MIZRAHI TEFAHOT BANK LTD
No. with the Registrar of Companies: 520000522

To	Israel Securities Authority	To	Tel Aviv Stock Exchange Ltd	T125 (Public)	Date of transmission: June 6, 2019
	www.isa.gov.il		www.tase.co.il		Ref: 2019-01-056365

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

On June 6th, 2019, *S&P Maalot* published:

⦿A rating report/notice *initial*

○A notice regarding rating cessation

1. Rating report or notice

☐ Corporation's rating: *ilAAA*

Comments/Notice summary:

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

Date	Rating subject	Rating	Comments/Notice summary

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
Bond certificate (Series 49)	0	Maalot S&P	Maalot S&P *ilAAA stable*	Initial rating
Bond certificate deferred bonds with a loss absorption capacity (Series 50)	0	Maalot S&P	Maalot S&P *ilAA- stable*	Initial rating

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

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

Attached rating report 06062019_Hanpakot_isa.pdf

2. On _______, __________ announced that it would cease rating __________

Maalot's rating was given in connection with the issuance of bond certificates (Series 49) and deferred bonds (Series 50), which is being examined by Mizrahi Tefahot Issuing Company Ltd, a subsidiary fully owned by the bank. It is hereby clarified that at the time of this report, there is no certainty regarding the execution of the issuance, its timing, its size and its conditions.

No change has been made to the bank's rating.

The above report was signed by Ms. Maya Feller, Bank Secretary

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

Securities of a Corporation Listed for Trading on the Tel Aviv Stock Exchange

Form structure revision date: April 30, 2019

Abbreviated Name: Mizrahi Tefahot

Address: 7 Jabotinsky Street
Ramat Gan, 52520, Israel

Tel: 03-7559720 Fax: 03-7559923

E-mail: mangment@umtb.co.il

Previous name of the reporting entity: United Mizrahi Bank Ltd.

Name of the person reporting electronically: Feller Maya Position: Bank Secretary Name of Employing Company:
Address: 7 Jabotinsky Street, Ramat Gan, 52520, Israel Tel: 03-7559720 Fax: 03-7559923 E-mail: mangment@umtb.co.il

Maalot

S&P Global Ratings

Mizrahi Tefahot Bank Ltd

Mizrahi Tefahot Issuing Company Ltd

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June 6 2019

New Issuance

Granting of an ‘ilAAA’ Rating to the Issuance of Bonds at up to ILS 1.5 Billion N.V. and the Granting of an 'ilAA-' Rating to the Issuance of Bonds with a Loss Absorption Capacity of up to ILS 250 Million N.V.

Primary Credit Analyst:

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New Issuance

Granting of an ‘ilAAA’ Rating to the Issuance of Bonds at up to ILS 1.5 Billion N.V. and the Granting of an 'ilAA-' Rating to the Issuance of Bonds with a Loss Absorption Capacity of up to ILS 250 Million N.V.

S&P Maalot hereby announces the granting of an ‘ilAAA’ rating to the issuance of a new series of bonds, Series 49, at a sum of up to ILS 1.5 billion N.V; and the granting of an 'ilAA-' rating to the issuance of a new series of deferred bonds with a loss absorption capacity, Series 50, at a sum of up to ILS 250 million N.V. These series will be issued by Mizrahi Tefahot Bank Ltd (ilAAA/Stable) through Mizrahi Tefahot Issuing Company Ltd.

In determining the rating of Series 50, we implement, among other things, the methodology for rating banks’ complex instruments and the methodology to determine regional scale ratings. The rating’s starting point is the bank’s stand-alone credit profile (SACP), and not the issuer’s rating, which also includes state support, as we estimate that these instruments will not receive support from the state. We are removing two rating levels (notches) off the SACP as follows:

- One notch to reflect the loss absorption capacity embedded in the instrument in the form of a principal write-off of the deferred bonds, should any of the trigger events defined in their conditions occur, i.e. a “formative principal loss absorption event”, when the bank’s tier 1 equity ratio falls below 5%, or a “formative nonviability event”, which is defined as the earliest between a written notice from the Supervisor of Banks to the bank that a write-off of debentures is necessary, since without it the bank would reach the point of nonviability, in the opinion of the Supervision of Banks; or written notice from the Supervisor of Banks to the bank regarding a decision to inject capital from the public sector, or support of equivalent value, without which the bank would reach the point of nonviability, as will be determined by the Supervision of Banks (insolvency).
- One notch to reflect the contractual deferral of the instrument, compared with the bank’s more senior debt (subordination).

The first rating level is removed off the bank’s SACP, as determined by the global ratings scale, in order to reflect the insolvency risk, according to our methodology for rating banks’ complex instruments. Afterwards, we convert to the regional rating, using the conversion tables. After the conversion to the regional ratings scale, we remove one more notch, in order to reflect the contractual subordination of the instrument, thus reaching the instrument’s rating on the regional scale.

An examination of the instrument in light of our complex instrument methodology does not, in our assessment, reveal additional default risks that would justify removing more notches beyond those specified above. In particular, we note that the current creditworthiness of the bank does not lead us to think that the likelihood of regulatory intervention with respect to the aforementioned bonds, as described above, requires an additional removal of rating levels.

For further details regarding Mizrahi Tefahot Bank Ltd’s rating and for additional regulatory requirements, see the rating report dated January 14st, 2019. For further details regarding the methodology behind the instrument's rating, please consult the list of methodology articles in the aforementioned rating report and the Q&A document "Rating of Complex Bank Instruments – Q&A" (November 29, 2015).

Methodology and Related Articles

- Use Of CreditWatch And Outlooks; September 14, 2009
- Bank Rating Methodology; November 9, 2011
- Banking Industry Country Risk Assessment Methodology and Assumptions; November 9, 2011
- Quantitative Metrics for Rating Banks Globally: Methodology and Assumptions; July 17, 2013
- Methodology: Timelines of Payments: Grace Periods, Guarantees, And Use of 'D' and 'SD' Ratings; October 24, 2013
- Group Rating Methodology; November 19, 2013
- Bank Hybrid Capital and Nondeferrable Subordinated Debt Methodology and Assumptions; January 29, 2015
- Methodology For Linking Long-Term and Short-Term Ratings; April 7, 2017
- Risk-Adjusted Capital Framework Methodology; July 20, 2017
- Methodology For National And Regional Scale Credit Ratings; June 25, 2018
- S&P Global Ratings Definitions; October 31, 2018
- Mapping Table – The Connection Between The Global Rating Scale And The Israeli Rating Scale; June 26, 2018

General details (as of June 6, 2019)	
Mizrahi Tefahot Bank Ltd	
Issuer Rating(s)	
Long term	ilAAA/Stable
Issuance rating(s)	
Complex subordinated debt	
Deferred capital notes (upper Tier II capital) A	ilA+
Deferred bonds with loss absorption capacity	ilAA-
Issuer rating history	
Long term	
December 23, 2014	ilAAA/Stable
November 15, 2010	ilAA+/Stable
September 14, 2009	ilAA+/Negative
May 28, 2007	ilAA+/Stable
October 01, 2003	ilAA+
Mizrahi Tefahot Issuing Company Ltd	
Issuance rating(s)	
Complex subordinated debt	
Deferred bonds with loss absorption capacity Series 47	ilAA-
Deferred bonds with loss absorption capacity Series 48	ilAA-
Deferred bonds with loss absorption capacity Series 50	ilAA-
Senior unsecured debt	
Series 37, 38, 39, 40, 41, 42, 43, 44, 45, 46	ilAAA
Series 49	ilAAA
Subordinated debt	
Deferred bonds 31	ilAA+
Additional details	
Time of the event's occurrence	June 6, 2019 11:13
Time at which the event first became known	June 6, 2019 11:13
Rating initiator	The rated company

[Standard and Poor's Maalot Legal Disclaimer]

MAALOT

S&P Global Ratings

Mizrahi Tefahot Bank Ltd.

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January 14, 2019

Primary Credit Analyst:

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Content

Mizrahi Tefahot Bank Ltd.

Issuer's Rating Affirmation	ilAAA/Stable

Strengths & Weaknesses

Strengths	Weaknesses
• The leading bank in the field of mortgages, strengthening its presence in its additional fields of operation. • Stable quality of credit due to a supportive economic environment and tight management of exposure to mortgages. • Wide local basis of deposits and continued good access to the local capital market, which are at the basis of the good financing and liquidity indicators.	• High exposure to the local residential real estate sector. • Competitive business environment which limits the potential for organic growth in the fields of business credit and small-medium businesses. • Uncertainty with regard to the effects of the investigation of US authorities on the bank's profitability.

Rating Outlook: Stable

Our stable rating outlook for Mizrahi Tefahot Bank Ltd ("**Mizrahi Tefahot**") reflects our estimation that the improvement in the operating environment and the local economy will provide additional support for the bank's rating in the current rating category. We believe that, especially in view of the bank's exposure to the residential real estate sector, it may enjoy a possible decrease in the economic risks in the market which may increase the rating anchor of the banks in Israel and lead to an improvement in the capital evaluation. However, we estimate that the improvement in the capital evaluation may be limited mainly pursuant to the uncertainty with regard to the effect of the final arrangement with the US authorities. In our base scenario we estimate that the good operating performance together with no dividend distribution will enable the bank to withstand the ramifications of the arrangement. We also estimate that the bank will continue to maintain high underwriting standards and will diversify its credit portfolio, in addition to maintaining efficiency ratios that are among the best in the reference group, despite the expected increase in expenses.

The negative scenario

We may consider a negative rating action in the event of a reversal of the economic trend, for example as a result of an imbalance in the housing market. Even though in our forecasts we included an additional provision for the arrangement with the US authorities, we may take negative rating action if the agreement costs will significantly deviate from our forecasts in terms of provisions or in case of other ramifications. Alternatively, we will consider negative rating action if the bank will find it hard to streamline its capital structure, which will burden its operating profitability potential, which may limit its ability to withstand the ramifications of the arrangement with the US authorities on the capital and profitability.

Main Rating Considerations

The bank's rating reflects its sound business position in the local banking system and its business focus in the field of housing loans, being the largest mortgage provider in Israel. The competition in the field of mortgages has increased recently and at the same time, the housing market has slightly cooled down in the past two years. Accordingly, and according to its strategic plan, the bank aspires to strengthen its presence in additional fields of activity such as credit for small and medium businesses and business credit. Even though we expect a certain slowdown in the growth of the residential credit segment, we estimate that the bank will maintain its position in the field. We now estimate that the likelihood of a merger with Union Bank is low, pursuant to the Antitrust Commissioner's objection however, we believe that the bank will continue to act to implement its strategic plan for growth in other operating segments also without the merger, and also considering the increasing competition in the other credit segments.

We estimate the bank's capital as 'adequate' and estimate that the risk-adjusted capital (RAC) ratio will gradually improve to 10% or so in the next two years. In our opinion, the uncertainty with regard to the final arrangement with the US authorities and the legal expenses entailed thereby may influence our estimation of the bank's capital and its compliance with the required regulatory capital, since the bank maintains a narrow margin above the minimum regulatory requirements and is constantly required to streamline its capital allocation to enable growth. We assume that the bank's current strong operating performance – as a result of good economic conditions, a stable mortgage market and good efficiency – may moderate the future ramifications of an arrangement with the US authorities, particularly after halt of the dividend payments. However, a renewed imbalance in the housing market concurrently with an economic slowdown and an increase in unemployment may affect the bank's stable profitability, however, that is not our base scenario for the next 18-24 months.

Mizrahi Tefahot's exposure to field of real-estate is the largest in comparison to the local banks, mainly through housing credit and to a lower degree, through construction and real estate credit. We believe that in the current economic conditions such exposure is being managed well and that the risk in the mortgage portfolio is offset, to a large extent, by a low rate of loan to value (LTV) of 52.8%, by a low rate of payment to income (PTI) of 26.7% as of September 2018, and by a good distribution of borrowers and geographic regions. Mizrahi Tefahot's exposure to borrower concentration in the business segment is lower than that of the majority of its competitors. We estimate the bank's financing profile as 'average' since it is supported by a wide and distributed depositor base. We estimate the liquidity as 'adequate' since we believe that the bank's inventory of liquid assets is sufficient for comfortable coverage of its liquidity needs, and reduces the reliance on short-term wholesale financing.

The bank's issuer rating is one notch higher than its stand-alone credit profile (SACP), due to our estimation of quite a high likelihood of unusual support by the State of Israel (AA-/Stable/A-1+), where necessary. We classify Bank Mizrahi as being systemically important and the State of Israel as supporting the local bank sector.

Anchor: Reflects the focus of the activity in Israel

S&P Global's rating methodology for banks is based on our evaluation of the Israeli banking industry from a global perspective (BICRA – Banking Industry Country Risk Assessment), as an anchor for bank ratings, i.e. a rating starting point. This assessment combines the economic risk assessment and the industry risk assessment. The BICRA score for the Israeli banking system is 4 on a scale of 1 to 10, with 1 reflecting the lowest risk.

We believe that the economic characteristics of Israel, that enjoys adequate resilience with no significant imbalance factors, support the local banking system. However, the bank segment remains sensitive to geopolitical risks and risks deriving from inequality and high exposure to the real-estate market, which has suffered from fluctuations in the past two years.

With regard to the industry risk, the banking segment in Israel has a proper institutional framework which is supported by a high and stable share of retail core deposits. We estimate that we will see increased activity by non-bank credit providers in the fields of small business credit and retail credit, in addition to strong competition on their part in corporate credit. In addition, the regulator has increased competition also from the direction of the credit card companies through various means.

Table 1.

Mizrahi Tefahot Bank Ltd. Key Figures (Mil. ILS)

	YTD Sep 2018	2017	2016	2015	2014
Adjusted assets	248,744	239,485	230,368	209,071	198,426
Customer loans (gross)	191,917	183,058	173,109	160,920	149,219
Adjusted common equity	14,956	13,777	12,789	11,916	10,711
Operating revenues	5,112	6,000	5,640	5,392	4,963
Noninterest expenses	2,748	3,611	3,299	3,226	3,039
Core earnings	1,315	1,391	1,308	1,194	1,123

Data are based on S&P Global Ratings adjusted number and ratios

Business position: the largest credit provider in the field of mortgages, gradually increasing its activity to other fields too

Our assessment of the "adequate" business position of Mizrahi Tefahot reflects the good positioning thereof in the local banking industry, as the third-largest bank in terms of assets. The bank's total asset was, as of the end of September 2018, approx. ILS 249 billion, and its market share in the local banking industry at such time was approx. 18.8% of the credit and approx. 16.2% of the deposits from the public.

Our assessment also reflects Mizrahi Tefahot's being a leading player in the field of residential credit, with a market share of approx. 33% of the mortgage inventory in the sector, and also its varied lines of business and customer base, which support the stability of the business and the visibility of the revenues. The bank has the highest exposure to the local housing market, and mortgages constitute approx. 65% of its total credit portfolio – a high rate in comparison to other local banks. Credit to households (including mortgages, other retail credit and private banking) constitute approx. 76% of the bank's credit to the public, with no significant change from previous years.

The rates of growth in the field of mortgages have slightly moderated in the past two years, mainly due to a decrease in demand pursuant to government plans for curbing prices in the residential real-estate sector and a decrease in the scope of the transactions on the free market. Concurrently, the competition in the sector from other banks is continuously increasing. In the first nine months of 2018 there was a 22% decrease in initiations of new mortgages versus the same period last year, such that total residential credit has grown by 4% in the first nine months of 2018 versus the same period last year. Even though it is difficult to foresee the development of housing prices, we estimate that the growth in the field of mortgages will continue, mainly due to continued demand for housing. At the same time we believe that Mizrahi Tefahot will aspire to maintain its leading position in the field of mortgages and is acting to increase its market share also in other fields in accordance with its strategic plan.

Based on the aforesaid plan, the bank is focusing on the fields of credit for small and medium businesses, business credit and non-collateralized retail credit. We believe that the bank may find it difficult to grow quickly in these sectors over time, in view of increasing competition from banks and non-banks players as one. The bank intends to deal with this competition by increasing marketing efforts and tailored customer approach. The bank operates in the field of credit to small and medium businesses also by expanding its activity in State-guaranteed funds.

Unlike its competitors, who act to reduce costs through reducing branches and manpower, Mizrahi Tefahot adopts the opposite strategy of growth in branches and of operating costs, while streamlining internal work procedures through the use of technology, opening smaller and more efficient branches and improvement of the output per employee. We believe that as long as the bank is growing in high rates and maintaining the narrow cost structure, it can allow itself an increase in operating expenses, while maintaining an efficiency ratio of approx. 55%, which is low compared to the market average.

We now estimate that there is a low likelihood of a merger with Union Bank, pursuant to the regulator's objection, but do believe that the bank will continue to act for the fulfillment of its strategic plan for growth in other operating segments also without the merger. We believe that the bank's management is experienced and can execute its strategic plans.

Table 2.

Mizrahi Tefahot Bank Ltd. Business Position (%)

	YTD Sep 2018	2017	2016	2015	2014
Total revenues from business line (Mil. ILS)	5,112	6,000	5,640	5,392	4,963
Commercial banking/total revenues from business line	37.26	38.68	37.73	37.85	39.40
Retail banking/total revenues from business line	52.69	54.87	54.31	52.30	54.97
Commercial & retail banking/total revenues from business line	89.95	93.55	92.04	90.15	94.37
Trading and sales income/total revenues from business line	10.05	6.45	7.96	9.85	5.53
Investment banking/total revenues from business line	10.05	6.45	7.96	9.85	5.53
Return on average common equity	9.52	10.20	10.31	10.02	10.58

Data are based on S&P Global Ratings adjusted number and ratios

Equity and profitability: uncertainty with regard to the effect of the arrangement vis-à-vis the US authorities

Our assessment of Mizrahi Tefahot's equity and profitability as "adequate" is based on our forecast that the RAC ratio before adjustments will be approx. 10% in the next 18-24 months, after being 9.2% in the end of 2017. Underlying the aforesaid forecast are several assumptions, including growth of approx. 4.0%-4.5% in the bank's credit portfolio in 2019-2020 and continued growth of operating expenses. The forecast increase in revenues, which is supported by the expected increase in the interest margins, will enable the bank, in our estimation, to maintain efficiency rates of 55% and less, better than the sector average. We assume that the expenses for credit loss will rise from the current level in the next 18-24 months, both at the bank and in the entire banking system, but will however remain reasonable. In the first nine months of 2018 the expenses to credit loss rate at the bank was 0.16%, and we estimate that it will rise to 0.20%-0.22% in the next two years.

We believe that Mizrahi Tefahot has the significant ability to create internal capital which constitutes a central source for capital accumulation. On the other hand, the bank operates with a spread of approx. 0.3% above the regulatory capital, which is low relative to other local banks, which fact, in our opinion, restricts the bank's flexibility to deal with unexpected scenarios. Thus, for example, the proposal for an arrangement with the US authorities that includes payment in the amount of $342 million at the end of Q2 2018, and the provision made pursuant thereto in the amount of $116 million, has led to a deviation from the required regulatory total capital ratio. The bank had to stop the dividend distribution and continued to take steps to increase the capital, including issuance of tier 2 capital instruments and continued sale of mortgage portfolios.

The bank's growth targets and diversification of business to other activity segments require ongoing streamlining in the allocation of risk assets which is also a result of the decision to maintain small capital margins. The main activity of the bank in this context is the sale of the credit risk to institutional investors, mainly risk that derives from the mortgage portfolio. We estimate that in the past three years the bank has sold housing loans in the amount of ILS 5 billion. It is our understanding that the bank intends to continue to manage its capital and risk assets in a proactive manner and, *inter alia*, continue to sell loan portfolios, and continue to arrange and lead other financial transactions together with others. In addition, the bank has purchased an insurance policy from international reinsurers with high credit ratings in order to cover guaranties that were given to new apartment owners in construction enterprises. As of March 31, 2018, the insurance covers 90% of all of the guaranties, which is equal to ILS 15.5 billion, which reduces the risk assets exposed to the real-estate segment.

It is our understanding that the bank intends to maintain the current gap above the regulatory capital requirement, and estimates that dividends will again be distributed during 2019. In our forecast for 2019-2020, we assume that the bank will make a provision for the entire amount that was proposed in the context of the arrangement with the US authorities and an increase in legal expenses and thereafter returning to distributing dividends. However, if the effect of the arrangement will significantly differ from our forecasts, it may affect the bank's capital adequacy.

Table 3.

Mizrahi Tefahot Bank Ltd. Capital and Earnings (%)

	YTD Sep 2018	2017	2016	2015	2014
Tier 1 capital ratio	10.11	10.20	10.10	9.50	9.05
S&P Global Ratings' RAC ratio before diversification	N/A	9.20	9.30	9.90	9.14
S&P Global Ratings' RAC ratio after diversification	N/A	7.80	7.88	9.04	8.47
Adjusted common equity/total adjusted capital	100.00	100.00	100.00	100.00	100.00
Net interest income/operating revenues	71.62	72.45	66.99	65.54	67.61
Fee income/operating revenues	21.34	23.72	25.41	26.45	27.94
Market-sensitive income/operating revenues	6.34	2.27	5.23	6.64	3.47
Noninterest expenses/operating revenues	53.75	60.18	58.49	59.83	60.88
Preprovision operating income/average assets	1.29	1.02	1.07	1.06	1.03
Core earnings/average managed assets	0.72	0.59	0.60	0.59	0.59

N/A – not applicable. Data are based on S&P Global Ratings adjusted number and ratios

Table 4.
Mizrahi Tefahot Bank Ltd. RACF [Risk-Adjusted Capital Framework] Data (Mil. ILS)

	EAD (1)	Basel III RWA (2)	Average Basel III RW (%)	S&P Global RWA	Average S&P Global RW (%)
Credit risk					
Government and central banks	52,134	1,453	3	555	1
Of which regional governments and local authorities	2,119	766	36	127	6
Institutions and CCPs	2,774	928	33	869	31
Corporate	54,041	46,679	86	64,553	119
Retail	138,943	76,482	55	60,482	44
Of which mortgage	120,079	62,265	52	44,043	37
Securitization (3)	0	0	0	0	0
Other assets (4)	5,699	4,355	76	8,795	154
Total credit risk	**253,590**	**129,897**	**51**	**135,253**	**53**
Credit valuation adjustment					
Total credit valuation adjustment	**--**	**529**	**--**	**0**	**--**
Equity in the banking book	99	99	100	865	874
Trading book market risk	--	1,605	--	2,407	--
Total market risk	**--**	**1,704**	**--**	**3,272**	**--**
Operational risk					
Total operational risk	**--**	**8,394**	**--**	**11,250**	**--**
Diversification adjustments					
RWA before diversification	--	140,586	--	149,776	100
Total Diversification/Concentration Adjustments	--	--	--	26,544	18
RWA after diversification	**--**	**140,586**	**--**	**176,319**	**118**

	Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global RAC ratio (%)
Capital ratio				
Capital ratio before adjustments	**14,333**	**10.2**	**13,777**	**9.2**
Capital ratio after adjustments‡	**14,333**	**10.2**	**13,777**	**7.8**

(1) EAD: Exposure At Default; (2) RWA: Risk-Weighted Assets; (3) Securitization Exposure includes the securitization tranches deducted from capital in the regulatory framework; (4) Other assets includes Deferred Tax Assets (DTAs) not deducted from ACE; (5) For Tier 1 ratio, adjustments are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons)

Risk profile: high exposure to the local residential real-estate sector

Our assessment of Mizrahi Tefahot's risk profile as "adequate" reflects the concentration of its exposure to the residential real-estate sector, which is high relative to its local competitors. This concentration continues to be the central risk factor for the bank exposing it to a risk of deterioration of the quality of the assets as a result of a significant increase in unemployment rate, economic slowdown and significant price correction.

The bank is exposed to the field of real-estate mainly through mortgages, but also through credit for financing of construction and development of real-estate. On September 30, 2018, such exposure was approx. 72% of the total credit to the public, much higher than local and global competitors. In this stage, the increase in prices of housing and related loans became more moderate, as a result of a combination of means that were instituted by the government and macro-stability steps that were instituted by the Bank of Israel which, in our opinion, helped to moderate the risk in high exposure to mortgages through limiting the LTV ratios, rates of monthly payment from available income and scope of the variable interest loan.

We estimate that the bank has a proper credit underwriting policy and good credit monitoring and control instruments for managing the risks deriving from its activity in real-estate credit. The average LTV of the bank's mortgage portfolio, as measured initiation of the loan, was 52.8% on September 30, 2018, and given the increase in housing prices in recent years and the current payments it is likely that, to date, the aforesaid ratio is lower. The average rate of the monthly payment from the available income is approx. 27%, and 82.8% of the mortgages in the portfolio were given to borrowers with a monthly payment rate below 35%. The bank's reduced appetite for continued accelerated growth in this credit segment, together with the cooling down of the residential real-estate market and the reduced increase in apartment prices contribute, in our estimation, to the management of the risk in this exposure. In addition, the increased margins increase the compensation to the bank for its exposure to such risk.

Loans for development and construction constitute approx. 9% of the bank's credit portfolio as of September 30, 2018, a rate that is low in comparison to local competitors. Recently there has been an increase in the number of contractors who suffered a decrease in profitability and financial problems however, the legal framework of the residential building sector, which includes guaranties that the banks give to the apartment buyers for a case of bankruptcy of the contractor, limits the bank's exposure to projects. Contractors are required to inject capital to projects and the bank's funding is given according to the progress of construction and marketing, such that in the event of the contractors' insolvency, the banks' losses are expected to be moderate. The transition to "Buyer's Price" (*Mehir Lamishtaken)* projects means that to date, many projects are sold in advance and in full. As aforesaid, the bank also insures the guaranties that are given in the context of a sale law which supports reducing the risk also. It is mainly exposed to developers, whose profitability is higher, and whose condition in the current low interest environment is still stable.

Due to the relatively small part of the business credit out of Mizrahi Tefahot's total portfolio, its structural exposure to a concentration of large borrowers is low relative to its competitors. In our estimation, the business credit concentration has dropped in recent years, in the entire sector and also at Mizrahi Tefahot. We estimate that the bank's exposure to the 20 large borrowers is low relative to the local competitors.

The bank is directing its growth to non-collateralized retail credit and business credit. We believe that competition from other banks and non-banks makes rapid growth in these segments, in which the bank is historically less active, difficult. Even though the margins in these segments are usually higher than in mortgages, it is likely that rapid growth will also result in an increase in credit loss expenses, from a low level of 0.12% in 2016 to 0.20%-0.22% in 2019-2020. However, we estimate that the average provision rates at the bank will continue to be low relative to the sector, with the support of stability in the field of residential real-estate.

The rate of problem loans (non-performing, undergoing restructuring and in arrears of more than 90 days) on the bank's balance sheet out of the total credit to the public was 1.16% on September 30, 2018, with no significant change from 2017, a level that is lower than average among the large local banks and relative to most of the global banks that operate in countries with similar economic risk. We attribute the low rate to the stable economic environment in Israel in recent years, and to the bank's low exposure relative to its local peers to the business segment that is less leveraged than the household segment. We estimate that the rate of problem credit will slightly rise above its current level in the next 18-24 months, to a level of more than 1% or so, but will remain at a level that is manageable and low compared to the competitors.

Mizrahi Tefahot's operating risks are material but are not unique thereto. They derive mainly from geopolitical tension in the area and from potential for damage in the event of a negative scenario, such as terrorist attacks or wars. These risks are reflected in our evaluation of the banking sector as a whole. We also expect that Israeli banks will be more exposed to cyber risks than banks in other countries, with a lower geopolitical risk.

Table 5.

Mizrahi Tefahot Bank Ltd. Risk Position (%)

	YTD Sep 2018	2017	2016	2015	2014
Growth in customer loans	6.45	5.75	7.57	7.84	6.44
Total managed assets/adjusted common equity (x)	16.64	17.39	18.02	17.55	18.53
New loan loss provisions/average customer loans	0.17	0.11	0.12	0.14	0.12
Net charge-offs/average customer loans	0.11	0.09	0.10	0.10	0.10
Gross nonperforming assets/customer loans + other real estate owned	1.16	1.02	0.95	1.14	1.19
Loan loss reserves/gross nonperforming assets	69.44	79.83	87.74	76.54	75.36

Funding & liquidity: 'average' funding and 'adequate' liquidity

Mizrahi Tefahot's financing profile is "average" and the liquidity situation is "adequate", in our estimation, similarly to these characteristics in the local banking sector in general. The financing profile of both the bank and the entire sector is stable, which we see as a strength in our BICRA assessment for Israel. We believe that the bank enjoys adequate liquidity, which is supported by a significant local financing basis, which includes retail deposits.

The bank relies mainly on deposits from local customers which, on September 30, 2018, were approx. 97% of the total deposits from the public. Household deposits were approx. 58% of the total deposits from the public, an increase of approx. 6% in the beginning of the year. Deposits from institutional customers were 20% of the total deposits from the public, and the business customers' deposits were approx. 22%. Mizrahi Tefahot is continuing its efforts to increase the share of household deposits and reduce the share of the institutional investors. Concurrently, the liquidity coverage ratio under Basel 3 rules has slightly increased in the first nine months of 2018 to a level of 125%, similarly to most of the local banks.

The bank's loans to deposits ratio was 98% on September 30, 2018, comparing to the sector range of 75%-85%. On that date, the liquid assets to short-term wholesale funding ratio was x4.34, a ratio which indicates low reliance on this type of financing, in the global comparison, but high, relative to other local banks. Wholesale funding, which is comprised of bonds and subordinated debentures, constituted approx. 13% of the bank's total liabilities on September 30, 2018. Wholesale funding is mostly for the longer term and linked to the consumer price index, which is appropriate for the bank's asset profile and provides certain hedging thereto against changes in the price index. Such hedging is especially important in view of the difficulty of increasing the scope of the index-linked deposits, while approx. one quarter of mortgages is linked to the price index, and therefore the bank is more exposed to inflation than its local competitors. The stable funding ratio as calculated by us was 111% relative to the sector range of 109%-131%. The bank has many liquid assets, that include cash, deposits in banks and the securities, and they constitute approx. 21% of the bank's total assets, as of September 30, 2018.

Table 6.
Mizrahi Tefahot Bank Ltd. Funding and Liquidity (%)

	YTD Sep 2018	2017	2016	2015	2014
Core deposits/funding base	86.38	85.54	86.16	86.68	87.33
Customer loans (net)/customer deposits	98.64	98.88	96.31	98.24	97.04
Long-term funding ratio	95.88	98.22	98.30	98.50	96.30
Stable funding ratio	111.18	114.78	116.47	113.43	110.81
Short-term wholesale funding/funding base	4.40	1.90	1.78	1.56	3.91
Broad liquid assets/short-term wholesale funding (x)	4.34	10.29	11.64	11.62	4.87
Net broad liquid assets/short-term customer deposits	21.25	25.84	27.54	23.94	21.66
Short-term wholesale funding/total wholesale funding	32.29	13.16	12.90	11.74	30.82

Data are based on S&P Global Ratings adjusted number and ratios

External support: one notch above the stand-alone credit profile (SACP) due to the potential of government support

The size of the local banking system relative to the size of the economy and the small number of banks are the reason that most of the banks in Israel are systemically important.

The bank's issuer rating is one notch higher than its stand-alone credit profile (SACP), which reflects its systemic importance in Israel and the government's "supportive" policy towards the local financial system. Consequently, we believe that the chances of unusual government support where necessary is quite high.

Additional factors affecting the rating: None

No further factors affected this rating.

Rating Adjustments

Business standing	Adequate
Equity and profitability	Adequate
Risk profile	Adequate
Financing and liquidity	Average and Adequate

Methodology and Related Articles

- Use Of CreditWatch And Outlooks; September 14, 2009
- Bank Rating Methodology; November 9, 2011
- Banking Industry Country Risk Assessment Methodology and Assumptions; November 9, 2011
- Quantitative Metrics for Rating Banks Globally: Methodology and Assumptions; July 17, 2013
- Methodology: Timelines of Payments: Grace Periods, Guarantees, And Use of 'D' and 'SD' Ratings; October 24, 2013
- Group Rating Methodology; November 19, 2013
- Bank Hybrid Capital and Nondeferrable Subordinated Debt Methodology and Assumptions; January 29, 2015
- Methodology For Linking Long-Term And Short-Term Ratings; April 7, 2017
- Risk-Adjusted Capital Framework Methodology; July 20, 2017
- S&P Global Ratings' Methodology For National And Regional Scale Credit Ratings; June 25, 2018
- S&P Global Ratings Definitions; October 31, 2018
- The Connection Between the Global Rating Scale and the Israeli Rating Scale; June 26, 2018

General details (as of January 7, 2019)	
Mizrahi Tefahot Bank Ltd	
Issuer Rating(s)	
Local rating – long term	ilAAA/Stable
Issuance rating(s)	
Complex subordinated debt	
Subordinated capital notes (upper Tier-II capital) A	ilA+
Contingent subordinated notes with loss absorbing capacity	ilAA-
Issuer rating history	
Long term	
December 23, 2014	ilAAA/Stable
November 15, 2010	ilAA+/Stable
September 14, 2009	ilAA+/Negative
May 28, 2007	ilAA+/Stable
October 01, 2003	ilAA+
Mizrahi Tefahot Issuing Company Ltd	
Issuance rating(s)	
Complex subordinated debt	
Contingent subordinated notes with loss absorbing capacity Series 47	ilAA-
Contingent subordinated notes with loss absorbing capacity Series 48	ilAA-
Senior unsecured debt	
Series 35, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46	ilAAA
Subordinated debt	
Subordinated debentures 31	ilAA+
Additional details	
Time of the event's occurrence	January 7, 2019 15:44
Time at which the event first became known	January 7, 2019 15:44
Rating initiator	The rated company

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