

Mizrahi Tefahot Bank Ltd.'s Immediate Reports are published in Hebrew on the Israel Securities Authority and the Tel Aviv Stock Exchange websites.

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MIZRAHI TEFAHOT BANK LTD

No. with the Registrar of Companies: 520000522

To	<u>Israel Securities Authority</u>	To	<u>Tel Aviv Stock Exchange Ltd</u>	T125 (Public)	Date of transmission: August 1 2023
	www.isa.gov.il		www.tase.co.il		Ref: 2023-01-088308

Immediate Report on the Rating of Bonds/Rating of a Corporation or Rating Cessation

On August 1 2023, *Midroog* published:

A rating report/notice *updated*

A notice regarding rating cessation

1. Rating report or notice

Corporation's rating: *Midroog Aaa.il*
stable

Comments/Notice summary: *Rating*
affirmation

Ratings history in the three years prior to the date of the rating/notice:

Date	Rating subject	Rating	Comments/Notice summary
August 28 2022	<i>Mizrahi Tefahot Bank Ltd</i>	<i>Midroog Aaa.il</i> <i>stable</i>	<i>Other</i> <i>Affirmation</i>

August 22 2021	<i>Mizrahi Tefahot Bank Ltd</i>	<i>Midroog Aaa.il stable</i>	<i>Other Affirmation</i>
September 10 2020	<i>Mizrahi Tefahot Bank Ltd</i>	<i>Midroog Aaa.il stable</i>	<i>Other Affirmation</i>

Explanation: The ratings history should only detail the rating history of the company rating the subject of the immediate report

Rating of the corporation's bonds:

Name and type of security	Security number on the stock exchange	Rating company	Current rating	Comments/Notice summary
<i>Contingent convertible bonds</i>	0	Midroog	Midroog Aa3.il stable	Rating affirmation

Ratings history for the three years prior to the rating/notice date:

Name and type of security	Security number on the stock exchange	Date	Type of rated security	Rating	Comments/Notice summary
<i>Contingent convertible bonds</i>	0	<i>August 28 2022</i>	<i>Contingent convertible bonds (CoCo)</i>	<i>Midroog Aa3.il stable</i>	Rating affirmation
<i>Contingent convertible bonds</i>	0	<i>August 22 2021</i>	<i>Contingent convertible bonds (CoCo)</i>	<i>Midroog Aa3.il stable</i>	Rating affirmation
<i>Contingent convertible bonds</i>	0	<i>September 10 2020</i>	<i>Contingent convertible bonds (CoCo)</i>	<i>Midroog Aa3.il stable</i>	Rating affirmation

Explanation: The ratings history should only detail the rating history of the company rating the subject of the immediate report

Attached rating report [Midroog 01082023 isa.pdf](#)

2. On _____, _____ announced that it would cease rating _____

Details of the signatories authorized to sign on behalf of the corporation

	Signatory's Name	Position
1	Hanan Kikozashvili	Other Bank Secretary & Head of the Bank's Headquarters

Explanation: According to Regulation 5 of the Securities (Periodic and Immediate Reports) Regulations, 5730-1970, a report filed under these regulations shall be signed by those authorized to sign on behalf of the corporation. The position of the senior staff on the matter (in Hebrew) can be found on the ISA's website: [Click here](#)

The reference numbers of previous documents on the subject (reference does not constitute incorporation by reference):

2022-01-109312

Securities of a Corporation Listed for Trading on Form structure revision date: June 20 2023

the Tel Aviv Stock Exchange

Abbreviated Name: Mizrahi Tefahot

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Previous name of the reporting entity: United Mizrahi Bank Ltd

Name of the person reporting electronically: Position: Name of Employing
Kikozashvili Hanan Bank Secretary Company: Mizrahi Tefahot
Bank Ltd

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Mizrahi Tefahot Bank Ltd¹

Follow-Up | August 2023

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¹ Mizrahi Tefahot Bank Ltd holds approx. 4.9% of Midroog Ltd's share capital via Mizrahi Tefahot Invest Ltd. The company's shares lack any means of control.

Mizrahi Tefahot Bank Ltd

Baseline credit assessment (BCA) for the bank	aa2.il	
Long-term deposits & bonds	Aaa.il	Outlook: stable
Contingent convertible bonds with contractual loss absorption mechanism (CoCo)	Aa3.il (hyb)	Outlook: stable
Short-term deposits/CP	P-1.il	-

Midroog is maintaining the rating of the baseline credit assessment (BCA) of Mizrahi Tefahot Bank Ltd (hereinafter: the “Bank”) at aa2.il.

The ratings of the Bank’s long-term deposits and senior debt have remained Aaa.il with a stable outlook, and they continue to embody the assumption of a high external support from the state, at two rating levels (notches) relative to the BCA.

The rating of the Bank’s contingent convertible bonds with contractual loss absorption mechanism (CoCo) through a write-off or partial write-off (classified as tier 2 capital) has remained at Aa3.il (hyb) with a stable outlook. This rating is one notch lower than the BCA and three notches below the senior debt and reflects the instrument’s conditions, including the structural subordination and loss-absorption mechanisms of this instrument and without an assumption of external support.

Midroog is likewise maintaining a P-1.il rating for short-term deposits and a P-1.il rating for the commercial papers.

The main considerations for the baseline credit assessment (BCA) and the Bank’s ratings

The Bank’s baseline credit assessment (BCA) is supported by its good positioning in the local banking system, which is based on a strong brand name, a significant market share and leadership in the housing credit sector, alongside a broad, dispersed customer base, which support the Bank’s good profitability, despite the concentration of the income sources. The Bank is universal and provides its customers with a variety of banking and financial services. The Bank is characterized by a conservative risk management policy which supports the Bank’s risk profile, as reflected also by the credit quality indicators, which stand out positively relative to the BCA over time. In our assessment, although the rate of problem debts within the portfolio is likely to rise, it will remain at a favorably positive level relative to the BCA. Accordingly, problem debts’ rate within the portfolio will move, in our assessment, in the range of 1.7%-1.8% in the forecast years (compared with an average of approx. 1.3% in 2021-2022).

The Bank is characterized by a sectorial credit concentration relative to a capital buffer that is high relative to the BCA (on par with the system), which weighs down the Bank's risk profile. The Bank's profitability rates have been improving in recent years, in view of the high asset quality, an operational efficiency that stands out positively over time, and an improvement in the financial margins of the Bank as a result of the rising interest and high inflation environment, as well as the implementation of its strategic plan. This improvement was also expressed during the first quarter of 2023 and, among other things, resulted from an increase in interest revenues, which occurred due to an increase in the balance of credit to the public compared to the parallel period last year, and due to a supportive macroeconomic environment that manifested as a rise in inflation and consequently, in the pace of the Bank of Israel's interest rate increases in the recent period.

In the base scenario for the years 2023-2024, Midroog anticipates that the Bank's profitability indicators will moderate somewhat relative to the first quarter of 2023 and the year 2022, but continue to support the ongoing accumulation of equity, as well as the financial profile, with the core return on risk weighted assets and ROA expected to move in the range between approx. 2.8%-3.1% and 0.9%-1.0%, respectively. It should be noted that as part of the Bank's capital management strategy, the Bank is characterized by a narrow margin over the regulatory barrier (tier 1 capital ratio), so that as of March 30, 2023, the Bank has maintained a margin of approx. 52 basis points (compared with 112 basis points in the comparison group), which might occasionally limit the Bank's business flexibility. We note that this margin is in accordance with the Bank's strategy and with a long-term conduct aimed towards capital efficiency.

Moreover, the Bank's leverage level is high relative to the BCA and the comparison group average and hinders the Bank's risk profile, as reflected by an equity to balance sheet ratio of approx. 5.7%, as of March 30, 2023, compared with an average of approx. 6.7% in the comparison group. In its base scenario, Midroog projects that the capital buffer will continue to accumulate, so that the capital adequacy ratio will be in the range of approx. 10.2%-10.4%. We note that regarding Midroog's extreme scenarios, the Bank's capital buffer absorbs unexpected losses appropriately and supports the Bank's stability throughout the economic cycle. The Bank's liquidity profile is adequate relative to the BCA and supported by a comfortable, wide and dispersed source structure, based on a stable (retail) deposit rate and a substantial inventory of low-risk liquid assets. At the same time, the liquidity profile might be affected by a relatively high wholesale deposits component, which in our assessment is less stable throughout the economic cycle. Liquidity management is also supported by a liquidity coverage ratio (LCR) of approx. 126% as of March 30, 2023, significantly higher the regulatory benchmark. This ratio also supports the liquidity profile and business flexibility of the Bank.

The ratings of the Bank's long-term deposits and senior debt were set at two rating levels (notches) above the BCA, embodying our assumption of a high probability of external support from the state, if necessary. The rating of the Bank's contingent convertible bonds with contractual loss absorption mechanism (CoCo) through a write-off or partial write-off is one notch lower than the BCA and two notches below the senior debt, reflecting the instrument's conditions, including the structural subordination and loss-absorption mechanisms of this instrument and without an assumption of external support.

Rating outlook

The stable outlook for the Bank's ratings reflect Midroog's assessment that the Bank will maintain an adequate financial profile in the forecast years, while keeping the risk metrics of the credit portfolio and the loss absorption buffers in a range that is appropriate for the rating.

Factors that could lead to raising the BCA and the Bank's ratings:

- A significant improvement in the dispersion of the Bank's activity mix
- A significant improvement in the Bank's capital adequacy ratios

Factors that could lead to lowering the BCA and the Bank's ratings:

- Substantial damage to the Bank's business status
- A significant worsening in the Bank's credit portfolio's quality
- An erosion of the capital buffer, profitability and the stability of the Bank

Mizrahi Tefahot Bank Ltd, financial data and main ratios, in millions (ILS) and in percentages:

₪ Million	Mar 31 2023	Mar 31 2022	2022	2021	2020	2019	2018
Loans to the public	315,416	285,457	310,356	273,531	247,958	206,401	195,956
Deposits from the public	348,469	312,653	344,514	307,924	284,224	210,984	199,492
Total equity attributed to the shareholders	24,844	21,199	23,780	20,770	18,804	16,033	14,681
Total assets	434,110	394,045	428,292	392,271	360,140	273,244	257,873
Revenue before taxes and credit loss expenses	2,389	1,825	7,495	4,752	3,654	3,318	2,505
Net profit attributed to the Bank's shareholders	1,367	1,154	4,472	3,188	1,610	1,842	1,206
(%)							
Exposure to largest industry to tier 1 shareholders' capital	144%	135%	143%	129%	120%	107%	126%
Problem debts from gross loans to the public	1.3%	1.2%	1.3%	1.3%	1.5%	1.8%	1.5%
Problem debts to total shareholders' capital and provision for credit losses	14.5%	14.1%	14.4%	14.5%	17.1%	19.9%	17.5%
Credit loss expenditure [income] to average loan to the public [1]	0.3%	0.1%	0.2%	(0.1%)	0.5%	0.2%	0.2%
Net profit to asset average [1]	1.3%	1.2%	1.1%	0.8%	0.5%	0.7%	0.5%
Revenue before taxes and credit loss expenses to risk weighted asset average [1]	3.8%	3.3%	3.2%	2.3%	2.0%	2.1%	1.7%
Efficiency ratio	37.6%	43.2%	45.2%	54%	53.9%	54.6%	63.6%
Tier 1 capital adequacy	10.1%	10.0%	9.9%	10.0%	10.0%	10.1%	10.0%
Total shareholders' capital to asset total	5.7%	5.4%	5.6%	5.3%	5.2%	5.9%	5.7%
Less stable finance resources [2] to asset total	20.8%	19.6%	20.2%	19.3%	15.0%	19.0%	16.5%
Liquidity balances [3] to deposits from the public	31%	30%	31%	35%	36%	29%	28%

[1] Calculated on an annual basis; [2] Financial institutions' deposits (wholesale), bonds and bonds deferred by up to one year and deposits from banks; [3] Cash and deposits at banks, US and Israel government bonds and assets backed by the US government

Details of the key considerations in the Bank's baseline credit assessment

A good business profile which supports the Bank's income generation capability throughout the economic cycle due to the substantial weight of retail income, but with a bias to the housing loans sector

Over time, Mizrahi Tefahot Bank is the leading banking group by size in the housing loan sector, with a market share of approx. 35% of total credit; and the third largest in the local economy, with a market share of approx. 18% of all assets in the system and approx. 21% of total credit, as of March 31, 2023. Likewise, the business profile, as is the case with the rest of the major banks, is supported by it being a universal bank, which provides a wide range of financial and banking services, leaning on a broad and dispersed customer base alongside a comprehensive value proposition that appeals to a variety of public tastes. The Bank is characterized by a strong brand in the housing credit sector, which in our assessment constitutes a platform to achieve growth in market shares, the retail customer base and as a result, in the income base, which support the establishment of its position as a leader in the retail field. All of these support the value proposition to the Bank's customers, and contribute, in our assessment, to the Bank's growth potential and profitability, as well as its ability to cope with changes in the business environment. In late 2022, Union Bank's merger with and into the Bank was finalized, with the Bank later expected to concentrate headquarter units' activities at a single central site in Lod by the end of 2025. We estimate that we will continue to see the expansion trend in all that concerns the provision of digital services in the banking system in the coming years, and that banks which will not adopt technological innovation, nor adjust their business model over time, might experience a substantial erosion of the business position in the medium-long term.

The stability of the Bank's revenues, as assessed by Midroog, stands out positively relative to the BCA and positively affected by its focus on mortgage credit. Accordingly, the weight of the Bank's retail revenues² is significant, constituting approx. 91% on average between 2020 and 2022, which is outstandingly positive relative to the comparison group, contributes to the revenue generation ability and moderates activities' volatility. However, the Bank is characterized by a low rate of commission revenues, which constituted approx. 18% on average between 2020 and 2022 and has eroded in recent years (approx. 15% in 2022 compared to approx. 21% in 2020) which we have characterized as a stable source of income throughout the economic cycle.

² Gross revenues from interest and non-interest revenues in accordance with the supervisory operation segments, and including the household and private banking (including housing) segments, as well as small and micro businesses, excluding financial management income.

This figure is low relative to the comparison group (2022: approx. 23% on average), which hinders the stability of the Bank's revenues. In addition, the dispersion of the Bank's sources of income is limited, in our assessment, and stands on two primary legs³ over time, as reflected by the revenue mix in 2022, which included approx. 73% of the housing loans sector and approx. 16% from small and micro businesses. Moreover, the Bank's concentration in the housing loans area has increased, with the total revenues in this area amounting to approx. 84% of the Bank's revenue mix as of the first quarter of 2023, reflecting a substantial increase compared to the average in the previous five years (approx. 62%). Moreover, in this scenario, the Bank is expected to continue working towards achieving the goals of the strategic plan approved by the Bank's Board of Directors during 2021, which, *inter alia*, aims towards growth in the business banking credit while establishing real investments, leading largescale and complex transactions and expanding the international activities of the Bank that are focused on business banking, alongside establishing leadership among households, particularly in the mortgage sector. These are expected to continue and support the growth of the Bank's activity aimed at increasing market shares, particularly in the business sector, in the short-medium term.

The risk management policy supports the Bank's risk profile; on the other hand, the industry concentration relative to the capital buffer is still relatively high

The Bank's risk management system is encompassing and includes a number of anchors and control circles, which support the formulation of risk management policies, in determining the Bank's risk appetite (in consistence with its strategy) and in monitoring and controlling risks. Credit risks are managed using statistical rating models (consumer credit) and expert evaluations (business credit). In our assessment, the Bank takes a conservative credit policy in the housing credit segment, which includes relatively strict restrictions on the business credit portfolio, underwriting processes, monitoring and management of collaterals, while this policy is also expressed by good risk indicators relative to the credit portfolio, that support the BCA. The Bank has no exposure over time to large borrowers. On the other hand, the Bank is characterized by a high industry credit concentration relative to the BCA, as measured in relation to the capital buffer, which weighs down the Bank's risk profile. Accordingly, the largest industry out of the Bank's tier 1 shareholders' capital is the real estate and construction industry, which constituted 144% on March 31, 2023, but which is low relative to the comparison group (approx. 193%).

³ An operating segment which constitutes over 15% of net revenues (interest and non-interest revenues from outsiders), excluding financial management income.

The Bank's market risks are estimated by the VaR model under conservative assumptions, similar to the entire banking system, and as a complementary action to the risk assessment, a number of stress scenarios (including holistic scenarios) at varying degrees of severity are examined. In Midroog's assessment, the Bank's market risk appetite is adequate, as reflected in the VaR limit of the Bank's total activity to a one-month investment prospect, established by the Board of Directors, of approx. 9% of the shareholders' capital, which is reasonable for the BCA but high relative to the other major banks.

The quality of the credit portfolio stands out positively relative to the BCA

The Bank is characterized by a high-quality credit portfolio, which supports its future profitability, as well as the capital buffer's accumulation potential, as reflected in the risk indicators which stand out positively relative to the BCA. Thus, as of March 31, 2023, the proportion of problem debts relative to the credit to the public amounted to a favorable rate of approx. 1.3%, compared with a rate of approx. 1.9% in the comparison group on that date. Furthermore, the rate of debts which are non-accumulating or in arrears for over 90 days out of the total gross credit to the public has remained without significant change compared to previous years and stood at approx. 0.9%.

We are of the opinion that the Bank's exposure to the mortgage and real estate industries is relatively high and amounts in aggregate at approx. 75% of the Bank's liabilities⁴ on March 31, 2023, while the comparison group had a much lower exposure rate of approx. 51% on that date. Exposure to the real estate industry alone (without mortgages) in Israel – which is characterized by us as relatively high level of risk, in view of homogeneous characteristics and due to high exposure relative to the capital absorption buffer, constitutes approx. 11% of the Bank's total liabilities (approx. 12.0% including credit to foreign operations) and substantially low relative to the comparison group. The exposure to the mortgage portfolio constitutes approx. 63% for that date, and it is characterized by the Bank's conservative underwriting processes, as reflected in the maintenance of a high repayment capability, which supports a low probability of failure. Accordingly, the average LTV rate in the Bank's housing loans portfolio amounted to approx. 53.8% as of March 31, 2023 (a rate reflecting the LTV when the credit was granted), with the share of the loans that had a relatively high leveraging rate (an LTV rate of over 75% of the total housing credit) being low and amounting to 0.6% of the portfolio for that period. In addition, the average repayment rate from disposable income in the housing credit portfolio⁵ amounted to approx. 26.2% on March 31, 2023 – likewise a low rate, reflecting a relatively low level of risk.

⁴ Credit to the public, credit to governments, deposits with banks and other debts, excluding bonds and borrowed securities.

⁵ Payments to income.

Midroog's base scenario regarding the quality of the Bank's credit portfolio is based on a number of exogenous macroeconomic influences, including: (1) An annual GDP growth rate of approx. 3.0% in 2023 and 2024; (2) An unemployment rate in the range between 3.7%-4.1%; (3) An interest rate environment that is similar to its current level; (4) An inflation rate of approx. 3.5% in 2023 and approx. 2.4% in 2024; (5) Continued competition on the part of the non-bank debt market in the consumer and business portfolio.

In this scenario, the Bank's credit portfolio will grow at a rate between 5.0%-6.5% in the years 2023-2024. We estimate that this growth will be supported by a continued maintenance of significant market shares in retail credit, and particularly in housing loans, alongside growth in the credit volumes to the business sector and international operations, in accordance with the aforesaid strategic plan.

Midroog is examining the development of the Bank's credit portfolio quality in the short and medium term, based also on a number of leading macroeconomic indicators. Accordingly, the rate of problem debts in the portfolio is expected to rise, but still remain at a level standing out positively relative to the BCA and move in our assessment in the range of approx. 1.7%-1.8% in the forecast years (vs. approx. 1.3% on average in 2021 and 2022) with the rate of problem debts out of the absorption buffers (shareholders' capital and provision for credit losses) projected to be in the range between 16.5%-17.5% in the forecast years (vs. approx. 14.1% on average in 2021 and 2022). Moreover, we are assuming a credit loss expenditure rate of approx. 0.4% out of the credit portfolio in the forecast years. This scenario takes into account moderation in the recovery rates and increase in the write-off rate relative to past years.

The BCA is supported by an ongoing improvement in the Bank's profitability in view of the Bank of Israel's interest rate increases and a relatively high inflation environment, alongside anticipation for some moderation in profitability ratios during the forecast range

The Bank's profitability metrics reflected an improvement trend in recent years, which, among other things, was the result of the strategic plan's implementation, which includes increased focus on the business sector, which is characterized by excess financial margins and by the rise of interest and inflation, which increased the financial margins alongside a low credit loss expenditure rate and a high operational efficiency, which stand out positively over time and derive from the mix of the credit portfolio and the business model. Profitability was also supported by the implementation of the Bank's efficiency processes starting in 2017, which included employees' early retirement, an organization of assets (asset realization and transitioning into a leasing model) and the signing of collective employment agreements for the Bank and Yahav Bank.

In addition, the Bank has worked to establish collaborations with financial institutions over the past few years, through the sale of housing loan portfolios, as part of its credit portfolio and regulatory capital management strategy, as well as increasing operating revenues from the management of sold portfolios,

The improvement in the Bank's profitability metrics was also expressed during the first quarter of 2023, with the net profit for shareholders amounting to ILS 1,367 million vs. ILS 1,154 million the year before, constituting an increase of approx. 18% and an ROE of approx. 22%. These, among other things, were due to an increase in interest income which occurred due to an increase in the balance of credit to the public over the parallel period last year, and the supportive macro-economic environment, which was reflected by the rising inflation and thus also by the recent pace of the Bank of Israel's interest rate hikes. In contrast, the portfolio quality indicators showed some erosion relative to the parallel period last year, which was reflected by an increase in credit loss expenditure, amid the worsening of the economy's macro-economic data. As aforesaid, all of these were expressed in the Bank's operational efficiency ratio, which stood at 37.6% as of the first quarter of 2023 (annualized) and the core return on risk-weighted assets and ROA which at that date stood at 3.8% and 1.3%, respectively, which stand out positively relative to the rating and constitute an improvement compared to recent years, as mentioned.

The main assumptions regarding the Bank's profitability, on which Midroog's baseline scenario for the years 2023-2024 is based, are as follows: (1) An annual credit portfolio growth of approx. 5.0%-6.5%, which in our assessment will be supported by a continued maintenance of significant market shares in retail credit, and particularly in housing loans, alongside growth in the credit volumes to the business sector and international operations, in accordance with the Bank's strategic plan; (2) An interest environment similar to its current level that supports the financial margin; (3) An inflation rate of approx. 3.5% in 2023 and approx. 2.4% in 2024; (4) Credit loss expenses for the credit portfolio of approx. 0.4% in the forecast years; and (5) A continued "creeping" of wage expenses, per the Bank's wage agreements, alongside an offsetting effect caused by streamlining processes. In this scenario, Midroog anticipates that during the forecast years, the Bank's profitability ratios will moderate, to some extent, relative to the first quarter of 2023 and the year 2022, but will continue to support the ongoing build-up of the capital and the financial profile, with the core yield on risk weighted assets and ROA expected to move in the range between 2.8%-3.1% and 0.9%-1.0%, respectively. In addition, the Bank is expected to concentrate headquarter units' activities at a single central site, as part of a strategic move by the Bank which supports a further potential for efficiency in the medium-long term (by 2025).

The capital buffer is reasonable relative to the BCA, due to a relatively high balance sheet leverage and a low buffer over the regulatory barrier, alongside anticipation that the capital buffer will continue its accumulation within the forecast range

The Bank is characterized by a capital buffer which is reasonable relative to the BCA that had been building up over the years through the accumulation of profits minus dividend distribution (a policy of 40% of the quarterly net profit), optimization and management of risk weighted assets and the asset mix. As of March 31, 2023, the Bank's tier 1 shareholders' capital, the central absorption buffer for unexpected losses, amounted to approx. 10.1%, demonstrating improvement compared to approx. 9.9% on December 31, 2022. It should be noted that as part of the Bank's capital management strategy, the Bank is characterized by a narrow margin over the regulatory barrier (tier 1 capital ratio). As of March 31, 2023, the Bank has maintained a margin of approx. 52 basis points (compared with 112 basis points in the comparison group), which might occasionally limit the Bank's business flexibility.

The Bank's leveraging level is high relative to the BCA and the comparison group's average, and hinders the Bank's risk profile, as reflected by a capital to balance sheet ratio⁶ of approx. 5.7%, as of March 31, 2023, compared with an average of approx. 6.7% in the comparison group. We are of the opinion that in light of the volatility in the capital market, the total profit of the Bank in particular - and that of the banking system in general - might be affected from adjusting securities available for sale according to fair value and changes the actuary undertaking for employee benefits.

Midroog tested a holistic stress scenario for one year ahead on the Bank's loss absorption buffers relative to its risk profile, while assuming various PD and LGD rates in the main sectors of the operation, losses from the securities portfolio, erosion in the financial margin and the loss of commission income, along with the build-up of the shareholders' capital through current profitability and the non-distribution of a dividend. The Bank's tier 1 capital ratio would amount to approx. 9.8% at the end of the scenario - a level that reflects the good ability of the Bank to absorb unforeseen losses, in our assessment, which supports its stability during the economic cycle.

Midroog's base scenario anticipates that the capital buffer will continue to be accumulated, so that the core capital adequacy ratio will move in the range between 10.2% and 10.4%. This ratio will be affected by the following factors: (1) Accrued profits; (2) Dividend distribution to the extent of up to 40% of the net revenues in the forecast years; and (3) A growth in risk weighted assets, similar to the credit portfolio's increase rate.

An adequate liquidity profile relative to the BCA and supported by a comfortable resource structure and a substantial liquid asset inventory

The Bank's resource structure, similarly to the entire local banking system, mainly relies on a broad retail deposit base, which is characterized by a relatively high stability throughout the economic cycle. The Bank's resource structure contains a substantial proportion of widely-dispersed stable (retail) deposits (approx. 44% households and private banking and approx. 16% small and micro businesses, as of March 31, 2023), which are appropriate for the Bank's risk profile, in Midroog's assessment. The Bank has a reasonable rate of financing sources which are less stable⁶ out of the total assets, per our definition, that amounted to approx. 20.8% on that date. Moreover, the Bank is characterized by a relatively high ratio between credit to the public and deposits from the public, which on March 31, 2023, amounted to 91% vs. a comparison group average of approx. 77% on that date. Moreover, the NSFR ratio on March 31, 2023, as calculated by us⁷, is appropriate for the rating and supports the Bank's financing profile. The Bank's liquidity buffer includes an inventory of liquid assets⁸ relative to the total deposit is high relative to the BCA and amounted to approximately 31% on March 31, 2023 and supports the Bank's good liquidity. This inventory mainly includes cash and deposits at banks; and the securities portfolio. This portfolio constituted approx. 4% of the total assets on that date and is characterised by a risk level (credit) that is relatively low in view of Israel and US government bonds constituting substantial components thereof (approx. 77% and approx. 8%, respectively). The portfolio serves as a tool to absorb excess resources and manage the Bank's various market exposures, but exposes it to an interest rate risk. The liquidity management is also supported by a high regulatory liquidity coverage ratio (LCR) which amounted to approx. 126% on March 31, 2023 - significantly higher than the regulatory bar (100%) but relatively low compared to the system (approx. 131%). This rate also supports the liquidity profile and business flexibility of the Bank. Midroog anticipates that the Bank's resource structure and good liquidity will be preserved throughout the forecast range, *inter alia* in view of our no-change assessment regarding the market's savings culture, and in light of the growth potential of the Bank's credit portfolio.

⁶ Deposits from banks, deposits from financial institutions, and bonds and debentures to be paid within the next 12 months

⁷ Calculated by us based on the definitions of the Basel Committee.

⁸ Cash and deposits at banks, Israeli government bonds, US government bonds and bonds backed by the US government.

Additional considerations

ESG considerations

Environmental considerations: In our assessment, the banking industry is exposed to environmental risks in a relatively moderate manner at this stage.

Social considerations: In our assessment, the banking industry faces moderate social risks. However, we are seeing a development in risks related to information security, client privacy and cyber, although these are partially mitigated by substantial investments in technology alongside the banking system's extensive experience in handling sensitive client data. Fines and reputation damages constitute another social risk. In addition, strict labor laws and strong labor unions in the banking system limit the flexibility of the workforce and increase wage costs. However, banks have reduced employee positions through early retirement programs and implemented cost control, which has allowed them to mitigate these challenges.

Corporate governance considerations: In our assessment, corporate governance risks have a substantial impact on the banking industry. These risks are a major credit consideration, where weaknesses in corporate governance may lead to a deterioration in the bank's credit repayment capacity, while strong corporate governance may positively impact the bank's credit repayment capacity. A mitigating factor for corporate governance risks is the regulatory framework under which banks operate, which outlines a system of internal reviews as well as tight controls on the side of the regulator.

Structural considerations and support

A review of the relative projected loss ranking

According to Midroog's methodology, the rating of the Bank's subordinated debts (deferred bonds) is based on the Bank's baseline credit assessment (BCA), which is the anchor for rating the Bank's liabilities and reflects the risk of failure and the Bank's ability to serve its liabilities independently, without the assumption of external support. Midroog adjusts the rating relative to the BCA to the credit risk of the subordinated debt instrument, according to its specific characteristics – taking into consideration the extent of the instrument's structural subordination, the loss absorption mechanisms per the instrument's conditions and the uncertainty regarding their point of activation (at the contractual trigger and/or at the discretion of the Supervisor of Banks). Midroog is removing one rating level (notch) off the Bank's BCA for the rating of the deferred bonds with contractual loss absorption mechanism (CoCo).

The removal of the notch embodies the legal-contractual deferral with respect to the rest of the Bank's liabilities (excluding tier 1 instruments and shareholders' capital) and the contractual loss absorption mechanism. Considering the Bank's BCA (aa2.il) and the current level of capital adequacy – tier 1 capital ratio (of approx. 10.1% on March 31, 2023), as well as the one anticipated in our base scenario (10.2%-10.4%) and the liquidity profile, which is appropriate relative to the BCA, the uncertainty regarding the likelihood of reaching the 'nonviability point'⁹ is low; therefore, it was not embodied by the reduction of another notch.

External support

The rating of the deposits and senior debt are granted the benefit of two rating levels (notches) due to the high probability of external support from the state, according to Midroog's JDA model. The assumption of external support probability is based on the following considerations: the banking system's high importance to the local economy and the payment system, and the need to maintain its stability; the high concentration of the banking and financial system; the relatively high connectivity between the banking system and financial institutions; the local financial system serving as a central credit provider to the government; some uncertainty regarding the behavior and trust of the different debtors, in terms of bail-ins close to the point of failure, in the absence of previous experience. Furthermore, the State of Israel had, in the past, proved its willingness to support failed banks, and we do not assume any change in this policy.

About the bank

Mizrahi Tefahot Bank was among the first banks to be established in Israel (1923) and is one of the five major banking groups in Israel.

In 2005, two banks – United Mizrahi Ltd. and Tefahot Israel Mortgage Bank Ltd. – were merged together into Mizrahi Tefahot Bank Ltd. On September 30, 2020, a tender purchase offer was finalized with regard to the shares of Union Bank. 100% of Union Bank's issued and outstanding share capital and voting rights was purchased in the offer. In December 2022, Union Bank's merger with and into the Bank was finalized. With the merger's finalization, Union Bank ceased to exist as an independent legal entity and all of its assets and liabilities were instilled with the Bank.

⁹ Establishing nonviability event: 1. A notice from the Supervisor of Banks that the write-off/conversion of a security is necessary to avoid the nonviability point. 2. The provision of external support, without which the Bank would reach the nonviability point. It should be noted that the Supervisor of Banks has yet to define the term 'nonviability point'.

The Bank group operates in Israel and abroad and includes Yahav Bank, which is held at 50%. The group engages in commercial (business and retail) banking activities, and mortgage activities in Israel, through a nationwide chain of 206 branches (as of late 2022) and business centers. The Bank's international activities are conducted through two banking units. In addition to its banking activities, the Bank Group is engaged in various activities related to the capital market, including: Consultancy for capital market activities, management of security portfolios for customers, pension advisory service, trust services, distribution of mutual funds, operation of provident funds and distribution of mortgage insurance. The Bank's controlling shareholders are the Ofer and Wertheim families.

The bonds rated by Midroog*:

Series	Security No.	Rating	Outlook	Final Repayment Date
51	2310324	Aaa.il	Stable	Oct 29 2023
Contingent subordinated notes (CoCo)	Not tradable	Aa3.il(hyb)	Stable	Jan 31 2024
59	2310449	Aaa.il	Stable	Apr 2 2024
60	2310456	Aaa.il	Stable	Sep 5 2024
45	2310217	Aaa.il	Stable	Sep 28 2024
57	2310423	Aaa.il	Stable	Mar 1 2025
40	2310167	Aaa.il	Stable	Jun 7 2025
49	2310282	Aaa.il	Stable	Jun 23 2026
61	2310464	Aaa.il	Stable	Dec 4 2026
46	2310225	Aaa.il	Stable	Sep 28 2027
48	2310266	Aa3.il(hyb)	Stable	Oct 21 2028
50	2310290	Aa3.il(hyb)	Stable	Dec 23 2029
42	2310183	Aaa.il	Stable	Jun 7 2030
52	2310381	Aaa.il	Stable	Jul 1 2030
53	2310399	Aa3.il(hyb)	Stable	Jun 24 2031
62	2310498	Aaa.il	Stable	Oct 21 2028
63	2310548	Aaa.il	Stable	Apr 12 2031
64	2310555	Aaa.il	Stable	Apr 12 2031
Series 1	1193887	P-1.il	-	Apr 20 2024
66	1191667	Aaa.il	Stable	Dec 8 2031
65	1191675	Aa3.il(hyb)	Stable	Jun 8 2033
67	1196807	Aaa.il	Stable	Jun 12 2033

** Issued by the Bank and by Mizrahi Tefahot Issuing Company Ltd – a subsidiary fully owned by the Bank*

Baseline Credit Assessment (BCA) Matrix

Category	Parameter	Sub-parameter	For Mar 31 2023		Midroog's outlook [1]		
			Measure [1]	Score	Measure	Score	Additional considerations
Business profile	Business positioning		-	aa.il	-	aa.il	<i>Market share positioning in housing loan segment</i>
	Income stability	% retail income	99%	aaa.il	>80%	aa.il	<i>Percentage of income from commissions low relative to the system</i>
	Income dispersion	Number of business lines over 15% of total revenues	2	baa.il	2	baa.il	<i>Retail sectors</i>
Risk profile	Corporate governance		-	aa.il	-	aa.il	
	Risk management policy		-	aa.il	-	aa.il	
	Credit portfolio concentration	Largest industry to tier 1 shareholders' capital	144%	aa.il	~144%	a.il	<i>Real estate sector</i>
	Credit portfolio concentration	Major borrowers to tier 1 shareholders' capital	0%	aaa.il	<5%	aaa.il	

	Market risk appetite	VaR limit on tier 1 shareholders' capital	9%*	a.il	~9%	a.il
Financial profile	Asset quality	Problem debts to loans to the public	1.3%	aaa.il	~1.8%	aaa.il
		Problem debts to total shareholders' capital and provision for credit losses	14.5%	aaa.il	~17%	aa.il
		Net profit to asset average	1.3%	aaa.il	0.9%-1.0%	aa.il
	Profitability	Profit before taxes and credit loss expenses to risk weighted asset average	3.8%	aaa.il	2.8%-3.1%	aaa.il
		Efficiency ratio	37.6%	aaa.il	42%-44%	aaa.il
	Capital adequacy	Tier 1 shareholders' capital to risk weighted assets	10.1%	aa.il	10.2%-10.4%	aa.il
		Shareholders' capital to total assets	5.7%	baa.il	5.9%-6.0%	baa.il

Liquidity & financing	Less stable finance resources to total assets	20.8%	aa.il	~20.8%	aa.il
	Liquid assets to deposits from the public	31%	aa.il	~31%	aa.il
Deriving baseline credit assessment				aa2.il	
Actual baseline credit assessment				aa2.il	

[1] The metrics presented in the table have been adjusted by Midroog, and are not necessarily identical to those presented by the company. Midroog's forecast includes Midroog's assessments regarding the issuer, per Midroog's base scenario, rather than the issuer's assessments.

**According to the data of December 31st, 2022*

Rating of the Bank's debts

	Baseline credit assessment (BCA)	Owner and/or affiliated party support	Adjusted BCA	Subordination and loss absorption capacity	State support	Rating
Deposits and bonds	aa2.il	0	aa2.il	0	+2	Aaa.il
Subordinated bonds with a contractual loss absorption capacity (tier 2 capital)	aa2.il	0	aa2.il	-1	0	Aa3.il(hyb)

Related reports

[Mizrahi Tefahot Bank Ltd – Related reports](#)

[Bank Rating – Methodology Report, September 2019](#)

[Promotion of Competition in the Banking System – Special Report, February 2023](#)

[Banking System – Guidelines for Examining Environmental, Social and Corporate](#)

[Governance Risks in Credit Ratings – Methodology Report, February 2022](#)

[Connections and Holdings Table](#)

[Midroog Rating Scales and Definitions](#)

The reports are published on Midroog's website: www.midroog.co.il

General information

Rating report date:	August 1 2023
Last date on which rating was updated:	June 8 2023
Date on which rating was first published:	September 10, 2017
Name of the rating initiator:	Mizrahi Tefahot Bank Ltd
Name of the party paying for the report:	Mizrahi Tefahot Bank Ltd

Information from the issuer

In its ratings, Midroog relies, inter alia, on information received from authorized parties at the issuer.

Baseline Credit Assessment (BCA) Scale

aaa.il	Issuers and issues assessed at aaa.il are those that, in Midroog's judgment, have the highest internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government.
aa.il	Issuers and issues assessed at aa.il are those that, in Midroog's judgment, have very high internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government.
a.il	Issuers and issues assessed at a.il are those that, in Midroog's judgment, have relatively high internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government.
baa.il	Issuers and issues assessed at baa.il are those that, in Midroog's judgment, have moderate internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government, and may have certain speculative characteristics.
ba.il	Issuers and issues assessed at ba.il are those that, in Midroog's judgment, have relatively weak internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government, and have speculative characteristics.
b.il	Issuers and issues assessed at b.il are those that, in Midroog's judgment, have very weak internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government, and have significant speculative characteristics.
caa.il	Issuers and issues assessed at caa.il are those that, in Midroog's judgment, have excessively weak internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government, and have very significant speculative characteristics.
ca.il	Issuers and issues assessed at ca.il are those that, in Midroog's judgment, have extremely weak internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government, and are very near default, with some prospect of recovery of principal and interest.
c.il	Issuers and issues assessed at c.il are those that, in Midroog's judgment, have the weakest internal or independent financial strength, relative to other local issuers, absent any possibility of external support from an affiliate or the government, and are usually in default, with little prospects of recovery of principal and interest.

Note: Midroog appends numeric modifiers 1, 2, and 3 to each rating category from aa.il to caa.il. The modifier '1' indicates that the debenture ranks in the higher end of its rating category, which is denoted by letters. The modifier '2' indicates that it ranks in the middle of its rating category and the modifier '3' indicates that the debenture ranks in the lower end of that category, denoted by letters.

Midroog does not publish the BCA forecast, unlike the publications that have been made so far, in order to separate the BCA from credit ratings.

Local Long-Term Rating Scale

Aaa.il	Issuers or issues rated Aaa.il are those that, in Midroog's judgment, have the highest creditworthiness relative to other local issuers.
Aa.il	Issuers or issues rated Aa.il are those that, in Midroog's judgment, have very high creditworthiness relative to other local issuers.
A.il	Issuers or issues rated A.il are those that, in Midroog's judgment, have relatively high creditworthiness relative to other local issuers.
Baa.il	Issuers or issues rated Baa.il are those that, in Midroog's judgment, have relatively moderate credit risk relative to other local issuers, and could involve certain speculative characteristics.
Ba.il	Issuers or issues rated Ba.il are those that, in Midroog's judgment, have relatively weak creditworthiness relative to other local issuers, and involve speculative characteristics.
B.il	Issuers or issues rated B.il are those that, in Midroog's judgment, have relatively very weak creditworthiness relative to other local issuers, and involve significant speculative characteristics.
Caa.il	Issuers or issues rated Caa.il are those that, in Midroog's judgment, have excessively weak creditworthiness relative to other local issuers, and involve very significant speculative characteristics.
Ca.il	Issuers or issues rated Ca.il are those that, in Midroog's judgment, have extremely weak creditworthiness and very near default, with some prospect of recovery of principal and interest.
C.il	Issuers or issues rated C are those that, in Midroog's judgment, have the weakest creditworthiness and are usually in a situation of default, with little prospect of recovery of principal and interest.

Note: Midroog appends numeric modifiers 1, 2, and 3 to each rating category from aa.il to caa.il. The modifier '1' indicates that the debenture ranks in the higher end of its rating category, which is denoted by letters. The modifier '2' indicates that it ranks in the middle of its rating category and the modifier '3' indicates that the debenture ranks in the lower end of that category, denoted by letters.

Local Short-Term Rating Scale

P-1.il	Issuers rated Prime-1.il, in Midroog's judgment, have a very good ability to repay short-term obligations relative to other local issuers.
P-2.il	Issuers rated Prime-2.il, in Midroog's judgment, have a good ability to repay short-term obligations relative to other local issuers.
P-3.il	Issuers rated Prime-3.il, in Midroog's judgment, have a moderate ability to repay short-term obligations relative to other local issuers.
NP.il	Issuers rated Not Prime.il do not belong in any of the Prime categories.

The Connection between the Long-Term and Short-Term Rating Scales

The following table shows the long-term ratings consistent with short-term ratings, when such long-term ratings exist¹⁴.

Long-term rating	Short-term rating
Aaa.il	Prime-1.il
Aa1.il	
Aa2.il	
Aa3.il	
A1.il	
A2.il	
A3.il	Prime-2.il
Baa1.il	
Baa2.il	
Baa3.il	Prime-3.il
Ba1.il, Ba2.il, Ba3.il	
B1.il, B2.il, B3.il	
Caa1.il, Caa2.il, Caa3.il	
Ca.il	
C.il	Not Prime

¹⁴ Structured finance short-term ratings are usually based on the short-term rating of a liquidity provider for the transaction or an assessment of cash flows available to repay the rated obligation.

[Midroog disclaimer]