

RISK MANAGEMENT REPORT AS OF 31.03.2021

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This report includes supplementary information to the Bank's financial statements and is prepared in accordance with the Supervisor of Banks' directives, which include disclosure requirements from Basel Pillar III and additional disclosure requirements by the Financial Stability Board (FSB). The Israel Securities Authority's MAGNA website includes the following reports: Condensed financial statements of interim periods, a detailed risk management report and additional supervisory information regarding supervisory capital instruments issued by the Bank. In conformity with the Supervisor of Banks' directives, these reports, including XBRL format, are also available on the Bank website at www.mizrahi-tefahot.co.il/en ► financial reports.

Mizrahi Tefahot Bank

Risks report for the first quarter of 2021

This report includes additional information to the Bank's financial statements and is compiled in conformity with directives of the Supervisor of Banks, which include disclosure requirements of Basel Pillar 3 and additional disclosure requirements of the Financial Stability Board (FSB).

The following reports are available on ISA's MAGNA website: This Risks Report and other supervisory information about supervisory capital instruments issued by the Bank (hereinafter: "the Reports"). In conformity with instructions of the Supervisor of Banks, the condensed financial statements for the interim period and the aforementioned Reports are also available on the Bank website:

www.mizrahi-tefahot.co.il > about the bank > investor relations > financial statements

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Risks Report

This risks report includes additional information to the condensed consolidated financial statements of Bank Mizrahi Tefahot Ltd. and its subsidiaries as of March 31, 2021. The condensed financial statements and additional information to the condensed financial statements, including the Report of the Board of Directors and Management, this Risks Report and other supervisory disclosures have been approved for publication by the Bank's Board of Directors at its meeting held on May 19, 2021.

The Risks Report and other supervisory disclosures are compiled in conformity with directives of the Supervisor of Banks, which include disclosure requirements of Basel Pillar 3, disclosure requirements published by the Financial Stability Board (FSB) and other disclosure requirements of the Financial Stability Board (FSB).

Pursuant to the Public Reporting Regulations of the Supervisor of Banks, the quarterly format of the risks report is limited and focused on qualitative and quantitative disclosures whose quarterly analysis and presentation are material for readers of the report.

If needed, this report should be read in conjunction with the 2020 Risks Report.

The disclosure in this report is designated to allow users to evaluate significant information included with regard to implementation of the framework for capital measurement and capital adequacy and to implementation of provisions of "Basel III: A global regulatory framework for more resilient banks and banking systems".

All of these reports are also available on the Bank's website.

www.mizrahi-tefahot.co.il >> about the bank >> investor relations >> financial statements.

As directed by the Supervisor of Banks, additional information with regard to risks is provided in the Report of the Board of Directors and Management in the financial statements as of March 31, 2021, in the following chapters:

- Chapter "Overview, targets and strategy" / major risks
- Chapter "Explanation and analysis of results and business standing" / Key and emerging risks
- Chapter "Risks Overview"

In conformity with the Equal Rights to Handicapped Persons Regulations (Service Accessibility Adaptations), 2013, the website also provides accessible reports.



Moshe Vidman

Chairman of the Board
of Directors



Moshe Lari

President & CEO



Doron Klauzner

Vice-president, Chief
Risks Officer (CRO)

Approval date of the financial statements and the Risks Report:
Ramat Gan, May 19, 2021

Forward-Looking Information

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

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

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

The information presented here relies, inter alia, on publications of the Central Bureau of Statistics and the Ministry of Finance, on data from the Bank of Israel data, the Ministry of Housing and others who issue data and assessments with regard to the capital market in Israel and overseas as well as forecasts and future assessments on various topics, as mentioned above so that there is a possibility that events or developments predicted to be anticipated would not materialize, in whole or in part.

Key supervisory ratios and overview of risk management and risk assets

Key supervisory ratios – key data

Below is key data relevant for the Bank's risk profile (NIS in millions):

	2021	2020				2020
	First quarter	Fourth quarter	Third quarter	Second quarter	First quarter	Annual
Key supervisory and financial ratios						
Available capital						
Tier I capital ⁽¹⁾	20,708	20,137	19,708	17,033	16,718	20,137
Tier I capital before effect of transitional provisions	20,607	20,017	19,571	16,956	16,653	20,017
Total capital	27,373	27,313	26,488	22,999	22,521	27,313
Total capital before effect of transitional provisions	26,825	26,300	25,458	22,029	21,563	26,300
Risk weighted assets						
Total risk weighted assets (RWA)	203,936	200,484	197,502	170,992	169,001	200,484
Capital adequacy ratio (in %)						
Tier I capital ratio ⁽¹⁾	10.15	10.04	9.98	9.96	9.89	10.04
Tier I capital ratio before effect of transitional provisions	10.10	9.98	9.91	9.91	9.85	9.98
Total capital ratio	13.42	13.62	13.41	13.45	13.33	13.62
Total capital ratio before effect of transitional provisions	13.15	13.11	12.89	12.88	12.75	13.11
Tier I capital ratio required by Supervisor of Banks ⁽²⁾	8.66	8.68	8.71	8.79	8.82	8.68
Available Tier I capital ratio, beyond what is required by the Supervisor of Banks ⁽²⁾	1.49	1.36	1.27	1.17	1.07	1.36
Leverage ratio						
Total exposure	401,308	388,370	376,614	317,759	309,863	388,370
Leverage ratio (in %) ⁽³⁾	5.16	5.19	5.23	5.36	5.40	5.19
Leverage ratio before effect of transitional provisions (in %)	5.13	5.15	5.20	5.34	5.37	5.15
Liquidity coverage ratio⁽⁴⁾						
Total high-quality liquid assets	84,754	78,145	59,709	53,992	49,568	78,145
Total outgoing cash flows, net	63,729	58,769	46,783	44,280	42,300	58,769
Liquidity coverage ratio (in %)	133	133	128	122	117	133
Performance benchmarks						
Net profit return on equity ⁽⁵⁾⁽⁶⁾	14.9	11.4	9.5	9.0	9.1	9.5
Profit return on risk assets ⁽⁶⁾⁽⁷⁾	1.34	1.02	0.89	0.85	0.86	0.89
Deposits from the public to loans to the public, net	117.7	115.8	114.2	108.1	106.2	115.8
Key credit quality benchmarks						
Ratio of balance of provision for credit losses to total loans to the public	0.96	0.98	0.95	0.96	0.91	0.98
Balance of provision for credit losses, including estimated credit losses in balance of loans to the public at Union Bank, as percentage of loans to the public	1.07	1.11	1.09	–	–	1.11
Ratio of impaired debts or debts in arrears 90 days or longer to loans to the public	1.23	1.18	1.20	1.34	1.41	1.18
Expenses with respect to credit losses to loans to the public, net for the period ⁽⁶⁾	0.02	0.19	0.59	0.50	0.66	0.43
Of which: With respect to commercial loans other than housing loans	0.16	0.49	0.87	1.17	1.55	0.86
Of which: With respect to housing loans	(0.06)	0.02	0.44	0.15	0.19	0.18
Ratio of net accounting write-offs to average loans to the public ⁽⁶⁾	0.06	0.06	0.13	0.15	0.16	0.12

Financial ratios indicate as follows:

- Net profit return on equity in the first quarter of this year was 14.9%, due to higher revenues, primarily due to increase in operations and decrease in expenses with respect to credit losses due to improvement in the economic environment; therefore, the provisions made were gradually attributed to specific areas and borrowers, concurrently with more moderate total provisions.
- The ratio of deposits from the public to loans to the public, net reached 117.7%, due to continued increase in deposits from the public.
- Ratio of Tier I capital to risk components increased to 10.15%. The minimum ratio required of the Bank is 8.66% (the minimum ratio without relief granted due to the Corona Virus crisis is 9.66%).
- Items of profit and loss, balance sheet items and various financial ratios are analyzed in detail in the Report of the Board of Directors and Management, in chapter "Explanation and analysis of results and business standing" and in chapter "Risks overview", as the case may be.

- (1) The Bank has no equity instruments included in "Additional Tier I capital", so that total Tier I capital equals total Tier I equity.
- (2) Including a capital requirement at 1% of the housing loan balance as of the date of the financial statements, excluding housing loans extended during the Corona Virus crisis.
- (3) Leverage Ratio – ratio of Tier I capital (according to Basel rules) to total exposure. This ratio is calculated in conformity with Proper Conduct of Banking Business Directive 218
- (4) Liquidity Coverage Ratio – ratio of total High-Quality Liquid Assets to net cash outflow. This ratio is calculated in conformity with Proper Conduct of Banking Business Directive 221, in terms of simple averages of daily observations during the most recent reported quarter.
- (5) Net profit attributable to shareholders of the Bank.
- (6) Calculated on annualized basis.
- (7) Net profit to average risk assets.

Risks Report

As of March 31, 2021

Below is the capital for calculating the capital ratio after supervisory adjustments and deductions:

	As of March 31, 2021	As of March 31, 2020	As of December 31, 2020
Tier I shareholders' equity	20,708	16,718	20,137
Tier II capital	6,665	5,803	7,176
Total capital	27,373	22,521	27,313

Total credit risk to the public⁽¹⁾:

	March 31, 2021	March 31, 2020	December 31, 2020
Total credit risk to the public	336,471	278,120	332,480

(1) For more information about total credit risk to the public, see the chapter "Risks overview" in the Report by the Board of Directors and Management.

Risk assets and capital requirements with respect to credit risk, market risk, CVA risk and operational risk are as follows:

	As of March 31, 2021		As of March 31, 2020		As of December 31, 2020	
	Weighted risk asset balances	Capital requirement ⁽¹⁾	Weighted risk asset balances	Capital requirement ⁽²⁾	Weighted risk asset balances	Capital requirement ⁽³⁾
Credit risk	187,829	22,848	155,968	19,215	184,905	22,520
Market risk	2,484	302	1,843	227	2,228	271
CVA risk with respect to derivatives ⁽⁴⁾	511	62	673	83	487	59
Operational Risk ⁽⁵⁾	13,112	1,595	10,517	1,296	12,864	1,567
Total risk assets	203,936	24,807	169,001	20,821	200,484	24,417

(1) The capital requirement was calculated at 12.16% of risk asset balances. For more information about reduction of minimum capital ratios which banks are required to maintain in the normal course of business, by one percentage point, see Note 9 to the financial statements.

(2) The capital requirement was calculated at 12.32% of risk asset balances.

(3) The capital requirement was calculated at 12.18% of risk asset balances.

(4) Credit Value Adjustments – mark to market with respect to credit risk of counter-party, in conformity with Basel III provisions.

(5) Capital allocation with respect to operational risk was calculated using the standard approach.

Bank approach to risk management (OVA)

General information regarding management of various risks and the risk profile

The Bank operates in conformity with directives of the Supervisor of Banks with regard to risk management and control, and in conformity with Proper Conduct of Banking Business Directives, and in particular with Directive 310 "Risks Management", which is based on the Basel Committee recommendations, which specifies the principles for risks management and control in the Israeli banking system and stipulates the standards required of the banks for creating their risks management and control framework in line with regulatory requirements, the Bank's risk profile and its business targets. All policy documents for risk management and control at the Bank are based on these basic principles.

The risks management and control framework at the Bank, as recommended by the Basel Committee, specifies three pillars:

Pillar 1 – minimum capital – minimum capital allocation requirements with respect to credit risk, market risk and operational risk calculated by standard models.

Pillar 2 – Supervision and control process over capital adequacy, the Internal Capital Adequacy Assessment Process (ICAAP) conducted by the Bank, as well as the Supervisory Review and Evaluation Process (SREP).

Pillar 3 – "market discipline" – reporting and disclosure to the regulating authority and to the public.

Efficient, comprehensive risks management is a key foundation for ensuring the Bank's stability over time. Risks management and control processes at the Bank and at the Group are designed to identify, manage, monitor, quantify and mitigate all material risks associated with Bank operations and to support achievement of the Bank's business objectives. The Bank is exposed to diverse risks which may potentially impact its financial results and its image. The Bank exposed to financial risks, such as: credit risks, liquidity risk and market and interest risks, as well as non-financial risks, such as: compliance and regulatory risk, operational Risk (including IT risk and information and cyber security risk), legal risk, reputational risk and other risks.

Risks management at the Group is conducted from a comprehensive viewpoint of Bank operations in Israel and at overseas affiliates and in conformity with regulatory requirements, so as to support achievement of the Group's strategic objectives, while assuming risks in an informed manner and maintaining a risk level in line with the overall risk appetite specified by the Bank's Board of Directors.

The risk appetite defines, at the highest level, the overall risk level which the Bank wishes to and can assume. The risk appetite defines where the Bank would like to be in terms of reward (proceeds/benefit) vs. risk (cost) from a forward-looking viewpoint. Risk appetite is defined in qualitative and quantitative terms in the normal course of business and under stress scenarios, and is based on the risk strategy and on basic principles of the Bank's business and strategic plan, on the required liquidity and capital for achieving the strategic objectives and on results of the various stress scenarios tested by the Bank.

Risk tolerance is a specific determination of risk levels for all risks to which the Bank is exposed. Risk levels are determined by a range of qualitative and quantitative benchmarks, in support of achieving the business goals, while keeping the Bank within the overall limits of the specified risk appetite and subject to strict regulatory restrictions. These risk restrictions, on aggregate, reflect the overall risk level which the Bank is willing and able to assume.

Union Bank merger

On August 30, 2020, the Bank issued a proposed exchange tender for Union Bank shares, which closed on September 30, 2020. In conjunction with the tender offer, the Bank acquired 100% of the issued and paid-in share capital of Union Bank and of voting rights in Union Bank.

On November 29, 2020, the Bank and Union Bank signed an agreement for merger of Union Bank with and into the Bank, such that as from the date when the Registrar of Companies shall provide to the Bank a certificate evidencing the merger, and subject to fulfillment of all suspensive conditions for the merger, as set forth in the merger agreement ("the Closing Date"), the Bank shall receive all assets, rights and liabilities of Union Bank as-is, retroactively as from December 31, 2020, such that immediately after the Closing Date, the Bank shall have all rights and obligations of Union Bank as they were immediately prior to December 31, 2020, and such transfer shall be deemed to have been made on December 31, 2020. The merger shall take place without any consideration paid nor payable to the Bank and/or to Union Bank, directly nor indirectly, in cash or in kind, due or with respect to the merger. The Bank Board of Directors resolved to approve the merger after discussion and review of the financial standing of the Bank and of Union Bank, and has determined that with due attention to the financial standing of the Bank and of Union Bank, the Board believes that there is no reasonable concern that due to the merger, the Bank would not be capable of meeting its obligations to its creditors, and based on other reasons cited in the Bank's report of the merger dated November 29, 2020.

On December 31, 2020, the Bank announced a resolution to merge Union Bank Issuance Ltd. into Mizrahi Tefahot Issuance Ltd., subject to fulfillment of suspensive conditions set forth in the merger agreement between these two entities, hence completion of this agreement is uncertain. Furthermore, on November 8, 2020, Mizrahi Tefahot Trust Company Ltd. announced it has signed a merger agreement with Union Bank Trust Company Ltd. The merger certificate was received on May 2, 2021 and the Trust Company reported the dissolution of Union Bank Trust Company Ltd., which was merged into Mizrahi Tefahot Trust Company Ltd.

Underlying the merger of the sixth largest bank in Israel with and into the Bank, the joining of Union Bank allows the Bank Group to make a significant step forward in market share of various operating areas, with improvement to the mix of sources and uses and increased competitiveness. Union Bank's lending operations in the various segments diversifies Mizrahi-Tefahot's lending mix, in conformity with the Bank's strategic targets, in particular with regard to the business lending segment. The acquisition would allow for economies of scale at the merged bank and would result in operational cost savings.

The merger transaction is a material, large-scale and highly complex process which entails a wide range of risks. The merger process was launched in the fourth quarter of 2020 and is carried out by several extensive joint work teams of Bank Mizrahi Tefahot and Union Bank, managed by a steering committee headed by the Bank President & CEO, with administrations established to carry out the merger plan and a special Board committee established to supervise this process. Risk management is an integral and dynamic part of all work teams, and the Group's Chief Risks Officer reviews and integrates all risks of the merger process and the measures applied to reduce and manage such risk.

Union Bank has a long-standing contract with Bank Leumi for obtaining IT and operating services, which has been extended from time to time. On May 12, 2020, the Board of Directors of Union Bank approved contracting an addendum to the agreement, whereby the parties agreed, inter alia, that the agreement would be extended through December 31, 2022.

The Bank manages the merger project gradually and separately from current business, in order to allow for achievement of the work plan targets concurrently with the merger process.

This information constitutes forward-looking information, as defined in the Securities Law, 1968, based on assumptions, facts and data (hereinafter jointly: "assumptions") brought before the Bank's Board of Directors. These assumptions may not materialize due to factors which are under the Bank's control.

For more information about acquisition of Union Bank, see Note 35 to the 2020 financial statements.

Effect of the Corona Virus outbreak

in the first quarter of 2021, the Bank continued to operate under Corona Virus routine, including the following: Compliance with work guidelines and maintaining hygiene and social distancing, working in split units, continuation of working remotely by means of a fast, structured process and so forth. Concurrently, the Bank continued to monitor cases of morbidity or infection at branches and at headquarters units and the date of return to work, including at Group level.

Business units continue to keep in close regular contact with clients, in order to help the business sector face the challenges resulting from this crisis.

Note that in the first quarter of 2021, the economy improved significantly upon lifting of the third lock-down and progress made in the vaccination campaign. Economic data, including the unemployment rate and purchases paid by credit card, indicate recovery in current economic activity. The Bank made some adjustments to its operations due to the improved morbidity situation.

In 2020, the Bank applied measures in response to client needs arising from the situation. Action taken by the Bank includes approval of a delay in current repayments for mortgage clients who needed this due to temporary hardship resulting from the crisis. The Bank also extended State-guaranteed loans from State-guaranteed foundations, as part of the economic assistance program announced by the State.

As of March 31, 2021, out of all housing loans subject to delay, some NIS 44.1 billion resumed payment (of which NIS 7.4 billion chose the partial payment track in conformity with the Bank of Israel outline). NIS 1.7 billion is still subject to full delay, ending through June 2021. Of the loans where payments were resumed in the first quarter of 2021, only NIS 0.6 billion are in arrears.

As of March 31, 2021, out of all other (non-housing) loans subject to delay, NIS 4.6 billion resumed repayment and NIS 1 billion are still subject to delay, mostly expected to end in 2021. Of the loans where payments were resumed by end of the first quarter of 2021, only NIS 0.6 billion are in arrears.

As of March 31, 2021, the Bank extended loans amounting to NIS 5.3 billion from State-guaranteed funds. Against the loans extended, in conformity with the Bank of Israel outline, the Bank participated and obtained a special-purpose monetary loan from the Bank of Israel whose balance as of March 31, 2021 amounted to NIS 2.2 billion, for 3 years bearing fixed interest at 0.1%, whose balance as of March 31, 2021 amounted to NIS 2.2 billion.

For more information about group-based provision for credit losses recognized, inter alia, considering identified risk in certain sectors and loans subject to repayment delay due to the Corona Virus crisis, in conformity with the risk attributes, see chapter Explanation and analysis of results and business standing in the Report of the Board of Directors and Management.

For more information about loans subject to repayment delay and loans extended from State-guaranteed funds, see chapter "Risks overview – Credit risk" in the Report of the Board of Directors and Management.

General mapping of risk factors and their impact

Below is a mapping of risk factors, their potential impact on the Bank Group and executives appointed Risk Owners for each risk factor:

Risk factor	Risk factor impact	Risk Owner
Overall effect of credit risks	Medium	Manager, Business Division
Risk from quality of borrowers and collateral	Medium	
Risk from industry concentration	Low-medium	
Risk from concentration of borrowers/borrower groups	Low	
Risk with respect to mortgage portfolio	Low-medium	
Overall effect of market risk ⁽¹⁾	Low-medium	Manager, Financial Division
Interest risk	Low-medium	
Inflation risk	Low-medium	
Exchange rate risk	Low	
Liquidity risk	Low-medium	Manager, Financial Division
Overall effect of operational risk	Medium	Manager, Risks Control Division
Cyber and information security	Medium	Manager, Risks Control Division
Information technology risk	Medium	Manager, Mizrahi-Tefahot Technology Division Ltd.
Legal risk	Low-medium	Chief Legal Counsel
Compliance and regulatory risk	Low-medium	Manager, Risks Control Division
AML and terror financing risk	Low-medium	Manager, Risks Control Division
Cross-border risk	Low-medium	Manager, Risks Control Division
Reputation risk ⁽²⁾	Low	Manager, Marketing, Promotion and Business Development Division
Business-strategic risk ⁽³⁾	Low-medium	President & CEO

(1) Includes options and shares risk mapped at Union Bank.

(2) The risk of impairment of the Bank's results due to negative reports about the Bank.

(3) The definition of business-strategic risk includes the capital planning and management process.

The impact of the various risks factors to which the Bank is exposed, set forth in the table above have been determined based on management assessment, as provided from time to time and includes risk associated with the Union Bank merger, which does not materially change the Group's overall risk level. These assessments are based on monitoring of various quantitative risk benchmarks specified by the Bank, includes the expected direction of their development and are based on qualitative assessment of risks management and the effectiveness of control circles, in line with the Bank's ICAAP process and its results, led by the Bank's Risk Managers.

The risk is in line with the risk appetite guidelines specified by the Bank.

Since the start of 2020, the Bank's overall risk profile increased due to higher credit risk due to implications of the global Corona Virus pandemic, which started in Israel in late February 2020, expanded in March and continued to develop and affect the Israeli and global economy throughout the year. The impact of this crisis on the quality of the Bank's loan portfolio may not be fully assessed as yet. The Bank regularly reviews the risk benchmarks and adapts them to current business operations as necessary, subject to and in line with the Bank's overall risk appetite for various risks.

Assessment of the impact of risk factors in the first quarter of 2021 remained unchanged from the previous two quarters, despite the improvement in the economy, due to the remaining uncertainty with regard to implications of this crisis.

The overall impact of credit risk and risk associated with quality of borrowers and collateral was Medium, a risk level reflecting the risk of effect of the Corona Virus crisis on the private segment, and to a larger extent on the business segment, primarily

small and medium businesses. Material risk factors are the unemployment rate, slow-down in economic activity, and in particular in specific economic sectors (such as: Aviation, fashion, hotels, accommodation and dining services, leisure and culture) which were impacted, and volatility in financial markets affecting the collateral value. These factors may result in more clients facing difficulties over time. The risk level remains unchanged, despite the improvement in the economy and resumed operations in most segments. The level of uncertainty remains high, and there is still concern that the impact of the Corona Virus crisis has yet to be fully reflected due, inter alia, to the various measures applied, some of which have yet to be concluded, including outstanding delayed payments and State-guaranteed loans that have yet to reach maturity. The Bank strictly manages and monitors its credit risk and has taken active steps in conformity with the situation, in order to help clients get through this crisis period and to reduce the likelihood of default, while maintaining the risk management policy of the Bank.

The risk level in the housing loan portfolio remains Low-Medium, due to uncertainty with regard to borrower risk, with the full repayment schedule yet to be resumed, as well as borrower behavior upon expiration of the delays granted. As from the end of 2020, in conformity with the Bank of Israel outline, clients who have asked for delays were allowed to resume partial mortgage repayments for up to two years. The Bank closely monitors this activity and risk aspects with regard to the following: The delayed amount and the partial repayment rates, delay period, borrower profile, LTV ratio and so forth. The Bank also monitors development of borrower behavior after expiration of the repayment delay. For more information about loans subject to repayment delay and loans extended from State-guaranteed funds, see chapter "Risks overview – Credit risk" in the Report of the Board of Directors and Management. In mid-May, further to operation "Guardian of the Walls" and events across the country, the alert level was raised to Elevated.

Furthermore, following these security events, the Bank is preparing for continued normal operation, in line with guidelines from the Home Front Command, and is regularly assessing the situation. At this stage, the impact of these events on Bank operations and risk assessment may not be assessed.

Technology risk and cyber and information security risk are material risks for the Bank and the potential damage due to materialization of such risk may be significant, during routine operations and even more so during an emergency. Activity is managed in a focused manner, with all efforts marshaled to provide the service required for the Bank, focused on changing needs in line with the Bank's business strategy and taking most of the steps to reduce potential risk in as much as possible. In actual fact, there were no material events related to technology nor to cyber and information security.

Liquidity risk remained low-medium. In the first quarter of 2021, the Bank maintained its Elevated state of alert. During the current period, the Bank closely monitors (at daily level) qualitative and quantitative indicators (both internal and external) and conducts daily reviews of multiple stress scenarios for various time frames – liquidity is appropriate across all these scenarios and the Bank is in compliance with all internal limitations. Due to the significant decrease in morbidity in Israel and return to normal operations, with significant lifting of restrictions, the Bank resolved at the end of April 2021 to lower the state of alert and to return to business as usual.

Reputational risk remained Low, with the Bank constantly monitoring various benchmarks and indicators with regard to the Bank's reputation, including impact of the Union Bank merger, and the client conversion process which started in the first quarter of the year. There was no material impact on the Bank's reputational risk.

The Bank regularly reviews the implications of this crisis on business-strategic risk. At this stage and due to the current uncertainty, the full impact of the crisis on Bank operations may not be assessed.

Strategic plan

Further to the Bank's 2020 annual report and in view of the Bank's achievements, changes in the banking industry and in the business environment, on April 26, 2021 the Bank Board of Directors approved a new five-year strategic plan for 2021-2025, based on the following:

- Position the Bank as a key player in business banking, based on supporting action including: set up operations for investments in non-banking corporations, lead large and complex transactions and expand the Bank's international operations at its branches in London and in the USA in areas focused on business banking;
- Establish the Bank Group's leadership position among households: Maintain the leadership position in the mortgage market while introducing innovations in products and processes, and increasing synergies with commercial operations, expand operations among target populations and set up a desk for unique consumer credit products;
- Provide personal, human banking services supported by advanced digital technology, including optimal combination of human and digital channels, with human service by expert bankers, including in digital, in accordance with client choice and needs, as well as offering personalized value propositions across all channels, which are customized for client needs.
- Align the operating model with future challenges and improve operating efficiency through, inter alia, locating the Bank headquarters in the central Lod campus, align branch structure with future challenges and optimize use of real estate, automate banking operations and streamline the work environment.

- Leverage the Union Bank merger to create operating and business synergies and to realize economies of scale.

The new strategic plan is designed to achieve the following targets:

- Achieve in 2025, net profit return on equity attributable to equity holders of 14% on average equity, as well as double-digit, growing and stable return over the term of the strategic plan; these rates are based on the ratio of Tier I capital to risk components for the Bank at the minimum set by the Supervisor of Banks plus appropriate margin;
- Grow banking operations so as to increase the Bank's market share in the Israeli banking system;
- Grow revenues at an annual average rate of 8% (although non-linear), while controlling the average annual expenses at a 5% growth rate (also non-linear) over the term of the new strategic plan;
- Maintain high operating efficiency and leverage economies of scale due to the Union Bank merger, to achieve a cost-income ratio lower than 50% in 2025.
- Under the new strategic plan, the Board of Directors shall monitor execution of the plan, in order to consider potential increase of the dividend rate, from 40% of net profit attributable to Bank shareholders, up to 50% of net profit, upon conclusion of the Union Bank merger process; This would be subject to Bank compliance with the ratio of Tier I equity to risk components, as required by the Supervisor of Banks, maintaining appropriate margins and subject to approval by the Supervisor of Banks.
- See also chapter "Dividend distribution policy".
- For more information see Immediate Report dated April 27, 2021 (reference: 2021-01-071448).

The Bank conducts processes for risk identification and measurement, based on a range of methodologies to assess risk levels and exposure to various risks, in the normal course of business and under stress scenarios. The Bank applies quantitative measurement methods (models, benchmarks / indicators, scenarios and sensitivity analysis, inter alia) and qualitative measurement methods (expert assessments and surveys).

Summary of Bank policy on major risks and developments in the first quarter of 2021

Business goals and strategy

For more information about the Bank's new strategic plan for 2021-2025, see chapter "Business goals and strategy" of the Report of the Board of Directors and Management for the first quarter of 2021.

Credit risk

The overall credit risk level remained Medium, a level which reflects the uncertainty with regard to the full impact of the crisis on the quality of the Bank's loan portfolio.

Loans in the micro and small business segment is highly diversified in terms of clients in various economic sectors, mostly in small industry, trade, business and financial services. Financing in the micro and small business segment is mostly provided for short terms, for current operations and for financing of working capital, covering gaps in cash flow, financing trade receivables, inventory and import activities. Such financing is provided against appropriate collateral, such as checks for collateral / checks receivable, credit card vouchers, invoices, pledging of contracts and current liens. Moreover, credit is extended against external collateral, such as deposits, securities portfolios and real estate. The risk level in the loan portfolio for small and micro-businesses is constantly monitored, including use of custom credit rating models and setting the appropriate risk appetite. The Bank also monitors high-risk economic sectors.

Loans to medium businesses are typically highly diversified across clients, total credit per client, economic sectors and by geography. Financing is provided to this segment for current operations through financing of working capital, including financing of trade receivables and inventory, which is typically short-term financing, expansion and investment in the firm, which is typically medium- and long-term financing. This financing is backed by most existing collateral types, such as: deposits, securities, real estate, equipment, vehicles, current liens, various guarantees and personal guarantees. In addition, financial covenants are used for these clients, in order to mitigate risk.

Loans to large business clients is typically less diversified than in other segments. These clients typically have complex financial activities and diverse financing sources, both from the banking system in Israel and overseas, from institutional investors and from the capital market. Collateral for such loans is typically general collateral, such as a current lien, negative pledge along with financial covenants. These clients are involved with various credit products, including credit for the capital market.

Loans to the individual client segment are highly diversified – by number of clients and by geographic location. Most clients in this segment are salaried employees with an individual account or joint household account. Clients of the Retail Division are rated using custom advanced models. These models quantify the probability of default (PD) and the loss given default (LGD) for small businesses and individual clients of the Retail Division. On-going management at the Retail Division is primarily based on the MADHOM system (advanced rating, underwriting and management system).

Business credit is managed based on multiple risk benchmarks, including internal models for assessment of client credit ratings. The Bank has the business, legal and operating infrastructure for flexible management of credit risk by selling and/or sharing risk. The Bank closely manages and monitors credit risk through, inter alia, on-going activity of forums headed by the Bank President & CEO and by the Business Division Manager, and attended by the Risk Control Division and representatives of the business divisions. The business units continue to be regularly in close contact with clients, in order to assess their business standing and the implications of the crisis for these clients, in order to help the business sector face the challenges resulting from this crisis, while maintaining balances and minimizing credit risk.

The Bank has applied a wide range of measures to provide an immediate response to needs arising from the situation, from operational response to clients to adjustments made to the credit underwriting and credit risk policy. The Bank is acting and constantly reviewing the risk profile against the risk appetite, in line with the scope of operations and risk.

Loans provided by the Bank from the State-guaranteed fund in the General track of the State-guaranteed foundation to assist small and medium businesses impacted by the Corona Virus crisis includes a State guarantee for 85% of each loan, with an aggregate total of 15% of the entire portfolio, against a deposit made by the client equal to 5% of the loan amount. These loans bear interest at the Prime lending rate + 1.5%. During the first year, no principal repayment is due for such loans, and interest is paid by the State. This fund also launched a special track for businesses at high risk ("enhanced track"), with state guarantee for 60% of the entire portfolio and loan terms identical to those in the general track of this fund. Concurrently, on April 30, 2020, a fund for large businesses was launched, which is guaranteed by the State at 75% per loan and up to 12% in total guarantee.

Housing loans account for a material share of total credit risk at the Bank; and the overall risk level in the mortgage portfolio is estimated to be Low-Medium due to on-going uncertainty.

The Bank constantly monitors the risk profile of the mortgage portfolio and its development over time, in view of the specified risk appetite. In particular, this monitoring is conducted through the Bank's quarterly risks document which is presented to and approved by Bank Management, the Board of Directors and its Risks Management Committee. Such monitoring reveals that leading risk benchmarks continue to remain relatively low. These benchmarks include: LTV ratios, repayment ratio, rate of oblige in default and, in particular, the rate of arrears for new loans (one year since origination), which is testimony to the high quality of underwriting at the Bank. Note that the average LTV ratio for the Bank's mortgage portfolio (at end of March 2021) was 53% (reflecting the LTV ratio upon loan origination). The Bank also estimates the "actual" LTV ratio for the portfolio, based on changes to property values, based on estimates by the Central Bureau of Statistics against the outstanding portfolio balances. This ratio is lower than the original LTV ratio due to the constantly higher housing prices, reflected by the mortgage inventory in the portfolio. These data support the Bank's estimate that the potential for loss due to the Bank's mortgage portfolio, even in scenarios involving material decline in housing prices, is low. In addition, the Bank regularly reviews its mortgage portfolio under stress conditions, including under significant change in macro-economic conditions, using multiple methodologies. The outcome of stress testing indicates that portfolio risk has decreased and that the potential impact of a severe stress event in the market is low.

Market and interest risk in the bank portfolio

Activity in the negotiable portfolio (portfolios managed by the trading room) is low, with most of the Bank's financial activity and risk associated with the banking portfolio. The Bank's banking portfolio mostly includes long-term uses (mortgages), against which the Bank raises resources which may be short-term. The portfolio structure exposes the Bank EV to erosion in case of rising interest rates. Note that Union Bank's nostro portfolio reflects risk that is higher than the Bank's risk appetite. However, at the Bank level on consolidated basis, the impact of this portfolio is not material and the overall risk level remained Low-Medium.

The first quarter of 2021 saw a decline in short-term yield and increase in medium- and long-term yield on the NIS interest rate curve (zero coupon).

Risk values measured in the normal course of business and under stress scenarios were slightly higher compared to those at the end of the year, due to current banking operations in the mortgage segment, and range at levels lower than the specified risk appetite. In this quarter, inflationary expectations increased. The Bank continued to strictly manage its CPI-linked position, based on creating a daily linkage balance sheet and establishing a forecast position under various scenarios.

Liquidity risk

In the first quarter of 2021, the Bank maintained appropriate liquidity by investing excess liquidity in liquid assets of very high quality – Level 1 assets. The average liquidity coverage ratio (consolidated, including data for Union Bank) for the first quarter of 2021 was 133%¹. In this quarter, there were no exceptions from the risk appetite limits and concentration benchmarks.

Following the raised state of alert due to the Corona Virus outbreak, in the third and fourth quarters of 2020 and in the first quarter of 2021, the state of alert at the Bank was Elevated. During the current period, the Bank closely monitored (at daily level) qualitative and quantitative indicators (both internal and external) and conducts daily reviews of multiple stress scenarios for various time frames – liquidity was appropriate across all these scenarios and the Bank was in compliance with all internal limitations. Due to the significant decrease in morbidity in Israel and return to normal operations, with significant lifting of restrictions, the Bank resolved at the end of April 2021 to lower the state of alert and to return to business as usual.

Operational risk

Throughout the Corona Virus outbreak and in the first quarter of 2021, operational risk remained Medium. The Bank maintained a low level of losses with respect to operating failure events, and in actual fact, no material operating events occurred. The risk level reflects the potential damage that may be caused by materialization of operational risks. Activity continued to improve monitoring, management and control of operational risks, with emphasis on upgrading the IT system for collection of failure events and management of risk surveys and the risk map, further processes of identification, analysis, debriefing and lesson-learning, and enhance awareness of the various operational risks.

Business continuity

The Bank applies Proper Conduct of Banking Business Directive 355 concerning "Management of business continuity".

In the first quarter, the Bank continued to handle the Corona Virus crisis, including the following: Compliance with work guidelines and maintaining hygiene and social distancing, working in split units, continuation of working remotely by means of a fast, structured process and so forth. Following the significant decrease in morbidity in Israel and at the Bank, and further to directives from the Ministry of Health and revised regulations for addressing the Corona Virus, the Bank applied some relief to its operations. This was done while maintaining social distancing, hygiene and mask wearing in conformity with directives of the Ministry of Health.

In the first quarter, the Bank started implementation of the 2021 work plan and drill plan, including participation in the Agam 21 drill, led by the Bank of Israel Currency Unit. The objective of this drill was to test the Bank's capacity to transfer funds from the collection point to delivery to clients at the end point. The drill tested the cash supply under an earthquake scenario, with related implications, including the following: Use of manual operations at branches and at the cash center, transfer of

¹ As from data for the fourth quarter of 2020, the average liquidity coverage ratio includes data for Union Bank.

cash under such conditions, impact to staffing, co-operation with national emergency authorities and so forth. The Business Continuity Department, in co-operation with business units at the Bank, expended the original drill outline and reviewed implications of this scenario on all emergency plans. The drill was successfully concluded and reported to management and to the Bank of Israel. A cyber security drill was conducted, with Bank management serving as the crisis management team, the Cyber and Information Security Department, the Business Continuity Department and the "Red Team". The drill event included disruption of significant systems, as well as removal of sensitive information and a ransom demand in order to release the systems and avoid publication of the information. The drill covered multiple elements, including the following: Containing the event from the business aspect and ensuring business continuity at the Bank, providing a response from communication and information aspects, exercise of various dilemmas arising as part of negotiations and so forth.

For more information see chapter "Significant Events in the Bank Group's Business" on the Report of the Board of Directors and Management.

Information security and cyber security

In the first quarter of 2021, the risk level remained Medium. In this quarter, a small number of fraud attempts against clients were identified (through fishing attacks), which resulted in stealing their account credentials in order to conduct unauthorized transactions in their accounts. Thanks to defensive measures applied by the Bank, despite these fraud attempts, there were no unauthorized transactions in client accounts. The Bank continues to reinforce the defense mechanisms applied in Bank systems, in order to further limit the ability to defraud clients and to conduct un-authorized transactions in client accounts. These actions were taken as part of debriefing processes and lessons learned by the Bank with regard to this emerging threat.

During the Corona Virus crisis, the Bank's information security team operates fully and continuously, improving and bolstering defense capabilities and mechanisms, in conformity with expansion of threats and challenging needs which the Bank is required to face.

We should note that the Corona Virus pandemic has elevated cyber risk across the world, both due to increase in working remotely, which provided more attack vectors for organizations and due to increased fraud attempts in the shadow of the outbreak. Bank operations during this period retained the risk level at the Bank unchanged.

Information technology risk

In recent years, the risks associated with IT management have increased, due to development and deployment of new technologies and evolution of new risk and threats. Other than under routine conditions, the IT management framework addresses system failures, such as: system faults and preparation for emergency situations. This is also intended to ensure that the Bank maintain business continuity during an alert or emergency. This may mitigate reputation risks and business risks which could arise under such conditions.

Risk appetite is defined in quantitative and qualitative terms under normal and emergency scenarios, with the Bank's risk appetite in operational aspects for IT risk included under management of operational risk appetite. Risk appetite for technology aspects is defined by multiple benchmarks, including risk levels on the map of technology risk and specific risk appetite for diverse risk factors.

The Bank operates multiple measures to mitigate risk, including use of indicators (KRI) and support systems.

IT risk remained Medium, reflecting the potential damage due to materialization of technology risks that are material for proper operations at the Bank.

The Technology Division operated in providing full support for regular operations at the Bank and for technology needs required for Bank operations during emergency routine operations. There were no material events and/or malfunctions during this period.

Legal risk

In the first quarter of 2021, the level of legal risk remained low-medium.

Review of legal risk level in 2020 included, inter alia, a review of potential implications of the Corona Virus crisis on legal risk, which found that in general, there was no impact on the level of legal risk and the quality of management of said risk.

Compliance risk

Compliance risk remained unchanged in the first quarter of 2021, at Low-Medium. This risk assessment is due, inter alia, to addressing of risks classified as high and to further enhancement of controls and training delivery and improvement in efficiency of work processes in this area, while incorporating technology improvements. In the current quarter, the Bank took action to implement the applicable directives by the various regulators. The Bank also applied regular controls, in order to monitor compliance risk that may materialize during this period.

The Bank has internal enforcement programs for securities and for anti-trust law.

Cross-border risk

The risk level remained unchanged in the first quarter of 2021, at Low-Medium. The Bank manages this risk, inter alia, by revising procedures, automating work processes, delivering training, activity of foreign residents in specialized branches and specification of work routines in processes required for reporting under both FATCA and CRS.

AML and terror financing risk

AML risk remained unchanged in the first quarter of 2021 and is defined as low-medium. The risk assessment is based, inter alia, on continued risk-focused management, as reflected by revision of operating procedures and processes, including IT support and process streamlining, training and deployment activities along with risk-focused controls, improvement of documents and classifications, and taking effective action to prevent recurrence of unusual events and compliance failures. The new AML system – MEA – in order to identify unusual activity and for reporting to the AML Authority, is operating in branches on regular basis and enables close control over the banking activity. In the first quarter of this year, the Bank provided to the Bank of Israel its semi-annual report of compliance risk, in the new format pursuant to Reporting Regulation 825.

Reputation risk

The Bank monitors and reviews the impact of the Corona Virus pandemic, globally and in Israel, on business activity as a whole and on reputation risk in particular, with regard to negative perception of the Bank specifically, and as part of the overall perception of the banking system. The Bank also monitors and reviews the impact of the Union Bank merger on reputational risk. Bank management believes that at this stage, the reputational risk level has not changed materially. The Bank continues to regularly monitor this matter.

Business-strategic risk

Business-strategic risk is the risk, in real time or potentially in future, of impact to Bank profits, capital or reputation, due to erroneous business decisions, improper deployment of decisions or insufficient preparation for changes in the business environment. This means the risk that the Bank chose the wrong strategy or that the Bank would not be able to implement the business and strategic plan as planned. The materiality of business-strategic risk requires the Bank to take measures which would allow it to manage this risk and take steps for assessment and early identification of events which may preclude implementation of the strategy.

The Bank operates in conformity with a five-year strategic plan, approved by the Bank's Board of Directors in April 2021, whose principles have been made public. Material deviation from Bank strategy is subject to approval by the Bank's Board of Directors. Risk is monitored by the Financial Information and Reporting Division, and is challenged by the Risks Control Division. For more information about the strategic plan, see chapter "Business goals and strategy" on the Report of the Board of Directors and Management.

Conclusion of DPA and termination of deferred indictment in the USA

On March 22, 2021, the Court in Los Angeles, USA ordered termination of the deferred indictment filed against Bank Group companies, in conformity with the DPA signed on March 12, 2019 by the Bank and by the US Department of Justice (DoJ), to conclude the DoJ investigation with regard to Bank Group business with its US clients. This order was handed down upon request from the DoJ noting, inter alia, in a motion filed with the Honorable Court upon expiration of the (two year) agreement period set forth in the DPA, that the Bank Group companies were in compliance with their obligations pursuant to this agreement.

See Note 10 to the financial statements for additional information.

On December 27, 2020, the Bank of Israel issued an update to Proper Conduct of Banking Business Directive 329 concerning "Restrictions on extending housing loans". The update includes elimination of the restriction on lending at the prime lending rate, so that the restriction of at least one third of the mortgage that must bear fixed interest remains, and up to two thirds may be extended bearing variable interest. The amendments to the directive pursuant to the circular are effective as from January 17, 2021. For housing loans intended to finance early repayment of a loan extended by the Bank or by another bank, the amendment applies as from February 28, 2021. At this stage, it is not possible to assess the impact on client applications to re-finance loans. The Bank is preparing, including in operational aspects, to provide a response to customers.

In the first quarter of 2021, as part of the annual process for approval of all policy documents, Bank management and the Board of Directors approved multiple Bank policy documents with regard to risk management and control, including: Reputational risk management policy; Open banking policy; Online banking policy; Insurance policy; Market and interest risk management policy; Supplier and outsourcing risk management policy.

Key and emerging risks

Bank business exposes it to various financial and non-financial risks, which may impact the Bank's business results and reputation.

Top risks and evolving risks are derived from the Bank's business environment, which is impacted by the macro-economic environment, by risk associated with regulation and legislation, by changes to the business model and by social and consumer trends. In recent years, due to changes to the competitive environment, to the consumer environment, to the regulatory environment and to the technology environment, a trend of evolving non-financial risks is becoming apparent.

Top risks are risks arising from developments in the Bank's business environment, which may materialize over the coming 12 months which potentially may materially impact the Bank's financial results and stability. Furthermore, evolving risks are identified, which are risks that may materialize in the longer term and their nature and impact on the Bank are uncertain. Such risks include cyber and information security risk, IT risk and reputational risk.

As noted, the risks mapping is regularly reviewed to ensure that it encompasses all risk associated with business operations at the Bank, and risk arising from market conditions and regulatory requirements.

Material top risks and evolving risks are:

Strategic business risk – increased competition, changes to client behavior and to business models, that may result in material impact on the banking system over the medium to long range. Moreover, regulatory changes (such as: the Credit Data Act, Open Banking and transfer of bank accounts) may impact the Bank's business results. Furthermore, this risk is impacted by the Corona Virus event which may potentially impact the Bank's entire risk profile, due to uncertainty as to further development of this risk and material macro-economic implications arising from it.

Macro-economic risk – the Corona Virus event has significantly impacted both the local and global economies, with a slow-down in economic activity and changes to the macro-economic environment, including: higher unemployment, changes to interest rates, market volatility and changes to asset prices. Materialization of this risk may increase troubled debts and may negatively impact the Bank's business results.

Cyber and information security risk – increasing cyber threats towards financial institutions. The Bank applies protective measures in order to limit the ability to conduct un-authorized transactions in client accounts. These actions were taken as part of debriefing processes and lessons learned by the Bank with regard to this emerging threat. The Corona Virus event elevates cyber risk, both due to increase in working remotely, which provided more attack vectors for organizations and due to increased fraud attempts in the shadow of the outbreak.

Technology risk – technology evolution and the age of current systems at the Bank, as well as multiple requirements by banking regulators within short time frames, increase the potential damage that may arise from technology risk that are material for proper operations at the Bank. **Regulatory risk** – Increased regulation in Israel and world-wide increased uncertainty and competition in the business environment. This may require the Bank to prepare and IT costs that may result in risk to the Bank's results. The Bank regularly acts to address the regulatory directives applicable for its operations, while allocating the required resources for addressing these risks. Note that the Bank has zero appetite for non-compliance with applicable regulatory directives of the Bank of Israel. Bank operations with regard to these risks are primarily qualitative actions designed to create the required framework for addressing these emerging risks.

Environmental risk and climate risk – Environmental risk is the risk of loss due to the impact of costs resulting from environmental protection provisions and enforcement thereof, such as impairment of realized collateral or deterioration in the financial standing of a borrower due to environmental costs resulting from environmental protection provisions. Environmental risk includes climate change, impact to bio-diversity and pollution of air, water and soil. Therefore, environmental risk may have direct and indirect consequences:

- Direct consequences – may result from cost of environmental hazards incurred by the Bank, direct damage related to climate change or financial loss that may result from adoption of environmental and climate policy, technological developments and changes to market preferences.
- Indirect consequences – may result from deterioration in financial standing of borrowers due to environmental impact and climate change (as part of the Bank's credit risk), materialization of other risks related to environmental risk, such as reputational risk.

The Bank is preparing to expand its activity to monitor and manage environmental risk, including climate risk, in conformity with expectations of the Supervisor of Banks and emerging global practice in this area.

Overview of weighted risk assets (OV1)

	Risk weighted assets		Minimum capital requirements ⁽¹⁾
	As of March 31, 2021	As of December 31, 2020	As of March 31, 2021
Credit risk (standard approach) ⁽²⁾	181,495	178,782	22,077
Counter-party credit risk (standard approach)	2,020	1,810	246
Credit risk value adjustment (CVA) ⁽³⁾	511	487	62
Amounts lower than discount thresholds (subject to 250% risk weighting)	4,314	4,313	525
Total credit risk	188,340	185,392	22,910
Market risk (standard approach)	2,484	2,228	302
Operational Risk ⁽⁴⁾	13,112	12,864	1,595
Total	203,936	200,484	24,807

- (1) An additional capital requirement was added to this requirement, at 1% of the housing loan balance as of the report date. For more information about reduction of minimum capital ratios which banks are required to maintain in the normal course of business, by one percentage point, see Note 9 to the financial statements.
- (2) Credit risk excludes counter-party credit risk, credit risk value adjustment, settlement risk, securitization exposures and amounts lower than the deduction thresholds.
- (3) Credit Value Adjustments – mark to market with respect to credit risk of counter-party, in conformity with Basel III provisions.
- (4) Capital allocation with respect to operational risk was calculated using the standard approach.

The change in risk assets in the first quarter of 2021 was primarily due to growth in business credit and to growth in the housing loan portfolio.

Capital and leverage

Composition of capital

Supervisory capital is composed of two tiers: Tier I capital (including Tier I capital and Tier I additional capital) and Tier II capital.

Tier I capital includes equity attributable to equity holders of the Bank and the interest of external shareholders in equity of subsidiaries (excess capital at subsidiaries is not taken into account).

Tier I capital includes supervisory adjustments and deductions from capital – goodwill, investments in capital components of financial institutions, cumulative other comprehensive income with regard to cash flow hedges for items not presented at fair value on the balance sheet adjustments with respect to liabilities for derivative instruments, due to change in the Bank's credit risk (DVA) and other supervisory adjustments and deductions.

Additional Tier I capital consists of equity instruments which fulfill the requirements specified in the directives. As of March 31, 2021, the Bank had no equity instruments included in additional Tier I capital.

Tier II capital consists of a group provision for credit losses and equity instruments which fulfill the specified requirements.

Restrictions on capital structure:

- Tier II capital shall not exceed 100% of Tier I capital after required deductions from such capital.
- Capital instruments qualified for inclusion in Tier II capital shall not exceed 50% of Tier I capital after required deductions from such capital.

For more information about reduction of minimum capital ratios which banks are required to maintain in the normal course of business, by one percentage point, see Note 9 to the financial statements. For more information about issue of CoCo subordinated notes, see Note 17 to the financial statements.

Below is a summary of supervisory capital components, capital ratios to risk components for the Group and minimum supervisory capital ratios specified by the Supervisor of Banks:

	March 31, 2021	March 31, 2020	December 31, 2020
	NIS in millions		
Tier I capital before regulatory adjustments and deductions	19,940	16,847	19,352
Total regulatory adjustments to and deductions from Tier I capital	⁽¹⁾ (768)	129	⁽¹⁾ (785)
Tier I shareholders' equity	20,708	16,718	20,137
Tier II capital	6,665	5,803	7,176
Total capital	27,373	22,521	27,313
Total risk weighted assets	203,936	169,001	200,484
Ratio of Tier I capital to risk components	10.15%	9.89%	10.04%
Ratio of total capital to risk components	13.42%	13.33%	13.62%
Minimum Tier I capital ratio required by Supervisor of Banks	8.66%	8.82%	8.68%
Minimum overall capital ratio required by Supervisor of Banks	12.16%	12.32%	12.18%

(1) Includes deferred credit balance from acquisition of Union Bank. For more information see Note 25.F. To the 2020 financial statements.

For more information and detailed composition of supervisory capital, in conformity with disclosure requirements of Basel Pillar 3, as of March 31, 2021 compared to March 31, 2020 and December 31, 2020, see Addendum A below.

Leverage ratio

The Bank applies Proper Banking Conduct Directive 218 with regard to leverage ratio, which adopts the Basel Committee recommendations with regard to leverage ratio, stipulated in January 2014.

The leverage ratio is reflected in percent, defined as the ratio of Tier I capital to total exposure. Total exposure for the Bank is the sum of balance sheet exposures, exposures to derivatives and to securities financing transactions and off-balance sheet items.

According to the directive, banking corporations must maintain a leverage ratio of 5% or higher on a consolidated basis.

The Bank's leverage ratio as of March 31, 2021 is 5.16%, compared to 5.19% as of December 31, 2020.

On November 15, 2020, the Supervisor of Banks issued a circular regarding "Adjustments to Proper Conduct of Banking Business Directives for addressing the Corona Virus (Interim Directive)", updating Proper Conduct of Banking Business Directive 250, whereby the leverage ratio shall be at least 4.5% on consolidated basis, compared to 5% prior to this change. In conformity with a circular dated March 22, 2021, the Directive is effective from the issue date thereof through September 30, 2021. After expiration of the Directive, the relief shall remain in effect for a further 24 months, provided that the leverage ratio would be no less than the leverage ratio upon expiration of the Directive, or the minimum leverage ratio applicable to the banking corporation prior to the Interim Directive, whichever is lower.

Below is information about the Bank's leverage ratio (NIS in millions):

Comparison of assets on balance sheet and exposure measurement for leverage ratio	As of March 31, 2021	As of March 31, 2020	As of December 31, 2020
Total assets in consolidated financial statements	370,410	284,731	360,140
Adjustments with respect to financial derivative instruments	1,093	611	(425)
Adjustments with respect to off-balance sheet items ⁽¹⁾	28,042	22,959	26,875
Other adjustments	1,763	1,562	1,780
Exposure for leverage ratio	401,308	309,863	388,370

(1) Conversion of off-balance sheet exposures to equivalent credit amounts, in conformity with Basel rules for capital adequacy measurement.

Risks Report

As of March 31, 2021

Disclosure with regard to leverage ratio (NIS in millions)

	As of March 31, 2021	As of March 31, 2020	As of December 31, 2020
Composition of exposures and leverage ratio (NIS in millions)			
Balance sheet exposure			
Assets on balance sheet	367,036	281,021	355,505
Amounts with respect to assets deducted to determine Tier I capital	(300)	(87)	(314)
Total balance sheet exposure	366,736	280,934	355,191
Exposure with respect to derivatives			
Cost of replacement with respect to all derivative transactions	3,207	2,922	3,694
Amounts added with respect to future potential exposure with respect to all derivative transactions	2,110	1,918	1,819
Gross-up of collateral provided with respect to derivatives, deducted from assets on the balance sheet in conformity with Public Reporting directives	—	—	—
Deduction of debtor assets with respect to variable cash collateral provided in conjunction with derivative transactions	(1,028)	(188)	(1,866)
Exempt central counter-party leg of commercial exposure settled by the client	—	—	—
Effective adjusted nominal amount of credit derivatives written	267	285	257
Adjusted effective nominal offsets and deduction of additions with respect to credit derivatives written	—	—	—
Total exposure with respect to derivatives	4,556	4,937	3,904
Exposure with respect to securities financing transactions			
Gross assets with respect to securities financing transactions (without offsets), after adjustment for transactions accounted for as an accounting sale	1,974	1,033	2,400
Offset amounts of cash payable and cash receivable from gross assets with respect to securities financing transactions	—	—	—
Credit risk exposure for central counter-party with respect to securities financing assets	—	—	—
Exposure with respect to transactions as agent	—	—	—
Total exposure with respect to securities financing transactions	1,974	1,033	2,400
Other off-balance-sheet exposures			
Off-balance sheet exposure at gross nominal value	97,500	77,839	97,326
Adjustments with respect to conversion to credit equivalent amounts	(69,458)	(54,880)	(70,451)
Off-balance sheet items	28,042	22,959	26,875
Capital and total exposure			
Tier I capital	20,708	16,718	20,137
Total exposure	401,308	309,863	388,370
Leverage ratio			
Leverage ratio in conformity with Proper Conduct of Banking Business Directive 218	5.16%	5.40%	5.19%

Credit risk

This chapter discusses credit risk, in conformity with disclosure requirements of the Basel Committee and the FSB; the chapter structure and topic order (adjusted for the nature of Bank operations) are also in conformity with these requirements. The chapter "Counter party credit risk" below includes qualitative and quantitative disclosures about the capital requirement with respect to this risk and adjustment to capital requirements with respect to credit risk (CVA).

Credit risk is the risk that a borrower or counter-party of the Bank would not fulfill its obligations towards the Bank. Credit risk is a material risk to Bank operations. This risk is affected by multiple factors: Business risk due to client activities, concentration risk due to over-exposure to a borrower / borrower group and to economic sectors, geographic concentration risk, risk due to exogenous changes which mostly involve changes to the borrower's macro-economic environment, environmental risks, overseas credit risks and operational risks which, should they materialize, would have implications for credit risks. This risk is also correlated with other risks, such as: Market and interest risk, liquidity risk, compliance risk and other risks.

Credit is at the core of banking operations and therefore, credit risk is the major risk addressed by the banking system. Accordingly, the lion's share of capital allocated in Tier I is with respect to credit risk.

For more information about credit risk, see chapter "Credit risk" in the 2020 Risks Report, available on the Bank website.

Credit quality of credit exposures (CR1)

March 31, 2021				
	Gross balances ⁽¹⁾		Provisions for credit losses	Net balance
	Impaired or in arrears 90 days or longer	Others		
Debt other than debentures	3,070	336,443	2,421	337,092
Debentures	–	17,547	–	17,547
Off-balance sheet exposure ⁽²⁾	106	97,702	229	97,579
Total	3,176	451,692	2,650	452,218

March 31, 2020				
	Gross balances ⁽¹⁾		Provisions for credit losses	Net balance
	Impaired or in arrears 90 days or longer	Others		
Debt other than debentures	2,995	262,786	1,936	263,845
Debentures	–	7,783	–	7,783
Off-balance sheet exposure ⁽²⁾	40	77,820	132	77,728
Total	3,035	348,389	2,068	349,356

December 31, 2020				
	Gross balances ⁽¹⁾		Provisions for credit losses	Net balance
	Impaired or in arrears 90 days or longer	Others		
Debt other than debentures	2,928	327,550	2,435	328,043
Debentures	–	15,453	–	15,453
Off-balance sheet exposure ⁽²⁾	108	97,264	232	97,140
Total	3,036	440,267	2,667	440,636

(1) Gross balances in conformity with reported carrying amounts on the financial statements for on- and off-balance sheet items, creating exposure to credit risk pursuant to Proper Conduct of Banking Business Directive 203.

(2) Off-balance sheet exposures are before credit conversion factors (CCF).

Risks Report

As of March 31, 2021

Below are details of the provision for credit losses with respect to housing loans for which a minimum provision for credit losses was made by extent of arrears, in accordance with appendix to Proper Conduct of Banking Business Directive 314, as of March 31, 2021 (NIS in millions):

	Extent of arrears						Balance with respect to refinanced loans in arrears ⁽²⁾	Total
	In arrears 90 days or longer							
	In arrears 30 to 89 days ⁽¹⁾	90 days to 6 months	6-15 months	15-33 months	Over 33 months	Total over 90 days		
Amount in arrears	8	27	17	22	200	266	34	308
Of which: Balance of provision for interest ⁽³⁾	—	—	—	1	110	111	7	118
Recorded debt balance	490	857	180	121	141	1,299	68	1,857
Balance of provision for credit losses ⁽⁴⁾	—	—	25	60	102	187	34	221
Debt balance, net	490	857	155	61	39	1,112	34	1,636

(1) In conformity with Public Reporting Directives, excludes the balance of housing loans in arrears up to 2 months.

(2) Loans for which an agreement was signed for repayment of arrears by borrower, where a change was made in the repayment schedule for the loan balance not yet due.

(3) With respect to interest on amounts in arrears.

(4) Excludes balance of provision for interest.

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As of March 31, 2021

Credit risk mitigation methods (CR3)

As of March 31, 2021									
	Unsecured				Secured				
	Total on-balance sheet balance ⁽¹⁾	Total on-balance sheet balance ⁽¹⁾	Of which: Secured amount ⁽²⁾	Balance sheet balance	Of which: By collateral		Of which: By financial guarantees		Of which: By credit derivatives
					Of which: Secured amount	Balance sheet balance	Of which: Secured amount	Balance sheet balance	Of which: Secured amount
Debt other than debentures	300,507	36,585	10,203	27,629	8,180	8,956	2,023	–	–
Debentures	17,547	–	–	–	–	–	–	–	–
Total	318,054	36,585	10,203	27,629	8,180	8,956	2,023	–	–
Of which: Accruing interest revenues, in arrears 90 days or longer	2,335	389	60	190	39	199	21	–	–
As of March 31, 2020									
	Unsecured				Secured				
	Total on-balance sheet balance ⁽¹⁾	Total on-balance sheet balance ⁽¹⁾	Of which: Secured amount ⁽²⁾	Balance sheet balance	Of which: By collateral		Of which: By financial guarantees		Of which: By credit derivatives
					Of which: Secured amount	Balance sheet balance	Of which: Secured amount	Balance sheet balance	Of which: Secured amount
Debt other than debentures	239,451	24,394	6,708	17,688	5,723	6,706	984	–	–
Debentures	7,783	–	–	–	–	–	–	–	–
Total	247,234	24,394	6,708	17,688	5,723	6,706	984	–	–
Of which: Accruing interest revenues, in arrears 90 days or longer	2,193	518	154	334	66	228	88	–	–
As of December 31, 2020									
	Unsecured				Secured				
	Total on-balance sheet balance ⁽¹⁾	Total on-balance sheet balance ⁽¹⁾	Of which: Secured amount ⁽²⁾	Balance sheet balance	Of which: By collateral		Of which: By financial guarantees		Of which: By credit derivatives
					Of which: Secured amount	Balance sheet balance	Of which: Secured amount	Balance sheet balance	Of which: Secured amount
Debt other than debentures	293,598	34,445	9,945	26,126	8,198	8,319	1,747	–	–
Debentures	15,453	–	–	–	–	–	–	–	–
Total	309,051	34,445	9,945	26,126	8,198	8,319	1,747	–	–
Of which: Accruing interest revenues, in arrears 90 days or longer	2,136	464	94	226	74	238	20	–	–

(1) Balance sheet balance in conformity with reported carrying amounts on the financial statements, after provisions for credit losses.

(2) Balance sheet balance of part of the debt amount secured by collateral, guarantee or credit derivative, after accounting for safety factors.

Credit risk – standard approach

Standard approach – exposures by asset type and risk weighting⁽¹⁾⁽²⁾ (CR5)

										As of March 31, 2021
Asset type / risk weighting	0%	20%	35%	50%	60%	75%	100%	150%	Other	Total credit exposures (after conversion factors and collateral deduction)
Sovereigns, central banks and national monetary authority	104,274	87	–	–	–	–	135	–	–	104,496
Public sector entities (PSE) other than central Government	239	1,850	–	9	–	–	1	–	–	2,099
Banks (including Multi-party Development Banks)	–	4,018	–	658	–	–	206	–	–	4,882
Securities companies	–	–	–	–	–	–	–	–	–	–
Corporations	–	6,495	–	451	–	–	52,193	–	–	59,139
Retail exposure to individuals	–	–	–	–	–	24,304	2	–	–	24,306
Loans to small businesses	–	–	–	–	–	13,383	3	–	–	13,386
Secured by residential property	–	–	55,446	38,823	27,019	36,776	1,218	–	–	159,282
Secured by commercial real estate	–	–	–	–	–	–	6,674	–	–	6,674
Loans in arrears	–	–	–	–	–	–	1,477	1,124	–	2,601
Other assets	2,477	–	–	–	–	–	3,808	77	4	6,366
Of which: with respect to shares	–	–	–	–	–	–	492	36	–	528
Total	106,990	12,450	55,446	39,941	27,019	74,463	65,717	1,201	4	383,231

										As of March 31, 2020
Sovereigns, central banks and national monetary authority	60,855	31	–	–	–	–	91	–	–	60,977
Public sector entities (PSE) other than central Government	297	1,041	–	25	–	–	–	–	–	1,363
Banks (including Multi-party Development Banks)	–	1,992	–	279	–	–	119	–	–	2,390
Securities companies	–	–	–	–	–	–	–	–	–	–
Corporations	–	6,055	–	503	–	–	42,923	–	–	49,481
Retail exposure to individuals	–	–	–	–	–	19,979	–	–	–	19,979
Loans to small businesses	–	–	–	–	–	10,894	6	–	–	10,900
Secured by residential property	–	–	50,905	33,186	16,108	35,974	1,215	–	–	137,388
Secured by commercial real estate	–	–	–	–	–	–	4,132	–	–	4,132
Loans in arrears	–	–	–	–	–	–	1,178	1,404	–	2,582
Other assets	1,769	–	–	–	–	–	2,693	59	5	4,526
Of which: with respect to shares	–	–	–	–	–	–	88	49	–	137
Total	62,921	9,119	50,905	33,993	16,108	66,847	52,357	1,463	5	293,718

										As of December 31, 2020
Sovereigns, central banks and national monetary authority	97,005	87	–	–	–	–	118	–	–	97,210
Public sector entities (PSE) other than central Government	252	1,627	–	25	–	–	1	–	–	1,905
Banks (including Multi-party Development Banks)	–	3,801	–	666	–	–	164	–	–	4,631
Securities companies	–	–	–	–	–	–	–	–	–	–
Corporations	–	6,212	–	466	–	–	51,870	–	–	58,548
Retail exposure to individuals	–	–	–	–	–	24,246	1	–	–	24,247
Loans to small businesses	–	–	–	–	–	13,329	4	–	–	13,333
Secured by residential property	–	–	55,220	38,010	23,996	37,561	1,205	–	–	155,992
Secured by commercial real estate	–	–	–	–	–	–	6,639	–	–	6,639
Loans in arrears	–	–	–	–	–	–	1,254	1,208	–	2,462
Other assets	2,414	–	–	–	–	–	3,467	119	5	6,005
Of which: with respect to shares	–	–	–	–	–	–	399	96	–	495
Total	99,671	11,727	55,220	39,167	23,996	75,136	64,723	1,327	5	370,972

(1) Balances in this disclosure include on- and off-balance sheet debt balances that reflect credit risk, excluding deferred tax amounts and investments in financial institutions below the discount thresholds (subject to 250% risk weighting), exposures with respect to counter-party credit risk and securitization exposures.

(2) The balances reflect the supervisory exposure amounts, net of provisions and write-offs, after credit conversion factors and after credit risk mitigators.

Counter-party credit risk

Analysis of exposure to counter-party credit risk (CCR) based on the supervisory approach (CCR1)

	As of March 31, 2021			
	Subrogation cost	Future potential exposure	Exposure after deduction of collateral	Risk assets
Current exposure method	2,079	1,806	2,670	1,760
Comprehensive approach to credit risk mitigation (for securities financing transactions)	–	–	195	195
Total	2,079	1,806	2,865	1,955

	As of March 31, 2020			
	Subrogation cost	Future potential exposure	Exposure after deduction of collateral	Risk assets
Current exposure method	2,584	1,902	3,094	1,826
Comprehensive approach to credit risk mitigation (for securities financing transactions)	–	–	126	126
Total	2,584	1,902	3,220	1,952

	As of December 31, 2020			
	Subrogation cost	Future potential exposure	Exposure after deduction of collateral	Risk assets
Current exposure method	1,782	1,494	2,408	1,380
Comprehensive approach to credit risk mitigation (for securities financing transactions)	–	–	365	365
Total	1,782	1,494	2,773	1,745

Capital allocation with respect to credit risk valuation adjustment (CVA) (CCR2)

	As of March 31, 2021		As of March 31, 2020		As of December 31, 2020	
	Exposure after deduction of collateral	Risk assets	Exposure after deduction of collateral	Risk assets	Exposure after deduction of collateral	Risk assets
Total – portfolios for which CVA is calculated using the standard approach	2,257	511	2,863	673	1,905	487

Market risk

Market risk – This is the risk of loss from on- and off-balance sheet positions, arising from change in fair value of financial instruments, due to change in market risk factors (interest rates, exchange rates, inflation, prices of equities and commodities). The Bank has no exposure to commodities and its exposure to equities is not material, so that Bank exposure to such risk is primarily due to basis risk – the risk exists when the Bank's assets and liabilities are denominated in different currencies or are in different linkage segments – and from interest rate risk, which the risk to Bank profit and to Bank capital, primarily due to fluctuations in interest rates, fluctuations of various curves used by the Bank in its business operations or from the fact that a change in interest rates may result in a change in composition of the Bank's assets and liabilities due to exercise of options for early repayment due to change in market interest rates. Changes in interest rates impact Bank profits (change in revenues) and the value of Bank assets (change in fair value).

For more information about market risk, see chapter "Market risk" in the 2020 Risks Report, available on the Bank website.

Market risk using the standard approach

Below are the capital requirement components under the standard approach for market risk (NIS in millions):

	Risk assets as of:		
	March 31, 2021	March 31, 2020	December 31, 2020
Direct products			
Interest rate risk (general and specific)	1,888	1,393	1,519
Stock position risk (general and specific)	34	–	40
Exchange rate risk	498	369	626
Commodities risk	–	–	–
Options	–	–	–
Delta Plus approach	64	81	43
Securitization	–	–	–
Total	2,484	1,843	2,228

As noted above, exposure in the negotiable portfolio is low and mostly associated with interest risk. Risk assets with respect to interest risk were impacted by positions in derivatives which were not offset according to the standard measurement approach.

Liquidity risk

Liquidity risk – risk resulting 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 a material and unique, due to the need to respond to it in the shortest possible time. Risk materialization may cause the Bank to incur significant loss and may even result in collapse of the Bank.

For more information about liquidity risk, see chapter "Liquidity risk" in the 2020 Risks Report, available on the Bank website.

Liquidity coverage ratio (LIQ1)

Below is information about liquidity coverage ratio⁽¹⁾ (NIS in millions):

	For the three months ended March 31, 2021	
	Total unweighted value ⁽²⁾ (Average)	Total weighted value ⁽³⁾ (Average)
Total high-quality liquid assets		84,754
Outgoing cash flows		
Retail deposits from individuals and from small businesses, of which:	150,048	9,699
Stable deposits	42,377	2,119
Less stable deposits	56,161	6,035
Deposits for terms longer than 30 days	51,510	1,545
Unsecured wholesale financing, of which:	88,372	55,504
Deposits for operational needs (all counter-parties) and deposits with networks of co-operative banking corporations	3,471	868
Deposits other than for operational needs (all counter-parties)	84,715	54,450
Unsecured debts	186	186
Secured wholesale financing	–	1,003
Additional liquidity requirements, of which:	110,780	24,404
Outflows with respect to derivatives exposure and other collateral requirements	16,983	16,983
Credit lines and liquidity	55,602	4,450
Other contractual financing obligations	476	476
Other contingent financing obligations	37,719	2,495
Total outgoing cash flows	35,105	26,881
Incoming cash flows		
Secured loans	2,135	1,080
Inflows from regularly repaid exposures	12,565	9,774
Other incoming cash flows	20,405	16,027
Total incoming cash flows	35,105	26,881
		Total adjusted value⁽⁴⁾
Total high-quality liquid assets		84,754
Total outgoing cash flows, net		63,729
Liquidity coverage ratio (%)		133

(1) Information is presented in terms of simple averages of daily observations during the reported quarter. The number of observations used in calculating the averages in the first quarter of 2021 is 74.

(2) Unweighted values are to be accounted for as outstanding balances payable or which may be payable by the holder, within 30 days (for both inflows and outflows).

(3) Weighted values are to be accounted for after applying appropriate security factors or inflow / outflow rates (for inflows and outflows).

(4) Adjusted value are to be calculated after applying: Safety factors and inflow / outflow rates; and all applicable restrictions (i.e. restriction on High-Quality Liquid Assets and restriction on inflows, as specified in Proper Conduct of Banking Business Directive 221).

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Below is information about liquidity coverage ratio⁽¹⁾ (NIS in millions):

	For the three months ended March 31, 2020	
	Total unweighted value ⁽²⁾ (Average)	Total weighted value ⁽³⁾ (Average)
Total high-quality liquid assets		49,568
Outgoing cash flows		
Retail deposits from individuals and from small businesses, of which:	111,504	6,520
Stable deposits	30,868	1,543
Less stable deposits	32,989	3,548
Deposits for terms longer than 30 days	47,647	1,429
Unsecured wholesale financing, of which:	57,649	38,088
Deposits for operational needs (all counter-parties) and deposits with networks of co-operative banking corporations	1,524	381
Deposits other than for operational needs (all counter-parties)	54,989	36,571
Unsecured debts	1,136	1,136
Secured wholesale financing	–	239
Additional liquidity requirements, of which:	85,230	19,335
Outflows with respect to derivatives exposure and other collateral requirements	14,126	14,125
Credit lines and liquidity	41,765	2,827
Other contingent financing obligations	29,339	2,383
Total outgoing cash flows		64,182
Incoming cash flows		
Secured loans	1,128	296
Inflows from regularly repaid exposures	9,530	6,931
Other incoming cash flows	19,671	14,655
Total incoming cash flows	30,329	21,882
		Total adjusted value⁽⁴⁾
Total high-quality liquid assets		49,568
Total outgoing cash flows, net		42,300
Liquidity coverage ratio (%)		117

- (1) Information is presented in terms of simple averages of daily observations during the reported quarter. The number of observations used in calculating the averages in the first quarter of 2020 is 76.
- (2) Unweighted values are to be accounted for as outstanding balances payable or which may be payable by the holder, within 30 days (for both inflows and outflows).
- (3) Weighted values are to be accounted for after applying appropriate security factors or inflow / outflow rates (for inflows and outflows).
- (4) Adjusted value are to be calculated after applying: Safety factors and inflow / outflow rates; and all applicable restrictions (i.e. restriction on High-Quality Liquid Assets and restriction on inflows, as specified in Proper Conduct of Banking Business Directive 221).

Below is information about liquidity coverage ratio⁽¹⁾ (NIS in millions):

	For the three months ended December 31, 2020	
	Total unweighted value ⁽²⁾ (Average)	Total weighted value ⁽³⁾ (Average)
Total high-quality liquid assets		78,145
Outgoing cash flows		
Retail deposits from individuals and from small businesses, of which:	148,396	9,526
Stable deposits	41,410	2,071
Less stable deposits	54,642	5,885
Deposits for terms longer than 30 days	52,344	1,570
Unsecured wholesale financing, of which:	83,017	50,718
Deposits for operational needs (all counter-parties) and deposits with networks of co-operative banking corporations	2,867	717
Deposits other than for operational needs (all counter-parties)	80,048	49,899
Unsecured debts	102	102
Secured wholesale financing	–	994
Additional liquidity requirements, of which:	106,705	22,600
Outflows with respect to derivatives exposure and other collateral requirements	15,210	15,210
Credit lines and liquidity	53,022	4,268
Other contractual financing obligations	382	382
Other contingent financing obligations	38,091	2,740
Total outgoing cash flows		83,838
Incoming cash flows		
Secured loans	2,081	1,036
Inflows from regularly repaid exposures	12,659	9,895
Other incoming cash flows	18,870	14,138
Total incoming cash flows	33,610	25,069
	Total adjusted value⁽⁴⁾	
Total high-quality liquid assets		78,145
Total outgoing cash flows, net		58,769
Liquidity coverage ratio (%)		133

- (1) Information is presented in terms of simple averages of daily observations during the reported quarter. The number of observations used in calculating the averages in the fourth quarter of 2020 is 79.
- (2) Unweighted values are accounted for as outstanding balances payable or which may be payable by the holder, within 30 days (for both inflows and outflows).
- (3) Weighted values are accounted for after applying appropriate security factors or inflow / outflow rates (for inflows and outflows).
- (4) Adjusted value are calculated after applying: Safety factors and inflow / outflow rates; and all applicable restrictions (i.e. restriction on High-Quality Liquid Assets and restriction on inflows, as specified in Proper Conduct of Banking Business Directive 221).

Key factors that impact the results of liquidity coverage ratio

The major factors affecting the liquidity coverage ratio results are composition of Bank sources and uses. High-Quality Liquid Assets ("HQLA") are Level 1 assets, which are typically highly negotiable and associated with low risk. These include cash, current accounts and deposits with central banks, debentures of sovereigns with a 0% risk weighting and debentures of the State of Israel. Cash outflows primarily consist of unsecured wholesale financing – deposits which corporations and financial institutions deposited with the Bank, as well as outflows with respect to exposure to derivatives. Cash inflows primarily consist of credit receipts and inflows with respect to exposure to derivatives.

The ratio is primarily cyclical and may be forecast based on internal estimates by the Bank. The key factor which affects evolution of this ratio over time is growth in Bank business, both in raising and management of source composition and increase in uses. There is some volatility between days of the month, due to current activity of clients and interchangeability between NIS and foreign currency, primarily due to activity in NIS / foreign currency derivatives.

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Composition of high quality liquid assets (HQLA)

Below are details of liquid assets by level, as required by Directive 221 (NIS in millions):

	March 31		Average for the first quarter	
	2021	2020	2021	2020
Level 1 assets	90,692	51,310	84,653	49,556
Level 2a assets	107	12	101	12
Level 2b assets	–	–	–	–
Total HQLA	90,799	51,322	84,754	49,568

There is a regulatory limit applicable to the Los Angeles branch, with regard to use of liquidity reserve by this entity; Bank scenarios assume use of branch liquidity in conformity with this limit.

Composition of pledged and un-pledged available assets:

	As of March 31, 2021		
	Total balance on balance sheet	Of which: Pledged	Of which: Un-pledged
Cash and deposits with central banks	89,320	1,331	87,989
Debentures of the Government of Israel	14,172	861	13,311
Debentures of others in Israel	1,322	–	1,322
Debentures of foreign governments	2,941	358	2,583
Debentures of foreign others	549	20	529
Loans to the public, net	249,541	2,273	247,268
Total	357,845	4,843	353,002

	As of March 31, 2020		
	Total balance on balance sheet	Of which: Pledged	Of which: Un-pledged
Cash and deposits with central banks	54,731	82	54,649
Debentures of the Government of Israel	7,618	496	7,122
Debentures of others in Israel	164	–	164
Debentures of foreign governments	678	217	461
Debentures of foreign others	112	–	112
Loans to the public, net	210,230	–	210,230
Total	273,533	795	272,738

	As of December 31, 2020		
	Total balance on balance sheet	Of which: Pledged	Of which: Un-pledged
Cash and deposits with central banks	84,450	339	84,111
Debentures of the Government of Israel	14,455	803	13,652
Debentures of others in Israel	1,390	–	1,390
Debentures of foreign governments	451	345	106
Debentures of foreign others	548	20	528
Loans to the public, net	245,525	2,057	243,468
Total	346,819	3,564	343,255

Developments in liquidity coverage ratio

In the first quarter of 2021, the Bank maintained appropriate liquidity by investing excess liquidity in liquid assets of very high quality – Level 1 assets. The average liquidity coverage ratio (consolidated, including data for Union Bank) for the first quarter of 2021 was 133%. In this quarter, there were no recorded deviations from ratio restrictions.

Additions

Addendum A – Composition of supervisory capital

		As of March 31, 2021	As of March 31, 2020	As of December 31, 2020
		NIS in millions		
Tier I shareholders' equity: Instruments and retained earnings				
1	Ordinary share capital issued by the banking corporation and ordinary share premium for shares included in Tier I capital	3,534	2,302	3,532
2	Retained earnings, including dividends proposed or declared after the balance sheet date	16,224	14,295	15,548
3	Accumulated other comprehensive income and retained earnings for which disclosure has been given	(248)	(167)	(160)
5	Ordinary shares issued by consolidated subsidiaries of the banking corporation, which are held by a third party (non-controlling interests)	430	417	432
6	Tier I capital before regulatory adjustments and deductions	19,940	16,847	19,352
Tier I shareholders' equity: Regulatory adjustments and deductions				
8	Goodwill, net of related deferred tax liability, if applicable	87	87	87
9	Other intangible assets, other than mortgage-servicing rights, net of related deferred tax liability	95	–	100
10	Deferred tax assets that rely on future profitability of the banking corporation for realization, excluding those arising from temporary differences	118	–	127
11	Accumulated other comprehensive income with respect to cash flows hedging of items not listed at fair value on the balance sheet	(9)	29	11
14	Unrealized gains / losses from changes to fair value of liabilities arising from change to own credit risk of the banking corporation. In addition, with regard to liabilities with respect to derivative instruments, all debt value adjustments (DVA) arising from own credit risk of the banking corporation is to be deducted	2	13	10
16	Investment in own ordinary shares, held directly or indirectly (including commitment to purchase shares subject to contractual obligations)	–	–	–
21	Deferred tax assets arising from temporary differences, whose amount exceeds 10% of Tier I capital	–	–	–
25	Of which: Deferred tax assets arising from temporary differences	–	–	–
26	Regulatory adjustments and other deductions stipulated by the Supervisor of Banks	(1,061)	–	(1,120)
26.C	Of which: Additional regulatory adjustments to Tier I capital, not included in sections 25.A. and 25.B.	–	–	–
28	Total regulatory adjustments to and deductions from Tier I capital	(768)	129	(785)
29	Tier I shareholders' equity	20,708	16,718	20,137
44	Additional Tier I capital	–	–	–
45	Tier I capital	20,708	16,718	20,137
Tier II capital: Instruments and provisions				
46	Instruments issued by the banking corporation (not included in Tier I capital) and premium on such instruments	222	339	258
47	Tier II capital instruments issued by the banking corporation, eligible for inclusion in regulatory capital during transitional period	447	893	894
48	Tier II capital instruments issued by subsidiaries of the banking corporation to third party investors	3,713	2,800	3,709
49	Of which: Tier II capital instruments issued by subsidiaries of the banking corporation, held by third party investors, subject to phase-out from Tier II capital	–	–	–
50	Group provisions for credit losses by effect of related tax	2,283	1,771	2,315
51	Tier II capital, before deductions	6,665	5,803	7,176
Tier II capital: Deductions				
57	Total deductions from Tier II capital	–	–	–

Risks Report

As of March 31, 2021

		As of March 31,	As of December 31,	
		2021	2020	2020
		NIS in millions		
58	Tier II capital	6,665	5,803	7,176
59	Total equity	27,373	22,521	27,313
60	Total risk weighted assets	203,936	169,001	200,484
Capital ratios and capital conservation buffer				
61	Tier I shareholders' equity	10.15%	9.89%	10.04%
62	Tier I capital	10.15%	9.89%	10.04%
63	Total capital	13.42%	13.33%	13.62%
Minimum requirements stipulated by the Supervisor of Banks				
69	Minimum Tier I shareholders' equity ratio required by Supervisor of Banks	8.66%	8.82%	8.68%
71	Minimum overall capital ratio required by Supervisor of Banks	12.16%	12.32%	12.18%
Amounts below deduction threshold (before risk weighting)				
72	Investments in capital of financial corporations (other than banking corporations and their subsidiaries), that do not exceed 10% of ordinary share capital issued by the financial corporation and that are below the deduction threshold	79	–	80
73	Investments in Tier I capital of financial corporations (other than banking corporations and their subsidiaries), that do exceed 10% of ordinary share capital issued by the financial corporation and that are below the deduction threshold	3	2	3
75	Deferred tax assets arising from temporary differences, that are below the deduction threshold	1,723	1,148	1,722
Cap for inclusion of provisions in Tier II				
76	Provision eligible for inclusion in Tier II with respect to exposures subject to standardized approach, prior to application of cap	2,283	1,771	2,315
77	Cap on inclusion of provisions in Tier II under standardized approach	2,354	1,950	2,317
Equity instruments not eligible as regulatory capital subject to transitional provisions				
84	Current cap for instruments included in Tier II capital that are subject to transitional provisions	1,195	893	1,195
85	Amount deducted from Tier II capital due to cap	2,275	1,792	1,819

(1) Includes deferred credit balance from acquisition of Union Bank. For more information see Note 25.F. to the 2020 financial statements.

Glossary and index of terms included in the Risks Report

Below is a summary of terms included on the Risks Report:

Terms with regard to risks management at the Bank and to capital adequacy

ABC	<p>ICAAP – Internal Capital Adequacy Assessment Process by the Bank. This process includes, inter alia, setting capital targets, capital planning processes and review of capital status under various stress scenarios. This process is part of Pillar 2 of the Basel II directive.</p> <p>HQLA – High-Quality Liquid Assets which may be easily and quickly converted into cash at a small loss (or no loss) under a stress scenario.</p> <p>PD (Probability Of Default) – Probability in percent of a borrower going into default within a specified time.</p> <p>LGD (Loss Given Default) – Loss as percentage of credit should the client go into default.</p>
B	Basel – Basel II / Basel III – Framework for assessment of capital adequacy and risk management, issued by the Basel Committee on Bank Supervision.
E	<p>Standard approach – An approach used to calculate the required capital with respect to credit risk, market risk or operational risk. Calculation of capital allocation is based on a formula, which is based on supervisory assessment components which have been specified by the Supervisor of Banks.</p> <p>Supervisory capital (total capital) – Supervisory capital consists of two tiers: Tier I capital, which includes Tier I capital, additional Tier I capital and Tier II capital. As defined in Proper Conduct of Banking Business Directive 202 "Measurement and capital adequacy – supervisory capital".</p>
J	Minimum capital ratio – This ratio reflects the minimum supervisory capital requirements which the Bank is required to maintain in conformity with Proper Conduct of Banking Business Directive 201.
M	<p>Stress tests – A title for various methods used to assess the financial standing of a banking corporation under a n extreme scenario.</p> <p>Risks document – A document which concisely presents the Bank's risk profile, in order to allow the Board of Directors to monitor action taken by management and to ensure that such action is in line with the risk appetite and with the risks management framework approved by the Board of Directors. The Risks Document is compiled and presented to the Board of Directors quarterly.</p>
N	<p>Pillar 2 – The second pillar of the Basel II project, refers to the Supervisory Review Process. This part consists of the following basic principles: The Bank shall conduct the ICAAP process, as defined above. The Supervisor shall conduct a process to assess the ICAAP process conducted by the Bank, to review the Bank's capacity to monitor and achieve supervisory capital ratios. The Bank is expected to operate above the specified minimum capital ratios.</p> <p>Pillar 3 – The third pillar of the Basel II project, designed to promote market discipline by developing a set of disclosure requirements, which would allow market participants to assess the capital, risk exposure and risk assessment processes – and use these to assess the Bank's capital adequacy.</p> <p>Risk assets – These consist of credit risk, operational risk and market risk, calculated using the standard approach as stated in Proper Conduct of Banking Business Directives 201-211.</p>
O	<p>CVA - Credit Valuation Adjustment – CVA is the component of the fair value of a derivative, which accounts for the credit risk of the counter-party to the transaction. CVA risk is the risk of loss due to mark-to-market with respect to expected counter-party risk for OTC derivatives. This means – loss due to impairment of fair value of derivatives, due to an increase in counter-party credit risk (such as: lower rating).</p> <p>Counter-party credit risk – The risk that the other party to a transaction would be in default before final settlement of cash flows in the transaction.</p>

Terms with regard to banking and finance

A	Debentures – Securities which are obligations by the issuer to pay to the debenture holder the principal issued plus interest, on specified dates or upon realization of a specified condition.
H	<p>Indebtedness – On- and off-balance sheet credit, as defined in Proper Conduct of Banking Business Directive 313.</p> <p>Impaired debt – Debt is classified as impaired when its principal or interest is in arrears over 90 days, unless the debt is well secured and is in collection proceedings. Further, any debt whose terms and conditions have been changed in conjunction with restructuring of problematic debt would be classified as impaired debt, unless prior to and following such restructuring, a provision for credit losses by extent of arrears was made with respect to the debt pursuant to the appendix to Proper Conduct of Banking Business Directive 314 on problematic debt in housing loans.</p>
J	<p>Recorded debt balance – The debt balance, including recognized accrued interest, premium or discount yet to be amortized, net deferred commissions or net deferred costs charged to the debt balance and yet to be amortized, net of the debt amount subject to accounting write-off.</p> <p>Financial instrument – A contract that creates a financial asset for one entity and a financial liability or capital instrument for another entity.</p>
N	Derivative – A financial instrument or contract whose value changes in response to changes in the price of the underlying asset (a financial instrument, physical asset, index, credit rating or other underlying asset), requires a small or minimal initial investment, compared to other contract types, and is expected to be settled on a future date.

Terms with regard to regulatory directives

ABC	LCR – Liquidity Coverage Ratio – Defined as the ratio of High Quality Liquid Assets and net cash outflow for the next 30 days, under a stress scenario. This ratio is a benchmark for the Bank's capacity to fulfill its liquidity needs for the coming month.
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