: “Heart wish” – project to realize dreams of seriously-ill children; project with ELEM, which works with at-risk youth to improve effective communications skills; and the “So Can I” project with the Ministry of Education in which students will assist in providing technological solutions for different handicaps.

In 2007, the Bank Group allocated NIS 3.1 million to social involvement and charitable donation, compared to NIS 2.6 million in 2006. In addition, Bank employees and managers invested in 2007 over 24,000 hours in community work on different projects.

Disclosure concerning the Internal Auditor

Details of the Internal Auditor

Below is information on the Chief Internal Auditor of the Mizrahi Bank Group:

Name	Haim Git
Start of term in office	February 1999
Education	Certified Public Accountant; BA in Accounting (Tel-Aviv University), Accountancy Certificate (Hebrew University)
Experience	Chief Internal Auditor – responsible for auditing with the Supervisor of Banks at the Bank of Israel. Deputy Chief Internal Auditor in Mizrahi Bank.

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 his position as Chief Internal Auditor, other than as Ombudsman. Furthermore, the Bank's Internal Auditor holds no position outside of the Bank which creates or may create conflict of interest with his position as Internal Auditor.

Pursuant to Section 8 of Banking Regulations (Internal Audit), 1992 audit staff is only appointed with consent of the Internal Auditor. Audit staff act on behalf of the Internal Auditor for the purpose of internal audit, and are only instructed on audit-related matters by the Internal Auditor. Internal audit staff do 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. Internal audit employees are terminated with due process and consent of the Internal Auditor.

The Internal Auditor holds 96,000 options to purchase 96,000 ordinary Bank shares of NIS 0.1 par value.

The Board of Directors believes that the extent of Bank securities owned by the Internal Auditor does not impact the quality of his work.

The Internal Auditor is a full-time employee of the Bank.

Appointment

In February 1999, appointment of the Internal Auditor was confirmed by the Audit Committee and the Board of Directors, based on the Auditors experience and educational qualifications.

Identity of the Internal Auditor's Supervisor

The official in the organization responsible for the Internal Auditor is 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 (for IT – 5 years), 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).
- Surveys of risk centers for embezzlement and fraud carried out in the Bank.
- Survey of risk of the IT system performed by the auditing group.
- Findings of the last survey of controls in the supplementary detailed report of the independent auditor.
- Regulatory requirements arising from directives of the Supervisor of Banks.
- Current audit reports of the Bank of Israel.
- Findings in audit reports of the auditing group.
- Decisions of the audit committee and requests of the Bank's President.

The multi-annual work plan is compiled by the Internal Auditor and brought up for discussion by the Board of Directors' Audit Committee. Concurrently, the plan is submitted to the President. After the Board's Audit Committee recommends approval of the plan, the plan is submitted for approval by the Chairman of the Board of Directors.

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 and the President.

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 compiled by the Internal Auditor and brought for discussion by the Board's Audit Committee. Concurrently, the plan is submitted to the President. After the Board's Audit Committee recommends approval of the plan, the plan is submitted for approval by the Chairman of the Board of Directors.

As for review of material transactions during the reported period by the Internal Auditor, note that the Internal Auditor has not reviewed the transactions for sale of provident funds and their operations.

Overseas audits or audits of held corporations

The Bank's Internal Auditor includes in the annual and multi-year audit program the active corporations held by the Bank, during his tenure as their internal auditor, except for two banking subsidiaries (Bank Adanim and Bank Mizrahi Switzerland) that had their own internal auditor during the reporting period. With respect to these companies, the Internal Auditor verifies on a regular basis that there is proper internal auditing as required by the banking regulations.

Scope of the employment of the Internal Auditor and his 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 2007, 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
(1) 39.25	6	(2) 1.5

(1) Includes 2 internal audit employees as well as assistance of external resource, at ¼ of a full time position, at Bank Adanim. In addition, internal audit at Bank Mizrahi-Tefahot had outsourced help equal to 1.5 full time positions through February 2007 and to 4.5 full time positions for the remainder of the year.

(2) Includes use of external resources at Mizrahi Switzerland and at the Los Angeles branch.

The Bank of Israel's Audit Report from December 2005 stated, that as a result of changes in the mapping and assessment of risk and the implications deriving from requirements, such as Basel II and implementation of the requirements of the Sarbanes Oxley Act regarding the nature and scope of the audit work, the manpower inputs reporting to the auditor should be increased, and personnel should be refreshed from the standpoint of the percentage of employees who have relevant degrees, the seniority of audit employees and the intensity of employee training.

The audit committee of the Bank's Board of Directors discussed the said Bank of Israel Audit Report at several meetings. At its meeting on February 12, 2007, it resolved to approve the audit plan for 2007 that was submitted by the Chief Internal Auditor. It was also decided that the additional manpower needed to carry out the plan for 2007 and the quality of the manpower would be met through outsourcing (addition equivalent to 4.5 full time positions), in accordance with the assignments needed to carry out the audit plan, and now by adding permanent job slots.

In October 2007 the Audit Committee decided to convert 2 such slots, approved as outsourcing in February 2007, into 2 permanent slots for internal staff. Internal audit is acting to implement the Committee’s decisions.

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 and regulatory authorities’ instructions relevant to the audited area, including guidelines and directives of the Supervisor of Banks.
- Standards for Professional Engagement in Internal Audit of the Institute of Internal Auditors in Israel.

  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, 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 a quarter, the Auditor files a summary of all the reports distributed during the quarter as part of the reporting to the audit committee members.

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 sits, in consultation with the Internal Auditor, and after the Chairman of the Board is informed, determines which internal audit reports are significant, to be brought for discussion before the audit committee.

In accordance with Section 6(B)(2) of the Banking Rules (Internal Audit), 1992, a semi-annual list was distributed on July 5, 2007, within the framework of the report on performance of the work plan for the audit for the first half of 2007. The report was presented at the meeting of the audit committee held on July 9, 2007. The annual summary report of the internal audit work for 2007 was submitted to members of the Audit Committee on February 13, 2008. The report was discussed at the meeting of the audit committee held on February 18, 2008. The other major reports were discussed during the year, at the monthly 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.

Compensation of the Internal Auditor

For details of compensation and payments to the Internal Auditor, see under the chapter on Remuneration of Senior Officers.

The Board of Directors believes that the size of compensation provided to the Internal Auditor should not influence his judgment with respect to his work.

Accounting Policy on Critical Matters

The consolidated financial statements of the Group are prepared in conformity with generally accepted accounting principles and in accordance with the directives and guidelines of the Supervisor of Banks on the preparation of the 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:

Specific provision for doubtful debt, except on housing loans, is based on a specific evaluation of the quality of the loans, while relating to a range of factors having influence, and also through an automatic mechanism that scans the Bank’s credit portfolio and indicates problem loans according to set parameters, for the purpose of a specific examination. The problem loans were classified and the provisions determined according to a ranking of authorities of various managers in the Group, based on the following criteria: the risk related to the loan portfolio, the scope and quality of information on the borrower held by management, his business activities, how he has fulfilled his obligations and the value of the collateral that he furnished. The actual losses could turn out to be different than the specific provisions made.

On December 31, 2007, the Supervisor of Banks issued a circular on “Measuring and Disclosure of Impaired Debt, Credit Risk and Provision for Credit Loss”. According to this circular, the Bank will implement, as of January 1, 2010, new directives with regard to impaired debt. Implementation of this directive would cause a change in estimate and recording of specific provision for doubtful debt. For further information on the new directives, see Note 1.X. to the financial statements.

Provision for doubtful debt according to length of arrears, which is calculated for housing loans in accordance with the guidelines of the Supervisor of Banks, whereby provision coefficients are determined based on the length of arrears in the repayment of the loan. The length of the arrears in repayment of a loan is an objective element of data, although the provision coefficients are prescribed by the Supervisor of Banks. A change in the coefficients or allocating them to other lengths of arrears, could cause a change in the amount of the provision for doubtful accounts. Likewise, the actual losses could turn out to be different from the provision made based on the length of arrears.

On January 1, 2006, the Bank of Israel published a circular on the manner in which the provision by extent of arrears is to be calculated. For details on guidelines included in this circular, see Note 1.P.3) to the financial statements.
The cumulative impact of implementation of this circular was additional provision for doubtful debt by extent of arrears amounting to NIS 54 million.

Supplementary provision for doubtful debt is computed in accordance with a formula prescribed by the Supervisor of Banks, and according to the classifications of problem loans that were determined at the discretion of the various managers, based on procedures prescribed on the matter, and additional principles that were prescribed in the Proper Banking Conduct Regulations. A change in the method of classifying debt and modifying the coefficients could cause a change in the level of the required provision. It should be noted that the supplementary provision is not recognized for tax purposes, so that its effect on net profit is the full amount of the provision.

For details of balance and movement of provision for doubtful debt in 2007, see Note 4.C. to the financial statements.

Financial derivatives are treated and presented in accordance with the public reporting guidelines of the Supervisor of Bank, which are based on the American Standards FAS 133, FAS 149 and FAS 155. According to the guidelines, all derivatives are stated in the balance sheet at fair value. The fair value of the derivatives is determined according to quoted market prices in active markets, or according to acceptable economic models, which include assumptions and variables that are evaluated regularly to adapt them to current market conditions. A change in the economic assumptions and variables will lead to a change in the fair value of the derivatives.

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. 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.

Liabilities for employee rights are computed 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%. For each 0.25% increase / decrease in the discount rate, the actuarial liability would decrease / increase by NIS 4 million.
The financial statements include the benefit value of the stock option plan for Bank managers, estimated 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 share, the standard deviation for the Bank's share and other factors which could affect the economic value of the benefit.
The benefit value in Bank accounts is allocated over the term in which Bank management assumed the options would be granted. For further details, see Note 1.M.

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. 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 assets is made in accordance with Accounting Standard No. 15 "Impairment of Assets". Provision for impairment, if needed, is based on assessor valuations and is updated by the assessor as required.

The Bank balance sheet as of December 31, 2007 includes a provision for impairment amounting to NIS 3 million.
In 2006, the Bank sold 5 assets whose carrying amount included provision for impairment, as per assessment obtained, amounting to NIS 19 million. In 2007, the Bank recoded an after-tax profit from extraordinary items amounting to NIS 7 million.

Deferred taxes are calculated for temporary differences between revenues and expenses included on the financial statements and amounts accounted for tax purposes. In cases where the revenue or expense recognition date for tax purposes is later than the date of recording the revenue or expense in Bank accounts, the deferred tax balances are calculated using the expected tax rates upon recognition of the expense or revenue for tax purposes, as known soon prior to the approval date of the financial statements.
Deferred tax benefits are recorded for temporary differences expected to generate a tax benefit on the date of reversal. As set forth in Note 28 to the financial statements, the Bank's balance sheet included net deferred taxes amounting to NIS 233 million.
An increase of 1% in tax rates would cause a decrease of NIS 6 million in the provision for taxes.

Critical estimates

The financial statements for the year ended December 31, 2007 include critical estimates with regard to impairment of a non-temporary nature of several investments in asset-backed securities, with a total original investment of $35 million (NIS 157 million).
In order to estimate the aforementioned impairment, it was assumed that quotes obtained from the security issuer reflect, as of the date of the financial statements, the value of these investments, and that the impairment compared to total original investment is of a non-temporary nature, mainly in view of the significant impairment and the extended time in which the quoted value has not increased. The value of these investments on financial statements for December 31, 2007 is $5 million (NIS 22 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 $5 million (NIS 22 million), should it emerge that the investment value continued to decline, to recording a further revenue amounting to $30 million (NIS 114 million) should it turn out that the full impairment was temporary.

Approval process of the financial statements

Bank financial statements are compiled by a professional department, headed by the Chief Accountant, pursuant to the disclosure policy set by the Bank's Board of Directors.
Concurrently with compiling the financial statements, 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 of 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 of the internal audit of 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.
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. The issues presented to the Disclosure Committee also include the professional opinion of the auditing CPA. These matters of principal include issues with material impact on the financial statements, of interest to the public, issues requiring disclosure to the public, material changes to application of accounting policy, requests or demands by regulatory authorities and issues on which Bank management and the auditing CPA differ.
The Disclosure Committee recommends to the Board's Balance Sheet Committee how to implement the disclosure policy. The Board's Balance Sheet Committee discusses the issues requiring disclosure and issues raised by the Disclosure Committee, and specifies the required disclosure in public statements on issues requiring disclosure. Pursuant to directives of the Supervisor of Banks on implementation of provisions of Section 302 of the US Sarbanes-Oxley Act, the Balance Sheet Committee receives a report on any significant fault discovered in the disclosure process in the financial statements. All said issues are also presented to the Board's Audit Committee, and reports on significant faults are also presented to the Board of Directors. Following discussion by the Board's Balance Sheet Committee and based on its recommendations; the financial statements are approved by the Bank's Board of Directors.

Independent Auditor’s report

The Independent Auditor drew attention in the Auditors' Opinion to the following:
See Note 19.D)13)a-c to the financial statements regarding claims filed against the Bank and motions for their recognition as class actions including in the matter of insurance.

Controls and Procedures

In accordance with the public reporting directives of the Supervisor of Banks, based on Section 302 of the American Sarbanes Oxley Act, beginning from the interim financial statements at June 30, 2005, 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 is part of an overall policy planned for implementation in the coming years, regarding the adoption of the provisions of Section 404 of the Sarbanes Oxley Act, which includes, *inter alia*, certification by the President and Chief Accountant on "the effectiveness of internal controls on the financial reporting", which will be attached to the financial statements in the future.

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 Disclosure Certification is not meant to cover the broad aspects of "the Effectiveness of the Internal Controls on the Financial Reporting", as noted.

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.

During the quarter ended December 31, 2007, 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 control over financial reporting.

Executive Management

Bank’s Executive Management team:

Eliezer Yones	President	
Menachem Aviv (1)	Vice-President	Manager, Accounting & Financial Reporting Sector and Chief Accountant
Israel Engel	Vice-President	Manager, Retail Division
Shimon Gal (2)	Vice-President	Manager, Corporate Banking Division and Credit Risk Manager
Na’ama Gat	Vice-President	Manager, Marketing, Promotion and Business Development
Eldad Fresher	Vice-President	Manager, Finance Division – CFO and Market Risk Manager
Sammy Keinan (3)	Vice-President	Manager, Customer Assets and Consultancy Division and Manager, Information Technology
Rita Rubinstein	Vice-President	Manager, Human Resources and Administration Division

Haim Git	Chief Internal Auditor
Dr. Shimon Weiss	Chief Legal Advisor and Legal Risk Manager
Maya Feller	Corporate Secretary
Benny Shoukroun	Bank Spokesman

(1) On May 31, 2007, Mr. Menachem Aviv was appointed member of the Bank Executive Management.

(2) On January 1, 2008, Mr. Shimon Gal was appointed Corporate Banking Division Manager and Credit Risk Manager, replacing Mr. Shaul Gelbard who resigned from the Bank's Executive Management.

(3) On October 31, 2007, Mr. Sammy Keinan was appointed Manager, Customer Assets and Consultancy Division, replacing Mr. Yosef Nitzani who resigned from the Bank's Executive Management on October 13, 2007.

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)	Consultant, CEO of Bank Hapoalim

Menachem 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	Chief Accountant Manager, Accounting & Financial Reporting Sector
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)	Manager, Accounting and Financial Reporting Division – Bank Mizrahi-Tefahot Ltd.

Senior Officers – Cont.

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
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)	Vice-president and Manager, Financial Division, Bank Tefahot President and Manager, Financial Division, Bank Tefahot

Haim Git

Start of term in office	February 1999
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Chief Internal Auditor Manager, Internal Audit Department
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.

Senior Officers – Cont.

Shimon Gal

Start of term in office	(1) 2.5.2004
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	BA in Economics and Statistics – Hebrew University, Jerusalem
Business experience (in past 5 years)	Manager, Comptrollership, Planning and Operations Division, Bank Mizrahi-Tefahot Ltd.; VP, Finance Division, Investec Bank

Na’ama Gat

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
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, Business Unit, Strauss-Elite

(1) On January 1, 2008, Mr. Shimon Gal was appointed Manager, Business Banking Division and left the position of Manager, Comptrollership, Planning & Operations Division.

Senior Officers – Cont.

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.Ju. – Hebrew University, Jerusalem; MBA – Tel Aviv University
Business experience (in past 5 years)	Chief Legal Counsel, Bank Mizrahi-Tefahot Ltd.

Dov Fogel

Start of term in office	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	MBA (Strategic Management) – Hebrew University, Jerusalem
Business experience (in past 5 years)	Manager, Logistics, Administration and Efficiency Division with the Bank

Senior Officers – Cont.

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)	Corporate Secretary

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
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)	Deputy Comptroller-General with the Ministry of Finance; Senior Deputy Comptroller-General with the Ministry of Finance

Senior Officers – Cont.

Sammy Keinan

Start of term in office	1.11.2007
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Customer Assets and Consultancy Division and Manager, Information Technology
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)	CEO, Mehish Computer Services Ltd.; Manager, Information Technology - Partner

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)	Senior VP, Human Resources at Paradigm

Remuneration of Senior Officers

(NIS in thousands)

	Salary and bonus	Share-based payment transactions	Severance pay, pension payments, study fund, vacation, national insurance (1)	Supplement to provisions for related expenses, due to changes in salary during fiscal year	Total salary and benefits, excluding payroll tax	Loans and guarantees provided under beneficial terms: Balance at end of year (2)	Loans and guarantees provided under beneficial terms: Average term to repayment (in years)	Loans and guarantees provided under beneficial terms: Benefit granted during the year	Loans and guarantees provided under normal terms	Other benefits
2007										
J. Perry	(3)2,220	-	175	5	2,400	27	-	5	193	62
E. Yones	4,690	(4) 4,800	643	36	10,169	-	-	-	34	64
R. Rubinstein	1,297	(5) 369	630	-	2,296	67	1.0	2	7	38
I. Angel	1,300	(5) 122	304	9	1,735	177	1.7	5	42	45
S. Gal	1,294	(5) 122	281	3	1,700	18	-	1	8	40
S. Gelbard (6)	1,347	(5) 122	2,944	15	4,428	488	2.2	4	31	54
Y. Nitzani (7)	979	(5) 122	1,779	3	2,883	797	6.3	2	-	39
H. Git (8)	1,188	(5) 97	277	9	1,571	142	2.1	2	17	51
2006										
J. Perry	2,140	-	307	5	2,452	118	-	4	261	60
E. Yones	4,692	(4) 4,800	751	39	10,282	-	-	-	49	60
S. Gelbard	1,305	(5) 257	230	8	1,800	543	6.3	4	22	55
E. Fresher	1,322	(5) 257	202	14	1,795	-	-	-	41	39
J. Nitzani	1,265	(5) 257	247	11	1,780	809	6.8	2	-	60
S. Messenberg (9)	773	(5) 134	5,585	-	6,492	303	6.3	3	25	42

(1) Includes provisions for severance rights and acclimation grants.

(2) Also includes loans that were given at identical terms to all of the Bank's employees.

(3) Includes bonus for 2007, approved by the Audit Committee of the Board of Directors and subject and is subject to approval of a General Meeting.

(4) Pursuant to his employment agreement, Mr. Yones is entitled to options to purchase the Bank's shares, in accordance with an approved plan. The options will be conveyed to Mr. Yones beginning from April 1, 2005, subject to exceptions provided in the agreement. NIS 4,800 thousand was recorded in the statement of profit and loss, representing the pro rata share of the theoretical benefits amount inherent in this plan. See Note 16.A.1 to the financial statements for details.

(5) Bank managers are entitled to an allotment of options to purchase the Bank's shares, in accordance with an approved plan. Options will vest in 3 parts. The pro rata share of the theoretical benefits amount inherent in this plan was recorded in the statement of profit and loss. See Note 16.A.2 to the financial statements for details.

(6) Resigned from the Bank's Executive Management on December 31, 2007.

(7) Resigned from the Bank's Executive Management on October 13, 2007.

(8) Salary of the Chief Internal Auditor is presented as required by Public Reporting regulations.

(9) Resigned from the Bank's Executive Management on July 16, 2006.

The Board of Directors based its determination of salary and bonuses on the contribution of the members of Executive Management to the Bank's operations and its profitability.

Auditors' Fees[1][2][3]

(NIS in thousands)

	Consolidated		The Bank	
	2007	2006	2007	2006
For audit activities[4]:				
Independent auditors [5]	4,177	4,391	4,121	4,255
Other auditors	1,222	1,659	-	535
Total	5,400	6,050	4,121	4,790
For other services:				
Services related to the audit[6]:				
Independent auditors	43	15	42	15
Other auditors	-	-	-	-
For tax services[7]:				
Independent auditors [5]	213	167	212	167
Other auditors	37	30	-	-
For other services:				
Independent auditors [5][8]	1,477	477	1,466	477
Other auditors	126	90	-	-
Total	1,896	779	1,720	659
Total fees to auditors	7,296	6,829	5,841	5,449

(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) Includes mainly: 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 are presented below:

Jacob Perry

Membership of Board of Directors' committees	Management, Credit, Remuneration
Independent Board member?	No
Has accounting and financial expertise?	No
Has professional qualifications?	Yes
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	Chairman, Board of Directors of Bank Mizrahi-Tefahot
Start date in office as member of the Bank's Board of Directors	24.2.2003
Education	BA in Oriental Studies and Jewish History – Tel Aviv University; Advanced Course in Budget Management, Marketing and Economy - Harvard Business School
Current occupation	Chairman, Magal Ltd.; Board member, Yeftel Holdings (privately held); Chairman, Pinpoint Advance Corp.; Board member, Fitech Technologies Ltd.; Chairman, B-Contact Ltd.; Chairman, MID Ltd.
Previous occupation (in past 5 years)	President and CEO, Cellcom Israel Ltd.; Chairman of the Board of Directors, Lipman Electronic Engineering Ltd.; Chairman, Allo Telecom; Chairman, Pinpoint Advance Corp.; Board member, Amad 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

Zvi Ephrat

Membership of Board of Directors' committees	Credit. Remuneration
Independent Board member?	No
Has accounting and financial expertise?	No
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	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
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 – Cont.

Joseph Bahat

Membership of Board of Directors' committees	Audit, Credit, Balance Sheet, Management, Remuneration
Independent Board member?	Yes
Has accounting and financial expertise?	No
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	14.12.2003
Education	B.Sc. in Economics – Hebrew University, Jerusalem
Current occupation and in the past 5 years	Chairman, Smart Energy Solutions Inc.
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	Credit
Independent Board member?	No
Has accounting and financial expertise?	No
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	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, Gover Radio Ltd.; Board member, R. Gazit Attorney (2002)
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 – Cont.

Moshe Wertheim

Membership of Board of Directors' committees	Management, Remuneration
Independent Board member?	No
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?	Board member, MWZ (Holding) Ltd.; Managing Partner, F&W (Registered Partnership); Chairman, Central Bottling Company Ltd. (Coca Cola)
Start date in office as member of the Bank's Board of Directors	24.1.1995
Education	LL.M; Attorney; Certificate in Business Administration – Hebrew University, Jerusalem
Current occupation and in the past 5 years	Chairman, Central Bottling Company Ltd. (Coca Cola), Keshet Broadcasting Ltd., Keshet Communication Services Group Ltd. Board member, Alony Hetz Ltd. (public), M. Wertheim (Holdings) Ltd., Ilanim Development and Investments Ltd., MWZ Holding Ltd., Info-Prod (Middle Eastern Research) Ltd., F&W (Registered Partnership), T.T. Transport and Marketing Services (1987) Ltd., Mada'im Shimushim (2000) Ltd., IMPG Management Ltd., TSRON Management Ltd., W.H.M. Properties Ltd., Alcorp Ltd., Ramcon 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 – Cont.

Avi Ziegelman

Membership of Board of Directors' committees	Audit, Balance Sheet
Independent Board member?	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	19.9.2007
Education	BA in Accounting and Economics – Tel Aviv University; MA in Business Economy (Finance) – Tel Aviv University; CPA
Current occupation	Financial consultant and Board member, Board member, Plastro Irrigation Systems Ltd. (independent Board member);Tafron Ltd.; Baram Industries Ltd.; Gindi Investments 1 Ltd.; Milomor Trade and Communication Ltd. (independent Board member); Pangaya Real Estate Ltd.; King Ltd. (independent Board member); Simcha Uriely and Sons Ltd.; Ilex Medical Ltd. (independent Board member); fox Wiesel Ltd., Orev Technologies 1977 Ltd. (independent Board member), PMS Group Ltd., Cialo Technolgoy Israel Ltd. (independent Board member), Clal Biotechnolgy Industries Ltd. (independent Board member), Arpal Aluminum Ltd.
Previous occupation (in past 5 years)	Senior Partner, Head of Professional Practice, KPMG Somech Chaykin; Board member and financial consultant
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 – Cont.

Dov Mishor

Membership of Board of Directors' committees	Audit, Credit, Balance Sheet
Independent Board member?	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	29.1.2007
Education	BA in Economics and Political Science, MA in Economics – Hebrew University, Jerusalem
Current occupation	Financial consultant, Board member, Guy Development Ltd. Instructor, Department of Economics, Ben Gurion University
Previous occupation (in past 5 years)	Board member, Bank Leumi; Ashot Ashkelon Industries Ltd.; Guy Development; President of Israel-Asia Trade Chamber
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 – Cont.

Abraham Natan

Membership of Board of Directors' committees	Audit, Credit, Balance Sheet, Management, Remuneration
Independent Board member?	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	31.7.2003
Education	BA in Economics, MA in Political Science (Public Administration) – Bar Ilan University
Current occupation	Board member, Kamor Ltd., Executive, Maccabi Israel, Member, Audit Committee, Israel Football Association
Previous occupation (in past 5 years)	Chairman, Ashot Ashkelon, Chairman of the Council of the Israel Broadcast Authority, Independent Board member, TAMAM Amnir, Chairman of the Board of Directors, Government Medals and Coins Company
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 – Cont.

Yehuda (Yuli) Ofer

Membership of Board of Directors' committees	Management
Independent Board member?	No
Has accounting and financial expertise?	No
Has professional qualifications?	Yes
Employed by the corporation, a subsidiary/affiliate or by an interested party in the corporation?	Chairman, Ofer Brothers Properties (1957) Ltd.
Start date in office as member of the Bank's Board of Directors	15.9.97
Education	High school
	Business manager and executive, Board member, Ofer Bros. Engineering and Development Ltd., Ofer Bros. (Eilat) Ltd., Ofer Bros. (Haifa 5734) Ltd., Ofer Bros. (Jerusalem) Ltd., Ofer Bros. (Ra'anana) Ltd., Ofer Bros. (Ashkelon Industries) Ltd., Ofer Bros. Holdings (1989) Ltd., Ofer Bros. Properties Holdings Ltd., Ofer Bros. Investments Ltd., Ofer Bros. Foreign Investments Ltd., Ofer Bros. Properties (1957) Ltd., Mercazim 2001 Management Company (1995) Ltd., Electric Wires (Properties) Ltd., Coral Beach Eilat Ltd., Coral Beach Haifa (1996) Ltd., Yuldan Investments Ltd., C.A.B.M. Ltd., Carmeli Yuliad Ltd., Mivnei Oferim Ltd., Melissa Ltd., Melisron Holdings (1997) Ltd., Melisron Ltd., Meliper Trading Company 93 Ltd., Meliper Kanyonim Ltd., Ne'ot Coral Beach (1990) Ltd., C.E.D. Israeli Investment and Development Co. Ltd., Sam Shechter (Trading) Ltd., E.A.B.M. Ltd., Ofer Mercazim Ltd., Ofer Properties Ra'anana Ltd., Ofer Industrial Properties (Nazareth) Ltd., Ofer Development and Investments Ltd., Ofer Sailing and Recreation Ltd., Ofer Commercial Centers Ltd., Ofer Commercial Centers (Maof Management) Ltd., Renanim Shopping Center (Management) Ltd., Kiriyon Shopping Center Ltd., Mi-Del Properties Ltd., Ashkelon Marina (Management) (1992) Ltd., Mistletoe Holding B.V., Chutzot Hamifratz – Management Company Ltd., "Sahaf" Contracted Projects (1975) Ltd. (inactive), Sahaf (Mechanical Engineering Equipment) Ltd. (inactive).
Current occupation	
Previous occupation (in past 5 years)	Business manager and executive
Family member of another interested party in the corporation?	Father of Ms. Liora Ofer
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 – Cont.

Liora Ofer

Membership of Board of Directors' committees	Credit
Independent Board member?	No
Has accounting and financial expertise?	No
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	23.1.06
Education	High school
Current occupation	Board member: Meliseron Ltd., Uru Investments Ltd., Uru Foreign Investments (1999) Ltd., Halidor Promoters Ltd.
Previous occupation (in past 5 years)	CEO, Almog Beach Company (Eilat) Ltd.
Family member of another interested party in the corporation?	Daughter of 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

Board of Directors – Cont.

Yossi Rosen

Membership of Board of Directors' committees	Management, Remuneration
Independent Board member?	No
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	27.6.2005
Education	BA in Economics and Political Science, MBA – Hebrew University, Jerusalem
Current occupation	Chairman, Oil Refineries Ltd., Chairman, Reshet Noga Ltd. (TV Channel 2), Rose Millennium Investment Ltd., CEO, Ofer Holdings Group Ltd. Board member, ICL Ltd., Zim Integrated Shipping Services Ltd., Carmel Ulpinim
Previous occupation (in past 5 years)	President, the Israel Corporation Ltd., Board member, Dead Sea Magnesium, Tower Semiconductor Ltd., Bromine Compounds Company Ltd., Dead Sea Bromine Ltd., Rotem Amfert Negev Ltd., Dead Sea Works Ltd., Chairman, ICL (through December 31, 2007)
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 – Cont.

Abraham (Beigah) Shochat

Membership of Board of Directors' committees	Audit, Credit, Balance Sheet, Remuneration
Independent Board member?	No
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	23.1.2006
Education	B.Sc. in Civil Engineering, Technion, Haifa
Current occupation	Board member, Israel Chemicals, Israel Chemicals Fertilizers, Energy Inc., Alon U.S.A., Clay Capital Mrakets Ltd., Direct Insurance and Financial Investments Ltd. Chairman, Investment Committee – Israel Infrastructure Fund, IDI Technologies Ltd
Previous occupation (in past 5 years)	Member of parliament
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

During 2007, the Bank Board of Directors held 29 plenary meetings and 61 committee meetings.

The permanent Board committees are: Audit Committee, Financial Statements Committee, Management Committee, Credit Committee and Remuneration Committee.

Presented below are the changes in the Board of Directors during the year 2007 and until the publication date of the financial statements:

- On January 29, 2007, Mr. Dov Mishor was appointed a director in the Bank.
- On May 15, 2007, Mr. Jacob Steinmetz resigned his office as Board member, for concern regarding conflict of interest between his office as independent Board member and his membership of a CPA firm which provided services of a negligible extent to the Bank.
- On September 19, 2007, Mr. Avi Ziegelman was appointed member of the Bank Board of Directors.

On May 21, 2007, Mr. Zvi Ephrat resigned his membership of the Audit Committee, having considered his membership of the Committee and believing that, in view of professional services provided by the law firm of which he is partner, in order to remove any doubt and for the sake of appearances (and not for any other reason), it would be best that he resign his membership of the Audit Committee.

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 each of the Audit Committee and Balance Sheet Committee would have as members at least 2 Board members having accounting and financial qualifications.

At the publication date of these financial statements, there are six directors on the Board having accounting and finance skills: Messrs. Moshe Wertheim, Avi Ziegelman, Dov Mishor, Abraham Natan; Yossi Rosen and Avraham (Beigah) Shochat. Each of the Audit Committee and Balance Sheet Committee has as members 4 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 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 as CPA. Provides financial consulting and serves as Board member with different companies. Was Senior Partner, Head of Professional Department with KPMG Somekh Chaykin CPA.

Dov Mishor

Graduate degree in Economics, Lecturer in the Economics Departments of Ben-Gurion University, Director Guy Yizum Ltd., served in the past as a director in Bank Leumi, Ashot Ashkelon and as President of the Israel-Asia Trade Office.

Abraham Natan

Bachelor of Economics and Business Administration, serves as chairman of the Government Medals and Coins Company, served in past as chairman of the commission and committee of the Broadcast Authority and director of TMM Amnir, as chairman of Ashot Ashkelon Ltd., as State Services Commissioner and a director in Bank Yahav.

Yossi Rosen

Academic education – Economics and Business Administration – President, Israel Corporation Ltd. Former CEO, Israel Corporation Ltd. Serves as chairman and Board member with several companies (see above).

Abraham (Beigah) Shochat

Former Minister of Finance, Member of Knesset, Chairman of the Knesset Economics Committee, Chairman of the Knesset Finance Committee, Minister of National Infrastructures – in these positions he acquired skills and understanding on business and financial statement matters.

The Bank's Board of Directors thanks the President, the management of the Bank and its employees for their efforts to promote the Bank, the result of their diligent efforts to maintain the Bank's services with the appropriate 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 customer base.

Jacob Perry	**Eliezer Yones**
Chairman of the Board of Directors	President

Ramat Gan, March 24, 2008

Management's Review of the Financial Position of the Group and the Results of its Operations

Table of Contents

Management Review - Addendum A
Consolidated Balance Sheet at Year Ends 2003-2007

(In NIS millions)

	2007	2006	2005	2004	2003
		Reported amounts (1)			Adjusted amounts (2)
Assets					
Cash and deposits with banks	10,701	10,797	12,252	10,537	12,725
Securities	6,145	5,979	6,570	5,754	3,976
securities loaned or sold in repurchase agreements (3)	5	-	-	-	-
Credit to the public	74,320	70,109	(4) 65,608	(4) 64,445	(4) 60,571
Loans to the Government	3	4	92	95	111
Investments in investees	17	42	87	120	166
Buildings and equipment	1,246	1,293	1,221	1,150	1,107
Other assets	2,880	2,487	1,409	1,881	1,399
Total assets	95,317	90,711	87,239	83,982	80,055
Liabilities and Shareholders' Equity					
Deposits from the public	75,290	73,234	71,346	69,769	66,221
Deposits from banks	3,752	3,073	3,132	2,900	3,227
Deposits from the Government	282	560	728	998	1,261
Debentures and subordinated notes	6,189	5,067	4,305	3,065	2,706
Other liabilities	4,247	3,710	(4) 3,046	(4) 3,111	(4) 2,482
Total liabilities	89,760	85,644	82,557	79,843	75,897
Minority interest	-	6	6	6	283
Shareholders' equity	5,557	5,061	4,676	4,133	3,875
Total liabilities and shareholders' equity	95,317	90,711	87,239	83,982	80,055

(1) See Note 1.B to the financial statements.
(2) Adjusted for the effect of inflation on the basis of the CPI for December 2003.
(3) See Note 1.G.1) to the financial statements.
(4) Reclassified.

Management Review - Addendum B

Consolidated Statement of Profit and Loss – Multi-period information

For the Years Ended December 31, 2003-2007

(In NIS millions)

	2007	2006	2005	2004	2003
	Reported amounts (1)				
Profit from financing operations before provision for doubtful debt	2,026	1,987	1,904	1,652	1,439
Provision for doubtful debt	228	305	292	359	300
Profit from financing operations after provision for doubtful debt	1,798	1,682	1,612	1,293	1,139
Operating and other revenues					
Operating commissions	1,034	991	924	874	852
Profits (losses) from investments in shares, net	65	50	3	3	(13)
Other income	91	174	187	159	116
Total operating and other income	1,190	1,215	1,114	1,036	955
Operating and other expenses					
Salaries and related expenses	1,169	1,395	1,154	1,089	882
Maintenance and depreciation of buildings and equipment	421	385	349	302	299
Other expenses	348	337	336	288	236
Total operating and other expenses	1,938	2,117	1,839	1,679	1,417
Operating profit before taxes in reported amounts	1,050	780	887	650	677
Erosion and adjustments	-	-	-	-	37
Pre-tax operating profit	1,050	780	887	650	714
Provision for taxes on operating profit	368	349	371	255	342
Operating profit after taxes	682	431	516	395	372
Share in net after-tax operating profits (losses) of affiliates	(1)	(4)	(3)	13	9
Minority interest in net after-tax operating profits of subsidiaries	-	-	-	(19)	(27)
Net operating profit	681	427	513	389	354
After-tax profit (loss) from extraordinary items	227	216	(2)	(3)	(14)
Cumulative after-tax effect, as at beginning of year, of change in accounting method	-	-	(4)	-	(5)
Net profit	908	643	507	386	335

(1) Except for 2003 figures after operating profit before taxes - see Note 1.B to the financial statements.

Management Review - Addendum B
Consolidated Statement of Profit and Loss – Multi-period information
For the Years Ended December 31, 2003-2007

	2007	2006	2005	2004	2003
	Reported amounts (1)				Adjusted amounts (2)
Profit per share (3)					
Basic profit per share (in NIS)					
Operating profit per share	3.08	1.95	2.35	1.78	1.62
Profit (loss) from extraordinary items	1.03	0.99	(0.01)	(0.01)	(0.07)
Cumulative after-tax effect, as of beginning of period, of change in accounting method	-	-	(0.02)	-	(0.02)
Total	411	2.94	2.32	1.77	1.53
Diluted profit per share (in NIS)					
Operating profit per share	3.03	1.91	2.33	1.78	1.62
Profit (loss) from extraordinary items	1.01	0.97	(0.01)	(0.01)	(0.07)
Cumulative after-tax effect, as of beginning of period, of change in accounting method	-	-	(0.02)	-	(0.02)
Total	4.04	2.88	2.30	1.77	1.53

(1) See Note 1.B to the financial statements.
(2) Adjusted for the effect of inflation on the basis of the CPI for December 2003.
(3) Share of NIS 0.1 par value each.

Management Review - Addendum C
Income and Expense Rates - of the Bank and its Subsidiaries (1)
For the Year Ended December 31

Reported amounts (2) (in NIS millions)

	2007				2006			
			Income (expense) rate				Income (expense) rate	
	Average balance (3)	Financing income (expense)	Excluding effect of derivatives	Including effect of derivatives	Average balance (3)	Financing income (expense)	Excluding effect of derivatives	Including effect of derivatives
			in %				in %	
Israeli currency - non-linked								
Assets (4)(5)	29,149	1,638	5.62		(6) 24,540	1,594	6.50	
Effect of embedded and ALM derivatives (7)	32,988	1,624			22,955	1,218		
Total assets	62,137	3,262		5.25	(6) 47,495	2,812		6.92
Liabilities (4)(5)	38,062	(1,210)	(3.18)		(6) 33,439	(1,338)	(4.00)	
Effect of embedded and ALM derivatives (7)	22,507	(1,060)			10,787	(546)		
Total liabilities	60,569	(2,270)		(3.75)	(6) 44,226	(1,884)		(4.26)
Interest margin			2.44	1.50			2.50	1.66
Israeli currency - linked to the CPI								
Assets (4)	35,172	2,729	7.76		34,985	1,743	4.98	
Effect of embedded and ALM derivatives (7)	4,778	181			1,585	8		
Total assets	39,950	2,910		7.28	36,570	1,751		4.79
Liabilities (4)	27,939	(2,070)	(7.41)		29,125	(1,336)	(4.59)	
Effect of embedded and ALM derivatives (7)	10,333	(511)			6,363	(181)		
Total liabilities	38,272	(2,581)		(6.74)	35,488	(1,517)		(4.27)
Interest margin			0.35	0.54			0.39	0.52
Foreign currency (8)								
Assets (4)	25,870	(290)	(1.12)		26,493	(153)	(0.58)	
Effect of derivatives (7)								
Hedging derivatives	637	(12)			637	47		
Embedded and ALM derivatives	34,389	(1,730)			27,549	(348)		
Total assets	60,896	(2,032)		(3.34)	54,679	(454)		(0.83)
Liabilities (4)	19,882	550	2.77		19,020	284	1.49	
Effect of derivatives (7)								
Hedging derivatives	625	45			636	(28)		
Embedded and ALM derivatives	39,274	1,452			34,904	639		
Total liabilities	59,781	2,047		3.42	54,560	895		1.64
Interest margin			1.65	0.08			0.91	0.81

(1) The data in this table is provided before and after effect of derivatives (including off-balance sheet effects of financial derivatives).
(2) See Note 1.B to the financial statements.
(3) Net of the average balance of the specific provision for doubtful debt.
(4) Excludes financial derivatives.
(5) Includes credit card transaction balance of NIS 954 million in the non-linked segment (December 31, 2006 – NIS 1,056 million).
(6) Reclassified.
(7) Hedging financial derivatives, embedded derivatives that were detached and derivatives (ALM) which comprise part of the Bank's asset and liability management system.
(8) Includes 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 Review - Addendum C
Income and Expense Rates - of the Bank and its Subsidiaries (1)
For the Year Ended December 31

Reported amounts (2) (in NIS millions)

	2007				2006			
			Income (expense) rate				Income (expense) rate	
	Average balance (3)	Financing income (expense)	Excluding effect of derivatives	Including effect of derivatives	Average balance (3)	Financing income (expense)	Excluding effect of derivatives	Including effect of derivatives
			in %				in %	
Total								
Monetary assets generating financing income (4)	90,191	4,077	4.52		(5) 86,018	3,184	3.70	
Effect of derivatives (6)								
Hedging derivatives	637	(12)			637	47		
Embedded and ALM derivatives	72,155	75			52,089	878		
Total assets	162,983	4,140		2.54	(5)138,744	4,109		2.96
Monetary liabilities generating financing expenses (4)	85,883	(2,730)	(3.18)		(5) 81,584	(2,390)	(2.93)	
Effect of derivatives (6)								
Hedging derivatives	625	45			636	(28)		
Embedded and ALM derivatives	72,114	(119)			52,054	(88)		
Total liabilities	158,622	(2,804)		(1.77)	(5) 134,274	(2,506)		(1.86)
Interest margin			1.34	0.77			0.77	1.10
On options		345				1		
On other derivative instruments (excludes options, hedging and ALM derivatives and embedded derivatives that were detached (6))		58				83		
Commissions from financing transactions and other financing income (7)		313				320		
Other financing expenses		(26)				(20)		
Profit from financing operations before provision for doubtful debt		2,026				1,987		
Provision for doubtful debt (includes general and supplementary provision)		(228)				(305)		
Profit from financing operations after provision for doubtful debt		1,798				1,682		
Total								
Monetary assets generating financing income (4)	90,191				(5) 86,018			
Assets deriving from derivatives (8)	1,880				1,248			
Other monetary assets (4)	552				613			
General and supplementary provision for doubtful debt	(183)				(208)			
Total monetary assets	92,440				(5) 87,671			
Total								
Monetary liabilities generating financing expenses (4)	85,883				(5) 81,584			
Liabilities deriving from derivatives (4)	1,135				869			
Other monetary liabilities (4)	1,541				1,606			
Total monetary liabilities	88,559				(5) 84,059			
Total surplus monetary assets over monetary liabilities	3,881				3,612			
Non-monetary assets	1,604				1,529			
Non-monetary liabilities	154				196			
Total capital resources	5,331				4,945			

(1) The data in this table is provided before and after effect of derivatives (including off-balance sheet effects of financial derivatives).
(2) See Note 1.B to the financial statements.
(3) Net of the average balance of the specific provision for doubtful debt.
(4) Excludes financial derivatives.
(5) Reclassified.
(6) Hedging financial derivatives, embedded derivatives that were detached and derivatives (ALM) which comprise part of the Banks asset and liability management system.
(7) Includes profits from the sale of investments in bonds and from the adjustment to fair value of bonds held for trading and available for sale.
(8) Average balance sheet balances of financial derivatives (excludes average off-balance sheet balances of financial derivatives).
Note: Complete data on income and expense rates for each sector, by balance sheet item, will be provided upon request.

Management Review - Addendum C

Income and Expense Rates - of the Bank and its Subsidiaries (1)

For the Year Ended December 31

In US$ Millions

	2007				2006			
			Income (expense) rate				Income (expense) rate	
	Average balance (2)	Financing income (expense)	Excluding effect of derivatives	Including effect of derivatives	Average balance (2)	Financing income (expense)	Excluding effect of derivatives	Including effect of derivatives
			in %				in %	
Foreign currency (5)								
Assets (3)	6,337	356	5.62		5,893	305	5.18	
Effect of derivatives (4)								
Hedging derivatives	155	(2)			143	9		
Embedded and ALM derivatives	8,369	422			6,182	230		
Total assets	14,861	776		5.22	12,218	544		4.45
Liabilities (3)	4,892	(199)	4.07		4,269	(148)	(3.47)	
Effect of derivatives (4)								
Hedging derivatives	152	10			143	(6)		
Embedded and ALM derivatives	9,643	(487)			7,832	(302)		
Total liabilities	14,687	(676)		(4.60)	12,244	(456)		(3.72)
Interest margin			1.55	0.62			1.71	0.73

(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 of the specific provision for doubtful debt.
(3) Excludes financial derivatives.
(4) Hedging financial derivatives, embedded derivatives that were detached and derivatives (ALM) which comprise part of the Banks asset and liability management system.
(5) Includes 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 Review - Addendum D

Exposure of Bank and consolidated companies to changes in interest rates

as of December 31, 2007

Reported amounts (in NIS 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						
Total assets	27,793	1,759	1,853	570	80	149
Total liabilities	32,631	1,696	3,380	1,173	307	48
Difference	(4,838)	63	(1,527)	(603)	(227)	101
Effect of forward transactions and special commitments	1,546	(18)	5,832	590	(288)	(28)
Effect of options	167	411	548	161	8	-
Exposure to interest rate fluctuations in the sector	(3,125)	456	4,853	148	(507)	73
Cumulative exposure in sector	(3,125)	(2,669)	2,184	2,332	1,825	1,898
Israeli currency - linked to the CPI						
Total assets	221	1,571	7,261	11,513	6,424	7,004
Total liabilities	1,263	1,126	4,874	7,457	4,401	7,446
Difference	(1,042)	445	2,387	4,056	2,023	(442)
Effect of forward transactions and special commitments	(785)	1,108	(4,813)	(635)	57	(93)
Effect of options	-	-	-	-	-	-
Exposure to interest rate fluctuations in the sector	(1,827)	1,553	(2,426)	3,421	2,080	(535)
Cumulative exposure in sector	(1,827)	(274)	(2,700)	721	2,801	2,266
Foreign currency (2)						
Total assets	12,838	7,670	1,943	343	235	861
Total liabilities	11,127	6,200	2,181	171	155	697
Difference	1,711	1,470	(238)	172	80	164
Effect of forward transactions and special commitments	(1,090)	627	(634)	41	(168)	(1,190)
Effect of options	(232)	(411)	(534)	(104)	(8)	-
Exposure to interest rate fluctuations in the sector	389	1,686	(1,406)	109	(96)	(1,026)
Cumulative exposure in sector	389	2,075	669	778	682	(344)
Total exposure to interest rate fluctuations						
Total assets (3)	40,852	11,000	11,057	12,426	6,739	8,014
Debit balances deriving from credit card transactions (4)	-	-	-	-	-	-
Total assets in the balance sheet	40,852	11,000	11,057	12,426	6,739	8,014
Total liabilities	45,021	9,022	10,435	8,801	4,863	8,191
Credits for credit card transactions (4)	-	-	-	-	-	-
Total liabilities in the balance sheet	45,021	9,022	10,435	8,801	4,863	8,191
Difference	(4,169)	1,978	622	3,625	1,876	(177)
Effect of forward transactions and special commitments	(329)	1,717	385	(4)	(399)	(1,311)
Effect of options	-	-	-	-	-	-
Total exposure to interest rate fluctuations	(4,498)	3,695	1,007	3,621	1,477	(1,488)
Total cumulative exposure	(4,498)	(803)	204	3,825	5,302	3,814

General note:
Complete data on exposure to interest rate fluctuations in every sector, by balance sheet item, will be provided upon request.
In this table, the data for each period presents the present value of future flows that are discounted by the internal rate of return of the balance sheet item. The discounted future flows include accrued interest until maturity date, or the date of change in interest rate, whichever is earlier.

(1) The column "without maturity" presents book value.
(2) Activity in Israel, including Israeli currency linked to foreign currency, and overseas affiliates acting integrated units of the Bank.
(3) Includes shares presented in the column "without maturity date".
(4) Assets and liabilities deriving from the use of credit cards, according to which the customers were already charged.

				2007		2006	
10-20 years	Over 20 years	Without maturity (1)	Total	Internal rate of return	Average time to maturity	Internal rate of return	Average time to maturity
				in %	Years	in %	Years
-	-	517	32,721	6.03%	0.12	6.02%	0.10
1	-	36	39,272	3.89%	0.16	4.29%	0.11
(1)	-	481	(6,551)	2.14%	-0.04	1.73%	-0.01
-	-	-	7,634				
-	-	-	1,295				
(1)	-	481	2,378				
1,897	1,897	2,378	2,378				
1,643	3	81	35,721	5.16%	3.44	5.38%	3.45
1,605	59	412	28,643	4.80%	3.87	5.06%	3.76
38	(56)	(331)	7,078	0.36%	-0.43	0.32%	-0.31
(59)	-	-	(5,220)				
-	-	-	-				
(21)	(56)	(331)	1,858				
2,245	2,189	1,858	1,858				
36	-	114	24,040	5.18%	0.41	5.11%	0.43
13	-	-	20,544	4.74%	0.30	4.82%	0.19
23	-	114	3,496	0.44%	0.11	0.29%	0.24
-	-	-	(2,414)				
-	-	-	(1,289)				
23	-	114	(207)				
(321)	(321)	(207)	(207)				
1,679	3	2,393	94,163		1.48		1.52
-	-	-	1,154				
1,679	3	2,393	95,317				
1,619	59	595	88,606		1.39		1.35
-	-	-	1,154				
1,619	59	595	89,760				
60	(56)	1,798	5,557		0.09		0.17
(59)	-	-	-				
-	-	-	-				
1	(56)	1,798	5,557				
3,815	3,759	5,557	5,557				

Management Review - Addendum E

Credit Risk of Loans to the Public   Classified by Economic Sector at December 31, 2007 - Consolidated

Reported amounts (in NIS millions)

	Balance sheet credit risk (1)	Off-balance sheet credit risk (2)	Total credit risk of the public	Annual expense in respect of specific provision for doubtful debt	Balance of problem loans (3)
Agriculture	715	154	869	1	53
Industry	4,645	2,298	6,943	34	206
Construction and real estate	6,609	7,653	14,262	67	1,568
Electricity and water	364	292	656	-	-
Commerce	4,437	1,432	5,869	37	204
Hotel and food services	221	47	268	3	32
Transport and storage	583	152	735	2	12
Communications and computer services	490	313	803	5	164
Financial services	8,134	2,073	10,207	4	82
Other business services	1,914	546	2,460	6	82
Public and community services	753	289	1,042	4	134
Private individuals - housing loans	38,931	2,865	41,796	39	1,309
Private individuals - other	3,856	4,148	8,004	44	500
Total	71,652	22,262	93,914	246	4,346
For borrowers' activities overseas	3,733	904	4,637	2	-
Total	75,385	23,166	98,551	248	4,346
Credit risk included in the various economic sectors:					
Settlement movements (4)	1,306	299	1,605	-	138
Local authorities (5)	185	25	210	-	34

(1) Includes loans to the public and investments in debentures of the public of NIS 127 million and other assets related to derivatives against the public totaling NIS 766 million.

(2) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of per-borrower credit limitations.

(3) Balance of problem loans net of loans covered by collateral that may be deducted for the purpose of computing the per-borrower credit limits of an individual borrower and a group of borrowers, including elements of off-balance sheet risk.

(4) Kibbutzim and Moshavim, regional and national organizations, and corporations controlled by the settlement movements.

(5) Includes corporations under their control.

Note: Credit risk and problem debt are stated net of the specific provisions for doubtful debt.

Management Review - Addendum E

Credit Risk of Loans to the Public Classified by Economic Sector at December 31, 2006 - Consolidated

Reported amounts (in NIS millions)

	Balance sheet credit risk (1)(2)	Off-balance sheet credit risk (2)	Total credit risk of the public	Annual expense in respect of specific provision for doubtful debt	Balance of problem loans (4)
Agriculture	714	140	854	(3)	45
Industry	4,579	1,908	6,487	17	400
Construction and real estate	6,550	8,585	15,135	62	1,345
Electricity and water	258	332	590	1	-
Commerce	3,582	988	4,570	24	257
Hotel and food services	312	47	359	5	48
Transport and storage	471	199	670	3	19
Communications and computer services	697	258	955	1	17
Financial services	8,853	1,852	10,705	7	390
Other business services	2,032	440	2,472	9	124
Public and community services	797	287	1,084	5	124
Private individuals - housing loans	36,097	2,198	38,295	157	1,385
Private individuals - other	3,418	4,816	8,234	37	571
Total	68,360	22,050	90,410	325	4,725
For borrowers' activities overseas	2,824	726	3,550	-	-
Total	71,184	22,776	93,960	325	4,725
Credit risk included in the various economic sectors:					
Settlement movements (5)	1,709	351	2,060	-	41
Local authorities (6)	191	21	212	-	41

(1) Includes loans to the public and investments in debentures of the public of NIS 119 million and other assets related to derivatives against the public totaling NIS 764 million.
(2) Reclassified.
(3) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of per-borrower credit limitations.
(4) Balance of problem loans net of loans covered by collateral that may be deducted for the purpose of computing the per-borrower credit limits of an individual borrower and a group of borrowers, including elements of off-balance sheet risk.
(5) Kibbutzim and Moshavim, regional and national organizations, and corporations controlled by the settlement movements.
(6) Includes corporations under their control.

Note: Credit risk and problem debt are stated net of the specific provisions for doubtful debt.

Management Review - Addendum F

Classification of Loans to Developing Countries at December 31 - Consolidated

Reported amounts (in NIS millions)

	2007			2006		
	Loans (1)	Off-balance sheet credit risk (2)	Total	Loans (1)	Off-balance sheet credit risk (2)	Total
South America	-	-	-	-	53	53
Asia	40	-	40	(3) 56	-	(3) 56
Europe	347	53	400	(3) 112	42	(3) 154
Total of all loans to developing countries	387	53	440	168	95	263

(1) Net of deduction of specific provisions for doubtful debt.
(2) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of per-borrower credit limitations.
(3) Reclassified.

Management Review - Addendum G

Consolidated balance sheets at end of each quarter in 2007

Reported amounts (in NIS millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Assets				
Cash and deposits with banks	10,701	12,463	13,240	13,595
Securities	6,145	6,763	7,115	6,894
securities loaned or sold in repurchase agreements (1)	5	13	500	157
Credit to the public	74,320	73,688	72,285	71,452
Loans to the Government	3	3	4	4
Investments in investees	17	18	17	26
Buildings and equipment	1,246	1,205	1,219	1,296
Other assets	2,880	2,727	2,268	2,323
Total assets	95,317	96,880	96,648	95,747
Liabilities and Shareholders' Equity				
Deposits from the public	75,290	76,074	76,845	75,250
Deposits from banks	3,752	4,357	4,112	5,821
Deposits from the Government	282	522	539	549
Debentures and subordinated notes	6,189	6,357	6,077	5,263
Other liabilities	4,247	4,124	3,628	3,437
Total liabilities	89,760	91,434	91,201	90,320
Minority interest	-	12	13	-
Shareholders' equity	5,557	5,434	5,434	5,427
Total liabilities and shareholders' equity	95,317	96,880	96,648	95,747

See Note 1.G.1) to the financial statements.

Management Review - Addendum G

Consolidated balance sheets at end of each quarter in 2006

Reported amounts (in NIS millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Assets				
Cash and deposits with banks	10,797	12,706	13,318	13,010
Securities	5,979	5,759	5,194	5,622
Credit to the public	70,109	(1) 69,428	(1) 66,885	(1) 66,406
Loans to the Government	4	5	86	91
Investments in investees	42	42	41	88
Buildings and equipment	1,293	1,252	1,240	1,223
Other assets	2,487	2,134	2,007	1,495
Total assets	90,711	91,326	88,771	87,935
Liabilities and Shareholders' Equity				
Deposits from the public	73,234	72,988	72,096	71,501
Deposits from banks	3,073	4,485	2,820	3,418
Deposits from the Government	560	586	597	611
Debentures and subordinated notes	5,067	4,846	4,795	4,595
Other liabilities	3,710	(1) 3,346	(1) 3,461	(1) 3,068
Total liabilities	85,644	86,251	83,769	83,193
Minority interest	6	6	6	6
Shareholders' equity	5,061	5,069	4,996	4,736
Total liabilities and shareholders' equity	90,711	91,326	88,771	87,935

(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 2007

Reported amounts (in NIS millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Profit from financing operations before provision for doubtful debt	507	523	529	467
Provision for doubtful debt	50	65	63	50
Profit from financing operations after provision for doubtful debt	457	458	466	417
Operating and other revenues				
Operating commissions	265	260	256	253
Profits (losses) from investments in shares, net	20	(1)	8	38
Other income	18	14	22	37
Total operating and other income	303	273	286	328
Operating and other expenses				
Salaries and related expenses	291	291	294	293
Maintenance and depreciation of buildings and equipment	110	105	106	100
Other expenses	110	82	82	74
Total operating and other expenses	511	478	482	467
Pre-tax operating profit	249	253	270	278
Provision for taxes on operating profit	95	72	86	115
Operating profit after taxes	154	181	184	163
Share in net after-tax operating losses of affiliates	(1)	-	-	-
Net operating profit	153	181	184	163
After-tax profit (loss) from extraordinary items	(6)	3	23	207
Net profit	147	184	207	370
Profit per share (1)				
Basic profit per share (in NIS)				
Operating profit per share	0.69	0.82	0.84	0.74
Profit (loss) from extraordinary items	(0.03)	0.01	0.10	0.95
Total	0.66	0.83	0.94	1.69
Diluted profit per share (in NIS)				
Operating profit per share	0.68	0.81	0.82	0.73
Profit (loss) from extraordinary items	(0.03)	0.01	0.10	0.92
Total	0.65	0.82	0.92	1.65

(1) Share of NIS 0.1 par value each.

Management Review - Addendum H

Consolidated Statement of Profit and Loss – Multi-quarter information

Condensed Consolidated Statement of Profit and Loss by Quarter - for 2006

Reported amounts (in NIS millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Profit from financing operations before provision for doubtful debt	552	499	532	404
Provision for doubtful debt	64	61	61	119
Profit from financing operations after provision for doubtful debt	488	438	471	285
Operating and other revenues				
Operating commissions	254	(1) 240	250	247
Profits from investments in shares, net	18	1	29	2
Other income	44	(1) 37	46	47
Total operating and other income	316	278	325	296
Operating and other expenses				
Salaries and related expenses	310	270	478	337
Maintenance and depreciation of buildings and equipment	106	98	93	88
Other expenses	92	72	95	78
Total operating and other expenses	508	440	666	503
Pre-tax operating profit	296	276	130	78
Provision for taxes on operating profit	158	113	53	25
Operating profit after taxes	138	163	77	53
Share in net after-tax operating losses of affiliates	-	(2)	(2)	-
Net operating profit	138	161	75	53
Net after-tax profit from extraordinary items	3	1	212	-
Net profit	141	162	287	53
Profit per share (2)				
Basic profit per share (in NIS)				
Operating profit per share	0.63	0.74	0.34	0.24
Profit from extraordinary items	0.01	-	0.97	-
Total	0.64	0.74	1.31	0.24
Diluted profit per share (in NIS)				
Operating profit per share	0.62	0.73	0.34	0.24
Profit from extraordinary items	0.01	-	0.95	-
Total	0.63	0.73	1.29	0.24

(1) Reclassified.
(2) Share of NIS 0.1 par value each.

Certification

I, Eliezer Yones declare that:

1. I have reviewed the quarterly report of Mizrahi Tefahot Bank Ltd. (formerly: United Mizrahi Ltd.) ("the Bank") for the year 2007 ("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, changes in shareholders' equity and cash flow statements of the Bank as of and for the periods presented in this Report.
4. I and others in the Bank who are declaring this certification, are responsible for determining and maintaining disclosure controls and procedures required for the Bank's Report, and:
   - 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 subsidiaries, particularly during the period in which the Report is being prepared;
   - B. We have evaluated the effectiveness of the Bank's disclosure controls and procedures and presented 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
   - C. 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 control over financial reporting, to the Bank's independent auditors, the board of directors and the audit and financial statements committees 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 control over financial reporting.

The aforesaid does not derogate from my responsibility or the responsibility of any other person according to the law.

E. Yones
President

March 24, 2008

Certification

I, Menachem Aviv, declare that

1. I have reviewed the quarterly report of Mizrahi Tefahot Bank Ltd. (formerly: United Mizrahi Ltd.) (“the Bank”) for the year 2007 (“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, changes in shareholders’ equity and cash flow statements of the Bank as of and for the periods presented in this Report.
4. I and others in the Bank who are declaring this certification, are responsible for determining and maintaining disclosure controls and procedures required for the Bank’s Report, and:
   - 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 subsidiaries, particularly during the period in which the Report is being prepared;
   - B. We have evaluated the effectiveness of the Bank’s disclosure controls and procedures and presented 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
   - C. 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 control over financial reporting, to the Bank’s independent auditors, the board of directors and the audit and financial statements committees 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 control over financial reporting.

The aforesaid does not derogate from my responsibility or the responsibility of any other person according to the law.

M. Aviv
Vice-president, Chief Accountant

March 24, 2008

Board of Directors and Management Report on Responsibility for the Annual Report

The annual report was prepared by the Bank's management, which is responsible for its fair presentation. This report includes financial statements prepared in conformity with generally accepted accounting principles and reporting rules prescribed by the directives and guidelines of the Supervisor of Banks, as well as supplementary and other information prepared in accordance therewith.

The preparation of periodic financial statements also requires the preparation of estimates in order to determine certain amounts and items in the statements. These estimates were prepared by management using its best judgment.

In order to ensure the fairness of the Bank's financial reporting, the Bank's management maintains a comprehensive system of internal control, whose purpose is to ensure that all of the Bank's transactions are properly authorized; that the assets of the Bank are safeguarded; that their integrity is assured; and that the accounting records serve as a reliable basis for the preparation of the financial statements. The internal control system is, by its nature, limited by the fact that it does not grant absolute assurance, but merely reasonable assurance, as to its ability to reveal and prevent errors and irregularities. The principle of reasonable assurance is based on the conviction that decisions regarding the resources invested in the operation of a system of controls must, by their nature, take into account, the benefits arising from their implementation.

The Bank's Board of Directors, which is responsible for preparation of the financial statements and their approval in accordance with Section 92 of the Companies Law, prescribes the accounting policies and supervises their application. It also determines the structure of the internal control system and monitors its functioning. The President is responsible for the day-to-day management of the Bank's affairs, within the framework of the policies set by the Board of Directors and subject to its instructions. Bank management operates based on policy set by the Board of Directors. The Board of Directors, by means of its committees, holds ongoing meetings with Bank management, with the Internal Auditor and with Independent Auditors of the Bank in order to review their work and its outcome.

The Bank's independent auditors, Brightman Almagor & Co., have audited the annual financial statements of the Bank in accordance with generally accepted auditing standards, including those prescribed in the Auditors' Regulations (Mode of Performance), 1973, and certain auditing standards issued by the American Institute of Certified Public Accountants, the application of which was mandated by the directives of the Supervisor of Banks. The audit's objective is to enable the independent auditors to express an opinion on the extent to which these statements reflect the Bank's financial position, results of operations, changes in shareholders' equity and cash flows, in conformity with generally accepted accounting principles, and the reporting rules prescribed by the directives and guidelines of the Supervisor of Banks. In accordance with Section 170 of the Companies Law, the independent auditors are responsible toward the Bank and its shareholders to express an opinion on the financial statements. The report of the independent auditors is attached to the annual financial statements.

In addition, the information contained in the Report of the Board of Directors and in the Management's Review (the accompanying information) was furnished to the independent auditors in order to enable them to notify the Bank in the event that there is a material inconsistency between the information contained in the financial statements and the ancillary information, or whether there is a material difference between the information provided in the ancillary information and the evidence or information that had come to the knowledge of the independent auditors in the course of their audit. The independent auditors have not reported any such material inconsistency or difference. The independent auditors did not adopt procedures for this purpose beyond those required for the purposes of auditing the financial statements, in order to ascertain such inconsistency or difference.

Jacob Perry	**Eliezer Yones**	**Menachem Aviv**
Chairman of the Board of Directors	President	**Vice-president,** **Chief Accountant**

Ramat Gan, March 24, 2008

Financial Statements

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Independent Auditors' Report to Shareholders of Bank Mizrahi-Tefahot Limited

We have audited the accompanying balance sheets of Mizrahi Tefahot Limited ("the Bank") at December 31, 2007 and 2006, and the consolidated balance sheets at 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, 2007. 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 audits.

We did not audit the financial statements of certain consolidated subsidiaries, whose assets included in the consolidated balance sheets constitute 4.18% and 4.1% of total consolidated assets at December 31, 2007 and 2006, respectively, and whose profits from financing operations before provision for doubtful debt included in the consolidated statement of profit and loss constitute 3.24%, 5.4% and 3.54% of the total profit from financing operations before provision for doubtful debt included in the consolidated statement of profit and loss for the years ended December 31, 2007, 2006 and 2005, respectively. Furthermore, we have not audited the financial statements of an affiliate, the investment in which amounts to NIS 11 million and NIS 37 million as of December 31, 2007 and 2006, respectively, and the share of whose profits amounts to NIS 10 million for the year ended December 31, 2005. The financial statements of this company were audited by other auditors, whose report was furnished to us, and our opinion, insofar as it relates to amounts included with respect to this company, is based on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards, including those prescribed by the Auditors' Regulations (Mode of Performance), 1973. 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, 2007 and 2006, 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, 2007, in conformity with generally accepted accounting principles. Also, in our opinion, the financial statements have been prepared in accordance with the directives and guidelines of the Supervisor of Banks.

As explained in Note 1.B, the financial statements are stated in reported amounts, in accordance with the Accounting Standards of the Israel Accounting Standards Board.

Without prejudice to our aforementioned opinion, we draw your attention to Note 19.D.13)A-C with regard to lawsuits filed against the Bank and motions for class action status, including with regard to insurance.

Brightman Almagor & Co.
Certified Public Accountants (Israel)

Tel-Aviv, March 24, 2008

Balance sheet – consolidated and the Bank – as of December 31

Reported amounts (in NIS millions)

		Consolidated		The Bank	
	Note	2007	2006	2007	2006
Assets					
Cash and deposits with banks	2	10,701	10,797	12,659	12,485
Securities	3	6,145	5,979	6,092	5,915
securities loaned or sold in repurchase agreements (1)		5	-	5	-
Credit to the public	4	74,320	70,109	70,094	66,038
Loans to the Government	5	3	4	3	4
Investments in investees	6	17	42	1,180	1,312
Buildings and equipment	7	1,246	1,293	1,234	1,270
Other assets	8	2,880	2,487	2,829	2,477
Total assets		95,317	90,711	94,096	89,501
Liabilities and Shareholders' Equity					
Deposits from the public	9	75,290	73,234	76,253	73,435
Deposits from banks	10	3,752	3,073	3,768	3,082
Deposits from the Government		282	560	275	551
Debentures and subordinated notes	11	6,189	5,067	4,057	3,724
Other liabilities	12	4,247	3,710	4,186	3,648
Total liabilities		89,760	85,644	88,539	84,440
Minority interest		-	6	-	-
Shareholders' equity	13	5,557	5,061	5,557	5,061
Total liabilities and shareholders' equity		95,317	90,711	94,096	89,501

See Note 1.G.1) to the financial statements.

The accompanying notes are an integral part of the financial statements.

Jacob Perry	**Eliezer Yones**	**Menachem Aviv**
Chairman of the Board of Directors	President	Vice-president, Chief Accountant

Approval date:
Ramat Gan, March 24, 2008

Statement of Profit and Loss - Consolidated and the Bank
For the Year Ended December 31

Reported amounts (in NIS millions)

	Note	Consolidated			The Bank		
		2007	2006	2005	2007	2006	2005
Profit from financing operations before provision for doubtful debt	22	2,026	1,987	1,904	1,944	1,904	1,830
Provision for doubtful debt	4C	228	305	292	226	312	282
Profit from financing operations after provision for doubtful debt		1,798	1,682	1,612	1,718	1,592	1,548
Operating and other revenues							
Operating commissions	23	1,034	991	924	934	899	835
Profits from investments in shares, net	24	65	50	3	65	50	2
Other income	25	91	174	187	75	113	95
Total operating and other income		1,190	1,215	1,114	1,074	1,062	932
Operating and other expenses							
Salaries and related expenses	26	1,169	1,395	1,154	1,108	1,340	1,100
Maintenance and depreciation of buildings and equipment		421	385	349	412	375	340
Other expenses	27	348	337	336	325	295	299
Total operating and other expenses		1,938	2,117	1,839	1,845	2,010	1,739
Pre-tax operating profit		1,050	780	887	947	644	741
Provision for taxes on operating profit	28	368	349	371	335	293	319
Operating profit after taxes		682	431	516	612	351	422
Share in net after-tax operating profits (losses) of investees	6B	(1)	(4)	(3)	69	76	91
Net operating profit		681	427	513	681	427	513
After-tax profit (loss) from extraordinary items	29	227	216	(2)	227	216	(2)
Cumulative after-tax effect, as of beginning of year, of change in accounting method		-	-	(4)	-	-	(4)
Net profit		908	643	507	908	643	507

The accompanying notes are an integral part of the financial statements.

Statement of Profit and Loss - Consolidated and the Bank
For the Year Ended December 31

	Note	New Israeli Shekels		
		2007	2006	2005
		Reported amounts		
Profit per share (1)	1U			
Basic profit per share (in NIS)				
Operating profit per share		3.08	1.95	2.35
Profit (loss) from extraordinary items		1.03	0.99	(0.01)
Cumulative after-tax effect, as of beginning of period, of change in accounting method		-	-	(0.02)
Total		4.11	2.94	2.32
Diluted profit per share (in NIS)				
Operating profit per share		3.03	1.91	2.33
Profit (loss) from extraordinary items		1.01	0.97	(0.01)
Cumulative after-tax effect, as of beginning of period, of change in accounting method			-	(0.02)
Total		4.04	2.88	2.30

(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 (in NIS millions)

	share capital and premium (1)	Capital reserve from benefit from share-based payment transactions	Total paid-up Share capital and premium	Total cumulative other profit: Adjustments for presentation of securities available for sale at fair value	Total cumulative other profit: Translation adjustments (2)	Retained earnings (3)	Dividend declared after balance sheet date	Total shareholders' equity
Balance at January 1, 2005	1,881	11	1,892	23	(51)	2,269	-	4,133
Net profit for the year	-	-	-	-	-	507	-	507
Benefit from share-based payment transactions	-	15	15	-	-	-	-	15
Related tax effect	-	8	8	-	-	-	-	8
Adjustments to present securities available for sale at fair value	-	-	-	15	-	-	-	15
Related tax effect	-	-	-	(2)	-	-	-	(2)
Balance at January 1, 2006	1,881	34	1,915	36	(51)	2,776	-	4,676
Net profit for the year	-	-	-	-	-	643	-	643
Dividend paid	-	-	-	-	-	(325)	-	(325)
Benefit from share-based payment transactions	-	26	26	-	-	-	-	26
Related tax effect	-	12	12	-	-	-	-	12
Adjustments to present securities available for sale at fair value	-	-	-	49	-	-	-	49
Related tax effect	-	-	-	(20)	-	-	-	(20)
Balance at January 1, 2007	1,881	72	1,953	65	(51)	3,094	-	5,061
Net profit for the year	-	-	-	-	-	908	-	908
Dividend paid	-	-	-	-	-	(400)	-	(400)
Benefit from share-based payment transactions	-	18	18	-	-	-	-	18
Related tax effect	-	8	8	-	-	-	-	8
Realized share-based payment transactions (4)	30	(30)	-	-	-	-	-	-
Adjustments to present securities available for sale at fair value	-	-	-	(57)	-	-	-	(57)
Related tax effect	-	-	-	19	-	-	-	19
Dividend declared after balance sheet date	-	-	-	-	-	(75)	75	-
Balance at December 31, 2007	1,911	68	1,979	27	(51)	3,527	75	5,557

(1) The premium on shares was created before March 31, 1986.
(2) Foreign currency translation adjustment of autonomous overseas units.
(3) For details on various limitations on dividend distributions, see Notes 13 and 14 below.
(4) In 2007, 872,824 ordinary NIS 0.1 par value shares were issued for exercise of options in conjunction with the Employee Stock Option Plan, and 1,938,771 ordinary NIS 0.1 par value shares were issued to the President for exercise of options.

The accompanying notes are an integral part of the financial statements.

Statement of Cash Flows - Consolidated and the Bank
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Cash flows generated by operating activities						
Net profit for the year	908	643	507	908	643	507
Adjustments to reconcile net profit to net cash generated by operating activities:						
Share in undistributed losses (profits) of investees, net	1	4	3	(69)	(76)	(91)
Depreciation of buildings and equipment and amortization	163	137	128	161	135	126
Amortization of goodwill in investees	1	1	1	1	1	1
Provision for doubtful debt	228	305	292	226	312	282
Profit on sale of securities available for sale	(35)	(18)	(35)	(35)	(18)	(35)
Decline in value of securities available for sale	115	2	6	115	2	6
Realized and unrealized gain from adjustment to fair value of securities held for trading	2	-	-	2	-	-
Profit on sale of investment in affiliates	(3)	(84)	-	(3)	(84)	-
Loss (profit) on sale of buildings	(21)	-	1	(11)	-	1
Cost reduction of buildings held for sale and unused leased properties	17	-	1	17	-	1
Deferred taxes, net	152	(290)	(22)	152	(295)	(17)
Severance pay - increase in excess of liability over amount funded	3	197	25	3	198	25
Benefit from share-based payment transactions	26	26	15	26	26	15
Bank's share in net profit from extraordinary items of subsidiaries	-	-	-	(38)	(130)	-
Minority interest in net profit from extraordinary items of subsidiaries	13	-	-	13	-	-
Profit from sale of provident fund operations, net	(218)	-	-	(199)	-	-
Deferred income, net	8	(49)	117	12	(44)	109
Net cash inflow generated by operating activities	1,360	874	1,039	1,281	670	930

The accompanying notes are an integral part of the financial statements.

Statement of Cash Flows - Consolidated and the Bank

For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Cash flows generated by activities in assets						
Acquisition of debentures held to maturity	-	(173)	(59)	-	(152)	(58)
Proceeds on redemption of debentures held to maturity	-	170	132	-	166	79
Proceeds on sale of debentures held to maturity	-	-	137	-	-	137
Acquisition of securities available for sale	(10,238)	(8,645)	(9,538)	(10,238)	(8,642)	(9,537)
Proceeds on sale and redemption of securities available for sale	9,993	9,333	8,530	9,982	9,333	8,525
Deposits with banks, net	378	34	(607)	98	(534)	(3,121)
Securities held for trading, net	(52)	(29)	17	(52)	(29)	-
securities loaned or sold in repurchase agreements, net	(5)	-	-	(5)	-	-
Loans to the public, net	(4,439)	(4,806)	(1,356)	(4,282)	(4,402)	(675)
Loans to the Government, net	1	88	3	1	88	1
Merger of subsidiary	-	-	-	-	-	95
Acquisition of shares in investees, including shareholder loans	(12)	(10)	-	(50)	(154)	(25)
Proceeds on sale of investment in affiliates	23	198	-	23	198	-
Proceeds from sale of provident fund operations	364	-	-	333	-	-
Acquisition of buildings and equipment	(206)	(194)	(197)	(203)	(192)	(197)
Proceeds on sale of buildings and equipment	138	7	3	120	7	3
Dividend received from investees	-	1	2	210	1	22
Other assets, net	(677)	(881)	532	(625)	(903)	534
Net cash outflow generated by activities in assets	(4,732)	(4,907)	(2,401)	(4,688)	(5,215)	(4,217)

The accompanying notes are an integral part of the financial statements.

Statement of Cash Flows - Consolidated and the Bank
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Cash flows generated by activities in liabilities and shareholders' equity						
Deposits from the public, net	2,056	1,888	1,577	2,852	3,616	1,899
Deposits from banks, net	679	(59)	232	686	(721)	725
Deposits from the Government, net	(278)	(168)	(270)	(276)	(163)	(262)
Issuance of debentures and subordinated notes	1,259	1,063	1,426	490	461	1,019
Redemption of debentures and subordinated notes	(137)	(301)	(186)	(157)	(269)	(158)
Other liabilities, net	487	514	(309)	484	522	(320)
Dividend paid to shareholders	(400)	(325)	-	(400)	(325)	-
Dividend paid to shareholders in subsidiary	(12)	-	-	-	-	-
Net cash inflow generated by activities in liabilities and shareholders' equity	3,654	2,612	2,470	3,679	3,121	2,903
Increase (decrease) in cash	282	(1,421)	1,108	272	(1,424)	(384)
Balance of cash at beginning of year	8,185	9,606	8,498	8,181	9,605	9,989
Balance of cash at end of year	8,467	8,185	9,606	8,453	8,181	9,605

Appendix 1 to Cash Flow Statement

Non-cash Transactions

During 2007, buildings and equipment were acquired - consolidated and the Bank - for which the related consideration of NIS 30 million was yet to be paid as of December 31, 2007. (2006 - consolidated and the Bank - NIS 22 million; 2005 - consolidated - and the Bank - NIS 14 million).

The accompanying notes are an integral part of the financial statements.

Notes to the Financial Statements at December 31, 2007

Note 1 - Reporting Principles and Accounting Policies

A. General

1) The financial statements have been prepared in accordance with the directives and guidelines of 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:

"Subsidiaries"	Companies in which the bank holds, directly or indirectly, over 50% of voting rights, or may appoint over half of their board members, and whose financial statements are consolidated with the bank's.
"Affiliates"	Companies, other than subsidiaries, the investment in which is included in the financial statements using the equity method.
"Investees"	Subsidiaries and affiliates.
"Transition date"	December 31, 2003.
"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.
"Reported amount"	An amount adjusted to the transition date, plus amounts in nominal value 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 at the transition date, as applicable.
"Cost"	Cost in reported amount.
"Related parties"	As defined in Opinion 29 of the Institute of Certified Public Accountants in Israel.
"Interested parties"	As defined in Section 1 of the Securities Law.
"Controlling shareholder"	As defined in the Securities Regulations (Financial Statement Presentation of Transactions between a Corporation and its Controlling Shareholder), 1996.

4) Beginning from January 1, 2005, the financial statements of the Bank include Bank Tefahot, which was merged into the Bank.

Note 1 - Reporting Principles and Accounting Policies

B. Financial statements in reported amounts

Reported amounts

1) The Bank prepares its financial statements on the basis of the historical cost convention, adjusted for changes in the Israeli Consumer Price Index through December 31, 2003. Pursuant to Accounting Standard 12 and Accounting Standard 17, as of January 1, 2004 financial statements are no longer adjusted.
   The aforementioned adjusted amounts, included in the financial statements as of the transition date, serve as basis point for nominal financial reporting. The additions made after the transition date are included in nominal values.

2) Balance sheet -
   a) Non-monetary items (mainly – buildings and equipment) are stated at reported amounts.
      Non-monetary items do not necessarily represent realization value or updated economic value.
   b) Monetary items are stated in the balance sheet at their nominal values at the balance sheet date.

3) Statement of profit and loss -
   a) Income and expenses that relate to non-monetary items or to balance sheet provisions derive from the change between the reported amount in the opening balance and the reported amount in the closing balance.
   b) The remaining statement of profit and loss items are stated at nominal value.

4) Comparative figures in the financial statements are included in reported amounts.

C. Translation of the financial statements of overseas units

In accordance with the directives of the Supervisor of Banks, the Bank's branches overseas are classified as an "integrated unit" of the Bank. Accordingly, their financial statements are translated into Israeli currency as set forth below.

1) Monetary items were translated at the exchange rate prevailing at the balance sheet date.
2) Non-monetary items – up to the transition date, these were translated using historical exchange rates on the acquisition date; after the transition date were adjusted for the changes in the general purchasing power of the Israeli currency until December 31, 2003. Additions and disposals of non-monetary assets after the transition date are stated at reported amounts, according to the exchange rate prevailing on the acquisition date.
3) Differences derived from the translation of the financial statements, as aforesaid, were included in the statement of profit and loss.

   Until 1994, overseas consolidated companies were classified as "autonomous units". Differences between the investment unit, adjusted for the CPI, in overseas consolidated companies, as included on the bank's books, and the bank's equity holding in the company, translated using the exchange rate on the reporting date, were included under "translation adjustment of autonomous overseas operating units" under shareholders' equity.

D. Foreign currency and linkage

1) Assets (other than investments in investees, securities, buildings and equipment and liabilities denominated in or linked to foreign currency or linked to the Consumer Price Index) are included in the financial statements as follows:
   a) In foreign currency or linked thereto - at the representative exchange rates published by the Bank of Israel on the balance sheet date or a more appropriate date, in accordance with the terms of the transactions.
   b) Fully linked to the Consumer Price Index – using the index known on the balance sheet date or another appropriate index, as set forth in agreements.
2) Income and expenses in foreign currency were translated for inclusion in the statement of profit and loss at current representative exchange rates. Exchange rate differentials on assets and liabilities are included in the appropriate statement of profit and loss items.

Note 1 - Reporting Principles and Accounting Policies

3) Information regarding the CPI and the representative exchange rates and changes there to as follows:

	As of December 31			Change in %		
	2007	2006	2005	2007	2006	2005
CPI in December (points)	106.4	102.9	103.0	3.4	(0.1)	2.4
CPI in November (points)	105.8	102.9	103.2	2.8	(0.3)	2.7
Exchange rate of U.S. dollar (in NIS)	3.846	4.225	4.603	(9.0)	(8.2)	6.8
Exchange rate of Euro (in NIS)	5.659	5.564	5.446	1.7	2.2	(7.3)

E. Investments in investees

1) Principles of consolidation

a) The financial statements of the Bank alone include the financial statements of wholly-owned and controlled companies, consolidated financial statements include the audited financial statements of the Bank and its subsidiaries most of whose properties are used by the Bank, and most of their services are provided to the Bank.

b) The consolidated financial statements include the audited financial statements of the Company and of its subsidiaries.

c) The financial statements of the provident funds, severance pay funds and continuing education funds managed by the Bank Group were not consolidated, since the Bank Group had no share in their assets or their profits.

d) Material inter-company balances and transactions among consolidated Group companies have been eliminated in the consolidated financial statements.

2) Principles of the application of the equity method -

a) In the Bank's financial statements, investments in the shares of investees, and in the consolidated financial statements, investments in the shares of affiliates, are presented using the equity method, on the basis of their audited financial statements.

The share of said companies' financial results is presented under "after-tax operating profit (loss)". After-tax profit (loss) from extraordinary items for investee companies is included under the Bank's "After-tax profit (loss) from extraordinary items".

b) Goodwill that results from the acquisition of investments in investees (positive or negative) is amortized over a 10-year period and is included in "investments in investees". Goodwill from the acquisition of the shares of Bank Tefahot, which was merged into the Bank, is included after the merger in "other assets". In the event of an expected loss of economic benefit, the goodwill is written-off in full. Goodwill amortization is recorded under "other expenses".

c) With respect to Accounting Standard No. 15 – "Impairment of Assets" – see O. below.

F. 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 at 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 trading - securities that were purchased or are held essentially for the purpose of selling them during the near term. These securities are included in the balance sheet at their fair value on the reporting date. Unrealized profits 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. Unrealized profits or losses from adjustment to fair value, net of tax effect, are charged directly to a separate item under shareholders' equity and transferred to the statement of profit and loss upon realization.

d) Investment in stocks is presented in the portfolio available for sale at fair value and as set forth in section c) above. Shares having no available fair value are presented at cost, net of provision for impairment which is not of a temporary nature, which is charged to the statement of profit and loss. Dividends received from an investment in shares available for sale, originating in the profits of the distributing company prior to the acquisition date, were charged to the statement of profit and loss.

e) A decline in value of securities, which, in the opinion of management, is not temporary, is recorded in the statement of profit and loss. For details of determination of fair value and provision for impairment, see section F.2) below.

2) Fair value and provision for impairment of securities.

The fair value of securities is based on sale prices on the stock exchange for securities trading on the stock exchange in Israel. Overseas securities are revalued using quoted sale prices from external sources, including quotes from well-known systems, such as Bloomberg, or current quotes obtained from the issuing entity. In cases where there is no quoted price in an active market, the bank uses a quote obtained from an independent, professional source in order to estimate the fair value of the security and to determine if there is any impairment of a non-temporary nature.

The nature of impairment in the portfolio is reviewed quarterly. Impairment may arise from two types of events:

a) Global events – changes to general market risk factors due to macro-economic changes.

b) Specific events – impaired financial standing of the issuer.

The decision as to whether impairment of an investment in securities is of a temporary nature, is based on the following parameters:

a) The length of the period in which the security value is lower than its amortized acquisition cost.

b) Extent of impairment out of total investment.

c) Assessment of the issuer's financial standing and ability to meet their obligations, based, inter alia, on rating of securities by international agencies and on review of safety cushions and securities which back the investment.

d) Assessment of the time at which market prices which impact the investment value are expected to return to their original level.

e) The bank's intention and ability to hold the securities for a sufficient period of time for their value to return to original cost, taking into account, inter alia, considerations of position management and liquidity.

G. Transfer and service of financial assets and discharge of liabilities

1) A new public reporting directive, "Transfers and Service of Financial Assets and Discharge of Liabilities", became effective January 1, 2007. This directive adopts the measurement and disclosure principles prescribed in American Standard No. 140 relating to all transfer and service transactions of financial assets and the discharge of liabilities, including: repurchase and lending of securities; sale of loan portfolios, securitization of financial assets; associations and partnerships in credit; bank acceptances and participation in their risk; discount agreements.
The provisions adopt the principles prescribed in American Standard 140 for distinguishing between transfers of financial assets that will be recorded as a sale and between other transfers. The principle was adopted, whereby a transferred financial asset will be stated in the balance sheet of the party that controls it, whether it is the transferor or recipient of the asset. The provisions prescribe control tests relating to repurchases, lending of securities, securitization of loans, sale and participation in loans.

The provisions also adopt the measurement and disclosure principles prescribed in Standard 140 relating to the measurement of financial assets, which according to their contractual terms, may be discharged in early repayment, so that the holder does not cover his investment.

The new directive applies to the lending of securities, repurchase of securities, securitization of financial assets, other transfers of financial assets, providing of services to financial assets and discharge of liabilities effected commencing January 1, 2007.

Pursuant to the directive, recorded in “other securities” in the Bank’s balance sheet will be securities that the Bank borrowed, which meet the conditions provided in the directive for transfer of control, including securities that were borrowed from the borrowing reserve of the Ministry of Finance. Securities held by the Bank which were loaned to others while fulfilling the conditions for transfer of control, will not be recorded in the balance sheet. The gain or loss from their sale will be recognized in the statement of profit and loss, and new assets or liabilities representing the rights or obligations that the Bank retained in the borrowed securities will be recorded in the balance sheet.

The securities that were loaned or borrowed, or securities sold or purchased in conjunction with REPO agreements, in all cases with receipt/payment of the full consideration for them, and which do not meet the conditions for transfer of control, are presented separately in the Bank’s balance sheet, as part of the item "securities", and the consideration for them is recorded in the balance sheet as “secured debt”: the consideration received for securities loaned or sold under REPO is recorded as “securities loaned or sold in repurchase agreements”, on the liabilities side, and the consideration paid for the securities borrowed or purchased under REPO is recorded as “securities borrowed or purchased in repurchase agreements” on the asset side. In conjunction with the application, security borrowings by the Bank from the Treasury repository, amounting to NIS 5 million as of December 31, 2007 were recorded under assets to the item "securities borrowed or purchased in repurchase agreements”.

2) The borrowing and lending of securities between the Bank's customers, brokered by the Bank, executed as credit transactions with no proceeds received for the securities borrowed, is stated in loans to the public and deposits from the public, or deposits from banks, respectively.

3) Transactions in securities are recorded based on their clearing date.

Note 1 - Reporting Principles and Accounting Policies

H. Buildings and equipment

1) Buildings and equipment are stated at cost, net of depreciation, computed using the straight-line method over their estimated useful life.

2) Assets designated for sale were stated at reported amounts, which does not exceed the estimated sales prices.

3) Certain costs (mainly salaries and related expenses) connected to the independent development of computer software for the Bank's own use, are allocated to the different projects. These costs are capitalized and recorded on the bank's balance sheet, in accordance with accounting treatment set forth in US Publication 98-1 Statement of Position, and are amortized from their date of operation, according to estimated duration of their use.

4) See O. below with respect to Standard No. 15 – "Impairment of Assets".
Provision for impairment of a non-temporary nature on investment in buildings and equipment is recorded under depreciation expense. The asset for which a provision for impairment has been recorded prior to the Standard's effective date, a provision is recorded as set forth in section "net after-tax loss from extraordinary operations".

5) Accounting Standard No. 27 – "Fixed Assets"
In September 2006, the Israel Accounting Standards Board published Standard No. 27 "Fixed Assets" ("the Standard"), which provides the accounting treatment for fixed assets, including the recognition of assets, determination of their book value and measurement of depreciation expenses and impairment losses that will be recognized in connection thereto. Likewise, the Standard provides the financial statements disclosure for fixed assets.

   The Standard provides among its provisions, that a fixed asset item will be measured on the first date of recognition at total cost, which includes, in addition to the purchase cost of the asset, all the costs that can be directly attributed to bringing the item to the required location and condition, so that it can be operated in the manner that management intended. The Standard defines, except in the specified exceptions, the principle of fair value measurement of the purchase cost of a fixed asset in consideration for non-monetary assets.

After the first recognition, the Standard prescribes that every part of fixed assets having significant cost is to be depreciated separately. The Standard allows an entity to elect to apply in its accounting policy the measurement of the fixed asset at cost, in which the asset is stated in the books at its depreciated cost net of impairment losses that accrued, or by the method of revaluation, in which the fixed asset is stated at its revalued fair value, net of depreciation and accrued impairment losses. According to the directives of the Supervisor of Banks, a banking corporation shall only apply the cost method.

The Standard applies to financial statements relating to periods commencing January 1, 2007, and was applied retroactively, except for several exceptions specified. For certain matters related to areas dealt with by the Standard, there are regulations issued by the Supervisor of Banks, and they apply to the Bank in these matters. Since the bank applies the cost method, application of the standard had no effect on the bank's financial statement.

6) Starting on January 1, 2007, the bank applies the provisions of Accounting Standard no. 30 "Intangible Assets", published by the Israeli Accounting Board. According to the directives of the Supervisor of Banks, the bank applies the cost method.

Cost of software recognized as an intangible asset is presented on the financial statements under "Buildings and equipment" at cost, net of accumulated depreciation and loss from impairment. Application of the standard had no impact on the bank's financial statements.

I. Expenses in conjunction with issuance of debentures and subordinated notes

Expenses for issuance of debentures and subordinated notes, as well as premium and discount, are amortized over the term of the debentures or subordinated notes, taking into account the balances in circulation.

J. 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. 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 in the item “operating commissions”.

K. 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: 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: 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 was made in the financial statements only for that part of the claim amount for which the probability of realization of damage to the bank is defined as Probable.

3) Remote: 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 (over 1% of equity).

   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. Beyond this, only in rare cases is the Bank permitted to determine that the prospects for realizing the exposure cannot be determined.

L. Employee rights

Pension and severance pay liabilities are covered by deposits to funds and by appropriate provisions. The financial statements included all of the liabilities for employee rights, including an appropriate provision for severance pay, which is recorded in accordance with the law, agreement, custom and management's expectations. The future contractual liabilities for pension and severance are calculated based on regular actuarial consultation, based on recommendation of the Supervisor of Insurance. Also, see Note 16 below.

M. Share-based payment transactions

In accordance with the directives of the Supervisor of Banks, starting on January 1, 2006 the bank applies Accounting Standard no. 24 "Share-Based Payment", published by the Israeli Accounting Board.

The Bank computes the fair value of the benefit deriving from the allotment of options to employees based on the Black & Scholes model. The expense for the value of the benefit is apportioned over the stock option vesting period. Under salary expenses in the Statement of Profit and Loss, against capital reserve from benefit from stock option allocation to employees, under shareholders' equity. Simultaneously, the Bank records deferred taxes for the expected tax benefit upon option exercise by employees, based on the naive value of the options as of the reporting date.

Salary expenses include an update to the provision for wage tax payment expected upon option exercise. The provision is updated in accordance with changes in the naive value of the options.

For details of share-based payment transactions, see Note 16.A.

N. Derivative instruments and hedging activities

1) The Bank trades in financial derivatives, including currency and interest contracts. The currency contracts include forwards, futures, swaps and options. These trades are executed in all the 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) The derivatives are recorded in the Bank's balance sheet in other assets or other liabilities, as applicable, at their fair value. Changes in the fair value of derivatives are recorded to the statement 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.

   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 recorded in the balance sheet at fair value.

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 policy. 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 do not arise from changes in the risk factor being hedged (which impacts the cash flows resulting from the hedged instrument), are charged to capital reserve from cash flow hedging, under shareholders' equity.

7) The Bank stops hedge accounting henceforth, 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 hedging discontinuation are recorded in the statement of profit and loss.

Note 1 - Reporting Principles and Accounting Policies

O. Basis of recognition of income and expenses

1) Income and expenses are included on the accrual basis.

2) Income and expenses from securities held for trading and derivative instruments are included at the changes in fair value of the related balance sheet item. See section F.1)d) above for dividend received from an investment in shares available for sale.

3) Delinquency interest and amounts of provisions made for housing loans are recorded in the statement of profit and loss upon actual collection. See also section P.3) below.

4) Interest supplement from the Treasury to the State to compensate for the difference in interest on housing loans given to borrowers eligible for benefits is recorded in the statement of profit and loss over the period of the loans, using the uniform return basis.

5) Revenues from commissions received due to early loan repayment after deduction of the share related to financial capital, which is immediately recognized as revenue, is charged to the statement of profit and loss. This income is mainly charged on a straight-line basis over three years from the payment date.

6) Interest expenses on deposits, in which the customer is given a graduated interest rate according to the period of the deposit, are recorded to the statement of profit and loss by the straight-line method, according to the average expense rate for the deposit.

7) Pursuant to Proper Conduct of Banking Business Directive no. 325 “Management of Credit Facility in Current Accounts", the Bank does not record to the statement of profit and loss any interest income on deviations arising in accounts classified as problem accounts, until the balance returns to within limits of the overall credit facility. When there is a deviation in the current account, the Bank considers the required classification of the debt, in accordance with the directives of the Supervisor of Banks.

Note 1 - Reporting Principles and Accounting Policies

P. Provision for doubtful debt

1) The financial statements include appropriate provisions for debt, the collection of which is in doubt.
   The provisions are made on the basis of estimates by the managements of the Bank and its subsidiaries regarding possible losses in the loan portfolio - including off-balance-sheet debt. Managements' estimates take into account the risk inherent in the loan portfolio, the scope and quality of the information available to management on the debtor, its business activities, how it honors its obligations, and the value of the collateral held.

2) The specific provision for housing loans is calculated, pursuant to directive of the Supervisor of Banks, according to length of arrears, whereby provision amounts increase the longer the arrears. With respect to housing loans above NIS 805 thousand, housing loans that are not repaid in monthly or quarterly payments and housing loans for which the existing specific provision exceeds the amount of the provision based on length of arrears, the provision is made on a specific basis and not based on the length of arrears.

3) A provision for doubtful debt made according to length of arrears is reduced upon receiving proceeds for loan repayment or sale of the pledged asset. Therefore, repayment of a debt in arrears after the balance sheet date, or foreclosure of the pledged asset for which payments were received to repay the debt after the balance sheet date, do not reduce the provision based on length of arrears in the reported period. Furthermore, it is not possible to reduce such provisions for loans in which the bank may, but is not required, to make provisions based on length of arrears by changing the provision policy to a policy of specific provisions.

4) Debt are written off only after all legal and other proceedings for their collection have been exhausted, and it is evident that there is no real prospect to collect them.

5) The financial statements include a general provision and a supplementary provision for doubtful debt that relate to the credit portfolio of the Bank Group in Israel. In accordance with the directives of the Supervisor of Banks, the supplementary provision for bad debt is computed based on the quality of the customer loan portfolio, the concentration of debt from an industry, and other risk characteristics. These directives also require banks to maintain a general provision of 1% of total credit to the

public as at December 31, 1991. Beginning from January 1, 2005, the adjustment of the general provision to the CPI was discontinued.

Q. Taxes on income

1) The bank and its subsidiaries implement a method of applying taxes for differences in timing of charging certain income and expenses between financial reporting and tax-related reporting. The utilization of deferred tax assets is contingent upon the existence of sufficient taxable income in the future. Management of the Bank and its subsidiaries believes that these taxes may be utilized in the future.

   Deferred taxes were computed using the liability method, at the tax rates expected to be in effect when they are realized, based on the data available upon preparation of the financial statements.

   In accordance with the directives of the Supervisor of Banks, deferred taxes are not recorded in respect of the general, supplementary and special provisions for doubtful debt.

2) The accumulated retained 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 a dividend distribution is not expected in the foreseeable future. A provision for tax is recorded on the profits of affiliates, if additional tax liability could arise.

   The computation of deferred taxes does not include taxes that would be imposed if the investments in investees are realized, if the intention is to hold them and not realize them. Deferred taxes are computed on investments in investees earmarked for sale.

3) The provision for taxes on the income of the Bank and subsidiaries that are financial institutions for V.A.T. purposes includes profit tax levied on earnings under the Value Added Tax Law. The value added tax levied on the salaries of financial institutions is included in “salaries and related expenses”.

4) Tax expenses on profit from extraordinary operations, including on capital gains for tax purposes, are included in the item "profit from extraordinary operations".

R. Impairment of Assets

The Bank applies the provisions of Accounting Standard No. 15, which prescribes the accounting treatment and presentation required in the event of impairment - decline in value - of assets. Pursuant to this standard, if there is a sign pointing to the decline in value of an asset, it is to be examined by comparing the book value of the asset to its recoverable amount.

The recoverable amount is the higher of the net sales prices of the asset and its utility value as determined by the present value of the future cash flows projected from use of the asset and its realization at the end of its life. If the carrying value of the asset in the balance sheet exceeds its recoverable amount, the Bank recognizes an impairment loss (and an allocation of deferred taxes), in the amount of the difference between the book value of the asset and its recoverable amount.

An impairment loss that was recognized (except for goodwill) will be reversed only if changes have occurred in the estimates used to determine the recoverable value of the asset, at the time an impairment loss was recognized.

In accordance with the directives of the Supervisor of Banks, Standard no. 15 does not apply to financial assets which require disclosure in a note on the fair value of financial instruments, including securities.

The main assets of the bank to which Standard no. 15 applies are:

1) Investments in affiliates - the recoverable amount is reviewed for each company separately, based on share prices on the stock exchange for a company whose shares are listed for trading, as well as on review of financial statements and forecasts for coming years for each company.
2) Buildings and equipment - the recoverable amount is calculated per branch, by discounting cash flows expected from branch income and expenses, with reference, as the case may be, to an independent valuation of the realization value of the asset.

For details of provision for impairment of buildings and equipment, see Note 7.

Note 1 - Reporting Principles and Accounting Policies

S. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles occasionally requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of income and expenses in the report periods. Actual results could differ from these estimates.

T. Statement of cash flows

1) The statement of cash flows presents the net cash flows from operations related to both assets and liabilities, except for changes in securities that are not securities held for trading, in non-monetary assets and in subordinated notes.

2) Cash includes cash and deposits with banks with an original period to maturity not exceeding three months.

U. Earnings per share

Earnings per share is calculated according to provisions of Accounting Standard no. 21 "Earnings per share", published by the Israel Accounting Standards Board. Basic earnings per share is calculated based on profit or loss attributable to holders of ordinary shares of the bank, divided by the weighted average number of ordinary shares outstanding during the reported period. In order to calculate the diluted profit per share, the corporation will adjust the profit or loss attributable to the ordinary shareholders of the reporting entity, and the weighted average number of outstanding ordinary shares, for the effects of all the dilutive potential ordinary.

Furthermore, pursuant to the standard, earnings per 1 share is presented.

V. Transactions with controlling shareholders and with corporations controlled by the bank

In December 2006, the Israel Accounting Standards Board published Accounting Standard No. 23 "Accounting Treatment of Transactions between an Entity and its Controlling Shareholder" ("the Standard").

The Standard prescribes that assets and liabilities for which a transaction was executed between the entity and its controlling shareholder, will be measured according to their value on the transaction date, and the difference between the fair value and the consideration prescribed in the transaction will be charged to shareholders' equity. A debit difference, which constitutes a benefit to the controlling shareholder, will be treated as a dividend and will be deducted from retained earnings. A credit difference, which essentially constitutes an investment by shareholders, will be presented in a separate shareholders' equity item to be called "capital reserve from transaction between an entity and its controlling shareholder".

The Standard prescribes principles related to the treatment of transfers of assets between an entity and its controlling shareholder, for loans given by an entity to the controlling shareholder and vice versa, and to the transfer of debt between an entity and its controlling shareholder with acceptance of the obligation by the controlling shareholder through indemnification or the forgiveness by the controlling shareholder of the debt of the entity toward him.

The Standard also prescribes the disclosure that must be provided in the financial statements related to transactions between an entity and its controlling shareholder during the period.

It was prescribed that the Standard would apply to transactions that will be executed between an entity and its controlling shareholder after January 1, 2007 and on a loan given to or received from a controlling shareholder before this Standard takes effect, which applies from its effective date.

The Supervisor of Banks intends to apply the Standard to banking corporations, with required adaptations. As of the publication date of these financial statements, directives have yet to be published by the supervisor with regard to adoption of the standard.

Application of the standard is not expected to materially impact the Group financial standing and operating results, since transactions with controlling shareholders are executed at market conditions, and are approved by the Board of Directors' Audit Committee, which also serves as the Committee for Transactions with Related Parties.

W. Accounting Standard No. 29 "Adoption of International Financial Reporting Standards (IFRS)"

In July 2006, the Israel Accounting Standards Board published Accounting Standard No. 29 – "Adoption of International Financial Reporting Standards (IFRS)" ("the Standard"). The Standard prescribes that companies subject to the Securities Law, 1968, and required to report in accordance with the regulations of this Law, will prepare their financial statements in conformity with the IFRS Standards, as from the reporting period commencing January 1, 2008.

This does not apply to entities which according to the Securities Regulations (Periodic and Immediate Reports of a Foreign Corporation), 2000, prepare their financial statements in accordance with the directives and guidelines of the Supervisor of Banks. The IFRS Standards will be adopted for the first time with the application of the provisions of IFRS 1 “First-time Adoption of IFRS Standards”, for transition purposes.

With respect to the manner in which the Standard will be applied by banking corporations, the Supervisor of Banks informed the banking corporations that:

1) He intends to prescribe, on a current basis, guidelines for applying the Israeli Standards published by the Israel Accounting Standards Board, which are based on IFRS, which do not involve the core banking business;
2) In the second half of 2009, he will publish his decision regarding the date for application of IFRS Standards relating to the core banking business. In doing so, he will take into consideration the results of the process of adopting these standards in Israel, on one hand, and the progress in the convergence process between the international reporting standards and the American standards, on the other hand.
3) Thus, with respect to the core banking business, the financial statements of a banking corporation which are prepared according to the directives and guidelines of the Supervisor of Banks will continue to be prepared in accordance with the American Standards that were prescribed in the public reporting regulations.

X. Measuring and disclosure of impaired debt, credit risk and provision for credit losses

On December 31, 2007, the Supervisor of Banks published his directive in a circular concerning: "Measuring and disclosure of impaired debt, credit risk and provision for credit losses" (hereinafter: "the circular" or "the directive"). This circular is based, inter alia, on USA Accounting Standards 5, 114 and 118 as well as on regulatory directives by banking supervision bodies and by the USA Securities and Exchange Commission. The guiding principles on which the directive is based introduce a material change over current directives on classification of problem debt and measuring of provisions for credit losses in conjunction with such debt.

According to the circular, the banking corporation is required to maintain adequate provision for credit losses so as to cover expected credit losses from its credit portfolio. Furthermore, according to the circular, the bank is required to maintain adequate provision so as to cover expected credit losses associated with off-balance sheet credit instruments, such as contracts for provision of credit and guarantees. The required provision to cover expected credit losses from the credit portfolio would be made under one of the following tracks: "Individual provision" or "group provision".

"Individual provision for credit losses" would be applied for any debt determined to be impaired, whose contractual balance (including accounting write-offs, unrecognized interest, provisions for credit losses and collateral) is NIS 1 million or higher. For other debt, the banking corporation may decide whether to make an individual assessment. The individual provision for credit losses will be estimated based on expected future cash flows, discounted using the original discount rate for the debt or, if the debt requires collateral or when the banking corporation determined that seizure of an asset is probable, based on the fair value of the collateral provided to secure said credit.

"Specific provision for credit losses using group estimate" would be applied for large, homogeneous groups of small debt (whose balance is below NIS 1 million) (such as: credit card debt, housing loans and consumer debt repaid by installments) as well as for large, non-impaired debt. The specific provision for credit losses from debt based on group estimate, except for loans for which a specific minimum provision based on length of arrears has been calculated as per directives of the Supervisor of Banks, shall be calculated based on rules set forth in USA Accounting Standard FAS 5: "Accounting for Contingencies" ("FAS 5"), using statistical models which take into consideration the extent of past losses for each homogeneous group of debt having similar risk attributes. The required provision with regard to off-balance sheet credit instruments would be assessed as per rules set forth in the USA Accounting Standard FAS 5.

Changes to provision for credit losses would be recorded under "Expenses for tax losses" in the statement of profit and loss. Furthermore, the directive specifies various definitions and classifications of on- and off-balance sheet credit risk, rules for recognizing interest income from impaired debt as well as rules for accounting write-off of problem debt. The circular stipulates, inter alia, that debt should be subject to accounting write-off. Based on group estimates and classified as impaired based on their length of arrears, taking into consideration the banking corporation's ability to assess that collection is probable, and considering the fact that they are secured by a residence.

This directive will be applied in financial statements of banking corporations starting on January 1, 2010, with no retroactive application to financial statements for previous periods. According to transition directives, the impact of changes due to the new directives shall be charged directly to equity upon initial application.

In conjunction with the bank's preparations for application of this directive, teams were formed and an external consultant has been hired to review required changes to bank work processes, both in terms of credit management and processing of impaired debt, as well as in terms of accounting treatment and impact on its financial statements. As of the publication date of these financial statements, the bank has completed specification of the processes and computer systems required for applying the directive, and has started the process to select a software vendor to make required development and changes to systems. Concurrently, the bank intends to update work processes in 2008-2009, including recompilation of procedures and delivery of training for professional staff in preparation for applying this directive.

At this stage in preparation for application of the directives, it is not possible to estimate the impact of application of the directives on the Bank's shareholders' equity, since the models for calculating provisions for credit losses have yet to be finalized, especially for small-size debt to be treated via group provision. Completion of the methodology and initial estimate of said application are anticipated in mid-2008.

Note 2 - Cash and Deposits with Banks
As of December 31
Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
Cash and deposits with central banks	2,668	1,571	2,666	1,570
Deposits with commercial banks	7,478	8,361	7,531	8,575
Deposits with special banking entities	555	865	2,462	2,340
Total cash and deposits with banks	10,701	10,797	12,659	12,485
Includes - cash, deposits with banks and deposits with central banks for an original period of up to three months	8,467	8,185	8,453	8,181

Note 3 - Securities – Consolidated
As of December 31, 2007

Reported amounts (in NIS millions)

	Balance sheet amount	Net book value	Total cumulative other profit		Fair value (1)
			Profits	Losses	
Composition					
1) Securities available for sale					
Debentures and bonds					
Of the Government of Israel (2)	4,010	4,026	5	21	4,010
Of foreign governments and their agencies (2)	69	69	-	-	69
Of others	1,587	1,628	-	41	1,587
Total debentures available for sale	5,666	5,723	5	62	5,666
Shares of others (3)(4)	399	295	104	-	(5) 399
Total securities available for sale	6,065	6,018	(6) 109	(6) 62	6,065

	Balance sheet amount	Net book value	Unrealized profits from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value (1)
2) Securities held for trading					
- Debentures					
of Government of Israel	79	79	-	-	79
of others	1	1	-	-	1
Total securities held for trading	80	80	-	-	80
Total securities	6,145	6,098	109	62	6,145

(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-F for information on liens on securities held by the Bank.
(3) The net book value and the balance sheet amount have been presented after a write-down for decline in value that is not temporary of NIS 46 million.
(4) In July 2003, a letter was received from the Supervisor of Banks, requiring the Bank to classify loans that had been given to a certain customer, which do not meet the repayment terms prescribed and against which shares of a leading telecommunication company were pledged, as “securities available for sale”, beginning from the financial statements as of June 30, 2003. The market value of these shares as of December 31, 2007, included in this item, amounts to NIS 322 million. This amount exceeds the amount of the loans, net of the provision for doubtful debt, by NIS 98 million.
(5) 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 46 million.
(6) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".

Note: Details of results of trading in investments in debentures – see Note 22; details on results of trading in shares - see Note 24.

Note 3 - Securities – Consolidated
As of December 31, 2006

Reported amounts (in NIS millions)

	Balance sheet amount	Net book value	Total cumulative other profit - Profits	Total cumulative other profit - Losses	Fair value (1)
Composition					
1) Securities available for sale (2)					
Debentures and bonds					
Of the Government of Israel (3)	3,074	3,069	8	3	3,074
Of foreign governments and their agencies (3)	72	72	-	-	72
Of others	2,399	2,401	3	5	2,399
Total debentures available for sale	5,545	5,542	11	8	5,545
Shares of others (4)(5)	404	303	101	-	(6) 404
Total securities available for sale	5,949	5,845	(7) 112	(7) 8	5,949

	Balance sheet amount	Net book value	Unrealized profits from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value (1)
2) Securities held for trading					
Debentures -					
Of Government of Israel	29	29	-	-	29
Of others	1	1	-	-	1
Total securities held for trading	30	30	-	-	30
Total securities	5,979	5,875	112	8	5,979

(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) In the Fourth quarter of 2005, the Bank realized debentures held to maturity amounting to NIS 137 million. The bonds were realized in a portfolio held by the Bank's London branch, in conjunction with a review of appropriateness of classification of the branch's security portfolios. The Bank recorded capital gains of NIS 0.7 million from said realization (NIS 0.4 million after tax). According to directives of the Supervisor of Banks, in case of sale of debentures held to maturity, in material contradiction to the Bank's statement of its intention to hold said debentures to maturity, these debentures should be reclassified from the debenture portfolio held to maturity to the debenture portfolio available for sale. Bank management believes that sale of said debentures by the London branch is not in contradiction with the Bank's statement of its intent to hold said debentures to maturity. However, for the sake of clarity, all debentured held to maturity, amounting to NIS 153 million, have been reclassified and transferred to the debenture portfolio available for sale. The security classification policy for the different portfolios was updated, and as of the date of these financial statements, determination of security classification is only made at Bank headquarters in Israel, with proper discretion exercised and documentd. Management believes that these steps are appropriate changes under the circumstances, which would allow its intent with regard to security classification to be treated with a high level of confidence.

(3) See Note 15.A-F for information on liens on securities held by the Bank.

(4) The net book value and the balance sheet amount have been presented after a write-down for decline in value that is not temporary of NIS 47 million.

(5) In July 2003, a letter was received from the Supervisor of Banks, requiring the Bank to classify loans that had been given to a certain customer, which do not meet the repayment terms prescribed and against which shares of a leading telecommunication company were pledged, as "securities available for sale", beginning from the financial statements as of June 30, 2003. The market value of these shares as of December 31, 2005, included in this item, amounts to NIS 271 million. This amount exceeds the amount of the loans, net of the provision for doubtful debt, by NIS 47 million.

(6) 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 64 million.

(7) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".

Note: Details of results of trading in investments in debentures – see Note 22; details on results of trading in shares - see Note 24.

Note 3 - Securities – the Bank
As of December 31, 2007
Reported amounts (in NIS millions)

	Balance sheet amount	Net book value	Total cumulative other profit: Profits	Losses	Fair value (1)
Composition:					
1) Securities available for sale					
Debentures and bonds					
Of the Government of Israel (2)	4,007	4,023	5	21	4,007
Of foreign governments and their agencies (2)	69	69	-	-	69
Of investees	1	1	-	-	1
Of others	1,537	1,578	-	41	1,537
Total debentures available for sale	5,614	5,671	5	62	5,614
Shares of others (3)(4)	399	295	104	-	(5) 399
Total securities available for sale	6,013	5,966	(6)109	(6) 62	6,013

	Balance sheet amount	Net book value	Unrealized profits from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value (1)
2) Securities held for trading					
Debentures -					
of Government of Israel	79	79	-	-	79
of others	-	-	-	-	-
Total securities held for trading	79	79	-	-	79
Total securities	6,092	6,045	109	62	6,092

(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-F for information on liens on securities held by the Bank.
(3) The net book value and the balance sheet amount are stated net of the write-down for a non-temporary decline in value of NIS 46 million.
(4) In July 2003, a letter was received from the Supervisor of Banks, requiring the Bank to classify loans that had been given to a certain customer, which do not meet the repayment terms prescribed and against which shares of a leading telecommunication company were pledged, as “securities available for sale”, beginning from the financial statements as of June 30, 2003. The market value of these shares as of December 31, 2007, included in this item, amounts to NIS 322 million. This amount exceeds the amount of the loans, net of the provision for doubtful debt, by NIS 98 million.
(5) Includes shares for which a fair value is not available, that are stated at cost, amounting to NIS 46 million.
(6) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".

Note: Details of results of trading in investments in debentures – see Note 22; details on results of trading in shares - see Note 24.

Note 3 - Securities – the Bank
As of December 31, 2006

Reported amounts (in NIS millions)

	Balance sheet amount	Net book value	Total cumulative other profit		Fair value (1)
			Profits	Losses	
Composition:					
1) Securities available for sale (2)					
Debentures and bonds					
Of the Government of Israel (3)	3,071	3,066	8	3	3,071
Of foreign governments and their agencies (3)	72	72	-	-	72
Of investees	1	1	-	-	1
of others	2,338	2,340	3	5	2,338
Total debentures available for sale	5,482	5,479	11	8	5,482
Shares of others (4)(5)	404	303	101	-	(6) 404
Total securities available for sale	5,886	5,782	(7) 112	(7) 8	5,886

	Balance sheet amount	Net book value	Unrealized profits from adjustments to fair value	Unrealized losses from adjustments to fair value	Fair value (1)
2) Securities held for trading					
- Debentures					
of Government of Israel	29	29	-	-	29
of others	-	-	-	-	-
Total securities held for trading	29	29	-	-	29
Total securities	5,915	5,811	112	8	5,915

(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) In the Fourth quarter of 2005, the Bank realized debentures held to maturity amounting to NIS 137 million. The bonds were realized in a portfolio held by the Bank's London branch, in conjunction with a review of appropriateness of classification of the branch's security portfolios. The Bank recorded capital gains of NIS 0.7 million from said realization (NIS 0.4 million after tax). According to directives of the Supervisor of Banks, in case of sale of debentures held to maturity, in material contradiction to the Bank's statement of its intention to hold said debentures to maturity, these debentures should be reclassified from the debenture portfolio held to maturity to the debenture portfolio available for sale. Bank management believes that sale of said debentures by the London branch is not in contradiction with the Bank's statement of its intent to hold said debentures to maturity. However, for the sake of clarity, all debentured held to maturity, amounting to NIS 153 million, have been reclassified and transferred to the debenture portfolio available for sale. The security classification policy for the different portfolios was updated, and as of the date of these financial statements, determination of security classification is only made at Bank headquarters in Israel, with proper discretion exercised and documented. Management believes that these steps are appropriate changes under the circumstances, which would allow its intent with regard to security classification to be treated with a high level of confidence.

(3) See Note 15.A-F for information on liens on securities held by the Bank.

(4) The net book value and the balance sheet amount are stated net of the write-down for a non-temporary decline in value of NIS 50 million.

(5) In July 2003, a letter was received from the Supervisor of Banks, requiring the Bank to classify loans that had been given to a certain customer, which do not meet the repayment terms prescribed and against which shares of a leading telecommunication company were pledged, as "securities available for sale", beginning from the financial statements as at June 30, 2003. The market value of these shares as of December 31, 2006, included in this item, amounts to NIS 317 million. This amount exceeds the amount of the loans, net of the provision for doubtful debt, by NIS 92 million.

(6) Includes shares for which a fair value is not available, that are stated at cost, amounting to NIS 52 million.

(7) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".

Note: Details of results of trading in investments in debentures – see Note 22; details on results of trading in shares - see Note 24.

Note 3 - Securities – Consolidated
As of December 31, 2007
Reported amounts (in NIS millions)

3) Further details on consolidated basis with regard to asset-backed securities available for sale

	Net book value	Total cumulative other profit		Fair value (book value)
		Profits	Losses	
Mortgage-backed securities				
"Pass-through" securities	-	-	-	-
Other mortgage-backed securities	-	-	-	-
Asset-backed securities (ABS)				
CDO	58	-	11	47
CDO, mostly mortgage-backed (1)	-	-	-	-
CLO	102	-	12	90
SIV	22	-	-	22
Total asset-backed securities available for sale	**182**	-	(2) **23**	**159**

(1) Fully amortized.
(2) Subsequent to the balance sheet date (as of end of February 2008), a further impairment of the aforementioned assets occurred, amounting to NIS 34 million.

4) For the balance if investments in asset-backed securities which include unrealized losses, the period in which the investment is at loss is less than 12 months.

5) During 2007, expenses amounting to NIS 114 million were recorded due to provision for impairment of a non-temporary nature of investments in asset-backed securities.

Asset-backed securities (ABS)

The fair value of Bank investments in asset-backed securities amounts to NIS 159 million. These investments include securities such as: CDO, CLO and SIV as follows:

A. CDO (Collateralized Debt Obligation) is a security backed by various types of debt instruments, which may include both direct debt and securitized debt. The CDO is set in lyers by priority. Each layer is a separate debt, with specific rating, entitled to principal or interest payment before all debt ranked lower. Total value of debt subordinate to a given debt layer is defined to be the protective layer for said debt.

The fair value of Bank investment in said securities, as of December 31, 2007 amounted to NIS 47 million. All Bank investments in this asset class are rated as investment grade with protection layers, and are managed by one of the leading investment management firms in the world. The backing assets are synthetic assets widely distributed across sectors and of different credit ratings, mostly investment grade (BBB- or higher).

The impairment charged to capital reserve as of December 31, 2007 for these investments amounted to NIS 11 million. According to information available to the Bank, this impairment is due to the crisis sentiment in markets and to general increase in credit spreads. The Bank believes there is no risk of default or risk of write-off of the protection layers in these investments. Furthermore, the Bank may hold said securities to redemption or until their fair value reaches the investment cost. Hence, the impairment is classified as temporary.

Note that in the first quarter of 2007, the Bank realized investments in said instruments amounting to NIS 67 million, recording limited capital gains.

B. CDO, mostly mortgage-backed – The Bank has invested in this type of security NIS 42 million ($10 million). The backing assets include 84% mortgages to individuals (RMBS[1]), about half of them – subprime. In the second half of 2007, the Bank recorded a loss from impairment of a non-temporary nature, amounting to the full investment amount, due to estimates that probability of future receipts from this transaction is low.

C. CLO (collateralized Loan Obligation) is a specific type of CDO. The debt instruments which back the CLO investment are senior and junior loan portfolios provided to commercial entities. The fair value of Bank investment in said securities, as of December 31, 2007 amounted to NIS 90 million. All Bank investments in this asset class are in layers with investment-grade rating (BBB- or higher) with a protection layer, managed by some of the largest investment management firms in the world, which are carefully selected. About 85% of loans backing these securities are senior secured loans. The Bank's CLO portfolio has no exposure to mortgages, including sub prime mortgages, or to any leveraged products whose value has declined due to the current crisis. The impairment charged to capital reserve as of December 31, 2007 for these investments amounted to NIS 12 million. According to information available to the Bank, this impairment is due to the crisis sentiment in markets and to general increase in credit spreads. The Bank estimates that there is no reason to assume that issuers will default on their obligations. Furthermore, the Bank may hold said securities to redemption or until their fair value reaches the investment cost. Hence, the impairment is classified as temporary.

[1] **RMBS (Residential Mortgage-Backed Securities)** – securities backed by mortgages to individuals, where principal and interest payments are base d on cash flow from repayment of loans backed by mortgages.

Note 3 - Securities – Consolidated

D. SIV (Structured Investment Vehicle) is a structured investment product (including mainly asset-backed securities: CMBS[2], RMBS, credit card receipts, student loans etc.) with high investment ratings for medium- to long term. A major share of financing for acquisition of asset-backed securities (the senior layer) is obtained by issuing short-term commercial paper and mid-term debentures (MTN). The balance (the junior layer) is financed by issuing capital notes which are inferior to the senior layer.

The Bank invests in a structured investment vehicle (SIV), in the Capital Notes layer.

The portfolio mainly consists of credit card receipts, insurance, CDO, CMBS, RMBS and corporate debentures. About 93% of the asset portfolio is rated as high investment grade, AA or higher. The Bank's original investment amount in the structured investment vehicle (SIV) amounted to NIS 115 million ($25 million). The liquidity crisis in the credit markets has led to increased credit spreads in all sectors, and hence to decline in the value of structured investment vehicles. Concurrently, the cost for issuing commercial paper has risen, so that current financing cost for the transaction has increased. The high leverage in this transaction intensified the impairment due to growing spreads. Therefore, even though the assets hold high ratings and the extent of their quality impairment was relatively low, there is significant impact on the total fair value of the structured investment vehicle (SIV).

The fair value of this investment, based on a quote provided by managers of the backed assets, as of December 31, 2007 amounted to NIS 22 million ($5 million). As of December 31, 2007 the Bank recognized impairment of non-temporary nature amounting to NIS 76 million, which was charged to the statement of profit and loss.

The assessment that this impairment is not of temporary nature is primarily due to the current erosion in the value of this investment due to high financing costs and high leverage, as well as to the assumption that it would take a long time before market financing costs would return to their pre-crisis level.

[2] **CMBS (Commercial Mortgage-Backed Securities)** – securities backed by mortgages to commercial entities, where principal and interest payments are based on cash flow from repayment of loans backed by mortgages.

Note 4 - Loans to the Public (1)
As of December 31
Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
A. 1) Composition				
Credit	74,314	70,110	70,086	66,036
Customers' liabilities for acceptances	178	191	178	191
Total loans	74,492	70,301	70,264	66,227
General and supplementary provision for doubtful debt	172	192	170	189
Total loans to the public	74,320	70,109	70,094	66,038

2) The balance of deposits based on level of collection (mainly from the Government) and loans issued there from that were set off, as of December 31, 2007, totaled NIS 16,856 million in the consolidated balance sheet and NIS 15,640 million in the Bank's balance sheet (December 31, 2006 – consolidated - NIS 17,043 million and the Bank - NIS 15,793 million).

3) Total housing loans in the consolidated balance sheet as of December 31, 2007 include loans at variable interest totaling NIS 17,468 million (December 31, 2006 – NIS 14,571 million).

(1) The specific provision for doubtful debt was deducted from the relevant loan items.

Note 4 - Loans to the Public
As of December 31
Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
B. Loans to the public includes:-				
1) Loans to problem borrowers which are not local authorities and for which a provision for doubtful debt based on level of arrears was not recorded				
a) Non-income-bearing loans to problem borrowers –				
In Israeli currency				
Non-linked	790	808	774	795
Linked to CPI	64	102	64	101
Foreign currency (1)	79	92	79	92
Total	933	1,002	917	988
b) Restructured loans without Income waiver				
In Israeli currency				
Non-linked	96	105	91	104
Linked to CPI	68	49	68	49
Foreign currency (1)	21	17	21	17
Total	185	171	180	170
c) Loans for which there is a decision to restructure, not yet implemented	2	15	2	15
d) Loans in temporary arrears (2)	1,027	1,457	998	1,427
Interest credited to statement of profit and loss	48	78	48	78
e) Loans under special supervision (3)	879	814	869	810

(1) Includes linked to foreign currency.
(2) Loans in temporary arrears – loans in arrears, which the Bank's management views as temporary and as not indicating expected credit losses.
(3) Loans under special supervision - loans for which the Bank's management deems it necessary to intensify monitoring and supervision, while not anticipating loan losses.

Note 4 - Loans to the Public

As of December 31

Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
2) Loans to local authorities	181	(1) 188	181	(1) 188
a) Loans to local authorities include:				
1) Non-income bearing loans	1	1	1	1
2) Restructured loans without Income waiver	-	1	-	1
3) Loans in temporary arrears	-	18	-	18
4) Loans under special supervision (2)	33	21	33	21
5) Loans to local authorities not included under loans to problem borrowers, as above	147	(1) 147	147	(1) 147
Interest on these loans included in statement of profit and loss	10	7	10	7

(1) Reclassified.

(2) Loans under special supervision - loans for which the Bank's management deems it necessary to intensify monitoring and supervision, while not anticipating loan losses.

Note 4 - Loans to the Public

b) Loans to local authorities

1) In 1989, an agreement was signed by several banks, including the Bank, and the Government of Israel, to reschedule the debt of certain local authorities to banks and other creditors. The pro rata share of the Bank and its investees in this arrangement, on the date it was signed, was about 12%. 208 local authorities have joined the arrangement with the banking system, including 181 with debt to the Bank.

   The essential elements of the arrangement are as follows:

   a) Short-term loans that the local authorities owed on September 1989, as well as certain loans coming due subsequent to signing the arrangement, are to be rescheduled over a period of 15 years, with linkage to the CPI plus interest, as agreed in the arrangement.
   b) Additional credit is to be made available to the local authorities in the form of 15-year loans, to enable the local authorities to discharge their debt to various creditors. As of December 31, 2007, the Bank has no share in these loans.
   c) Security to the banks includes the assignment by pledge of Ministry of the Interior grants to the local authorities, and the assignment by pledge of 40% of the transfers from the Ministry of Education and Culture and the Ministry of Labor and Welfare to those local authorities.

2) As a follow-up to the above agreement, separate agreements were signed on different dates between the Bank and each local authority, regarding their debt to the Bank for loans at the Bank's risk.

3) In addition to the balance of debt included in the arrangement with the authorities, some of local authorities which are party to the arrangement have, from time to time, received additional credit in the ordinary course of business, the balance of which, as of December 31, 2007, totaled NIS 64.6 million.

4) The law, "Arrangements in the State Economy (Amended Legislation to Achieve Budgetary Targets and Economic Policies in Fiscal Year 2000), 1999 imposes, inter alia, the "creditors' arrangement" mechanism prescribed in Section 233 of the Companies' Ordinance also on municipalities and local councils, so that at the request of a creditor of a municipality or local authority or at the request of the Minister of the Interior, with the consent of the Minister of Justice, the court will be empowered to rule that the mechanism for the arrangement of debt prescribed in Section 233 of the

Companies' Ordinance will be imposed, with the required changes, on the municipality or local authority. The significance of the amendment, inter alia, is that creditors holding 75% of the value represented at the vote of a meeting of creditors can force an arrangement on the minority, and the court may ratify an arrangement that will include the restructuring of debt, write-off of debt, or freezing of proceedings.
Furthermore, an argument could be raised in the future that the amendment gives the court authority to impose on a majority of creditors, against their will, a settlement that reschedules or writes off the debt, if the good of the residents of the local authority requires it.
In the estimation of the Bank's management, the effect of this Law on the Group is not material.

5) The Budget Foundations Law (Amendment No. 31 and Temporary Order), 2004 applies to various kinds of local authorities, such as: a local authority for which a recovery plan was approved, a local authority in difficulty and a religious council.
The purpose of the amendment is that in the recovery period prescribed for each local authority, all the income of the local authority should be earmarked for specific purposes stipulated in the law, and not to repay debt to creditors.
Pursuant to the amendment of the law, the local authority must open specific bank accounts, and it will not be possible to attach, pledge or assign the monies deposited in them and are only intended for use for the objectives designated in the statute.
A secured creditor, in whose favor the local authority created a lien, will be unable to begin proceedings to foreclose the liens, during the recovery period prescribed in the law. The prohibition on a lien or attachment also applies to collateral securing credit that was given before the law took effect, thus causing some impairment to the proprietary rights of the banks.

Total indebtedness to the Bank of authorities that are covered by the law, as of December 31, 2007, stands at NIS 38.6 million (as of December 31, 2006 – NIS 42 million). Total indebtedness to the Bank of authorities to which the law could apply, stands at NIS 41.5 million as of December 31, 2007 (December 31, 2006 - NIS 27 million). After reviewing the economic standing of these authorities, Bank management estimates that said credit does not indicate anticipated credit loss, hence no provision was made for this liability in the financial statements.

Note 4 - Loans to the Public

Reported amounts (in NIS millions)

C. Provision for doubtful debt

	2007			
	Specific provision (1)			
	By extent of arrears	Other	Supplementary provision	Total
Consolidated				
Balance of provision as of beginning of year	798	1,877	192	2,867
Transfer (3)	8	(8)	-	-
Effect of new guidelines (2)	-	-	-	-
Provisions in reporting year	248	262	-	510
Decrease in provisions	(218)	(42)	(20)	(280)
Recovery of debt written off in previous years	-	(2)	-	(2)
Amount charged to statement of profit and loss	30	218	(20)	228
Write-off of debt	(15)	(164)	-	(179)
Balance of provision as of end of year	821	1,923	172	2,916
Includes - Balance of provision that was not deducted from loans to the public	-	104	-	104
The Bank				
Balance of provision as of beginning of year	759	1,842	189	2,790
Merged subsidiary	-	-	-	-
Transfer	8	(8)	-	-
Effect of new guidelines (2)	-	-	-	-
Provisions in reporting year	242	250	-	492
Decrease in provisions	(213)	(32)	(19)	(264)
Recovery of debt written off in previous years	-	(2)	-	(2)
Amount charged to statement of profit and loss	29	216	(19)	226
Debt write-off	(15)	(164)	-	(179)
Balance of provision as of end of year	781	1,886	170	2,837
Includes - Balance of provision that was not deducted from loans to the public	-	100	-	100

(1) Loans for which the provision was based on extent of arrears, does not include a provision for interest on debt in arrears. For other loans, does not include doubtful debt, after the debt were determined as doubtful.
(2) In a circular published by the Supervisor of Banks on January 1, 2006, guidelines regarding the way to calculate the provision for doubtful debt for housing loans were detailed.
(3) Balance of provision for mortgages previously specifically reviewed.
(4) Reclassified.

2006				2005			
Specific provision (1) (4)				Specific provision (1) (4)			
By extent of arrears	Other	Supplementary provision (2)	Total	By extent of arrears	Other	Supplementary provision (3)	Total
668	1,777	212	2,657	534	1,741	199	2,474
-	-	-	-	-	-	-	-
59	(5)	-	54	-	-	-	-
289	257	7	553	205	192	13	410
(217)	(57)	(27)	(301)	(71)	(46)	-	(117)
-	(1)	-	(1)	-	(1)	-	(1)
131	194	(20)	305	134	145	13	292
(1)	(94)	-	(95)	-	(109)	-	(109)
798	1,877	192	2,867	668	1,777	212	2,657
-	111	-	111	-	100	-	100
635	1,727	210	2,572	2	1,503	140	1,645
-	-	-	-	501	196	57	754
-	-	-	-	-	-	-	-
54	-	-	54	-	-	-	-
279	253	6	538	194	182	13	389
(209)	(43)	(27)	(279)	(62)	(44)	-	(106)
-	(1)	-	(1)	-	(1)	-	(1)
124	209	(21)	312	132	137	13	282
-	(94)	-	(94)	-	(109)	-	(109)
759	1,842	189	2,790	635	1,727	210	2,572
-	107	-	107	-	90	-	90

Note 4 - Loans to the Public

Reported amounts (in NIS millions)

D. Loans for housing in arrears for which a provision for doubtful debt was made based on extent of arrears

	December 31, 2007				
	3-6 months	6-15 months	15-33 months	Over 33 months	Total
Consolidated					
Amount in arrears	21	45	70	397	533
Includes: delinquency interest	-	1	3	133	137
Balance of provision for doubtful debt based on extent of arrears (1)	-	82	170	569	821
Balance of loans net of provision for interest on arrears and for doubtful debt	475	384	164	122	1,145
The Bank					
Amount in arrears	20	42	68	363	493
Includes: delinquency interest	-	1	3	114	118
Balance of provision for doubtful debt based on extent of arrears	-	77	163	541	781
Balance of loans net of provision for interest on arrears and for doubtful debt	449	360	159	106	1,074

	December 31, 2006 (2)				
	3-6 months	6-15 months	15-33 months	Over 33 months	Total
Consolidated					
Amount in arrears	19	49	80	364	512
Includes: delinquency interest	-	1	5	109	115
Balance of provision for doubtful debt based on extent of arrears (1)	-	85	189	524	798
Balance of loans net of provision for interest on arrears and for doubtful debt	417	423	193	116	1,149
The Bank					
Amount in arrears	18	46	77	335	476
Includes: delinquency interest	-	1	4	93	98
Balance of provision for doubtful debt based on extent of arrears	-	80	181	498	759
Balance of loans net of provision for interest on arrears and for doubtful debt	395	401	187	113	1,096

(1) Excludes provision for delinquency interest.
(2) Reclassified.

Note 4 - Loans to the Public

Reported amounts (in NIS millions)

E. Information on housing loans and way to compute the specific provision for doubtful debt

	December 31, 2007					
	Balance sheet loan balance(1)	Debt balance (2)	Includes: Amount in arrears (3)	Specific provision		
				By extent of arrears	Other	Total
Housing loans for which specific provision according to length of arrears must be calculated	35,939	1,131	529	816	-	816
Large loans (4)	2,551	123	30	5	27	32
Other loans	625	55	9	-	7	7
Total	39,115	1,309	568	821	34	855

	December 31, 2006 (5)					
	Balance sheet loan balance(1)	Debt balance (2)	Includes: Amount in arrears (3)	Specific provision		
				By extent of arrears	Other	Total
Housing loans for which specific provision according to length of arrears must be calculated	33,398	1,141	509	793	-	793
Large loans (4)	2,022	142	29	1	22	23
Other loans	832	102	14	4	6	10
Total	36,252	1,385	552	798	28	826

(1) The balance of housing loans, after deducting specific balance for doubtful debt and provision for delinquency interest.
(2) Balance of problem loans (in arrears by more than three months) and net of the balance of the provisions.
(3) Includes delinquency interest before deduction of the provisions balance.
(4) Housing loans, the balance of each of which exceeds NIS 805 thousand (on December 31, 2006 – NIS 783 thousand).
(5) Reclassified.

For details of rules for reduction in provision for doubtful debt by depth of arrears, as published in the circular dated January 1, 2006 by the Supervisor of Banks, see Note 1.P.3).

Note 4 - Loans to the Public
As of December 31, 2007 - Consolidated
Reported amounts (in NIS millions)

F. Balances of loans to the public and off-balance sheet credit risk according to the size of the loans and the credit risk of the borrower:

Loan ceiling and credit risk (in NIS thousands)		Number of Borrowers (1)	Loans (2)	Credit Risk (3)
	Up to 10	138,730	213	231
Above 10	Up to 20	55,745	420	627
Above 20	Up to 40	66,691	1,150	820
Above 40	Up to 80	88,921	2,840	2,092
Above 80	Up to 150	62,549	5,398	1,427
Above 150	Up to 300	60,493	12,285	673
Above 300	Up to 600	38,457	15,172	937
Above 600	Up to 1,200	10,159	7,479	705
Above 1,200	Up to 2,000	2,050	2,704	423
Above 2,000	Up to 4,000	1,237	2,844	591
Above 4,000	Up to 8,000	695	2,858	947
Above 8,000	Up to 20,000	487	4,548	1,741
Above 20,000	Up to 40,000	190	3,543	1,788
Above 40,000	Up to 200,000	189	8,656	7,266
Above 200,000	Up to 400,000	20	3,313	1,381
Above 400,000	Up to 677,387	5	1,069	1,517
Total		526,618	74,492	23,166

(1) Number of borrowers is based on total loans and credit risk.
(2) Net of specific provision for doubtful debt.
(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits.

Note 4 - Loans to the Public
At December 31, 2006 – Consolidated
Reported amounts (in NIS millions)

F. Balances of loans to the public and off-balance sheet credit risk according to the size of the loans and the credit risk of the borrower:

Loan ceiling and credit risk (in NIS thousands)		Number of Borrowers (1)(2)	Loans (3)	Credit Risk (2) (4)
	Up to 10	132,704	208	355
Above 10	Up to 20	53,765	420	604
Above 20	Up to 40	64,822	1,156	937
Above 40	Up to 80	91,208	3,066	2,541
Above 80	Up to 150	58,378	5,134	1,171
Above 150	Up to 300	60,522	11,991	564
Above 300	Up to 600	35,558	13,683	751
Above 600	Up to 1,200	8,399	6,028	555
Above 1,200	Up to 2,000	1,757	2,249	383
Above 2,000	Up to 4,000	1,150	2,550	549
Above 4,000	Up to 8,000	659	2,630	979
Above 8,000	Up to 20,000	496	4,372	1,651
Above 20,000	Up to 40,000	157	2,908	1,418
Above 40,000	Up to 200,000	220	9,546	7,420
Above 200,000	Up to 400,000	16	2,721	1,811
Above 400,000	Up to 696,864	5	1,639	1,087
Total		509,816	70,301	22,776

(1) Number of borrowers is based on total loans and credit risk.
(2) Restated.
(3) Net of specific provision for doubtful debt.
(4) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits.

Note 4 - Loans to the Public
At December 31, 2007 – The Bank
Reported amounts (in NIS millions)

F. Balances of loans to the public and off-balance sheet credit risk according to the size of the loans and the credit risk of the borrower - continued

Loan ceiling and credit risk (in NIS thousands)		Number of Borrowers (1)(2)	Loans (2)	Credit Risk (3)
	Up to 10	137,057	208	230
Above 10	Up to 20	54,863	409	626
Above 20	Up to 40	65,360	1,112	818
Above 40	Up to 80	86,905	2,722	2,089
Above 80	Up to 150	59,312	5,036	1,419
Above 150	Up to 300	56,165	11,370	652
Above 300	Up to 600	35,338	13,922	543
Above 600	Up to 1,200	9,137	6,681	445
Above 1,200	Up to 2,000	1,872	2,451	340
Above 2,000	Up to 4,000	1,155	2,643	509
Above 4,000	Up to 8,000	662	2,744	893
Above 8,000	Up to 20,000	468	4,474	1,532
Above 20,000	Up to 40,000	181	3,497	1,562
Above 40,000	Up to 200,000	182	8,613	6,948
Above 200,000	Up to 400,000	20	3,313	1,381
Above 400,000	Up to 677,387	5	1,069	1,517
		508,682	70,264	21,504

(1) Number of borrowers is based on total loans and credit risk.
(2) Net of specific provision for doubtful debt.
(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits.

Note 4 - Loans to the Public
At December 31, 2006 – The Bank
Reported amounts (in NIS millions)

F. Balances of loans to the public and off-balance sheet credit risk according to the size of the loans and the credit risk of the borrower - continued

Loan ceiling and credit risk (in NIS thousands)		Number of Borrowers (1)(2)	Loans (3)	Credit Risk (2) (4)
	Up to 10	130,713	202	354
Above 10	Up to 20	52,799	408	603
Above 20	Up to 40	63,345	1,116	935
Above 40	Up to 80	89,010	2,939	2,539
Above 80	Up to 150	55,140	4,772	1,168
Above 150	Up to 300	56,089	11,052	560
Above 300	Up to 600	32,664	12,519	276
Above 600	Up to 1,200	7,657	5,464	331
Above 1,200	Up to 2,000	1,593	2,013	302
Above 2,000	Up to 4,000	1,081	2,361	473
Above 4,000	Up to 8,000	625	2,518	880
Above 8,000	Up to 20,000	467	4,223	1,402
Above 20,000	Up to 40,000	147	2,826	1,136
Above 40,000	Up to 200,000	211	9,454	7,021
Above 200,000	Up to 400,000	16	2,721	1,811
Above 400,000	Up to 696,864	5	1,639	1,087
		491,562	66,227	20,878

(1) Number of borrowers is based on total loans and credit risk.
(2) Restated.
(3) Net of specific provision for doubtful debt.
(4) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits.

Note 5 - Loans to the Government
As of December 31

Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
Loans related to savings plans	1	1	1	1
Loans from debenture issuance proceeds	2	3	2	3
Loans as part of Ministry of Construction and Housing program to supplement interest of eligible borrowers (1)	-	38	-	38
Less - prepaid supplementary interest from the Government	-	(38)	-	(38)
Total loans to the Government	3	4	3	4

(1) As agreed with the Israeli Government with regard to loans given to certain borrowers deemed eligible by the Ministry of Housing and Construction, the Government undertook to supplement to the Bank the difference between the average interest rate prevailing at the mortgage bank during the period preceding the granting of the loans and the interest rate on loans to the above eligible borrowers. The supplemented interest, which is discounted at an annual rate of 2%, was placed as a deposit with the Accountant-General in favor of the Bank. In January 2007, the Government of Israel repaid all its obligations.

Note 6 - Investments in Investees and Details thereof
As of December 31

Reported amounts (in NIS millions)

A. Consolidated

	2007			2006		
	Affiliates	Subsidiaries	Total	Affiliates	Subsidiaries	Total
Investments in shares stated on the equity basis (including goodwill) (1)	(14)	7	(7)	15	4	19
Other investments -						
Subordinated notes and capital notes	24	-	24	23	-	23
Total investments	10	7	17	38	4	42
Includes:						
Loss accrued since acquisition date	(14)	-	(14)	(19)	-	(19)
Details of Goodwill (1)						
Amortization rate in years	-	10	10	-	10	10
Original amount	-	9	9	-	6	6
Net book value	-	7	7	-	4	4
Details of book value and market value of negotiable investments (2)						
Book value	-	-	-	20	-	20
Market value	-	-	-	21	-	21

(1) After the merger of “Tefahot” Israel Mortgage Bank Ltd. (hereinafter: “Bank Tefahot”), goodwill from acquisition of Bank Tefahot is presented under “other assets” with an amortized value, as of December 31, 2007, of NIS 26 million.

(2) See section E.3) for information on the sale of Mofet Israel Technology Fund Ltd.

Note 6 - Investments in Investees and Details thereof
As of December 31

Reported amounts (in NIS millions)

B. The Bank

	2007			2006		
	Affiliates	Subsidiaries	Total	Affiliates	Subsidiaries	Total
Investments in shares stated on the equity basis (including goodwill) (1)	(14)	1,038	1,024	15	1,106	1,121
Other investments -						
Payments on account of shares	-	-	-	-	72	72
Subordinated notes and capital notes	24	132	156	23	96	119
Total investments	10	1,170	1,180	38	1,274	1,312
Includes:						
Profits accrued since acquisition date	(14)	447	433	(19)	576	557
Post-acquisition items accrued in shareholders' equity:						
Adjustments on translation of financial statements	-	(51)	(51)	-	(51)	(51)
Details of Goodwill (1)						
Amortization rate in years	-	10	10	-	10	10
Original amount	-	9	9	-	6	6
Net book value	-	7	7	-	4	4
Details of book value and market value of negotiable investments (2)						
Book value	-	-	-	20	-	20
Market value	-	-	-	21	-	21

(1) After the merger of “Tefahot” Israel Mortgage Bank Ltd. (hereinafter: “Bank Tefahot”), goodwill from acquisition of Bank Tefahot is presented under “other assets” with an amortized value, as of December 31, 2007, of NIS 26 million.

(2) See section E.3) for information on the sale of Mofet Israel Technology Fund Ltd.

Note 6 - Investments in Investees and Details thereof
As of December 31

Reported amounts (in NIS millions)

Bank's share in profits (losses) of investees:

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Bank's share in operating profits (losses) of investees	(1)	(4)	9	69	76	103
Deferred taxes	-	-	(12)	-	-	(12)
Bank's share in operating profits of investees after tax effect	(1)	(4)	(3)	69	76	91

Note 6 - Investments in Investees and Details thereof

Reported amounts (in NIS millions)

	Company detail	Share in capital conferring rights to profits		Share in voting rights	
		December 31		December 31	
		2007	2006	2007	2006
C. Details of principal investees (2)					
1) Subsidiaries					
I. Bank Adanim Mortgages & Loans Ltd. ("Bank Adanim") (3)	mortgage bank	100%	96.5%	100%	98.2%
Mizrahi International Holding Company Ltd. (B.V. Holland) (4)	international holding company.	100%	100%	100%	100%
Mizrahi Tefahot Leasing and Finance Company Ltd.	equipment leasing company	100%	100%	100%	100%
Mashavim United Mizrahi Bank Issuing Company Ltd. (6)	issuance and finance company	-	100%	-	100%
Mizrahi Tefahot Underwriting and Issuance (1980) Ltd.	securities underwriter	100%	100%	100%	100%
Mizrahi Tefahot Management Ltd. (formerly Mizrahi Provident Fund Management Company Ltd.) (7)	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 Financial Holdings Ltd. (2)	previously managed mutual funds	100%	100%	100%	100%
Mizrahi Tefahot Issue Company Ltd.	issuance company	100%	100%	100%	100%
Mizrahi Tefahot Management Ltd. (formerly Tefahot Provident Fund Management Company Ltd.) (7)	previously managed provident funds	100%	100%	100%	100%
Tefahot Insurance Agency (1989) Ltd.	insurance agency	100%	100%	100%	100%
UMT Re Ltd. (Guernsey-resident company)	Insurance company	100%	100%	100%	100%
Netivot Finance Ltd.	previously managed provident funds	60%	60%	60%	60%

(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) See section E.1 for additional information.
(4) The company is incorporated in Holland; for a subsidiary of the Company, see section 3).
(5) Includes loss due to appreciation of the shekel, relative to foreign currency exchange rates, totaling NIS 11 million (2006 –NIS 10 million).
(6) On January 1, 2007, Mashavim United Mizrahi Bank Issuing Company Ltd. was merged into Netzivim Properties and Equipment Ltd., a company holding property used by the Bank, and its assets, liabilities and operating results are included in the Bank's financial statements.
(7) See section E.2) for information on the sale of provident fund operations.

Equity investment				Goodwill balance		Other capital investments (1)		Contribution to net operating profit (loss)		Dividend recorded	
At equity value		At market value									
December 31				December 31		December 31		For the year ended December 31		December 31	
2007	2006	2007	2006	2007	2006	2007	2006	2007	2006	2007	2006
296	188	-	-	7	4	124	168	22	22	-	-
246	244	-	-	-	-	-	-	(5) 2	(5) -	-	-
54	53	-	-	-	-	-	-	1	2	-	-
-	38	-	-	-	-	-	-	-	1	-	-
32	31	-	-	-	-	-	-	1	2	-	-
27	26	-	-		-	-	-	1	3	-	-
10	8	-	-	-	-	-	-	2	2	-	-
7	196	-	-	-	-	-	-	3	15	192	-
32	33	-	-	-	-	-	-	(1)	3	-	-
2	2	-	-	-	-	-	-	-	-	-	-
314	272	-	-	-	-	-	-	42	30	-	-
7	6	-	-	-	-	-	-	1	1	-	-
1	1	-	-	-	-	-	-	(1)	-	18	-

Note 6 - Investments in Investees and Details thereof

Reported amounts (in NIS millions)

Company name	Company detail	Share in capital conferring rights to profits		Share in voting rights	
		December 31		December 31	
		2007	2006	2007	2006
C. Details of principal investees – cont.					
2) Affiliates					
Psagot Jerusalem Ltd. (“Psagot”)	land for construction.	20%	20%	20%	20%
Mofet Israel Technology Fund Ltd. (“Mofet”) (2)	investment in hi-tech companies.	-	20%	-	20%
3) Major subsidiary of a subsidiary of Mizrahi International Holdings Ltd. (B.V. Holland) United Mizrahi Bank (Switzerland) Ltd. (4)	commercial bank	100%	100%	100%	100%

(1) Includes capital notes.

(2) See section E.3) for information on the sale of Mofet.

(3) Includes loss due to appreciation of the shekel, relative to the exchange rate of the Swiss franc, totaling NIS 2 million (2006 – NIS 1 million).

(4) United Mizrahi Bank (Switzerland) Ltd. is a commercial bank registered in Switzerland, and is presented at arm’s length on Bank financial statements.

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Equity investment				Other capital investments (1)		Contribution to net operating profit		Dividend recorded	
At equity value		At market value				For the year ended		For the year ended	
December 31				December 31		December 31		December 31	
2007	2006	2007	2006	2007	2006	2007	2006	2007	2006
(13)	(13)	-	-		23	-	1	-	-
-	20	-	21		-	-	(4)	-	-
153	146	-	-		-	(3)7	(3) 6	-	-

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Note 6 - Investments in Investees and Details thereof

D. Balance of goodwill related to subsidiaries – consolidated and the Bank (NIS in millions)

	Positive goodwill Reported amounts December 31, 2007
Cost	9
Accumulated amortization	2
Unamortized balance	7

Goodwill from acquisition of Bank Tefahot, which was merged into the Bank, whose amortized balance as of December 31, 2007 amounted to NIS 26 million, is presented under "Other assets".

E. Additional details

1) The Bank's rights in Bank Adanim are as follows:

a) As part of its undertakings toward the Bank of Israel to increase its capital sources, to maintain minimum capital, Bank Adanim issued subordinated notes to the Bank, which are convertible at any time to ordinary shares of Bank Adanim, after meeting several cumulative conditions requiring approval of the Audit Committee, the board of directors and a general meeting of Bank Adanim.

b) Commencing from July 2003, the shares of Bank Adanim were de-listed from trading on the Tel Aviv Stock Exchange.

c) On May 18, 2006, the Bank's Board of Directors approved the undertaking with Bank Adanim, in order to provide it with the shareholders' equity needed for its day-to-day business activities.

In conjunction with this undertaking:

(1) The Bank paid Bank Adanim NIS 72 million on account of 6,212 ordinary shares allocated to the Bank on February 18, 2007.

(2) The Bank acquired subordinated notes issued by Bank Adanim, in the principal amount of NIS 36 million, for a 10-year term from the issue date. The principal bears fixed interest at the interest rate of 10-year CPI-linked government bonds, plus a margin of 0.75% per annum; principal and interest will be linked to the CPI.

Note 6 - Investments in Investees and Details thereof

d) On February 4, 2007, Tel Aviv District Court ruled to adopt the arrangement plan under Section 350 of the Companies Law, whereby the Bank will purchase from all the other shareholders in Bank Adanim that hold ordinary shares, NIS 1 par value, all of the shares they own. Following this ruling, on February 9, 2007, the Bank purchased from all the said shareholders, all of the shares they had owned. As a result of the acquisition, Bank Adanim changed from a public company to a private company wholly-owned by the Bank.

2) On November 13, 2005, after having received approval of the Audit Committee, the Bank's board of directors approved the sale of the provident funds managed by the Bank, as follows:

- The sale of the assets or operations of all the provident funds managed by the Bank as a single block, to Excellence Investments Ltd., for NIS 405 million, as of September 30, 2005, subject to adjustments.
- The sale of all of the Bank's holdings (60%) in the shares of Netivot Management Company Ltd. ("Netivot") for NIS 37 million. Netivot manages 4 provident funds with total assets of NIS 1.9 billion.

On October 30, 2006, the Bank's Board of Directors approved the signing of an agreement for the sale of the Bank's provident fund activities.

On October 31, 2006, a sale agreement was signed, subject to various suspending conditions.

On March 5, 2007, after obtaining all required regulatory approvals, the transaction was closed in consideration for NIS 343 million, after adjustments that were agreed by the parties to the transaction. The proceeds were calculated at 3.63% of total provident fund assets under Bank management as of February 28, 2007, amounting to NIS 9.4 billion, after net decrease in assets, excluding returns, compared to total assets under management as of September 30, 2005.

As part of the transaction, in addition to the sales agreement, an operating agreement, distribution agreement and special services agreement were signed between the parties.

Note 6 - Investments in Investees and Details thereof

Pursuant to the agreement, the Bank will remain guarantor for 5 years from March 5, 2007, three of those years without consideration, for the nominal value of the deposits of members that are members of several provident funds included in the transaction, according to their provisions and bylaws. The guaranteed amount is NIS 151 million, which are considered risk assets according to the Bank of Israel directives, against actual assets of NIS 3.2 billion.

From this transaction, the Bank recorded in its financial statements for 2007 net profit from extraordinary operations in the amount of NIS 199 million.

Consequently to the Bank's announcement dated February 25, 2007 that it is in negotiations, along with remaining shareholders of Netivot, to sell all of Netivot's provident fund operations, on March 25, 2007, Netivot's Audit Committe and Board of Directors approved sale of all of Netivot's provident fund operations. On March 26, 2007, the Bank's Audit Committee and Board of Directors approved the Bank's consent to the transaction. The sale agreement was signed on March 28, 2007.

On June 28, 2007, the transaction for sale of provident fund operations managed by Netivot was completed, in exchange for NIS 51.8 million, which is 2.7% of average total assets under management by Netivot in the 3 months preceding completion of this transaction. The transaction was completed after obtaining all required regulatory approvals.

Netivot's profit from completion of this transaction amounted to NIS 32 million after tax. For this transaction, the Bank recorded in its statement of profit and loss for the second quarter of 2007, net profit from extraordinary operations in the amount of NIS 19 million (60% - equal to Bank share in holdings in Netivot).

In conjunction with this transaction, and in addition to the sale agreement, the parties signed other agreements, including an agreement for provident fund operation by the Bank and agreement on provision of services to provident fund members by the Bank in 2007.

Note 6 - Investments in Investees and Details thereof

3) On January 28, 2007, the Bank signed an agreement for the sale of 7.95% of the rights in capital and voting in Mofet Israel Technology Fund Ltd. ("Mofet"), which are held by the Bank, in consideration for NIS 8.3 million, subject to adjustments.

   Under the terms of the agreement, the Bank granted the buyer a call option, which is exercisable for 12 months, commencing from the closing date of the sale ("the call period"), to purchase the balance of the Bank's holdings in Mofet, representing 11.9% of the rights in capital and voting ("option shares”). Likewise, the buyer granted the Bank a put option, exercisable for one month from the end of the call period, for the sale of the option shares at an amount equal to the option proceeds.

   On January 30, 2007, all the suspending conditions for executing the transaction were fulfilled. On May 1, 2007, the option was exercised and the Bank sold its remaining holding in Mofet shares in exchange for NIS 14.5 million.

   Completion of this transaction, including exercise of the option, after adjustment for impact of changes in deferred taxes, contributed NIS 8 million to the Bank's net profit from extraordinary operations.

4) On March 27, 2007, the Bank signed a memorandum of understandings, whereby the Bank would acquire 50% of the issued capital of Bank Yahav for Government Employees Ltd. (“Bank Yahav”) inclusive of all rights associated therewith (“the acquired shares”). In exchange for the acquired shares, the Bank would pay proceeds as follows, based on Bank Yahav’s required shareholders’ equity for maintaining a minimum capital ratio of 10% (“required shareholders’ equity”). It was agreed that Bank Yahav would continue to obtain computer services from Bank Hapoalim, under terms currently in place between Bank Hapoalim and Bank Yahav, for a 3-year period from the transaction completion date. On September 9, 2007, a detailed agreement was signed for sale of the acquired shares based on principles set forth in the memorandum of understandings dated March 27, 2007.

   On November 13, 2007 an addendum to the agreement was signed by the parties, whereby, inter alia, the date for completion of the transaction was set to March 27, 2008; however, if by that date, sale of provident funds owned or controlled by Bank Yahav (“the funds”) would not be completed - the completion date would be postponed to June 27, 2008. Furthermore, arrangements were agreed, subject to the statute, with regard to Bank Yahav's preparations in conjunction with competition in the sector in which it operates. The parties also agreed on the final proceeds to be paid by the Bank for Bank Yahav shares owned by Bank Hapoalim, in accordance with principles for such calculation set forth in the agreement, at NIS 371 million, such that the proceeds would no longer be adjusted to changes in Bank Yahav's capital or results through the completion date (other than potential adjustment due to dividend distribution). Furthermore, Bank Hapoalim would be entitled to receive 50% of the additional shareholders' equity expected at Bank Yahav from sale of the funds.

Completion of this transaction is contingent on multiple suspensive conditions, including obtaining approval of the Commissioner of Restrictive Business Practices; obtaining a permit from the Bank of Israel Governor for sale and holding of the shares sold and for control of Bank Yahav by the Bank; completion of sale of the funds; transfer of the founding share at Bank Yahav (which is part of the acquired shares), in accordance with provisions of the "Share Capital" chapter of Bank Yahav's articles of incorporation.

5) On November 13, 2007, the Bank signed a memorandum of understandings with Isracard Ltd. and Europay (Eurocard) Israel Ltd. ("Isracard" and "Europay", respectively), whose highlights are set forth below. Isracard, Europay and the Bank would enter into accelerated negotiations (aiming to conclude them by April 3, 2008, pursuant to the addendum to the MOU signed on March 4, 2008) to replace their current agreed arrangements with a new agreement (for a 10-year term) aimed at issuing Mizrahi-Tefahot branded credit cards and agreeing on arrangements for operation and servicing by Isracard and/or Europay of debit cards to be issued by them and to be distributed by the Bank to its customers ("the new agreement").

The new agreement shall be signed no later than April 3, 2008 (as per the aforementioned addendum to the MOU), and in return the Bank would be eligible to receive allocation, at no further consideration, of 3.6% of Isracard and Europay ordinary shares in exchange for the new agreement and its provisions.

Note 6 - Investments in Investees and Details thereof

Should the new agreement not be signed by April 3, 2008, the Bank would be eligible to receive allocation of 1.8% of Isracard and Europay ordinary shares in exchange for continuing the current agreements in place for a 10-year term from the date of signing the MOU. In this case the Bank may distribute its branded card through any party of its choice. In December 2007, the Bank received allocation of 1.8% of the aforementioned shares.

Note that the maximum total shares to be allocated to the Bank in exchange for the aforementioned agreements, would be 3.6% of Isracard and Europay shares. The shares would be allocated subject to customary first-right-of-refusal to Bank Hapoalim Ltd. upon transfer of the shares by Mizrahi-Tefahot to any third party, and subject to a blocking period, whereby Mizrahi-Tefahot may not transfer the shares to any third party (other than Bank Hapoalim) during a 1-year period (the aforementioned right-of-first-refusal and blocking period shall be in effect for as long as Isracard and/or Europay shares are not listed for trading on the stock exchange).

The MOU is subject to all regulatory requirements required by statute, if any.

Note 7 - Buildings and Equipment

Reported amounts (in NIS millions)

a. Composition	Consolidated			The Bank		
	Buildings and land (including installations and leasehold improvements)	Equipment, furniture, and vehicles	Total	Buildings and land (including installations and leasehold improvements)	Equipment, furniture, and vehicles	Total
Average depreciation rate:	4%	20%		4%	20%	
Cost of the assets - December 31, 2006 (1)	1,156	1,113	2,269	1,129	1,092	2,221
Merger of subsidiary	-	-	-	8	-	8
Additions in 2007	46	190	236	43	190	233
Disposals in 2007	(170)	(45)	(215)	(158)	(42)	(200)
Cost of assets as of December 31, 2007 (2)	1,032	1,258	2,290	1,022	1,240	2,262
Accumulated depreciation as of December 31, 2006 (1) (3)	375	601	976	364	587	951
Merger of subsidiary	-	-	-	4	-	4
Depreciation	32	131	163	31	130	161
Recognized loss from impairment (4)	3	-	3	3	-	3
Disposals	(55)	(43)	(98)	(50)	(41)	(91)
Accumulated depreciation as of December 31, 2007	355	689	1,044	352	676	1,028
Net book value						
As of December 31, 2007 (2)	677	569	1,246	670	564	1,234
As of December 31, 2006 (2)	782	511	1,293	765	505	1,270

	Consolidated		The Bank	
	December 31		December 31	
	2007	2006	2007	2006
B. The above assets include assets not used by the Group:				
Not designated for sale	14	18	14	16
Designated for sale	3	69	3	69
Includes - leased to others	5	12	5	10

(1) Re-classified.

(2) Includes amortized capitalized cost of independently developed computer software as of December 31, 2007 amounting to NIS 71 million - consolidated and for the Bank (December 31, 2006 - NIS 64 million consolidated and for the Bank).

(3) Accumulated depreciation includes accumulated loss from impairment.

(4) Loss from impairment of buildings and equipment recognized in the reported period, were recorded under "Maintenance and amortization of properties and equipment". Impairment loss for assets where previously a similar loss has been recorded, are recorded under "profit from extraordinary items".

Note 7 - Buildings and Equipment

Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
C. Leasehold rights (mostly until 2025) in buildings				
Capitalized lease	77	74	77	74
Non-capitalized lease	22	28	22	28

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. Some of the buildings and leasehold rights, amounting to NIS 284 million – consolidated and for the Bank (December 31, 2006 - NIS 308 million consolidated and for the Bank), have not yet been registered in the Land Registry in the name of the Bank or its subsidiaries. Most of these properties are in the process of being registered.

F. On October 6, 2006, the Bank signed agreements for the sale of five real properties in Tel-Aviv from the Bank and from a wholly-controlled subsidiary of the Bank ("the sellers"), for total consideration of $26 million. Under the terms of the transaction, the Bank's subsidiary will rent two of the sold properties for a period of three years from the date conveyed to the buyers. The Bank also gave its agreement in principle to provide credit to the buyers for partial financing (not to exceed 50%) of the proceeds, at the same credit terms that the parties will agree to separately, according to the Bank's procedures and against collateral that will be agreed by the parties.

In June 2007 all suspensive conditions were met and the transaction was completed.

The (after-tax) profit from this transaction, based on self-assessment by the Bank with regard to liability for Appreciation Tax, amounts to NIS 10 million. According to assessment by the tax authorities of Appreciation Tax for this transaction (which the Bank has appealed), the Bank has additional tax liability of NIS 8 million, inter alia due to technical reasons to be remedied by the Bank. Should the Bank’s appeal of the Appreciation Tax assessment be rejected, net profit from extraordinary operations recorded by the Bank for this transaction would be NIS 2 million. Net profit from extraordinary operations was recorded for this transaction in the statement of profit and loss for the second quarter of the year, which Bank management believes would be no less than the net profit expected upon completion of the assessment proceedings.

Note 8 - Other Assets
As of December 31
Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
Deferred tax asset, net (see Note 28)	261	399	246	384
Related to loans	39	38	39	38
Excess of advance tax payments over current provisions	48	1	42	-
Debit balances for financial derivatives (except for embedded derivatives)	2,298	1,871	2,298	1,871
Goodwill from investment in merged company	26	30	26	30
Income receivable	46	44	36	41
Other receivables and debit balances	162	104	142	113
Total other assets	2,880	2,487	2,829	2,477

Note 9 - Deposits from the Public
As of December 31
Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
On-call deposits	6,948	6,522	6,828	6,458
Time and other deposits	65,160	61,888	66,412	62,378
Deposits in savings plans	3,182	4,824	3,013	4,599
Total deposits from the public	75,290	73,234	76,253	73,435

Note 10 - Deposits from Banks
As of December 31

Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
Commercial banks:				
On-call deposits	35	31	35	30
Term deposits	3,154	2,727	3,116	2,719
Acceptances	178	191	178	191
Special banking entities:				
On-call deposits	385	94	385	94
Term deposits	-	30	54	48
Total deposits from banks	3,752	3,073	3,768	3,082

Note 11 - Debentures and Subordinated Notes
As of December 31

Reported amounts (in NIS millions)

	Average maturity in years (1)		Internal rate of return (2)					
	Consolidated	The Bank	Consolidated	The Bank	Consolidated		The Bank	
	2007				2007	2006	2007	2006
Debentures and subordinated notes not convertible into shares:								
In Israeli currency, CPI-linked								
Debentures (3)	5.85	-	3.74%	-	1,364	1,044	-	1
Subordinated notes (4)	5.82	5.51	4.60%	4.86%	4,825	4,023	4,057	3,723
Total debentures and subordinated notes	5.83	5.51	4.41%	4.86%	6,189	5,067	4,057	3,724

(1) Average maturity is the average of the repayment periods, weighted by the 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) The debentures are secured by floating liens (some, also by fixed liens) on all of the assets of the issuing company. For details, see Note 15.F.
(4) Due for repayment upon liquidation after all other liabilities. This item includes subordinated notes issued by the Bank.

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 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.

Note 11 - Debentures and Subordinated Notes

In November 2006, subordinated notes, as noted above, amounting to NIS 460 million par value were issued to institutional investors in exchange for NIS 451 million; maturity date is January 1, 2106. These capital notes may be called by the Bank starting on December 31, 2021 – once every 5 years.

On May 20, 2007, the Bank's Board of Directors approved the prospectus for listing of the issued complex subordinated notes for trading. Based on this prospectus, the series may be expanded by further issuance of complex subordinated notes (Series A) up to a cumulative total of NIS 2 billion. On May 21, 2007, the Israel Securities Authority approved publication of the prospectus. The issued subordinated notes were listed for trading in early June 2007. In June 2007, the Bank issued and listed for trading additional subordinated notes amounting to NIS 500 million par value in exchange for NIS 490 million in proceeds.

B. Mizrahi Tefahot Issue Company ("the Company"), a company wholly-owned and controlled by the Bank, issued debentures and subordinated notes under the terms of a prospectus to the public, with a par value of NIS 1,158 million as of December 31, 2007, and 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 545 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.

Under the terms of a shelf registration prospectus published by the Company for the public on November 28, 2006, the Company may issue to the public additional bonds having par value of NIS 5 billion. In January 2007, the Company issued CPI-linked debentures having par value of NIS 300 million.

In May 2007, the Company issued under a shelf prospectus subordinated notes (Series 30), with principal and interest linked to the CPI amounting to NIS 450 million par value, maturing on May 28, 2017.

Note 12 - Other Liabilities
As of December 31

Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
Provision for deferred taxes, net (see Note 28)	11	16	11	16
Excess of current provisions for income taxes over advances paid	1	273	-	259
Excess of provision over funding severance pay, retirement and pension (see Note 16)	438	435	437	434
Deferred income	179	171	157	145
Credit balances for financial derivatives (except for embedded derivatives)	1,745	883	1,745	883
Accrued expenses	167	255	161	252
Provision for unutilized vacations and long- service bonus	104	115	104	114
Guarantees payable	23	20	23	20
Provision for doubtful debt for off-balance sheet and other items	104	(1) 111	100	(1) 107
Payables for credit card operations	1,154	1,056	1,154	1,056
Other payables and credit balances	321	(1) 375	294	(1) 362
Total other liabilities	4,247	3,710	4,186	3,648

(1) Reclassified.

Note 13 – Share Capital and Shareholders' Equity (1)

A. Details on share capital of the Bank (in NIS):

	Authorized		Issued and paid-up	
	December 31		December 31	
	2007	2006	2007	2006
Ordinary shares, NIS 0.1 (2)	40,000,000	40,000,000	22,181,255	21,900,093

(1) For allocation of stock options – see Note 16.A.
(2) The shares are listed for trading on the Tel Aviv Stock Exchange.

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%, a dividend 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.

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 a cash dividend, as long as its non-monetary assets exceed its adjusted shareholders' equity. As of December 31, 2007, the Bank’s reported capital exceeds its non-monetary assets by NIS 2,856 million.
- The permit issued to the purchasers of the controlling interest by the Bank of Israel Governor stipulates that a dividend will not be distributed out of profits accruing until September 30, 1994, the amount of which (after capitalization to a capital reserve in 1998) is NIS 100 million.
- See Note 14 for additional limitations.

D. After the balance sheet date, on February 19, 2008, a dividend of NIS 75 million was paid, which is 338% of issued capital, or NIS 0.34 per NIS 0.1 par value share.

Note 14 – Capital Adequacy
As of December 31, 2007 - Consolidated

Reported amounts (in NIS millions)

A. Capital adequacy is computed in accordance with Directives No. 341 and 311 of the Supervisor of Banks regarding the "minimum capital ratio" and "issuance of capital for exposure to market risks".

1. Bank capital for calculating minimum capital ratio (1)	
Tier I capital:	
Paid-up share capital and capital reserves	1,979
Retained earnings (2)	3,551
Minority interest in equity of subsidiaries	-
Amortization (3)	(37)
Total tier I capital	5,493
Upper Tier II capital (4)	1,068
Other Tier II capital	2,749
Total capital	9,310

	Balances (5)	Risk balances	Capital requirement (6)
2. Weighted average balance of credit risks			
Assets			
Cash and deposits with banks	10,701	1,604	144
Securities	6,145	998	90
securities loaned or sold in repurchase agreements	5	-	-
Loans to the public (4)	74,427	59,790	5,381
Loans to the Government	3	-	-
Investment in affiliates	17	11	1
Buildings and equipment	1,246	1,246	112
Fair value of derivtives	2,298	1,177	106
Other assets	582	508	46
Total assets	95,424	65,334	5,880
Off-balance sheet instruments			
Transactions in which the balance represents credit risk	10,112	9,463	852
Financial derivatives	11,876	5,326	479
Others	447	210	19
Total off-balance sheet instruments	22,435	14,999	1,350
Total credit risk assets and capital requirement	117,859	80,333	7,230
Market risk	1,866	1,866	168
Total risk assets and capital requirements	119,725	82,199	7,398

(1) There is no difference between the basis of consolidation according to accounting rules and the supervisory basis of consolidation according to instructions of the Supervisor of Banks with regard to minimum capital ratio.
(2) Including foreign currency translation adjustment of autonomous overseas units.
(3) Includes goodwill.
(4) The general provision for doubtful debt of NIS 107 million represents part of Tier II capital and is not deducted from loans to the public.
(5) Assets - balance sheet balances; off-balance sheet instruments - balance of stated values weighted by the conversion coefficients for loans.
(6) Capital requirement was calculated at a rate of 9%, in accordance with instructions of the Supervisor of Banks.

Note 14 – Capital Adequacy
As of December 31, 2007 - Consolidated

Reported amounts (in NIS millions)

	Balances	0%	20%	50%	100%	Risk Balances
3. Weighted credit risk balances by risk groups						
Assets						
Cash and deposits with banks	10,701	2,679	8,022	-	-	1,604
Securities loaned or sold in repurchase agreements	5	5	-	-	-	-
Securities	6,145	3,964	1,479	-	702	998
Loans to the public	74,427	5,490	72	18,179	50,686	59,790
Loans to the Government	3	3	-	-	-	-
Investment in affiliates	17	(2) 6	-	-	11	11
Buildings and equipment	1,246	-	-	-	1,246	1,246
Positive fair value of derivatives	2,298		1,401	-	897	1,177
Other assets	582	(3) 74	-	-	508	508
Total assets	95,424	12,221	10,974	18,179	54,050	65,334
Off-balance sheet instruments						
Transactions in which the balance represents credit risk	10,112	116	499	268	9,229	9,463
Financial derivatives	11,876	-	8,187	-	3,689	5,326
Others	447	-	296	-	151	210
Total off-balance sheet instruments	22,435	116	8,982	268	13,069	14,999
Total credit risk assets	117,859	12,337	19,956	18,447	67,119	80,333
Market risk	1,866	-	-	-	1,866	1,866
Total risk assets	119,725	12,337	19,956	18,447	68,985	82,199

(1) Assets - balance sheet balances; off-balance sheet instruments - balance of stated values weighted by the conversion coefficients for loans.
(2) Deducted from capital.
(3) Included NIS 26 million deducted from capital.

Note 14 – Capital Adequacy
As of December 31, 2007 - Consolidated
Reported amounts (in NIS millions)

4. Details of capital requirement for market risk:	
Interest risk	134
Share price risk	-
Exchange rate and inflation risk	26
Risk associated with options trading	8
Total capital requirement for market risk	168

5. Ratio of capital to elements of risk	in %
Ratio of Tier I capital to elements of risk	6.68
Ratio of total capital to elements of risk	11.33
Minimum capital ratio required by the Supervisor of Banks	9.00

Note 14 – Capital Adequacy

As of December 31, 2006 - Consolidated

Reported amounts (in NIS millions)

1. Bank capital for calculating minimum capital ratio (1)	
Tier I capital:	
Paid-up share capital and capital reserves	1,953
Retained earnings (2)	3,043
Minority interest in equity of subsidiaries	6
Amortization (3)	(33)
Total tier I capital	4,969
Upper Tier II capital (4)	558
Other Tier II capital	2,485
Total capital	8,012

	Balances (5)	Risk balances	Capital requirement (6)
2. Weighted average balance of credit risks			
Assets			
Cash and deposits with banks	10,797	1,845	166
Securities	5,979	1,232	111
securities loaned or sold in repurchase agreements	-	-	-
Loans to the public (4)	70,216	53,343	4,801
Loans to the Government	4	-	-
Investment in affiliates	42	38	3
Buildings and equipment	1,293	1,293	116
Debit balances for derivatives	1,871	1,053	94
Other assets	616	616	55
Total assets	90,818	59,420	5,348
Off-balance sheet instruments			
Transactions in which the balance represents credit risk (7)	8,371	8,192	737
Financial derivatives	9,558	4,899	441
Others (7)	342	186	17
Total off-balance sheet instruments	18,271	13,277	1,195
Total credit risk assets	109,089	72,697	6,543
Market risk	1,791	1,791	161
Total risk assets and capital requirements	110,880	74,488	6,704

(1) There is no difference between the basis of consolidation according to accounting rules and the supervisory basis of consolidation according to instructions of the Supervisor of Banks with regard to minimum capital ratio.
(2) Including foreign currency translation adjustment of autonomous overseas units.
(3) Includes goodwill.
(4) The general provision for doubtful debt of NIS 107 million represents part of Tier II capital and is not deducted from loans to the public.
(5) Assets - balance sheet balances; off-balance sheet instruments - balance of stated values weighted by the conversion coefficients for loans.
(6) Capital requirement was calculated at a rate of 9%, in accordance with instructions of the Supervisor of Banks concerning minimum capital ratio.
(7) Reclassified.

Note 14 – Capital Adequacy
As of December 31, 2006 - Consolidated

Reported amounts (in NIS millions)

	Balances	%0	%20	%50	%100	Risk Balances
3. Weighted credit risk balances by risk groups						
Assets						
Cash and deposits with banks	10,797	1,571	9,225	-	-	1,845
Securities	5,979	3,175	1,965	-	839	1,232
Loans to the public	70,216	6,442	917	19,393	43,463	53,343
Loans to the Government	4	4	-	-	-	-
Investment in affiliates	42	(2)4	-	-	38	38
Buildings and equipment	1,293	-	-	-	1,293	1,293
Positive fair value of derivatives	1,871	2	1,020	-	849	1,053
Other assets	616	-	-	-	616	616
Total assets	90,818	11,200	13,127	19,393	47,098	59,420
Off-balance sheet instruments						
Transactions in which the balance represents credit risk (3)	8,371	-	38	298	8,035	8,192
Financial derivatives	9,558	61	5,747	-	3,750	4,899
Others (3)	342	-	195	-	147	186
Total off-balance sheet instruments	18,271	61	5,980	298	11,932	13,277
Total credit risk assets	109,089	11,261	19,107	19,691	59,030	72,697
Market risk	1,791	-	-	-	1,791	1,791
Total risk assets and capital requirements	110,880	11,261	19,107	19,691	60,821	74,448

(1) Assets - balance sheet balances; off-balance sheet instruments - balance of stated values weighted by the conversion coefficients for loans.
(2) Deducted from capital.
(3) Reclassified.

Note 14 – Capital Adequacy
As of December 31, 2006 - Consolidated

Reported amounts (in NIS millions)

4. Details of capital requirement for market risk:	
Interest risk	119
Share price risk	2
Exchange rate and inflation risk	15
Risk associated with options trading	25
Total capital requirement for market risk	161

5. Ratio of capital to elements of risk	in %
Ratio of Tier I capital to elements of risk	6.67
Ratio of total capital to elements of risk	10.75 .
Minimum capital ratio required by the Supervisor of Banks	9.00

B. On May 14, 2007 the Board of Directors passed a resolution, effective as of May 17, 2007, instructing Bank management to act so as to have capital adequacy ratios (including upper tier II capital) of no less than 11.2% starting with financial statements for the second quarter of 2007. On February 25, 2008, the Bank's Board of Directors resolved to instruct Bank management to act so as to have the capital adequacy ratio (including upper tier II capital) be no less than 12% by end of 2009. These resolutions are in conjunction with the resolution by the Bank's Board of Directors from April 2006, stipulating that the capital adequacy ratio, excluding upper tier II capital, shall be no less than 10%.

C. Upper Tier II capital includes complex capital notes amounting to NIS 961 million as of December 31, 2007 and to NIS 451 million as of December 31, 2006. Their terms are as 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 components would decrease significantly, if the Bank's retained earnings balance would turn negative, or if the Bank's auditing CPA should raise significant doubt with regard to continued Bank status as a going concern - all under conditions set forth 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.

Note 15 - Liens

A. Stock exchange members are required to deposit a system of collateral that 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, toward 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) In the account opened by the stock exchange clearinghouse in its name ("collateral account in clearinghouse") government bonds of the Bank were deposited 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. The value of the bonds deposited is NIS 92 million as of December 31, 2007.
   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 in the event the Bank chooses to deposit cash as collateral instead of bonds, as well as the cash 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, 2007, no such amounts were deposited in this account.
   3) The accounts discussed in Par. 1 and 2 above will be 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).

Note 15 - Liens

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 the bonds deposited is NIS 1,305 million as of December 31, 2007.
2) Additionally, in the account opened by the Bank in its name in the stock exchange clearinghouse, government bonds are on deposit, valued at not less than 25% of the value of the collateral discussed in A. above. The value of the bonds deposited is NIS 323 million as of December 31, 2007. In accordance with a decision by the MAOF Clearinghouse Board of Directors dated January 31, 2008, the requirement for deposits in this account has been discontinued.
3) Additionally, in the account opened by the Maof Clearinghouse in its name for the Bank in another bank, cash will be deposited that the Bank will furnish as collateral in the event the Bank chooses to deposit cash as collateral instead of bonds, as well as the cash that will be paid as income on securities that will be deposited in the Bank's main Maof collateral account, or cash originating in any other financial right deriving from these securities, including monetary proceeds of sale. As of December 31, 2007, there were no amounts deposited in this account.
4) The accounts discussed in Par. 1-3 above will be pledged under a floating lien in favor of the Maof Clearinghouse and the accounts discussed in Par. 1 and 3 are also pledged under a fixed lien in favor of the Maof Clearinghouse.

C. In August 2007, the Bank of Israel launched the Real Time Gross Settlement framework ("RTGS"). This system 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. The value of debentures, deposited to the Bank of Israel account at the Stock Exchange Clearinghouse, amounts to NIS 282 million as of December 31, 2007.

Note 15 - Liens

D. To secure the credit lines received from overseas clearinghouses in the amount of USD 15 million, the Bank pledged securities held in the clearinghouse. The value of the securities held in the account totaled USD 16 million as of December 31, 2007. Pursuant to the agreement between the Bank and the clearinghouse, the clearinghouse has been given the right of offset in connection with the Bank's assets deposited with it.

E. In accordance with the requirement of the regulatory agencies in the U.S., the Bank’s branch there pledged securities worth USD 18 million, at the balance-sheet date, to secure deposits of the public or to comply with other government regulations, or to fulfill other governmental directives. Most of the lien, which amounted to USD 15.1 million as of December 31, 2007, relates to a demand by U.S. regulatory agencies to provide security for 10% of the branch’s liabilities, as defined by the authorities there.

F. Debentures and subordinated capital notes issued by a subsidiary, whose amortized cost as of December 31, 2007 amounted to NIS 788 million and NIS 227 million, respectively, are secured by current and fixed liens on deposits where proceeds of the issuances have been deposited.

G. The Bank and subsidiaries enter into credit support annex (CSA) agreements with foreign banks, intended to minimize the mutual credit risk created between banks in trading in derivatives. Pursuant to the agreements, the value of the inventory of trades in derivatives executed between the parties is measured, and if the net exposure of one of the parties exceeds a limit specified in advance, then that party transfers to the other party deposits by means of a lien, until the next measurement date. As of December 31, 2007, the Bank Group did not provide or receive deposits opposite foreign banks.

Note 16 – Employees's Rights

A. The employment terms of the vast majority of the Bank's employees and managers (except for those detailed in paragraphs B - I below) are determined in accordance with the provisions of collective labor agreements. The Bank's liability to these employees is 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. In respect of several previous Tefahot employees, the bank is legally absolved from making compensation payments only for the period commencing on February 1st, 2006 (In respect of previous Tefahot management, the bank is absolved from its obligation commencing January 1st, 2006). In respect of the banks' obligation until the end of 2005 (until January 2006 for previous Tefahot management), the bank has deposited funds in the pension and retirement funds.

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. The Bank's retired employees also receive non-pension benefits. The Bank's liability for these payments is covered by provisions, based on an actuarial calculation.

C. The Bank's Chairman of the Board is eligible, upon his resignation, to amounts that were regularly deposited on his behalf, at customary rates, in various funds.

D. The Bank's President ("the President") entered into an agreement with the Bank whereby he would be employed by the Bank for a 5-year term starting March 29, 2004. Under terms of the agreement, the President will be entitled, inter alia, to receive:

- Upon termination of his employment, severance pay equal to two salaries for each year of employment in the Bank, net of the monies provided to managers' insurance for severance pay, an acclimation grant equal to six months' salary and current amounts at acceptable rates deposited for him in the different funds. The financial statements included provisions for the said liabilities.
- A variable annual bonus, based on the rate of return of net profit to shareholders' equity, beginning at 200 thousand dollars for a rate of return of 8.5% to 11%, and up to 500 thousand dollars, if an annual rate of return of 14% or higher is achieved.
- See Note 16.A for details of options to acquire Bank shares granted to the President.

Note 16 – Employees's Rights

E. 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.
The Bank does not intend to dismiss any of these senior employees employed in the Bank, however, after taking into consideration the experience gained from the retirement of senior employees in the past, and taking into account the terms of their retirement, the financial statements include a provision for the full possible liability for these employees as of the date of the financial statements. These employees are also eligible, upon retirement, to other sums and rights, as accrued in their favor in various funds.
Further to that, in line with management expectations based on previous experience with payments to senior employees who have retired, a suitable provision has been made in the financial statements.

F. Several senior employees are eligible upon their retirement to an acclimation grant of three to six months' salary, for which a provision was recorded in the financial statements.

G. Three 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. In respect of this allowance, a full provision has been made in the financial statements.

H. Pension agreements were signed with three employees of an overseas affiliate of the Bank, whereby they will 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%.

Note 16 – Employees's Rights

I. On April 27, 2006, the Bank's Board of Directors approved a special collective agreement (labor agreement) reached with the employee representatives – clerk sector – for a period until December 31, 2010.

Under the agreement, the Bank may terminate up to 50 permanent employees during the term of the agreement for reason of incompatibility, as well as to institute a voluntary retirement plan (with veto rights to management) to terminate up to 200 other employees during the term of the agreement.

As of December 31, 2007, 143 employees who had signed personal retirement agreements under the terms of the voluntary retirement plan had terminated their employment. Additional employees who signed retirement agreements are expected to terminate their employment during 2008 and thereafter.

According to management's expectations for these employees, and based on management's assessment that the number of employees who will retire and will be dismissed will be 250, a pre-tax provision in the amount of NIS 208 million (NIS 131 million after tax) was recorded in 2006, which was calculated based also on an actuarial calculation, while using a 4% discount rate. The provision was included in "salaries and related expenses" in the statement of profit and loss.

J. In January 2007, management of Mehish Computer Services Ltd. ("Mehish"), a wholly-owned and wholly-controlled subsidiary of the Bank, whose financial statements are included in the Bank's financial statements, and the and the Employee Council of Mehish signed a collective bargaining agreement that contains a voluntary retirement plan. 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 Mehish.

As of December 31, 2007, 10 employees who had signed personal retirement agreements under the terms of the voluntary retirement plan had terminated their employment. Additional employees who signed retirement agreements are expected to terminate their employment during 2008.

In 2006 the Bank made a provision for cost of the voluntary retirement plan, based on management estimates, of NIS 25 million (NIS 15 million after tax).

Note 16 – Employees's Rights

K. 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 computation based on past experience and the likelihood that the employee will still be employed by the Bank on the vesting date.

L. Reserves 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.

See Note 1.L regarding implementation of the recommendations of the Superintendent of Insurance on the computation of provisions for annuity-type life insurance.

M. The provisions and deposits for employees' rights to pension, severance pay and acclimation grants are included in "other liabilities", as follows: (in reported amounts)

	Consolidated		The Bank	
	2007	2006	2007	2006
Amount of provision (1)	460	471	455	466
Amount funded (2)	22	36	18	32
Excess of provision over funding	438	435	437	434
(1) Includes in respect of pension liabilities	172	181	172	181

(2) The Bank and its subsidiaries may not withdraw the funded amounts other than for severance payment.

N. Provisions for employees' rights to vacation and seniority grants are included in "other liabilities" as follows (in reported amounts):

	Consolidated		The Bank	
	2007	2006	2007	2006
Provision for vacation	94	105	94	104
Provision for seniority bonuses	10	10	10	10

Note 16.A. – Share-based Payment Transactions

1. Share-based payment transactions

   Pursuant to the President's employment agreement ("the President"), the President is entitled to receive options to purchase Bank shares, according to a plan approved by the Audit Committee and board of directors of the Bank on October 25, 2004. Under the terms of the plan, the Bank will grant the President 5,464,442 non-marketable options which may be exercised for 5,464,442 shares of the Bank, subject to adjustments. The options offered to the President comprised, upon signing the agreement, 2.44% (after allocation) of the Bank's issued and paid-up capital.

   The President is entitled to receive the options in five equal annual installments, once every 12 months beginning April 1, 2005, subject to the exceptions stipulated in the agreement. The exercise price of the shares will be based on the stock market value of the Bank's shares on March 4, 2004 – NIS 14.39 – plus linkage to the CPI, and will be subject to adjustments deriving from the distribution of cash dividends and/or bonus shares, as well as issuance of rights of the Bank.

   The President will be eligible to exercise the options, in full or part, not later than two years after the actual termination of his employment, or by April 6, 2009, whichever is later, but not later than April 6, 2011.

   In the event of termination of the agreement by the Bank, and under the circumstances provided in the agreement, the President will be entitled to receive from the Bank, despite the termination, all of the salaries and related terms, except for the annual bonus, until the end of the agreement period. Likewise, under the said circumstances, the President will be entitled to receive all of the options under the option plan, and to exercise them for shares, as though he continued to work until the end of his period of employment.

   In accordance with the directives of the Supervisor of Banks, for the purpose of the financial statements, the value of the benefit inherent in the options granted to the President was measured, at the time that the agreement with him was signed, at its fair value.

   The amount of the theoretical benefit inherent in this plan, according to the Black & Scholes model, amounts to NIS 24 million, is being recorded in the statement of profit and loss over the five-year period commencing in April 2004, unless the special circumstances provided in the agreement apply (see Note 1.K. for a description of the relevant accounting policies). For a description of accounting policy on this issue, see Note 1.M.

   In applying this accounting treatment, the Bank was required to make several principal estimates: For the purpose of computing the amount of the benefit, management assumed that the President will exercise his options at the end of 5 years from the commencement date of his employment at the Bank.

   The expense charged to the statement of profit and loss in 2007 amounted to NIS 5 million.

The annual standard deviation of share returns was calculated, based on historical share prices for the 5 years prior to the calculation date, at 25.1%. The risk-free interest rate was determined using the yield of "Galil" CPI-linked government bonds bearing fixed interest for a 5-year term, at 3.9%. No assumptions were made as to dividend distribution.

Since the President's eligibility for the options will be in accordance with Section 102 of the Income Tax Ordinance – the capital track, the said expense will not be tax deductible to the Bank.

On November 23, 2004, approval was received from the TASE to register the shares for trading, which will be allotted after the exercise of the options.

On April 19, 2007 the President exercised 3,278,664 options in exchange for 1,938,771 shares. The average share price upon the exercise date was NIS 31.10. As of December 31, 2007, the President holds 2,185,778 stock options with an expected contractual term of 3 years, exercisable into 2,185,778 shares.

2. Options to 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, 2007, 11,620,973 options were allotted to 296 offerees.

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 totalling 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 will be recorded in 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.

In the year 2007, salary expenses of NIS 13 million were recorded for the option plan (compared with NIS 26 million last year), reducing after-tax net profit by NIS 7 million (compared with NIS 14 million last year).

B. Details of the number of stock options and their exercise price are as follows:

		2007		2006
	Number of stock options	Weighted average exercise price (in NIS)	Number of stock options	Weighted average exercise price (in NIS)
In circulation at year start	10,245,751	19.51	11,715,300	19.06
Granted during the year (1)	420,205	29.33	633,953	25.4
Forfeited during the year (2)	337,122	17.73	811,363	18.77
Exercised during the year	2,286,230	17.51	1,292,139	18.85
In circulation at year end (3)	8,042,604	18.84	10,245,751	19.51

(1) The weighted average fair value of stock options granted during the year, upon measuring, was NIS 5.23. (In 2006 – NIS 4.81).

(2) The weighted average share price upon exercise of options into shares during 2007 was NIS 30.19 (2006 – NIS 29.36).

(3) Stock options in circulation at year end by exercise price range:

	December 31, 2007		December 31, 2006	
Exercise price (NIS)	24-17	31-25	24-17	31-25
Number of options	7,331,142	711,462	9,920,642	325,109
Weighted average exercise price (in NIS)	17.79	27.86	19.26	27.03
Weighted average remaining contractual term (in years)	0.4	1.8	1.4	2.6
Of which vested:				
Number of options	2,931,530	68,126	1,423,858	-
Weighted average exercise price (in NIS)	17.79	25.72	19.29	-

Note 17 - Assets and Liabilities by Linkage Basis - Consolidated
As of December 31, 2007

Reported amounts (in NIS millions)

	Israeli currency		Foreign currency (1)			Non-monetary items	Total
	Non-linked	CPI-linked	U.S. dollars	Euro	Other currencies		
Assets							
Cash and deposits with banks	2,009	616	5,338	1,527	1,211	-	10,701
Securities	1,742	1,207	1,165	1,581	51	399 (3)	6,145
Securities loaned or sold in repurchase agreements	5	-	-	-	-	-	5
Loans to the public (2)	27,911	33,586	8,167	2,237	2,419	-	74,320
Loans to the Government	-	2	1	-	-	-	3
Investment in affiliates	24	-	-	-	-	(7)	17
Buildings and equipment	-	-	-	-	-	1,246	1,246
Other assets	2,184	310	242	66	35	43	2,880
Total assets	33,875	35,721	14,913	5,411	3,716	1,681	95,317
Liabilities							
Deposits from the public	36,125	20,020	13,651	3,256	2,238	-	75,290
Deposits from banks	1,052	1,633	748	106	213	-	3,752
Deposits from the Government	-	243	39	-	-	-	282
Debentures and subordinated notes	-	6,189	-	-	-	-	6,189
Other liabilities	3,249	558	150	82	61	147	4,247
Total liabilities	40,426	28,643	14,588	3,444	2,512	147	89,760
Difference	(6,551)	7,078	325	1,967	1,204	1,534	5,557
Non-hedging financial derivatives:							
Derivatives (except for options)	7,634	(5,220)	421	(1,592)	(1,243)	-	-
Net in-the-money options (in terms of underlying asset)	1,213	-	(837)	(413)	50	(13)	-
Net out-of-the-money options (in terms of underlying asset)	82	-	7	4	(100)	7	-
Total	2,378	1,858	(84)	(34)	(89)	1,528	5,557
Net in-the-money options (capitalized par value)	(1,841)	-	2,536	(660)	(41)	6	-
Net out-of-the-money options (capitalized par value)	84	-	(505)	415	(20)	26	-

(1) Includes amounts linked to foreign currency.
(2) The general, special and supplementary provisions for doubtful debt were deducted ratably from the various linkage categories.
(3) Includes NIS 322 million in respect of shares received to secure credit - see footnote (4) in Note 3 to the financial statements for 2007.

Note 17 - Assets and Liabilities by Linkage Basis - Consolidated

As of December 31, 2006

Reported amounts (in NIS millions)

	Israeli currency		Foreign currency (1)			Non-monetary items	Total
	Non-linked	CPI-linked	U.S. dollars	Euro	Other currencies		
Assets							
Cash and deposits with banks	1,265	1,127	6,484	897	1,024	-	10,797
Securities	1,823	398	1,518	1,758	78	(3) 404	5,979
Loans to the public (2)	24,399	33,044	8,065	2,133	2,468	-	70,109
Loans to the Government	-	3	1	-	-	-	4
Investment in affiliates	23	-	-	-	-	19	42
Buildings and equipment	-	-	-	-	-	1,293	1,293
Other assets	1,846	142	341	42	70	46	2,487
Total assets	29,356	34,714	16,409	4,830	3,640	1,762	90,711
Liabilities							
Deposits from the public	34,187	20,986	12,528	2,992	2,541	-	73,234
Deposits from banks	143	1,645	1,067	91	127	-	3,073
Deposits from the Government	221	296	43	-	-	-	560
Debentures and subordinated notes	-	5,067	-	-	-	-	5,067
Other liabilities	2,972	289	136	45	102	166	3,710
Total liabilities	37,523	28,283	13,774	3,128	2,770	166	85,644
Difference	(8,167)	6,431	2,635	1,702	870	1,596	5,067
Non-hedging financial derivatives:							
Derivatives (except for options)	10,828	(5,410)	(2,724)	(1,897)	(797)	-	-
Net in-the-money options (in terms of underlying asset)	(399)	-	225	243	(69)	-	-
Net out-of-the-money options (in terms of underlying asset)	11	-	(79)	7	61	-	-
Total	2,273	1,021	57	55	65	1,596	5,067
Net in-the-money options (capitalized par value)	(606)	-	340	139	127	-	-
Net out-of-the-money options (capitalized par value)	(2,015)	-	1,188	551	276	-	-

(1) Includes amounts linked to foreign currency.

(2) The general, special and supplementary provisions for doubtful debt were deducted ratably from the various linkage categories.

(3) Includes NIS 317 million for shares received to secure credit - see footnote (4) in Note 3 to the financial statements for 2006.

Note 17 - Assets and Liabilities by Linkage Basis - The Bank
As of December 31, 2007

Reported amounts (in NIS millions)

	Israeli currency		Foreign currency (1)			Non-monetary items	Total
	Non-linked	CPI- linked	U.S. dollars	Euro	Other currencies		
Assets							
Cash and deposits with banks	2,869	1,441	5,389	1,733	1,227	-	12,659
Securities	1,740	1,207	1,165	1,581	-	399 (4)	6,092
Securities loaned or sold in repurchase agreements	5	-	-	-	-	-	5
Loans to the public (2)	26,851	30,928	8,012	1,992	2,311	-	70,094
Loans to the Government	-	2	1	-	-	-	3
Investments in investees (3)	24	124	8	-	-	1,024	1,180
Buildings and equipment	-	-	-	-	-	1,234	1,234
Other assets	2,136	309	241	66	34	43	2,829
Total assets	33,625	34,011	14,816	5,372	3,572	2,700	94,096
Liabilities							
Deposits from the public	36,569	20,556	13,673	3,248	2,207	-	76,253
Deposits from banks	1,106	1,599	748	106	209	-	3,768
Deposits from the Government	-	236	39	-	-	-	275
Debentures and subordinated notes	-	4,057	-	-	-	-	4,057
Other liabilities	3,224	555	143	82	56	126	4,186
Total liabilities	40,899	27,003	14,603	3,436	2,472	126	88,539
Difference	(7,274)	7,008	213	1,936	1,100	2,574	5,557
Non-hedging financial derivatives:							
Derivatives (except for options)	7,634	(5,220)	421	(1,592)	(1,243)	-	-
Net in-the-money options (in terms of underlying asset)	1,213	-	(837)	(413)	50	(13)	-
Net out-of-the-money options (in terms of underlying asset)	82	-	7	4	(100)	7	-
Total	1,655	1,788	(196)	(65)	(193)	2,568	5,557
Net in-the-money options (capitalized par value)	(1,841)	-	2,536	(660)	(41)	6	-
Net out-of-the-money options (capitalized par value)	84	-	(505)	415	(20)	26	-

(1) Includes amounts linked to foreign currency.
(2) The general, special and supplementary provisions for doubtful debt were deducted ratably from the various linkage categories.
(3) Includes investments in overseas subsidiaries totaling NIS 258 million.
(4) Includes NIS 322 million in respect of shares received to secure credit - see footnote (4) in Note 3 to the financial statements for 2007.

Note 17 - Assets and Liabilities by Linkage Basis - The Bank
As of December 31, 2006

Reported amounts (in NIS millions)

	Israeli currency		Foreign currency (1)			Non-monetary items	Total
	Non-linked	CPI- linked	U.S. dollars	Euro	Other currencies		
Assets							
Cash and deposits with banks	1,937	1,788	6,712	1,071	977	-	12,485
Securities	1,821	397	1,517	1,758	18	404 (4)	5,915
Loans to the public (2)	23,573	30,302	7,794	1,953	2,416	-	66,038
Loans to the Government	-	3	1	-	-	-	4
Investments in investees (3)	23	95	-	-	-	1,194	1,312
Buildings and equipment	-	-	-	-	-	1,270	1,270
Other assets	1,839	141	340	42	69	46	2,477
Total assets	29,193	32,726	16,364	4,824	3,480	2,914	89,501
Liabilities							
Deposits from the public	34,800	20,532	12,595	2,985	2,523	-	73,435
Deposits from banks	191	1,601	1,068	91	131	-	3,082
Deposits from the Government	221	287	43	-	-	-	551
Debentures and subordinated notes	-	3,724	-	-	-	-	3,724
Other liabilities	2,947	284	133	45	99	140	3,648
Total liabilities	38,159	26,428	13,839	3,121	2,753	140	84,440
Difference	(8,966)	6,298	2,525	1,703	727	2,774	5,061
Non-hedging financial derivatives:							
Derivatives (except for options)	10,828	(5,410)	(2,724)	(1,897)	(797)	-	-
Net in-the-money options (in terms of underlying asset)	(399)	-	225	243	(69)	-	-
Net out-of-the-money options (in terms of underlying asset)	11	-	(79)	7	61	-	-
Total	1,474	888	(53)	56	(78)	2,774	5,061
Net in-the-money options (capitalized par value)	(606)	-	340	139	127	-	-
Net out-of-the-money options (capitalized par value)	(2,015)	-	1,188	551	276	-	-

(1) Includes amounts linked to foreign currency.
(2) The general, special and supplementary provisions for doubtful debt were deducted ratably from the various linkage categories.
(3) Includes investments in overseas subsidiaries totaling NIS 253 million.
(4) Includes NIS 317 million in respect of shares received to secure credit - see footnote (4) in Note 3 to the financial statements for 2006.

Note 18 - Assets and Liabilities by Linkage Basis
& Term to Maturity (1) - Consolidated
As of December 31, 2007

Reported amounts (in NIS millions)

	Expected contractual future cash flows				
	On call to 1 month	1 month to 3 months	3 months to 1 year	1 year to 2 years	2 years to 3 years
Israeli currency - unlinked					
Assets (3)	10,195	3,153	7,676	2,937	2,159
Liabilities	32,947	2,154	4,003	1,766	107
Difference	(22,752)	999	3,673	1,171	2,052
Derivatives (except for options)	2,545	651	3,158	1,081	(28)
Options (in terms of underlying asset)	167	411	548	161	8
Israeli currency - linked to the CPI					
Assets	166	901	4,158	4,622	4,528
Liabilities	500	814	4,803	4,931	3,132
Difference	(334)	87	(645)	(309)	1,396
Derivatives (except for options)	(766)	1,102	(4,774)	(981)	47
Options (in terms of underlying asset)	65	-	(14)	(57)	-
Foreign currency - Israeli operations (4)					
Assets (3)	5,792	3,077	3,307	1,561	958
Liabilities	9,445	5,653	2,042	207	53
Difference	(3,653)	(2,576)	1,265	1,354	905
Derivatives (except for options)	(1,779)	(1,753)	1,616	(100)	(19)
Options (in terms of underlying asset)	(232)	(411)	(534)	(104)	(8)
Foreign currency - overseas operations					
Assets	708	1,330	1,454	484	491
Liabilities	724	1,015	501	115	81
Difference	(16)	315	953	369	410
Non-monetary items					
Assets	5	-	-	-	-
Liabilities	105	-	-	-	-
Difference	(100)	-	-	-	-
Total					
Assets	16,866	8,461	16,595	9,604	8,136
Liabilities	43,721	9,636	11,349	7,019	3,373
Difference	(26,855)	(1,175)	5,246	2,585	4,763

(1) Presented in this note are expected contractual future cash flows in respect of 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 debt.
(2) Includes assets totaling NIS 895 million which are past due.
(3) Includes NIS 5,480 million of loans at debitory account terms and NIS 299 million exceeding limits in debitory account facilities.
(4) Includes linked to foreign currency.
(5) As in Note 17 "Assets and Liabilities Classified According to Linkage Basis", includes off-balance sheet items related to derivatives.

Expected contractual future cash flows - continued						Balance sheet balance (5)	
3 years to 4 years	4 years to 5 years	5 years to 10 years	10 years to 20 years	Over 20 years	Total cash flows	Without fixed maturity	Total
1,304	1,319	3,517	5,071	1,104	38,435	1,483 (2)	33,875
14	282	(924)	1	0	40,350	36	40,426
1,290	1,037	4,441	5,070	1,104	(1,915)	1,447	(6,551)
726	7	-	-	-	8,140	0	7,634
-	-	-	-	-	1,295	0	1,295
3,953	3,839	14,238	10,597	1,855	48,857	801	35,721
3,426	2,874	10,962	3,084	205	34,731	407	28,643
527	965	3,276	7,513	1,650	14,126	394	7,078
(122)	(92)	-	-	-	(5,586)	-	(5,220)
-	-	-	-	-	-	-	-
767	632	2,249	1,466	227	20,036	826	18,075
23	55	19	36	0	17,533	6	17,381
744	577	2,230	1,430	227	2,503	820	694
(604)	85	-	-	-	(2,554)	-	(2,414)
-	-	-	-	-	(1,289)	-	(1,289)
427	355	1,038	164	197	6,648	68	5,965
36	117	604	187	0	3,380	(1)	3,163
391	238	434	(23)	197	3,268	69	2,802
-	-	-	-	-	5	1,678	1,681
-	-	-	-	-	105	63	147
-	-	-	-	-	(100)	1,615	1,534
6,451	6,145	21,042	17,298	3,383	113,981	4,856	95,317
3,499	3,327	10,661	3,308	205	96,099	511	89,760
2,952	2,817	10,381	13,990	3,178	17,882	4,345	5,557

Note 18 - Assets and Liabilities by Linkage Basis
& Term to Maturity (1) – the Bank
As of December 31, 2007

Reported amounts (in NIS millions)

	Expected contractual future cash flows				
	On call to 1 month	1 month to 3 months	3 months to 1 year	1 year to 2 years	2 years to 3 years
Israeli currency - unlinked					
Assets (3)	10,075	3,260	7,612	2,815	2,258
Liabilities	32,981	2,530	4,012	1,766	108
Difference	(22,906)	730	3,600	1,049	2,150
Derivatives (except for options)	2,545	651	3,158	1,081	(28)
Options (in terms of underlying asset)	167	411	548	161	8
Israeli currency - linked to the CPI					
Assets	179	932	3,851	4,262	4,207
Liabilities	461	730	4,492	4,505	2,912
Difference	(282)	202	(641)	(243)	1,295
Derivatives (except for options)	(766)	1,102	(4,774)	(981)	47
Options (in terms of underlying asset)	65	0	(14)	(57)	0
Foreign currency - Israeli operations (4)					
Assets (3)	5,786	3,073	3,290	1,537	936
Liabilities	9,439	5,638	1,839	207	53
Difference	(3,653)	(2,565)	1,451	1,330	883
Derivatives (except for options)	(1,779)	(1,753)	1,616	(100)	(19)
Options (in terms of underlying asset)	(232)	(411)	(534)	(104)	(8)
Foreign currency - overseas operations					
Assets	540	1,287	1,599	484	491
Liabilities	788	978	660	115	81
Difference	(248)	309	939	369	410
Non-monetary items					
Assets	5	-	-	-	-
Liabilities	105	-	-	-	-
Difference	(100)	-	-	-	-
Total					
Assets	16,585	8,552	16,352	9,098	7,892
Liabilities	43.774	9,876	11,003	6,593	3,154
Difference	(27,189)	(1,324)	5,349	2,505	4,738

(1) Presented in this note are expected contractual future cash flows in respect of 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 debt.
(2) Includes assets totaling NIS 895 million which are past due.
(3) Includes NIS 5,480 million of loans at debitory account terms and NIS 299 million exceeding limits in debitory account facilities.
(4) Includes linked to foreign currency.
(5) As in Note 17 "Assets and Liabilities Classified According to Linkage Basis", includes off-balance sheet items related to derivatives.

		Expected	contractual future cash flows - continued			Balance sheet balance (5)	
3 years to 4 years	4 years to 5 years	5 years to 10 years	10 years to 20 years	Ov er 20 years	Total cash flows	Without fixed maturity	Total
1,545	1,361	3,141	4,647	1,069	37,783	1,455 (2)	33,625
14	274	(924)	1	0	40,762	36	40,899
1,531	1,087	4,065	4,646	1,069	(2,979)	1,419	(7,274)
726	7	-	-	-	8,140	-	7,634
-	-	-	-	-	1,295	-	1,295
3,716	3,620	13,736	10,342	1,845	46,690	801	34,011
3,246	2,706	10,504	2,999	205	32,760	404	27,003
470	914	3,232	7,343	1,640	13,930	397	7,008
(122)	(92)	-	-	-	(5,586)	-	(5,220)
-	-	-	-	-	(6)	-	(6)
744	610	2,146	1,395	185	19,702	826	17,856
23	55	19	36	-	17,309	6	17,163
721	555	2,127	1,359	185	2,393	820	693
(604)	85	-	-	-	(2,554)	-	(2,414)
-	-	-	-	-	(1,289)	-	(1,289)
427	355	1,038	164	197	6,582	68	5,904
36	117	604	187	-	3,566	(1)	3,348
391	238	434	(23)	197	3,016	69	2,556
-	-	-	-	-	5	2,694	2,700
-	-	-	-	-	105	42	126
-	-	-	-	-	(100)	2,652	2,574
6,432	5,946	20,061	16,548	3,296	110,762	5,844	94,096
3,319	3,152	10,203	3,223	205	94,502	487	88,539
3,113	2,794	9,858	13,325	3,091	16,260	5,357	5,557

Note 18 - Assets and Liabilities by Linkage Basis & Term to Maturity (1) – Consolidated & the Bank As of December 31, 2006

Reported amounts (in NIS millions)

	Expected contractual future cash flows				
	On call to 1 month	1 month to 3 months	3 months to 1 year	1 year to 2 years	2 years to 3 years
Consolidated					
Assets (1)	18,027	7,271	16,810	9,336	6,856
Liabilities	38,108	10,138	12,424	7,139	4,040
Difference	(20,081)	(2,867)	4,386	2,197	2,816

The Bank					
Assets (1)	17,924	7,189	16,533	8,852	6,390
Liabilities	38,313	10,380	12,216	6,781	3,629
Difference	(20,389)	(3,191)	4,317	2,071	2,761

(1) Includes NIS 5,915 million of loans at debitory account terms and NIS 319 million exceeding limits in debitory account facilities.

(2) Includes assets totaling NIS 739 million which are past due.

Expected contractual future cash flows - continued						Balance sheet balance	
3 years to 4 years	4 years to 5 years	5 years to 10 years	10 years to 20 years	Over 20 years	Total cash flows	Without fixed maturity	Total
5,221	5,065	19,407	16,847	2,975	107,815	(2) 7,459	90,711
2,990	3,199	10,535	3,099	247	91,919	657	85,644
2,231	1,866	8,872	13,748	2,728	15,896	6,802	5,067
5,119	5,124	18,523	16,090	2,927	104,671	8,563	89,501
2,771	3,020	10,059	2,985	247	90,401	627	84,440
2,348	2,104	8,464	13,105	2,680	14,270	7,936	5,061

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

Reported amounts (in NIS millions)

	Consolidated		The Bank	
	2007	2006	2007	2006
A. Off-balance sheet financial instruments				
Contract balances or their stated amounts at the end of the year				
Transactions in which the balance represents a credit risk:				
- Documentary credit	707	502	707	502
- Loan guarantees	2,847	1,718	2,694	1,595
- Guarantees to purchasers of homes	5,613	5,705	4,888	5,043
- Other guarantees and liabilities (1)	1,655	1,127	1,641	1,113
- Unutilized revolving credit card facilities	3,192	2,900	3,192	2,900
- Unutilized debitory account and other credit facilities in accounts available on demand	23,895	(2) 19,912	23,895	(2) 19,912
- Irrevocable commitments for loans approved but not yet granted	4,391	(3) 4,243	3,490	(3) 3,238
- Commitments to issue credit to savers (4)	1,686	1,676	1,686	1,676
- Commitments to issue guarantees	4,017	(2) 5,390	3,554	(2) 4,696

(1) Includes the Bank's liabilities for its share in the risks fund of the Maof Clearinghouse of NIS 225 million. (December 31, 2006 – NIS 144 million), see Note 19.D.2) and Note 15.B.
(2) Restated.
(3) Reclassified.
(4) See Note 19.d.19).

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

Reported amounts (in NIS millions)

	Consolidated	
	2007	2006
B. Off-balance sheet liability for activities based on extent of collection (1) as of end of year		
1. Balance of loans from deposits based on extent of collection (2)		
Israeli currency - linked to the CPI	16,192	16,445
Israeli currency - unlinked	423	321
In foreign currency	241	277
Total	16,856	17,043

2. Flows in respect of collection commissions on activities based on extent of collection (3)

	2007							2006
	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
Flows of futures contracts	102	198	187	409	359	13	1,268	1,342
Expected future flows net of management's estimate of early repayments	102	195	181	377	273	5	1,133	1,196
Discounted expected future flows net of management's estimate of early repayments (4)	100	178	151	272	154	2	857	871

3. Information on loans made available during the year

	Consolidated	
	2007	2006
Loans out of deposits according to extent of collection	773	766
Standing loans and grants	167	223

(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 in respect thereof totaling NIS 5,037 million (previous year - NIS 5,570 million) are not included in this table.
(3) Includes unlinked shekel sector and foreign currency sector.
(4) Discounted at the rate of 4.5% (2006 - 4.9%).

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

Reported amounts (in NIS millions)

	2007	2006	2007	2006
C. Special commitments:				
Liabilities in respect of:				
Long-term rental contracts (1)	351	207	308	204
Computerization and software services contracts	100	110	100	110
Acquisition of buildings and their renovation	19	1	19	1
Receipt of deposits on future dates (2)	5	28	5	12

(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	
	2007	2006	2007	2006
First year	31	22	27	21
Second year	31	21	28	21
Third year	28	21	26	21
Fourth year	26	20	24	19
Fifth year	25	18	23	17
Sixth year and thereafter	210	105	180	105

(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

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 risks fund was established, which totaled NIS 942 million as of December 31, 2007. The Bank's share in the fund as of December 31, 2007 is estimated at NIS 71 million. The risks fund will be updated in March of every year, based on the daily average of trading volume cleared in the calendar year that ended prior to the date of update. In no case will the amount fall below NIS 150 million. Each member's share in the risks 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 will be no less than NIS 500 thousand.
   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, at the balance sheet date, totals NIS 332 million (December 31, 2006 – NIS 307 million).
   Likewise, the Bank has undertaken to refund its share in the risk fund of the Maof Clearinghouse, which totaled NIS 1,094 million as of December 31, 2007.
   The Bank's share in the fund as of December 31, 2007 is estimated at NIS 225 million.
   For information regarding charges that the Bank undertook to furnish in respect of 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) The Bank has deposited debentures, which were valued at 64 million dollars at the balance sheet date, with an overseas brokerage firm as collateral for the securities activity of its customers with that brokerage firm. The brokers were

given the right of set-off with regard to these debentures against amounts owed to them, and the Bank also undertook to refrain from pledging these debentures.

5) Pursuant to the sale agreement of provident fund operations managed by the Bank (for details see Note 6.E.2), the Bank guarantees for 5 years starting on March 5, 2007 to members of the provident funds and the severance pay fund, to refund nominal principal amounts deposited by them on time. As of the balance sheet date, the funds' assets are deposited mostly in bonds approved for investment, and they exceed the amount of the banks' guarantees. The principal amount of the deposits as of December 31, 2007 is NIS 3,175 million.
The fair value of this guarantee, which constitutes a put option written by the Bank, is not material.

6) 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.

7) In December 2001, a General Meeting of the Bank's shareholders ratified the granting, in advance, of exemption from liability and undertook to indemnify the board of directors and other officers (collectively – "officers") by the Bank.
According to the indemnification obligation, the Bank exempts its officers, in advance, from any liability thereto, due to damage to be caused to the Bank as a result of the breach of the duty of care by an officer toward the Bank in his

activity as officer, by virtue of his being an officer of the Bank, and all that is stipulated in the indemnity undertaking.

The cumulative indemnity amount to be paid by the Bank to all officers will not exceed 25% of the Bank's shareholders' equity as reported in its 2000 financial statements, adjusted for the changes in the CPI, beginning December 2000. The indemnification applies to all activities relating – directly or indirectly – to one or more of the events listed in the addendum to the indemnification undertaking.

On October 28, 2004, the General Meeting of the Bank resolved to add to the Bank's indemnification undertaking toward the directors and officers in the Bank, which was approved in 2001, a clause prescribing that the indemnification undertaking will also apply in the event of a merger, as defined in the Companies Law, including any resolution, action, agreement or reporting related to the 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 in respect of the indemnification.

8) 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 the Companies Ordinance.

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 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 the terms of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

9) 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 in respect of any reasonable legal expenses (including fees to attorneys and other experts), which may be indemnified in accordance with the provisions of the Companies Law, all up to a limit of NIS 1 billion, linked to the CPI.

Bank Tefahot undertook toward the Tefahot Issuance that, if is will be unable to fulfill its obligations to the indemnity recipients, or any one of them, Bank Tefahot

will pay to Tefahot Issuance any amount that Tefahot Issuance will be found liable to indemnify, beyond the amounts paid by Tefahot Issuance.
Under the terms of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

10) 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.

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 at 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 the terms of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

11) 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, on a matter covered by the indemnification, as discussed in Par. A) and B) above, 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.

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 is 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.

12) 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 exceeds 1% of the Bank's shareholders' equity:

A. In March 1999, a claim was filed in Tel Aviv District Court against the Bank in the amount of NIS 20 million (for fee purposes), for damages of NIS 108 million that the plaintiffs (a company in liquidation and its former shareholders) alleged were caused as a result of the Bank's refusal to continue to approve an agreed upon credit facility for the plaintiff company to conduct his business activities, freezing the plaintiff company's account, and not honoring checks that had been deposited for collection. The plaintiffs allege that this led to the collapse of the plaintiff company. In July 1999, a defense motion was filed by the Bank, rejecting the plaintiff's claims of an alleged violation of the Bank's obligations as a bank corporation. The Bank claims that all his aforementioned actions were lawful.

Bank management estimates, based inter alia on information available to it and on opinion of legal counsel obtained on this issue, which assumes that the Bank's version makes plaintiffs' claims unfounded, and due to the fact that questioning of witnesses and findings thus far during said investigations indicate that probability of rejection of plaintiffs' claims with regard to Bank liability to them is very high. The probability of realization of risk exposure in this lawsuit is very low; hence no provision was made in the financial statements.

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.

Bank management estimates, based on opinion of legal counsel, that the probability of the Bank being required to pay the claim amount is very low, hence no provision was made in the financial statements.

C. In December 2002, the Supervisor of Banks submitted a motion to the Standard Contracts Tribunal against Bank Tefahot, to cancel or modify the wording of the guarantees that Bank Tefahot issues under the Sale (Apartments) (Assurance of Investment of Persons Acquiring Apartments) Law, 1974 ("the Law"), claiming that the guarantees contain unduly onerous conditions.The Supervisor also wishes to cancel or modify the provisions of guarantees that were issued prior to the delivery of the Tribunal's ruling, which have not been realized in full.

The Bank reached agreement with the Supervisor of Banks, whereby the guarantee provided by the Bank under the Sale (Apartments) (Assurance of Investment of Persons Acquiring Apartments) Law, 1974, would be rephrased. This agreement was adopted as a verdict by the Uniform Contract Court in October 2007.

D. In April 2003, a claim was filed against the Bank in Tel Aviv District Court, for NIS 12 thousand, as well as a motion for recognition as class action for the total payment of approximately NIS 300. The plaintiffs allege that the Bank must refund to them, personally and to the entire group, charges that were recorded in the seven years preceding the filing date of the claim, in accounts classified by the Bank as "legal customers", for "treasury" and "journal", which the Bank is not permitted to collect because of the Bank's improper disclosure of the substance of the charges. The plaintiffs are requesting for themselves, in addition to the claim amount, fees for their filing of the claim and legal costs.

In view of the District Court's opinion in a verdict dated April 2005, that the remedy it would have approved had the claim been accepted as a class action suit, would be to instruct the Bank to correct its accounts such that charges not in line with the verdict are cancelled, and to instruct the Bank to provide information to customers in legal proceedings of their accounts with the Bank - Bank exposure is to costs associated with compliance with Court instructions, and not to any monetary remedy over and above payment of fees for the plaintiff and his attorneys, as set forth above. The Bank complies with provisions of the verdict dated April 2005 from the date it received the verdict and thereafter.

Therefore, under the circumstances, Bank management estimates, based on opinion of legal counsel, that the risk of additional remedies for the plaintiffs is very low, hence no provision was made in the financial statements.

E. In July 2003, an action was filed with Tel Aviv District Court as well as a motion for recognition as a class action (“the claim”) against Bank Tefahot, other banks and the Commissioner of Customs and Stamp Duty. The claim relates to the calculation of the stamp duty.

One of the plaintiffs, who received a loan from Bank Tefahot, is claiming differences on stamp duty of NIS 36. The claim was filed for a total of NIS 300 million. The claim alleges that the Bank failed to comply with a ruling by the Supreme Court, which held that when an agreement includes consideration to be paid in installments, the nominal amount that is to be valued for stamp duty purposes is to be according to the present value of the loan principal only. It was the practice at Bank Tefahot, like at the other banks, to take all the future interest into account for stamp duty purposes, without discounting it, in accordance with the requirements of the Stamp Duty Authorities.

Due to the fact that every amount collected by Bank Tefahot for the stamp duty was collected in accordance with the requirements of the authorities, and the amounts were transferred to the authorities, it appears that this claim is inappropriate and should be only be brought against the Stamp Duty Authorities, which should refund the duty that was unlawfully collected, if it was unlawfully collected. Therefore, according to bank management estimate, based on opinion of legal counsel, probability of the lawsuit against the Bank prevailing is very low; hence no provision was made in the financial statements.

F. In August 2003, an action was filed in Haifa District Court against five banks, including the Bank, as well as a motion for recognition as a class action ("the Action"). The amount of the action was left to the discretion of the Court.
In December 2003, the plaintiffs filed an amended action, in which they allege that the Bank does not comply with Amendment No. 2 to Proper Conduct of Banking Business Regulations (Service to Customer) (Proper

Disclosure and Delivery of Documents), 2003, as amended by the Bank of Israel in August 2003. They allege that when they deposited checks in the Bank, they were not informed that a transaction recording fee would be charged in the account.
The Bank argues that it had fulfilled the new rules of proper disclosure, as set forth in the aforementioned Amendment 2 of the Banking Regulations (Customer Service) (Proper Disclosure and Provision of Documents), 2003 with respect to the plaintiffs and to all of its customers.

The Court has not yet issued its ruling on recognition of the claim as a class action.
According to the assessment of the Bank's management, based on a legal opinion it has obtained, the prospects that the plaintiffs will succeed in their claim are remote. Therefore, no provision was recorded in the financial statements for this claim.

G. 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. 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 as set forth in section 12)l. below.

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 the estimation of the Bank's management, based on the opinion of its legal counsel, the prospects that the appeal, the claim and the motions for recognition of the action as a class action are "reasonably possible". In the opinion of management, the financial statements include an appropriate provision.

H. In October 2004, an action was lodged in Tel Aviv District Court against the Bank and against Bank Tefahot, as well as a motion for recognition as a class action.
According to the Statement of Claim and the motion for recognition as a class action, the plaintiffs allege that their shares were acquired from them in a forced purchase and at a value below their fair value, in the process of a tender offer that the Bank published on June 24, 2004, to acquire the shares of Bank Tefahot, even though one of the plaintiffs accepted the tender offer in part. Therefore, the plaintiffs appealed, inter alia, to receive the remedy of appraisal under Section 338 of the Companies Law, 1999.
In the purchase offer, the Bank offered to purchase from Bank Tefahot shareholders all 6,909,842 of their shares, in exchange for NIS 49.50 per share (after amendment of the purchase offer).

As of the purchase offer date, the book value of Bank Tefahot's shareholders' equity was NIS 2.06 billion, and the value of Bank Tefahot, based on the share price in the purchase offer, was NIS 2.4 billion. The intrinsic value of the purchase offer was 118% of Bank Tefahot's (book value of) shareholders' equity as of March 31, 2004.
The plaintiffs allege that the amount of their personal claim is NIS 171 thousand, and for all of the plaintiffs that they are petitioning to represent, they estimate the amount of the claim at NIS 2,149 million.

In the estimation of the Bank's Management, based on the opinions of an economic expert expressed at the request of the Bank and based on the opinion of its legal counsel, and in view of the plaintiff's allegations, such as that the value of Bank Tefahot is NIS 17.7 billion, an unreasonable amount, lacking all proportion to the value of banks in Israel, the prospects that the claim will be accepted are remote, hence no provision was made in the financial statements.

I. In March 2005, an action against the Bank was lodged against with Tel Aviv District Court in the amount of NIS 6 million, as well as a motion for recognition as a class action in an amount ranging between NIS 50 million, direct damage from the forced repayment of loans in foreign currency, as provided below, and between NIS 500 million, including addition for alleged damages sustained as a result of the initial damage ("the Action").

The plaintiff alleges that the Bank forced the repayment of foreign currency loans before the end of the loan period, contrary to the customer's instructions, at the peak of the temporary devaluation in the NIS in the fall of 1988, when several months later, the NIS stabilized and returned to the original exchange rates. The plaintiff alleges that as a result of the forced repayment of the loans, a debt balance was created in his account, which prevented the execution of transactions in his account and increased his damages.

In October 2005, the Bank filed its Response to the motion for recognition as a class action and argued that it had acted lawfully. In the estimation of the Bank's management, based on the opinion of its legal counsel which it obtained, the outcome of the action and whether the action will be recognized as a class action is within the realm of "possible". In the opinion of Bank management, the financial statements include an appropriate provision.

J. 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.
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.
According to the assessment of the Bank's management, based on a legal opinion it has obtained, the prospects that the plaintiffs will succeed in their claim are remote. Therefore, no provision was recorded in the financial statements for this claim.

Note 19 - Contingent Liabilities and Special Commitments

K. In April 2006, a claim in the amount of NIS 183 million was filed with the Haifa District Court, against the Bank and against Bank Hapoalim Ltd., alleging that credit promised to the plaintiffs was not granted, allegedly causing their demise. In June 2006, another claim was filed in Haifa District Court by those plaintiffs, as discussed in the previous paragraph, in the amount of NIS 108 million. The claim was filed against the Bank and against an officer of the Bank, alleging that credit promised to the plaintiffs was not granted, allegedly causing their demise. The District Court Registrar dismissed the plaintiffs' motion for exemption from court fees. The plaintiffs appealed to the district court the Court Registar's ruling on exemption from the fee.

At the bank's request, rulings were issued dismissing the plaintiffs' motion due to non-payment of court fees by the plaintiffs. However, the Court ruled that due to the fact that appeals were filed regarding the fee, should the appeals filed by the plaintiffs be accepted, the rulings would be cancelled. In March 2007, the plaintiffs' appeals were dismissed by the District Court, and they filed in May 2007, requesting the right to appeal to the Supreme Court, wherein they also requested to be exempted from court fees and deposits. Rulings in this case are yet to be handed down.

In the estimation of Bank management, based on the opinion of its legal counsel, the prospects that the plaintiffs will succeed in their motion to appeal their requests for exemption from the fee, which were dismissed by two Courts before, are remote. Even should the plaintiffs' appeals be accepted, the probability of the actual claims to be accepted are remote, since their claims reveal no cause for the claim, as well as the fact that rulings handed down by the District Court have rejected their claims. Therefore, no provision was recorded in the financial statements for these claims.

L. 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 files to dismiss out of hand the plaintiffs' motion for class action status, arguing that its actions were and are lawful.
In the estimation of the Bank's management, based on the opinion of its legal counsel, the prospects that the appeal, the claim and the motions for recognition of the action as a class action are "reasonably possible". In the opinion of management, the financial statements include an appropriate provision.

M. 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 – Execution Department, the entire banking system and insurance companies and provident funds.
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.
In the estimation of the Bank's management, based on the opinion of its legal counsel, the prospects that the appeal, the claim and the motions for recognition of the action as a class action are "reasonably possible". In the opinion of management, the financial statements include an appropriate provision.

N. 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 its response the Bank claims that plaintiff's claims are not only in contradiction with the Bank price list, but also in contradiction with logic and common sense. The Bank further argues that the plaintiff has no cause and therefore no foundation for a personal claim against the Bank. The Bank also argues 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.

Bank management estimates, based on opinion of legal counsel, that the probability of the claim and motion for class action status being accepted is remote, hence no provision was made for it in the financial statements.

O. In December 2006, an action and motion for recognition as a class action were lodged in Tel Aviv District Court against the Bank in the amount of NIS 150 million for reducing the interest on deposits, allegedly in violation of the benefit mechanism promised to the plaintiff when the deposit account was opened, without informing him in advance and without enabling him to decide whether he is interested in renewing his deposits at the reduced interest. Alternatively, the plaintiff alleges that even if the said benefit mechanism had expired on the renewal date of the deposit, the Bank should have informed and altered him prior to renewing the deposit. The plaintiff's claim is based on Section 3 of the Banking Act (Customer Service), 1981, whereby a banking corporation is prohibited from misleading customers on any material issue related to providing customer service.

In February 2007, the Bank filed a response to the motion for class action status, arguing preliminary arguments for the motion to be dismissed out of hand, including absence of personal cause for the plaintiff's claim against the Bank, expiration of the statute of limitation and claim of basic error in the claim foundation. On the facts of the matter, the Bank argued that it had acted lawfully, and that the plaintiff and the claim for which he filed a motion for class action status, fail to meet preliminary statutory conditions for grant of class action status – hence they should be dismissed. Recently, the parties have started arbitration proceedings on these issues.

Bank management estimates, based on opinion of legal counsel, that the probability of the claim and motion for class action status being accepted is remote, hence no provision was made for it in the financial statements.

For all claims against the Bank Group in individual amounts over NIS 2 million, excluding claims listed in section 13 below, there is additional, non-remote exposure for which no provision was made, amounting to NIS 118 million.

13) 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, hence no provision was made for these.

A. Two motions are 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 deny all plaintiffs’ claims and reject them out of hand. The banks claim, inter alia, that their actions were lawful both in charging the commissions and in the rates of these commissions.

In the estimation of the Bank's management, based on the opinion of its legal counsel, it is not possible at this stage to assess whether the claims will be recognized as class actions and what the possible outcome will be.

B. In December 2007, a claim was filed against the Bank with the Tel Aviv District Court, along with a motion for class action status, amounting to NIS 114 million. The plaintiffs cite two causes. According to the first cause, estimated at NIS 54 million, the Bank charged property insurance premiums to borrowers in addition to property insurance purchased independently by the plaintiffs, allegedly under coercion and unlawfully. According to the second cause, estimated at NIS 60 million, the Bank coerced its customers to pay insurance premiums based on the full property value and not on the loan balance, i.e. at an amount which was higher than the debt amount.
Bank management estimates, considering the preliminary stage of the action, it is not yet possible to assess the prospects of the action and motion for recognition as a class action.

C. 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 for 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 rate on deposits was 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 the estimation of the Bank's management, based on the opinion of its legal counsel, and taking into consideration that the action is in a very preliminary stage, it is still not possible to assess the outcome of the action or whether the action will be recognized as a class action.

14) Matters related to insurance operations of the Bank:

A. The Superintendent of Insurance informed the insurance companies in his letter dated August 20, 2003, that he intends to approve the insurance tariffs for the insurance brokerage activities of mortgage banks, directly or through subsidiaries, for brokerage of housing insurance related to the issuance of mortgages, so that the rate of minimum damages, which was 57% in 2003, will rise gradually, beginning in 2004, up to the rate of 70% in 2008 and thereafter. The minimum damage rate will be computed based on the net premium paid to the sub-insurers.

The rate of the damages, means that part of the premium paid to the sub-insurer, after deducting the commissions paid to the insurance companies and banks (directly or through insurance agencies), so that an increase in the rate of damages reduces the part of the premium that constitutes the commission of the Bank and of the insurance companies for the insurance.

B. On February 17, 2005, the Superintendent of Insurance and the Supervisor of Banks announced their policy “on the marketing of life insurance and building insurance incidental to a mortgage by a bank”, beginning October 1, 2005. According to the new policy, a bank will be permitted to set up unmanned marketing stations in its branches for the sale of insurance incidental to the mortgage, to a customer who received a mortgage from that bank. The marketing stations will be clearly separate from the bank’s other activities, and will be operated using only technological means.

Accordingly, beginning from December 1, 2005, the Bank's insurance is marketed by a wholly-owned insurance agency of the Bank whose operations are separate from the Bank’s and are limited solely to property insurance, including water damage, and life insurance incidental to the loan given by the Bank. According to the directives of the Superintendent of

Insurance, the Bank's employees may not serve as employees of the insurance agency or act on its behalf. The new arrangement only applies to new policies and does not apply to the run-off portfolio of borrowers insured through the mortgage banks.

The new arrangement increases competition in the marketing of insurance incidental to the purchase of a home, and therefore, could cause a gradual reduction in the Bank's income from insurance. The Bank is prepared to contend with the strong competition in the industry. For example, the shift from uniform tariffs to differential tariffs, which enables the Bank to offer attractive tariffs to all borrowers, and especially young borrowers. In any case, since the arrangement only applies to new loans given as from December 1, 2005, the decrease in income, as of the date of the financial statements, is not significant, and in the Bank's opinion, will not be significant in the upcoming years.

c. The income of the Bank and its subsidiary engaged in insurance totaled as below (NIS millions):

Year	From life insurance	From property insurance
2007	72	42
2006	73	45

Impact of the aforementioned issues is reflected in Bank Group revenues from insurance operations in 2007, as presented above. In 2008, in which the minimum damage rate would be at a maximum based on the letter of the Supervisor of Insurance, a further decrease may occur in these revenues, by an amount which is not material.

In view of the changes to minimum damage rate and to rules for insurance marketing, Bank preparations for application of these changes and for adaptation of its business strategy to operating under the new conditions, and reflection of impact of changes on actual Bank revenues from insurance – it is not possible to estimate the degree of impact on future bank revenues.

Note 19 - Contingent Liabilities and Special Commitments

15) On June 26, 2007, the amendment to the Banking Act (Customer Service) (Amendment 12), 2007 was enacted. The amendment is aimed at increasing competition among banks, and sets forth arrangements concerning supervision of commission prices and increased transparency of banking service prices, such that customers may practically compare prices of banking services.

Pursuant to the Act, the Bank of Israel Governor would be authorized, after consulting with the Governor’s Consultative Committee pursuant to provisions of the Bank of Israel Act, 1954, to specify a list of all commissions which a banking corporation may charge for banking services, and how they are to be calculated (“the full pricelist"). This provision is aimed at reducing the number of commissions and generating uniform commission names among all banking corporations. Furthermore, the Governor is authorized to specify limited lists, based on the full pricelist, by type of banking services or by customer type (“limited pricelists”).

The banking corporation would be required to set the price charged by it for each service included in the full pricelist, and to inform its customers of the pricelists and commission prices it charges. Charging of any commission not included in the pricelists would be prohibited. These provisions shall apply to individual customers and to corporations which are “small businesses”, as specified by the Governor in regulations, considering their business turnover.

The Act specifies causes which, upon occurrence, the Supervisor is authorized to declare a banking service to be under supervision. Should a service be placed under supervision, the Governor would be authorized to set prices for commissions for such service or to set, if appropriate, maximum prices and to prohibit charging of a certain commission. Furthermore, the Supervisor of Banks would be authorized to discuss and decide on applications by a banking corporation to raise its commissions for a service under supervision. The Act also explicitly prohibits charging a commission for any service under supervision in contradiction to instructions of the Governor and Supervisor. Should any service be placed under supervision and the Governor has not set a price for it and has not prohibited charging of commission, and the banking corporation would wish to increase its price compared to the price charged prior to its placement under supervision - the bank would have to apply for permission. The Act also required prior notification to the Supervisor of any raise in commissions for services not under supervision.

On January 8, 2008 the Banking Regulations (Customer Service) (Commissions), 2008 were enacted pursuant to the Act.
These regulations set forth the full pricelists for customers serviced by a banking corporation, as well as limited pricelists for customers of the banking corporation who are provided services of current account management and housing loan, and for customers to whom the banking corporation has issued credit cards. The regulations require the banking corporation to prominently display the pricelists in its branches, and to enable customers to receive them at its branches and via its website, and to also enable customers to receive the limited pricelists via automated machines provided to customers. The banking corporation is required to provide the customer with the applicable limited pricelist upon initial provision of the service.

The regulations apply as of July 1, 2008 and the Bank is preparing to implement them. In conjunction with said preparations, the various services provided by the Bank were adapted to rules set forth in the regulations. Bank management estimates that application of these rules is expected to impact the Bank's revenue mix, however at this stage it is impossible to estimate the impact on total Bank revenues.

16) 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.

17) Pursuant to an agreement signed in 1993 with representatives of the employees, the Bank granted its employees long-term loans at repayment terms provided for in the agreement, with linkage increments and interest at a fixed rate. It was agreed that if, on the maturity date, it becomes clear that the linkage increments 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. A provision has been made for the difference created, as aforesaid. At the balance sheet date, the balances of these loans total NIS 41 million.

18) The Bank has undertaken toward 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 additional details, see Note 11.

19) Bank Tefahot has undertaken toward borrowers in certain savings plans to issue them loans at fixed terms, as follows:

	December 31	
	2007	2006
At ordinary terms on the commitment date for issuing the loan	66	82
90% of the interest rate prevailing at the time the loan was issued (1)	1,182	1,153
0.25% less than the interest prevailing at the time the loan was issued (1)	438	441
	1,686	1,676

(1) The commitment may be utilized only if certain conditions stipulated in the savings plans are met. There is a provision, which in the opinion of the Bank's management covers this commitment at the balance sheet date.

20) Beginning July 1, 2004, a new two-year agreement went into effect between Bank Tefahot, at that time, and the Government, whereby the commission rate determined by the tender held by the Finance Ministry, with the participation of the mortgage banks will apply to loans issued beginning July 1, 2004, which are significantly lower than the commission rate on loans issued until June 30, 2004. According to a letter from the Ministry of Finance, the agreement was extended until June 30, 2008.

In February 2008, the Ministry of Finance issued a tender for a new contract to provide loans to eligible borrowers, to be effective from April 2008 for 1 year. After this year, the agreement would be renewed for one more year, unless one of the parties announces its wish to terminate the agreement. In any case, the agreement would expire after 5 years. Pursuant to terms of the new agreement, as specified in the tender, loans will be granted to eligible borrowers with low point rating out of Bank funds, under terms commonly used in the past for loans out of Ministry of Finance funds, including waived early repayment commission. For the loans to eligible borrowers, the Ministry of Finance would make up for lending banks the difference between interest rates for eligible borrowers and the average market interest rate, plus a margin of 0.2% for a loan-to-value ratio over 60%, plus a margin of 0.2% for regions specified by the Ministry of Finance, plus a margin ranging from 0%-0.5%, as determined by tender, based on the winning bids and the ranking of each bidding bank relative to the winning bid. Concurrently, 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 at any time 8% of total bank loans to this group. For other eligible borrowers terms are unchanged.

Following the new tender, in continuation of the trend started by previous Ministry of Finance tenders, the gradual decline of revenue rates for new loans in the eligible borrower loan portfolio is expected to continue in coming years. Consequently, the gradual reduction in the Bank's income from this activity will continue. Bank revenues from said operations in 2007 amounted to NIS 98 million, compared to NIS 104 million in 2006.

21) An outside consultant was asked to perform an economic valuation of Bank Tefahot, and to express an expert's opinion in a class action lodged against the Bank with respect to the tender offer of Tefahot. The total financial liability of the consultant toward the Bank, jointly and severally, from any sources and according to any cause of action, including damages, except for a case of bad faith on the part of the consultant, in all that relates to his obligation in connection with the valuation, will be limited, including expenses of a legal defense, to a sum in shekels equal to 0.5 million dollars. Beyond the aforesaid, the Bank will have no argument and/or claim toward the consultant, including through third party notice, in all that relates to his services on this matter.

Likewise, the Bank has undertaken toward the consultant that if the latter is sued in legal or other proceedings, to pay any amount to a third party in connection with the performance of the said services, the Bank will bear reasonable expenses (taking into account the size of the action and the attorneys the Bank will hire to handle it), that the consultant will incur or be demanded to pay for legal advice and representation, professional consulting, expert opinions, defense against legal proceedings, negotiations, etc. in connection with any claim, demand or other proceedings deriving from or related in any way to the valuation.

Additionally, and without derogating from the generality of the aforesaid, the Bank has undertaken that if the consultant is charged or required to pay any amount whatsoever to a third party in connection with the valuation, in a legal proceeding or another proceeding, the Bank will indemnify the consultant for any amount exceeding 0.5 million dollars (net of any amount to be paid by the consultant, as aforesaid).

The indemnification undertaking will also apply to an arbitration ruling, provided that the Bank gave its prior written consent to the arbitration proceedings, and that all conditions were met on which its consent was contingent (if any), and on any arrangements according to which an amount will be paid that is not within the framework of a legal proceeding, provided that the Bank gave its prior written consent.

22) On July 25, 2005, the Knesset enacted the Financial Services Supervision Law (Engagement in Pension Consulting and Marketing), 2005 (“Pension Consulting Law”).

- The law stipulates that engaging in consulting regarding pension products will be permitted to licensed individuals, partnerships or companies, but licenses may not be obtained by institutions (provident funds and their managers, fund managers and insurers), pension agents, insurance agents, investment marketers, those who control any of the aforesaid or holding more than 10% of the means of control in them, except for a banking corporation that controls an insurance agent in accordance with the provisions of the Banking (Licensing) Law, 1981, an organization of employers, or anyone controlled by one of the aforesaid. However, a bank controlled by a party holding more than 10% of the means of control in an institution or in those controlling an institution, will be permitted to obtain a pension consultant's license subject to the conditions that will be prescribed by the Superintendent of the Capital Markets.

  Pension products include: provident funds for benefits, personal provident funds for severance pay, provident funds for annuities, advanced education funds and insurance plans that insure the risk or death or disability that is included in the abovementioned provident fund or advanced education fund, or sold incidentally to one of them.

- As an exception to the aforesaid generality, it was explicitly stipulated that a banking corporation with shareholders’ equity of not more than NIS 10 billion (such as the Bank) will be permitted to obtain a pension consultant's license and to sell pension products (subject to the limitations prescribed in the Law), once it has completed the sale of its holdings in provident funds, so that it no longer controls them, even if it continues to control mutual funds.

The Law adds an additional permitted activity (with a license), which is marketing pensions that is engaging in pension consulting, when the consulting has a direct connection to the pension product.

- It was stipulated that entering into an agreement and any transaction to provide services between the bank and an institution requires approval from the Superintendent of the Capital Market and the Supervisor of Banks, if it is not in the course of ordinary business of the pension consultant or which might materially affect the profitability of the consultant or are not at market conditions.

- The Supervisor of Capital Market, Insurance and Savings was authorized to supervise matters pertaining to the law. It was stipulated that the authority of the supervision over the matters contained in the Law was granted to the Superintendent of the Capital Market, Insurance and Savings, and that applicable to the licensee are various normative provisions from the Law for Supervision of Insurance Businesses in its modified format, which include loyalty obligations, capabilities, obligation to refrain from preferring a personal matter, obligation of proper disclosure, obligation to refrain from conflicts of interest and the obligation to tailor the service to the customer's needs, the objectives of the savings, his financial status and other circumstances.

On January 1, 2008, an amendment to the Pension Consulting Law was published in conjunction with enactment of the Arrangements in the State Economy (Amended Legislation to Achieve Budgetary Targets and Economic Policies in Fiscal Year 2008), 2008. The amendment stipulates that banking corporations whose shareholders' equity does not exceed NIS 10 billion, would be permitted, starting January 1, 2009, and subject to obtaining an appropriate license from the Supervisor of Capital Market, Insurance and Savings in the Ministry of Finance, to consult, in conjunction with pension consulting services they provide, also on pension products with an insurance component, including: Pension insurance, life insurance with a savings component and disability insurance – provided it is part of a pension insurance or life insurance policy. Banking corporations whose shareholders' equity is higher than NIS 10 billion would be allowed to provide pension consulting, including on insurance-related pension products, at later dates.

On December 30, 2007 the Extension Ordinance for Comprehensive Pension Insurance was published, to be effective starting January 1, 2008. The Ordinance stipulates that employers are required to provide appropriate amounts for pension insurance for employees with 9 months of service or more, subject to terms set forth in the Ordinance. Provisions of the ordinance stipulate that pension provisions replace severance pay in accordance with provision rates. Provisions would be at 2.5% of salary in the first year, of which 1.667% by the employer and 0.833% by the employee, and would be updated as per provisions of the Ordinance.

On August 7, 2007 the Bank was granted a license to engage in pension consulting to salaried employees and to the self-employed, having met all required conditions, and the Bank started providing pension consulting and selling pension products. At this early stage of these operations, it is not possible to estimate the expected contribution to Bank profits from these operations in the future.

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

E. Financial derivatives activity – volume, credit risk and maturity dates

a) Activity on a consolidated basis

	2007				
	Interest contracts				
	NIS – CPI	Other	Currency contracts	Contracts for shares	Commodities and other contracts
1. Stated amounts of financial derivatives					
A. Hedging derivatives (1)					
Forward contracts	1,331	-	-	-	-
Swaps	-	1,013	-	-	-
Total	1,331	1,013			
Includes interest rate swaps on which the Bank agrees to pay a fixed interest rate	-	539	-	-	-
B. ALM derivatives (1) (2)					
Forward contracts	14,377	3,438	38,421	615	120
Option contracts traded on stock exchange:					
Options written	-	-	1,228	-	-
Options purchased	-	-	456	-	-
Other option contracts:					
Options written	-	-	16,035	739	-
Options purchased	-	-	18,966	785	-
Swaps	10,163	13,718	1,555	-	-
Total	24,540	17,156	76,661	2,139	120
Includes interest rate swaps on which the Bank agrees to pay a fixed interest rate	5,498	7,275	-	-	-
C. Other derivatives (1)					
Forward contracts	-	-	2,210	-	-
Option contracts traded on stock exchange:					
Options written	-	-	2,725	14,748	1
Options purchased	-	-	2,712	14,748	1
Other option contracts:					
Options written	-	1,742	3,177	3,002	-
Options purchased	-	1,742	2,220	2,681	-
Swaps	-	32	-	-	-
Total	-	3,516	13,044	35,179	2
D. Credit derivatives and foreign currency spot swaps					
Credit derivatives in which the Bank is guarantor	-	-	-	-	692
Foreign currency spot swap contracts	-	-	2,700	-	-
Total	-	-	2,700	-	692

(1) Except for credit derivatives and spot contracts for foreign currency swaps.
(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

E. Financial derivatives activity – volume, credit risk and maturity dates - Cont.

a) Activity on a consolidated basis - - Cont.

	2007				
	Interest contracts			Contracts	Commodities
		Other	Currency	for	and other
	NIS - CPI		contracts	shares	contracts
2. Fair value, gross, of financial derivatives					
A. Hedging derivatives (1)					
Positive fair value, gross	9	10	-	-	-
Negative fair value, gross	8	10	-	-	-
B. ALM derivatives (1) (2)					
Positive fair value, gross	187	133	1,530	67	1
Negative fair value, gross	213	62	1,078	56	1
C. Other derivatives (1)					
Positive fair value, gross	-	74	102	187	-
Negative fair value, gross	-	74	100	217	-
d. Credit derivatives					
Credit derivatives in which the Bank is guarantor					
Positive fair value, gross	-	-	-	-	1
Negative fair value, gross	-	-	-	-	3

(1) Except for credit derivatives.
(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

E. Financial derivatives activity – volume, credit risk and maturity dates - Cont.

a) Activity on a consolidated basis - - Cont.

	2006				
	Interest contracts				
	NIS - CPI	Other	Currency contracts	Contracts for shares	Commodities and other contracts
1**. Stated amounts of financial derivatives**					
A. Hedging derivatives (1)					
Swaps	-	1,199	-	-	-
Includes interest rate swaps on which the Bank agrees to pay a fixed interest rate	-	580	-	-	-
B. ALM derivatives (1) (2)					
Forward contracts	9,308	575	36,936	386	83
Option contracts traded on stock exchange:					
Options written	-	-	475	-	-
Options purchased	-	-	281	-	-
Other option contracts:					
Options written	-	-	13,472	-	-
Options purchased	-	-	15,810	-	-
Swaps	2,120	13,577	1,592	-	-
Total	11,428	14,152	68,566	386	83
Includes interest rate swaps on which the Bank agrees to pay a fixed interest rate	2,120	2,674	-	-	-
C. Other derivatives (1)					
Forward contracts	-	-	2,013	-	-
Option contracts traded on stock exchange:					
Options written	-	-	1,969	9,890	-
Options purchased	-	-	1,965	9,890	-
Other option contracts:					
Options written	-	2,216	2,073	3,659	-
Options purchased	-	2,216	2,026	3,331	-
Swaps	-	61	-	-	-
Total	-	4,493	10,046	26,770	-
D. Credit derivatives and foreign currency spot swaps					
Foreign currency spot swap contracts	-	-	1,711	-	-

(1) Except for credit derivatives and spot contracts for foreign currency swaps.

(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

E. Financial derivatives activity – volume, credit risk and maturity dates - Cont.

a) Activity on a consolidated basis - - Cont.

	2006				
	Interest contracts			Contracts	Commodities
	Shekel/ CPI	Other	Currency contracts	for shares	and other contracts
2. Fair value, gross, of financial derivatives					
A. Hedging derivatives (1)					
Positive fair value, gross	-	12	-	-	-
Negative fair value, gross	-	2	-	-	-
B. ALM derivatives (1) (2)					
Positive fair value, gross	240	167	1,155	42	6
Negative fair value, gross	101	41	491	42	6
C. Other derivatives (1)					
Positive fair value, gross	-	21	78	154	-
Negative fair value, gross	-	21	81	159	-

(1) Except for credit derivatives.
(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 19 - Contingent Liabilities and Special Commitments
As of December 31

E. Financial derivatives activity – volume, credit risk and maturity dates - Cont.

b) Credit risk on financial derivatives according to counter-party to the contract – Consolidated

	2007					
	Stock exchanges	Banks	Dealers/ Brokers	Governments and central Banks	Others	Total
Positive fair value, gross, of financial derivatives (1)	116	1,402	97	-	686	2,301
Off-balance sheet credit risk on financial derivatives (2)	51	8,187	534	-	3,104	11,876
Total credit risk on financial derivatives	167	9,589	631	-	3,790	14,177

	2006					
	Stock exchanges	Banks	Dealers/ Brokers	Governmen ts and central Banks	Others	Total
Positive fair value, gross, of financial derivatives (1)	152	1,033	73	14	603	1,875
Off-balance sheet credit risk on financial derivatives (2)	28	5,747	535	61	3,187	9,558
Total credit risk on financial derivatives	180	6,780	608	75	3,790	11,433

(1) Of which positive gross fair value of embedded derivatives amounting to NIS 3 million (in 2006 – NIS 4 million) and a balance-sheet balance of stand-alone derivatives amounting to NIS 2,298 million, included under "other assets" (in 2006 - NIS 1,871 million).

(2) Off-balance sheet credit risk for financial derivatives (including those with negative fair value) as computed for the purposes of the per-borrower limitation.

c) Maturity dates – stated amounts: year-end balances - Consolidated

	2007				
	Up to 3 months	Over 3 months to 1 year	1-5 years	Over 5 years	Total
Interest contracts					
NIS-CPI	3,775	11,830	8,396	1,870	25,871
Other	1,841	14,885	2,755	2,204	21,685
Currency contracts	54,082	35,442	2,094	787	92,405
Contracts for shares	33,832	2,131	1,355	-	37,318
Commodities and other contracts	108	14	654	38	814
Total	93,638	64,302	15,254	4,899	178,093

	2006				
Total	82,784	42,716	11,351	1,983	138,834

Note 19 - Contingent Liabilities and Special Commitments

e) 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 (trades 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

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 Fair Value Estimates 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 computed by the managements in the Bank Group, taking into account the possibility of early repayment.

   b) Deposits from the public, deposits with banks and loans to the Government, 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.

c) Marketable securities – at market value.

d) Asset-backed securities held for sale – by quote issued by the manager of the backed assets.

e) 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.

f) 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. 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 computed.

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.

g) The fair value of problem debt is computed 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 computed after deducting the specific provisions for doubtful debt.

A decrease of 1% in the discount rate affects the fair value of the problematic debts of the Group by NIS 59 million.

Non-accrual loans in all the linkage segments are discounted in the Bank, at the unlinked shekel interest rate.

The general and supplementary provision for doubtful debt was not deducted from the loan balances for the purpose of computing cash flows and estimating fair value.

h) 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 at the balance sheet date approximates the fair value.

i) Financial derivatives – Financial derivatives that have an active market were valued at market value. Derivative instruments that are not traded in an active market were valued according to models used by the Bank in its current activities. See Note 19.E for information.

Note 20 – Balances and Fair Value Estimates of Financial Instruments

Reported amounts (in NIS millions)

3. Information on the fair value of financial instruments is presented below:

	Consolidated							
	December 31, 2007				December 31, 2006			
	Book balance			Fair	Book balance			Fair
	(1)	(2)	Total	value	(1)	(2)	Total	value
Financial assets								
Cash and deposits with banks	2,658	8,043	10,701	10,707	1,142	9,655	10,797	10,867
Securities	6,145	-	6,145	6,145	5,601	378	5,979	5,979
securities loaned or sold in repurchase agreements	5	-	5	5	-	-	-	-
Loans to the public	20,846	53,474	74,320	75,888	19,377	50,732	70,109	70,616
Loans to the Government	1	2	3	3	1	3	4	3
Other financial assets	2,834	-	2,834	2,834	2,425	-	2,425	2,425
Total financial assets	32,489	61,519	94,008	95,582	28,546	60,768	89,314	89,890
Financial liabilities								
Deposits from the public	14,866	60,424	75,290	75,961	13,322	59,912	73,234	73,765
Deposits from banks	1,929	1,823	3,752	3,812	947	2,126	3,073	3,138
Deposits from the Government	2	280	282	282	223	337	560	551
Debentures and subordinated notes	-	6,189	6,189	6,324	-	5,067	5,067	5,191
Other financial liabilities	3,704	-	3,704	3,704	3,121	-	3,121	3,121
Total financial liabilities	20,501	68,716	89,217	90,083	17,613	67,442	85,055	85,766

Off-balance sheet financial instruments

The fair value of transactions in which the balance represents credit risk is not materially different from the carrying value in the financial statements (see Note 19.A above).

(1) Financial instruments in which the balance sheet balance constitutes an estimate of fair value. For further details, see 2) above.

(2) Other financial instruments.

Note 20 – Balances and Fair Value Estimates of Financial Instruments

Reported amounts (in NIS millions)

	The Bank							
	December 31, 2007				December 31, 2006			
	Book balance			Fair	Book balance			Fair
	(1)	(2)	Total	value	(1)	(2)	Total	value
Financial assets								
Cash and deposits with banks	3,248	9,411	12,659	12,672	2,213	10,272	12,485	12,546
Securities	6,092	-	6,092	6,092	5,537	378	5,915	5,915
securities loaned or sold in repurchase agreements	5	-	5	5	-	-	-	-
Loans to the public	19,569	50,525	70,094	71,574	18,056	47,982	66,038	66,502
Loans to the Government	-	3	3	3	-	4	4	3
Other financial assets	2,804	-	2,804	2,804	2,427	-	2,427	2,427
Total financial assets	31,718	59,939	91,657	93,150	28,233	58,636	86,869	87,393
Financial liabilities								
Deposits from the public	14,959	61,294	76,253	76,819	13,852	59,583	73,435	73,932
Deposits from banks	1,754	2,014	3,768	3,820	1,021	2,061	3,082	3,147
Deposits from the Government	1	274	275	275	223	328	551	542
Subordinated notes	-	4,057	4,057	4,193	-	3,724	3,724	3,822
Other financial liabilities	3,662	-	3,662	3,662	3,082	-	3,082	3,082
Total financial liabilities	20,376	67,639	88,015	88,769	18,178	65,696	83,874	84,525

Off-balance sheet financial instruments

The fair value of transactions in which the balance represents credit risk is not materially different from the carrying value in the financial statements (see Note 19.A above).

(1) Financial instruments in which the balance sheet balance constitutes an estimate of fair value. For further details, see 2) above.

(2) Other financial instruments.

Note 21 - Interested and Related Parties - Consolidated

Reported amounts (in NIS millions)

	2007							
	Interested parties						Related parties held by the Bank	
	Controlling shareholders		Directors and President		Others (4)		Affiliates	
	Balance as of balance sheet date	Highest balance for the year (1)	Balance as of balance sheet date	Highest balance for the year (1)	Balance as of balance sheet date	Highest balance for the year (1)	Balance as of balance sheet date	Highest balance for the year (1)
A. Balances								
Assets								
Loans to the public	10	10	5	5	429	679	50	60
Investments in affiliate (including subordinated notes)	-	-	-	-	-	-	10	38
Off-balance sheet financial instruments (2)	-	-	6	6	98	123	1	1
Liabilities								
Deposits from the public	9	11	4	10	31	309	2	7
Shares (included in shareholders' equity) (3)	2,548	2,548	48	48	-	-	-	-

(1) Based on balances at the end of each month.

(2) Credit risk in off-balance sheet financial instruments, as computed for the purposes of per-borrower limitations.

(3) The share of interested and related parties in the Bank's capital.

(4) A corporation in which the interested party holds 25% or more of its issued share capital or voting rights, or may appoint 25% or more of members of its Board of Directors.

Note 21 - Interested and Related Parties - Consolidated

Reported amounts (in NIS millions)

	2006							
	Interested parties						Related parties held by the Bank	
	Controlling shareholders		Directors and President		Others (4)		Affiliates	
	Balance as of balance sheet date	Highest balance for the year (1)	Balance as of balance sheet date	Highest balance for the year (1)	Balance as of balance sheet date	Highest balance for the year (1)	Balance as of balance sheet date	Highest balance for the year (1)
A. Balances								
Assets								
Loans to the public	8	11	3	3	200	383	53	72
Investments in affiliate (including subordinated notes)	-	-	-	-	-	-	38	38
Off-balance sheet financial instruments (2)	-	1	-	-	91	175	-	1
Liabilities								
Deposits from the public	11	94	4	21	36	523	2	71
Shares (included in shareholders' equity) (3)	2,339	2,339	-	-	-	-	-	-

(1) Based on balances at the end of each month.
(2) Credit risk in off-balance sheet financial instruments, as computed for the purposes of per-borrower limitations.
(3) The share of interested and related parties in the Bank's capital.
(4) A corporation in which the interested party holds 25% or more of its issued share capital or voting rights, or may appoint 25% or more of members of its Board of Directors.

Note 21 - Interested and Related Parties - Consolidated

Reported amounts (in NIS millions)

B. In statement of profit and loss

The results of financing operations before provision for doubtful debt and operating expenses from the transactions of the Bank and its subsidiaries with interested and related parties:

	For the Year Ended December 31								
	2007			2006			2005		
	Interested parties		Related parties held by the Bank	Interested parties		Related parties held by the Bank	Interested parties		Related parties held by the Bank
	Controlling share-holders	Others	Affiliates	Controlling share-holders	Others	Affiliates	Controlling share-holders	Others	Affiliates
Related to assets from loans to the public	-	9	4	-	10	6	-	14	2
Related to liabilities from deposits from the public	-	4	-	1	4	-	-	1	5
Total results from financing operations before provision for doubtful debt	-	5	4	(1)	6	6	-	13	(3)
Operating and other expenses	-	16	-	-	15	-	-	16	-

Note 21 - Interested and Related Parties - Consolidated

Reported amounts (in NIS millions)

C. Benefits to interested parties (of the Bank and of investees):

	For the Year Ended December 31					
	2007		2006		2005	
	Number of recipients	Amount	Number of recipients	Amount	Number of recipients	Amount
Salary of board members and President						
Chairman of the Board of Directors and President employed by the Bank (1)	2	13	2	13	2	12
Directors who are employed by the Bank Group	-	-	-	-	-	-
Directors who are not employed by the Bank Group	12	2	12	2	12	2

(1) In accordance with his employment agreement, the President is entitled to options to purchase shares of the Bank, in accordance with a plan that was approved by the Audit Committee and the board of directors of the Bank on October 24, 2004. For details, see Note 16.A.1).

To the best of the Bank's knowledge, transactions with related parties were executed in the ordinary course of business, at market terms and under terms similar to those of transactions effected with unrelated entities. The income or expenses connected with these transactions are included in the appropriate items in the statement of profit and loss.

D. During 2007 the Bank completed transactions to sell the Bank Group's provident fund management operations. See Note 6.E.2) regarding the sale.

Note 22 - Profit from Financing Operations before Provision for Doubtful Debt For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
A. From assets (1)						
From loans to the public	4,087	3,133	4,789	3,804	2,925	4,574
From loans to the Government	(1)	20	7	(1)	20	7
From deposits with the Bank of Israel and from cash	84	(4)	34	84	(4)	34
From deposits with banks	(239)	(130)	781	(163)	(67)	796
From securities loaned or sold in repurchase agreements	5	3	-	5	3	-
From debentures	174	181	145	173	181	150
	4,110	3,203	5,756	3,902	3,058	5,561
B. On liabilities (1)						
On deposits from the public	(2,048)	(1,879)	(3,368)	(2,074)	(1,827)	(3,248)
On deposits from governments	(22)	(23)	(41)	(22)	(23)	(40)
On deposits from the Bank of Israel and from cash	(40)	(10)	(2)	(40)	(10)	(2)
On deposits from banks	(160)	(258)	(172)	(141)	(290)	(205)
On debentures and subordinated notes	(460)	(220)	(307)	(319)	(170)	(263)
	(2,730)	(2,390)	(3,890)	(2,596)	(2,320)	(3,758)
C. On financial derivatives and hedging activities						
Income, net, from ALM derivatives (2)	(44)	790	(276)	(44)	790	(276)
Income, net, from other derivatives	403	84	74	403	84	74
	359	874	(202)	359	874	(202)
D. Other						
Commissions from financing transactions	85	84	78	81	80	75
Financing income from collection of interest on arrears from individual borrowers	45	41	28	45	41	24
Interest income on problem loans	126	70	35	124	68	35
Other financing income	57	125	106	54	122	101
Other financing expenses	(26)	(20)	(7)	(25)	(19)	(6)
	287	300	240	279	292	229
Total profit from financing operations before provision for doubtful debt	2,026	1,987	1,904	1,944	1,904	1,830
Includes: exchange rate differences, net	(20)	(7)	3	(8)	3	7

(1) Includes the effective element in the hedging ratios.
(2) Financial derivatives constitute part of the Bank's asset and liability management which were not intended for hedging.

Note 22 - Profit from Financing Operations before Provision for Doubtful Debt For the Year Ended December 31

Reported amounts (in NIS millions)

E. Details of results of investments in debentures

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Financing income on an accrual basis						
From debentures:						
Held to maturity	-	6	-	-	6	4
Available for sale	176	175	146	175	175	146
Held for trading	(2)	-	(1)	(2)	-	-
Total included in profit from financing operations from assets	174	181	145	173	181	150
Gain on sale of debentures available for sale	26	5	34	26	5	34
Provision for impairment of debentures held for sale (1)	(114)	-	-	(114)	-	-
Realized and unrealized loss from adjustment to fair value of debentures held for trade, net	(2)	-	-	(2)	-	-
Total included in other financing income	(90)	5	34	(90)	5	34
Total from investments in debentures	84	186	179	83	186	184

F. Details of net effect of hedging financial derivatives on profit from financing operations

Financing expenses on assets (1)	33	19	4	33	19	4

(1) For more details, see Note 3.3.

Note 23 - Operating Commissions
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Account management fees (1)	102	99	103	102	99	103
Payment services (1)	219	213	182	219	212	181
Income from credit cards	84	74	63	84	74	63
Handling of credit and preparation of contracts	116	120	103	110	113	97
Computerized services, information and confirmations	13	12	12	13	12	12
Foreign trade and special services in foreign currency	44	41	37	42	40	36
Income from securities transactions	205	178	163	189	167	153
Collection commission on credit from Ministry of Finance funds	112	115	115	105	108	108
Management fees and commissions on housing insurance	42	45	46	-	-	-
Management fees and commissions on life insurance	72	73	73	54	62	64
Commissions from transfer of rental payments	-	4	12	-	3	10
Other	25	17	15	16	9	8
Total operating commissions	1,034	991	924	934	899	835

(1) In Israeli and foreign currency

Note 24 – Profits from Investments in Shares, Net
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Dividend from shares available for sale	57	39	8	57	39	8
Profits on the sale of shares available for sale	9	13	1	9	13	-
Provision for decline in value of shares available for sale	(1)	(2)	(6)	(1)	(2)	(6)
Total profits from investments in shares, net	65	50	3	65	50	2

Note 25 - Other Income
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Provident fund management fees	28	102	93	21	83	82
Provident fund operating fees	20	-	-	20	-	-
Mutual fund management fees	-	33	72	-	-	-
Management fees from subsidiaries	-	-	-	1	1	1
Mutual fund distribution fees	26	11	-	26	11	-
Other	17	28	22	7	18	12
Total other income	91	174	187	75	113	95

Note 26 – Salaries and Related Expenses
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Salaries (including bonuses)	852	832	798	804	789	757
Expense arising from share-based payment transactions (1)	18	26	15	18	26	15
Severance pay, provident and pension, continuing education fund and vacation	101	92	98	94	86	91
National Insurance and VAT on salaries	183	185	185	177	179	179
Other related expenses	13	12	13	13	12	13
Supplement to provisions for related expenses, due to changes in salaries during the current year	2	4	2	2	4	2
Retirement expenses (2)	-	244	43	-	244	43
Total salaries and related expenses	1,169	1,395	1,154	1,108	1,340	1,100
Includes: salaries and related expenses overseas	38	35	30	38	35	30

(1) See Note 16.A.

(2) Also includes expenses as set forth in Note 16.I and 16.J.

Note 27 - Other Expenses
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Marketing and advertising	46	40	42	41	35	36
Communications	37	40	40	36	39	39
Computer	30	33	36	25	29	31
Office	20	14	11	18	13	10
Insurance	16	18	20	15	17	19
Legal, audit and professional advisory services	67	54	68	61	49	61
Directors' remuneration and fees for participation in meetings	3	3	4	2	2	3
Training and continuing education	7	9	8	7	9	7
Commissions	37	26	29	37	24	27
Sundry	85	100	78	83	78	66
Total other expenses	348	337	336	325	295	299

Note 28 - Provision for Taxes on Operating Profit
For the Year Ended December 31

Reported amounts (in NIS millions)

	Consolidated			The Bank		
A. Composition	2007	2006	2005	2007	2006	2005
Current taxes -						
For the current year	339	436	394	307	386	338
For prior years	-	1	5	(1)	1	5
Total current taxes	339	437	399	306	387	343
Changes in deferred taxes -						
For the current year	29	(88)	(28)	29	(94)	(24)
Total provision for taxes on income	368	349	371	335	293	319
Includes provision for taxes overseas (includes deferred taxes)	6	9	3	-	4	-

Note 28 - Provision for Taxes on Operating Profit
For the Year Ended December 31
Reported amounts (in NIS millions)

B. Reconciliation between the theoretical tax amount that would be applicable had the operating profits been taxable at the statutory tax rate applicable to banks in Israel, and between the provision for taxes on operating profit as included in the statement of profit and loss:

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Statutory tax rate applicable to a bank in Israel	38.53%	40.64%	43.59%	38.53%	40.64%	43.59%
Tax amount based on statutory tax rate	405	317	386	365	262	323
Tax (tax saving) from:						
Deduction for inflation	(39)	7	(31)	(33)	6	(28)
Subsidiaries' income:						
In Israel	(5)	(4)	(4)	-	-	1
Overseas	(1)	(2)	(1)	-	-	-
General, special and supplementary provision for doubtful debt	(7)	(8)	6	(7)	(8)	6
Exempt income	(2)	(5)	(4)	(2)	(5)	(4)
Adjustment differences on depreciation, amortization and capital gains	(4)	(1)	(7)	(4)	(1)	(7)
Other non-deductible expenses	5	9	3	4	8	3
Deferred taxes for losses in investee that was merged into the Bank (1)	-	-	-	-	-	-
Temporary differences and losses for which deferred taxes have not been recorded	7	8	2	7	8	2
Profit tax on VAT on salaries,net	12	13	12	12	13	12
Taxes for prior years	-	-	5	(1)	-	5
Change in deferred tax balances due to change in tax rates (2)	3	(2)	6	3	(3)	6
Adjustment differences on monetary assets and other differences, net	(6)	17	(2)	(9)	13	-
Total provision for taxes on income	368	349	371	335	293	319

(1) See section F below.
(2) See section C below.

Note 28 - Provision for Taxes on Operating Profit

C. On July 25, 2005, the Knesset enacted Amendment No. 147 to the Income Tax Ordinance, 2005 (“the Amendment”). Pursuant to the Amendment, the pace of gradual reduction of the corporate tax rate will be accelerated, as provided below: in 2006 - 31% (instead of 32%), in 2007 – 29%; in 2008 – 27%, in 2009 – 26%, in 2010 and thereafter – 25%.

On June 27, 2006, the Minister of Finance signed a Value Added Tax Order (Tax Rate on Not-for-Profit Corporations and Financial Institutions) (Amendment), 2006, which stipulates that the rate of profit tax will be reduced from 17% to 15.5%, in the manner provided in the Order. The overall tax rate that will be imposed on the Bank is 40.6% in 2006, in 2007 - 38.5%, in 2008 - 36.8% and will continue to gradually decline to a rate of 35.1% in 2010 and thereafter.

D. On February 26, 2008 the Knesset passed the Income Tax Act (Adjustments for Inflation) (Amendment no. 20) (Restriction of Applicable Period), 2008 ("the amendment"), whereby the Inflationary Adjustment Act would be rescinded in the 2007 tax year, and starting in the 2008 tax year, provisions of the Act shall no longer apply, other than interim provisions aimed at avoiding distortions in tax calculations.

Pursuant to the amendment, from the 2008 tax year onwards, revenues will no longer be adjusted, for tax purposes, to a real measuring base. In addition, linkage to the CPI of depreciation amounts for fixed assets and carry-forwards tax losses would be discontinued, such that these amounts would be adjusted to the CPI through the 2007 tax year, and hence forward would no longer be linked to the CPI.

The amendment also amends the definitions of “profit” and “salary” in the VAT Act.

Pursuant to the amendments, in calculating profit for tax purposes, the salary tax paid by the financial institution would be deducted. Furthermore, payment of the employer’s share of insurance fees paid for his employer under the National Insurance Act (Combined Version), 1995 (hereinafter: “the National Insurance Act”) would be taxable for salary tax purposes.

In 2008, as interim provision, half of the salary tax paid by the financial institution would be deducted in calculating profit for profit tax purposes, and salary tax shall also apply to half of the employer’s share of national insurance fees paid for their employee pursuant to the National Insurance Act.

The impact of discontinuation of the Inflationary Adjustments Act, as of December 31, 2007, is estimated at lowering Bank net profit by NIS 15 million for each 1% in annual rise of the CPI.

Note 28 - Provision for Taxes on Operating Profit

Amendments to the VAT Act, based on salary expenses in 2007, are expected to increase the Bank's net profit by NIS 5 million in 2008, and by NIS 10 million in 2009 and later.

E. The Bank has final assessments or those deemed final for the tax years through 2003, inclusive, and for the former Bank Tefahot through 2004. Bank Adanim has final tax assessments for the tax years through 2006, inclusive.

F. Following the merger of the Investment Corporation with the Bank, a tax asset ("deferred tax") of NIS 25 million was included in the year 2004, for carry forward losses in the Investment Corporation that may be set off against the Bank's profits for 10 years. Furthermore, there are additional tax losses in the amount of NIS 51 million that accrued in the Investment Corporation, which will also be allowed to be set off for tax purposes for a period of 10 years, if certain conditions that were prescribed in the approval of the Income Tax Commission are fulfilled. Deferred taxes were not recorded for these amounts.
On March 6, 2006, certification was received from the income tax authorities on fulfillment of the conditions of the merger with the Investment Corporation of Mizrahi Bank Ltd. It should be noted that, as aforesaid in section E., the Bank has no final tax assessments for the year 2004.

G. Following the merger of "Tefahot" Israel Mortgage Bank Ltd. on January 1, 2005, certification was received from the Income Tax Authority on February 4, 2007, 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 2005.

H. Adjustment amount for non-monetary assets, whose amortization would not be tax deductible in the future, and for which no provision for deferred taxes is to be created:

	Consolidated		The Bank	
	2007	2006	2007	2006
Balance as at beginning of year	55	65	55	65
Amount not deductible in reported year	(1)	(10)	(1)	(10)
Balance as at end of year	54	55	54	55

Note 28 - Provision for Taxes on Operating Profit
For the Year Ended December 31

Reported amounts (in NIS millions)

I. 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 %	
	2007	2006	2007	2006	2007	2006	2007	2006
Deferred taxes for:								
Specific provision for doubtful debt (1)	14	13	36.0	36.4	-	-	-	-
Provision for vacation pay, long-service bonuses and employee rights (1)	41	50	33.3	35.5	41	50	33.3	35.5
Excess provision for employee rights on retirement, net (1)	158	157	35.6	36.1	158	156	35.6	36.0
Other securities (1)(3)	24	17	36.8	38.5	24	17	36.8	38.5
Adjustment of depreciable non-monetary assets (2)	(11)	(16)	25.0	25.0	(11)	(16)	25.0	25.0
Monetary assets (1)(4)	21	160	36.8	38.5	20	159	36.8	38.5
Non-monetary assets, net (1)	3	2	36.8	38.5	3	2	36.8	38.5
Total deferred taxes	250	383	36.1	37.6	235	368	36.1	37.6
Deferred taxes include:								
(1) Deferred tax assets included in "other assets"	261	399	35.6	37.1	246	384	35.6	37.1
(2) Deferred taxes payable included in "other liabilities"	(11)	(16)	25.0	25.0	(11)	(16)	25.0	25.0
Deferred taxes, net	250	383	36.1	37.6	235	368	36.1	37.6

(3) Changes in this item of NIS 19 million on a consolidated basis and for the Bank derive from the adjustment to fair value of securities available for sale (last year - NIS 20 million) were charged to a separate item in shareholders' equity.

(4) This item includes a decrease in deferred tax balance for profit from extraordinary items, which in 2007 amounted to NIS 123 million (in 2006 – increase in deferred tax balance by NIS 136 million).

Note 29 - Net After-Tax Profit (Loss) from Extraordinary Items

Reported amounts (in NIS millions)

	Consolidated			The Bank		
	2007	2006	2005	2007	2006	2005
Profit from sale of provident fund operations (1)	385	-	-	333	-	-
Profit from sale of mutual fund operations	-	213	-	-	-	-
Profit from sale of shares of investees (2)	3	148	-	3	148	-
Capital gain from sale of buildings and equipment	21	-	-	11	-	-
Capital loss from sale of buildings and equipment	-	-	(1)	-	-	(1)
(Provision) cancelled provision for losses anticipated on buildings for sale and leased properties not in use	(14)	4	(2)	(14)	4	(2)
Pre-tax profit (loss)	395	365	(3)	333	152	(3)
Provision for taxes on profit from extraordinary items:						
Current taxes	32	163	(1)	8	80	(1)
Deferred taxes	123	(14)	-	123	(14)	-
Total provision for taxes	155	149	(1)	131	66	(1)
After-tax profit	240	216	(2)	202	86	(2)
Share in net, after-tax profit from extraordinary items of subsidiaries	-	-	-	25	130	-
Minority interest in net, after-tax profit from extraordinary items of subsidiaries	(13)	-	-	-	-	-
After-tax profit (loss) from extraordinary items	227	216	(2)	227	216	(2)

(1) For sale of provident fund operations, see Note 6.E.2).
(2) For sale of shares of Mofet Israel Technology Fund Ltd., see Note 6.E.3).

Note 30 - Operating Segments and Geographic Regions

A. General

The Bank manages its operations in seven major operating segments, which are distinguished by customer 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 set forth below. The operations in the seven operating segments include all areas of banking operations including classic banking activity (loans and deposits), securities activity for customers 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.

In view of changes in presentation of operating segments in line with changes in Bank organizational structure, and with operation of the new measuring system, as set forth below, the results presented for 2007 are not comparable to results presented for 2006.

In recent years the Bank has been reorganized, including renewed determination of the operating segments and customer types for the various units. The following principles apply to operating segment assignment to organizational units, with description of major changes:

- The Business Banking division was re-organized to concentrate handling of major customers in specialized units at Bank headquarters or at specially designated centers. The Major Corporations sector in Bank HQ is responsible for the Business Banking segment, which is the focal point for handling the largest business customers. Criteria by which customers 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. Other mid- to large business customers are handled by the Business sector (commercial banking sector), using six business centers 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.
- In 2007, private banking was transferred to the Retail division. Private banking customers are individual customers with liquid assets (primarily short-term deposits and security investments) over NIS 2.5 million, and corporations with liquid assets in excess of NIS 8 million.

Note 30 - Operating Segments and Geographic Regions

- The Retail division is also in charge of the Household segment, which includes smaller individual customers and the Mortgage sector, as well as the Small Business segment, which includes small corporate customers. Most of the business customers in the retail division have indebtedness level of less then NIS 6 million, sales of less than NIS 30 million and liquid asset balance of less than NIS 10 million.
- International operations, including Bank branches overseas and operations of banking centers for tourists in Israel, have been placed under the Financial division. The Financial division is also in charge of financial management, including management of assets and liabilities, liquidity, security portfolio investments and trading room operations in the money- and capital markets.

The Bank's operating segments are:

Household segment - under responsibility of the Retail Division, which provides segment household customers with appropriate banking services and financial products, including mortgages;

Small business segment - under responsibility of the Retail Division, which provides segment customers - small businesses - with banking services and financial products, including commercial banking services appropriate for their needs;

Private banking - under responsibility of the Retail Division. This segment includes customers with 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 – under responsibility of the Business Banking Division, including the business sector, the construction and real estate sector and the corporate sector, which divide among themselves the servicing of business customers, depending on the amount of their debt, turnover and nature of their activities; The commercial banking segment includes mainly operations vis-à-vis medium-sized private and public companies (middle market), which are characterized by medium-sized indebtedness, highly scattered among different economic sectors.

Business banking - with this segment, the Business Division provides a range of banking and financial services to the largest corporations, in a range of sectors, having relatively high indebtedness. This segment also includes the banking services group for major customers in the construction and real estate sector.

Note 30 - Operating Segments and Geographic Regions

International operations – operations in this segment include international operations in the Bank's overseas branches as well as operations vis-à-vis foreign resident customers at tourist banking centers in Jerusalem and Tel Aviv.

Financial management - operations in this segment include, inter alia, management of the nostro portfolio, management of exposure to market risk and liquidity management as well as trading room operations in the finance- 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.

Along with re-organization, changes have also been made to internal product composition of the segments. The capital market attributes have been redefined to include income and expenses from customer transactions in securities both in Israel and overseas, in addition to the management and operation of provident funds and mutual funds – which were part of this segment in the past. The definition of the credit card sector was also updated to include, in addition to operating income and expenses, also the profit from credit card financing operations.

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 customers, including a checking account, a current loan account, different kinds of credit and guarantees, 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 customers on stock exchanges in Israel and overseas, provident fund operating services (management of provident funds and mutual funds until sold) which are among investment tracks available to Bank customers.
- **Credit cards –** A set of financial products and banking services given in conjunction with credit cards issued to Bank customers 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.

Note 30 - Operating Segments and Geographic Regions

- **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.

During 2007 the Bank launched a new system for profitability measurement, which measures results of Bank operations and provides a break-down of asset and liability balances from the individual transaction level through the organizational structure hierarchy up to the enterprise-wide level. Bank management uses the new system to analyze operating results by organizational criteria and by product offered by the Bank to customers. Profit is assigned in the system to customers and to products, which are presented in accordance with the Bank's organizational structure.

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

- Credit interest income and deposit interest expenses are directly attributed to the customer. For credit, an expense set at cost of capital raised is attributed to customers, against an inter-segment credit to the Financial Management segment. For deposits, a revenue set at cost of capital raised is attributed to customers, against an inter-segment debit to the Financial Management segment.
- For derivative instrument operations, profits are attributed to the customer at the spread incorporated in the price of the derivative instrument quoted to the customer. 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.
- Provision for doubtful debt is directly attributed to customers for whom it is made.
- Commission- and other income is specifically attributed to customers.
- Salary expense is attributed to customers assigned to specific contact persons. In addition, salary expenses of managers and staff of headquarter departments not referring to specific customers, are assigned to customers.
- Maintenance and other expenses are assigned to customers using the appropriate ratios.

Note 30 - Operating Segments and Geographic Regions

- 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 customers services by the branches.
- Provision for tax on operating profit is attributed to customers, 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 customers.
- Fixed assets are attributed based on appropriate ratios.

In order to analyze results of Bank operations by relevant criteria, customers have been assigned in the system to the organizational units in charge of servicing them. Information presented below by operating segment is based on the Bank's organizational structure, including recent changes, on customer assignment to various departments and hence to operating segments, and on attribution of results and balances to customers and segments in the new system.

Note 30 - Operating Segments and Geographic Regions - Consolidated
For the Year Ended December 31, 2007

Reported amounts (in NIS millions)

B. Information on operating segments

Presented results for 2007 are not comparable to results presented for 2006 and 2005, as indicated above.

	Household	Private banking	Small business	Commercial banking	Business banking	Financial Division International operations	Financial Division Financial management	Total consolidated
Profit (loss) from financing operations before provision for doubtful debt								
From outside operating segments	1,822	(100)	(309)	185	657	(105)	(124)	2,026
Inter-segment	(906)	149	586	(70)	(195)	96	340	-
Profit (loss) from financing operations before provision for doubtful debt	916	49	277	115	462	(4) (9)	216	2,026
Operating and other income	589	21	173	42	163	56	146	1,190
Total income	1,505	70	450	157	625	47	362	3,216
Provision for doubtful debt	67	-	74	7	77	3	-	228
Operating and other expenses								
From outside operating segments	1,012	11	361	124	133	130	167	1,938
Inter-segment	(62)	1	(26)	(9)	68	-	28	-
Other operating expenses - total	950	12	335	115	201	130	195	1,938
Operating profit (loss) before taxes	488	58	41	35	347	(86)	167	1,050
Provision for taxes on operating profit	171	20	15	12	121	(30)	59	368
Operating profit (loss) after taxes	317	38	26	23	226	(56)	108	682
Share in net after-tax operating profits (losses) of affiliates	-	-	-	-	-	-	(1)	(1)
Net operating profit	317	38	26	23	226	(56)	107	681
Net after-tax profit from extraordinary items	121	52	39	1	5	-	9	227
Net profit (loss)	438	90	65	24	231	(56)	116	908
Return on equity	19.2%	-	21.6%	9.2%	13.0%	(24.0%)	26.3%	-
Average balance of assets	42,430	-	4,938	4,349	17,499	5,873	18,955	94,044
Average balance of liabilities	33,219	2,210	9,796	2,167	12,240	5,999	23,082	88,713
Average balance of risk assets(1)	33,999	-	4,561	3,801	26,298	3,456	8,681	80,796
Average balance of provident and mutual fund assets	-	-	-	-	-	-	45,472	45,472
Average balance of securities	19,565	4,731	21,091	2,149	37,711	766	6,790	92,803
Credit to the public (end balance)	43,603	-	4,806	4,087	17,412	4,412	-	74,320
Deposits from the public (end balance)	30,731	2,204	11,106	2,432	10,753	2,570	15,494	75,290
Average balance of other assets managed	17,110	-	158	50	113	-	-	17,431

(1) Includes off-balance-sheet balances, as computed for capital adequacy.

Note 30 - Operating Segments and Geographic Regions - Consolidated
For the Year Ended December 31, 2007

Reported amounts (in NIS millions)

C. Information on profit from financing operations before provision for doubtful debt

						Financial Division		
	Household	Private banking	Small business	Commercial banking	Business banking	International operations	Financial management	Total consolidated
Margin from credit granting operations	491	-	168	80	312	88	-	1,139
Margin from receiving deposits	360	47	86	18	72	17	-	600
Other	65	2	23	17	78	(114)	216	287
Total	916	49	277	115	462	(9)	216	2,026

D. Information on geographic regions (2)

	Income for the year ended December 31, 2007 (3)	Net profit for the year ended December 31, 2007	Average total asset balance For 2007
Israel	3,214	993	88,844
Outside of Israel	2	(85)	5,200
Total consolidated	3,216	908	94,044

(2) Income and assets according to geographic regions were allocated on the basis of the location of the Group's offices.
(3) Includes operating profit from financing operations before provision for doubtful debt and other operating income.
(4) Includes provision for impairment of asset-backed securities, amounting to NIS 114 million.

Note 30 - Operating Segments and Geographic Regions - Consolidated
For the Year Ended December 31, 2006

Reported amounts (in NIS millions)

B. Information on operating segments

	Household (1)	Private banking	Small business	Commercial banking	Business banking	Financial management (1)	Total consolidated
Profit (loss) from financing operations before provision for doubtful debt							
From outside operating segments	814	(562)	452	211	883	189	1,987
Inter-segment	18	751	(16)	(139)	(393)	(221)	-
Profit (loss) from financing operations before provision for doubtful debt	832	189	436	72	490	(32)	1,987
Operating and other income	610	140	329	24	79	33	1,215
Total income	1,442	329	765	96	569	1	3,202
Provision for doubtful debt	174	-	65	6	60	-	305
Operating and other expenses							
From outside operating segments	1,849	72	53	3	112	28	2,117
Inter-segment	(922)	206	553	53	110	-	-
Operating profit (loss) before taxes	341	51	94	34	287	(27)	780
Provision for taxes on operating profit	160	19	38	14	131	(13)	349
Operating profit (loss) after taxes	181	32	56	20	156	(14)	431
Share in net after-tax operating profits (losses) of affiliates	-	-	-	-	-	(4)	(4)
Minority interest in net after-tax operating profits of subsidiaries	-	-	-	-	-	-	-
Net operating profit	181	32	56	20	156	(18)	427
Net after-tax profit from extraordinary items	72	33	23	-	3	85	216
Cumulative effect	-	-	-	-	-	-	-
Net profit	253	65	79	20	159	67	643
Return on capital (net profit as % of average capital)	12.4%	76.7%	13.3%	11.1%	10.0%	14.7%	-
Average balance of assets	38,437	2,498	7,018	2,916	15,793	21,482	88,144
Average balance of liabilities	31,261	17,115	14,919	914	7,684	11,306	83,199
Average balance of risk assets(2)	30,571	1,272	8,880	2,700	23,774	6,828	74,025
Average balance of provident and mutual fund assets	7,439	3,490	2,361	41	341	66	13,738
Average balance of securities (1)	1,956	7,392	43,106	4,797	14,281	-	71,532
Average balance of other assets managed	17,442	12	138	137	216	74	18,019

(1) Reclassified.
(2) Includes off-balance-sheet balances, as computed for capital adequacy.

Note 30 - Operating Segments and Geographic Regions - Consolidated
For the Year Ended December 31, 2006
Reported amounts (in NIS millions)

C. Information on profit from financing operations before provision for doubtful debt

	Household	Private banking	Small business	Commercial banking	Business banking	Financial management	Total consolidated
Margin from credit granting operations	625	54	275	61	325	-	1,340
Margin from receiving deposits	181	118	118	5	42	-	464
Other	26	17	43	6	123	(32)	183
Total	832	189	436	72	490	(32)	1,987

D. Information on geographic regions (3)

	Income for the year ended December 31, 2006 (4)	Net profit for the year ended December 31, 2006	Average total asset balance For 2006
Israel	3,153	621	83,941
Outside of Israel	49	22	4,203
Total consolidated	3,202	643	88,144

(3) Income and assets according to geographic regions were allocated on the basis of the location of the Group's offices.
(4) Includes operating profit from financing operations before provision for doubtful debt and other operating income.

Note 30 - Operating Segments and Geographic Regions - Consolidated
For the Year Ended December 31, 2005

Reported amounts (in NIS millions)

B. Information on operating segments

	Household (1)	Private banking	Small business	Commercial banking	Business banking	Financial management (1)	Total consolidated
Profit (loss) from financing operations before provision for doubtful debt							
From outside operating segments	570	(410)	265	264	797	418	1,904
Inter-segment	141	559	168	(142)	(456)	(270)	-
Profit from financing operations before provision for doubtful debt	711	149	433	122	341	148	1,904
Operating and other income	584	131	310	27	38	24	1,114
Total income	1,295	280	743	149	379	172	3,018
Provision for doubtful debt	119	-	97	3	73	-	292
Operating and other expenses	821	208	536	66	176	32	1,839
Operating profit before taxes	355	72	110	80	130	140	887
Provision for taxes on operating profit	142	30	46	34	63	56	371
Operating profit after taxes	213	42	64	46	67	84	516
Share in net after-tax operating profits (losses) of affiliates	-	-	-	-	-	(3)	(3)
Minority interest in net after-tax operating profits of subsidiaries	-	-	-	-	-	-	-
Net operating profit	213	42	64	46	67	81	513
Net after-tax loss from extraordinary items	-	-	-	-	-	(2)	(2)
Cumulative effect	-	-	-	-	-	(4)	(4)
Net profit	213	42	64	46	67	75	507
Return on equity	11.9%	57.5%	9.4%	13.1%	5.8%	18.2%	-
Average balance of assets	36,235	2,423	8,142	5,354	12,059	19,133	83,346
Average balance of liabilities	34,326	16,302	15,722	1,374	3,913	7,324	78,961
Average balance of risk assets(2)	27,521	1,119	10,403	5,363	17,850	6,136	68,392
Average balance of provident and mutual fund assets	8,828	4,351	2,787	247	507	88	16,808
Average balance of securities (1)	1,442	5,606	37,281	3,652	5,369	-	53,351
Average balance of other assets managed	17,732	12	140	163	204	77	18,328

(1) Reclassified.
(2) Includes off-balance-sheet balances, as computed for capital adequacy.

Note 30 - Operating Segments and Geographic Regions - Consolidated
For the Year Ended December 31, 2005

Reported amounts (in NIS millions)

C. Information on profit from financing operations before provision for doubtful debt

	Household	Private banking	Small business	Commercial banking	Business banking	Financial manage ment	Total consolid ated
Margin from credit granting operations	538	35	274	96	253	-	1,196
Margin from receiving deposits	148	101	94	6	15	-	364
Other	25	13	65	20	73	148	344
Total	711	149	433	122	341	148	1,904

D. Information on geographic regions (3)

	Income for the year ended December 31, 2005 (4)	Net profit for the year ended December 31, 2005	Average total asset balance For 2005
Israel	2,910	478	79,439
Outside of Israel	108	29	3,907
Total consolidated	3,018	507	83,346

(3) Income and assets according to geographic regions were allocated on the basis of the location of the Group's offices.

(4) Includes operating profit from financing operations before provision for doubtful debt and other operating income.

Note 31 - Nominal Historical Data for Tax Purposes - the Bank

(In NIS millions)

	As of December 31	
	2007	2006
Total assets	93,849	89,205
Total liabilities	88,543	84,433
Total shareholders' equity	5,306	4,772

	For the Year Ended December 31		
	2007	2006	2005
Nominal net profit	947	654	503