2016 Annual Report

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The Bank has received approval from the Supervisor of Banks to publish its annual financial statement on consolidated basis only.

Note 36 to the financial statements provides a summary of the Bank's solo financial statements.

A brochure providing Bank information is available on demand and on the Bank's website:
www.mizrahi-tefahot.co.il >> financial reports

Message from the Chairman of the Board of Directors

In the name of members of the Bank's Board of Directors, I am honored to present you with Mizrahi Tefahot's 2016 financial statements.

This year, too, the Bank maintained its growth momentum of recent years, with significant growth in various areas:

Thus, *inter alia*, compared to 2015 loans grew by 7.6%, deposits from the public grew by 9.8%, total assets grew by 10.2%, financing revenues from current operations grew by 10.4% and net profit reached a record NIS 1,266 million - an impressive 11.6% growth. Return on equity reached 10.2%, compared to 10.0% in the previous year - a noteworthy achievement given the 7.3% increase in the Bank's capital base, to NIS 12.7 billion. Concurrently, the Bank has achieved all of the required regulatory targets: Ratio of Tier I capital to risk elements increased to 10.1%, leverage ratio reached 5.27% and liquidity coverage ratio in the fourth quarter was at 117%.

Concurrently, the Bank continued to maintain control over expenses, with a moderate 2.3% growth in operating expenses, which resulted in further improvement of the Bank's cost-income ratio to 58.5% at the end of the year, compared to 59.8% at the end of 2015 – an outstanding positive figure even by international standards.

In 2016, too, the mortgage market was intensively active, although slightly less than in the previous year due, inter alia, to uncertainty with regard to the success of government measures and their impact on housing supply and prices. Mizrahi Tefahot continued to be the dominant, leading player in the market, adapting its pricing to the regulatory environment with strict adherence to quality underwriting processes and maintaining the portfolio's low risk profile.

It bears noting that continued growth and improvement across all operating areas are a remarkable achievement, given the macro-economic data for the economy in 2016 – extremely low interest rates and inflation and the complex regulatory and legislative environment in which the Bank operates.

Over the past year, the differentiation between Mizrahi Tefahot and other banks was further emphasized by the human, personal service concept promoted by the Bank. In 2016, the Bank continued to open new branches and at year end, Mizrahi Tefahot Group had 184 branches and affiliates, compared to 177 at end of 2015. As in the previous year, in 2016, too, the Bank opened two new branches in the Arab segment: in Baka El Gharbiya and in Kafr Kassem, based on an earlier resolution by the Board of Directors to significantly expand the Bank's physical presence in Arab cities and towns.

The Group's head count grew from 6,047 to 6,141, primarily in service-oriented positions at the Bank.

The Bank continued to develop advanced tools and operating channels, designed to improve the client experience and to reinforce the link between clients and their personal banker at the branch. This is part of Mizrahi Tefahot's unique Hybrid operating model, which strives to deploy technology for banking services not as replacement for branches and bankers – but rather as a complementary factor in aid of human service.

Consequently, and given streamlining measures by major competitors, in 2016 the bank successfully recruited tens of thousands of new clients - both individuals and businesses.

The Bank's growth strategy, designed for significant expansion of business across all operating segments with strict adherence to operating efficiency and controlled expenses, has helped Mizrahi Tefahot to establish itself as the third top bank in the Israeli banking system and as market leader with regard to retail credit, including housing loans.

After achieving most of the targets of the previous strategic plan and achieving regulatory targets for capital, leverage and liquidity coverage earlier than required, in November 2016 the Bank made public a new five-year strategic plan, which would be the platform for its continued growth and business development over coming years.

Along with retaining its leadership position in the retail segment in general – and in the mortgage market in particular – with a concerted effort to increase its share of potential demographics such as Jewish Orthodox, Arab and retirees, the Bank intends to enhance its business focus and to significantly expand its operations with all business segments: small, medium and corporate. To this end, the Bank increases the number of business bankers, develops specific marketing plans and IT systems, reinforces synergies between the Business Division and other divisions and reviews possible ways to increase cooperation with the institutional investor market.

Another growth engine for the Bank in coming years would be the leveraging of its infrastructure and abilities to provide banking operating services to other financial institutions. This involves, *inter alia*, providing operating services to provident funds, study funds and mutual funds, trustee services to institutional investors and cash transportation and cash center services. The goal is to turn the Bank into the key operator of financial assets and to significantly increase its share, as well as Bank revenues from these operating segments.

The 2017 work plan already reflects these objectives and I am certain that these changes would be reflected in our business results in coming years.

As a business organization whose activities and achievements depend on the community in which it operates, the Bank sees itself as obligated to show involvement in the community and to support populations with special needs.

As part of this effort, Bank branches and headquarters units conduct volunteer activities with various social organizations acting on behalf of children and youth in need. The Bank also conducts various endeavors to benefit populations in need. These activities are carried out with involvement of Bank employees, their families and even Bank clients.

The Bank continued to strictly maintain fair, transparent conduct vis-à-vis its clients and all stake holders, based on the Bank's values and Code of Ethics adopted as an integral part of our organizational culture.

I would like to take this opportunity to thank, myself and on behalf of all Board members, all stake holders at the Bank, primarily our loyal clients and to express our deep appreciation of Bank management and our thousands of dedicated, outstanding employees and managers for their tireless efforts, investment and significant contribution to the success of Mizrahi Tefahot.

Sincerely yours,

M. Vidman

Moshe Vidman
Chairman of the Board of Directors
Mizrahi Tefahot

Report of the Board of Directors and management

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List of tables included on the Report of the Board of Directors and Management

Report of the Board of Directors and management

Submitted to the General Meeting of Shareholders

At the meeting of the Board of Directors of Mizrahi Tefahot Bank held on March 20, 2017, it was resolved to approve and publish the Report of the Board of Directors and Management, the Risk Management Report and Other Supervisory Disclosures and the consolidated financial statements of Mizrahi Tefahot Bank Ltd. and its subsidiaries as of December 31, 2016.

Report of the Board of Directors and management,

Risks Report and Other Supervisory Disclosures of the Bank are prepared in conformity with directives of the Supervisor of Banks.

The Bank's financial statements are prepared in conformity with generally accepted accounting policies in Israel (Israeli GAAP) and in accordance with Public Reporting Directives of the Supervisor of Banks.

For most topics, the Supervisor of Banks' directives are based on generally acceptable accounting principles for US banks (see also Note 1 to these financial statements).

The Report of the Board of Directors and Management and the 2016 Financial Statements are prepared in conformity with the format stipulated by the Supervisor of Banks. After the Notes to the financial statements is a chapter on corporate governance, audit, other information about the Bank and its management and addendums to the annual financial statements.

Additional information to the financial statements is provided on the Bank website:

www.mizrahi-tefahot.co.il >> financial reports

This additional information includes:

- Detailed Risks Report in conformity with disclosure requirements of Basel Pillar 3 and in conformity with additional recommendations by the Financial Stability Board (FSB).
- Notes to the financial statements for the Bank solo, on demand.

The Bank website also includes additional supervisory information with details of capital instruments issued by the Bank.

Forward-Looking Information

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

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

Forward-looking information is characterized by the use of certain words or phrases, such as: "we believe", "expected", "forecasted", "estimating", "intending", "planning", "readying", "could change" and similar expressions, in addition to nouns, such as: "plan", "goals", "desire", "need", "could", "will be". These forward-looking information and expressions involve 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; changes and developments in the inter-currency markets and the capital markets, and other factors affecting the exposure to financial risks, changes in the financial strength of borrowers, the public’s preferences, legislation, supervisory regulations, the behavior of competitors, aspects related to the Bank’s image, technological developments and human resources issues.

The information presented here relies, inter alia, on publications of the Central Bureau of Statistics and the Ministry of Finance, on 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, so that there is a possibility that events or developments predicted to be reasonable would not material, in whole or in part.

Overview, targets and strategy

This Chapter describes the Bank, its lines of business, performance, risks to which it is exposed as well as its targets and strategy.

Condensed financial information and key performance indicators for the Bank Group

	For the year ended December 31,				
	2016	2015	2014	2013	2012
	NIS in millions				
Statement of profit and loss – highlights					
Interest revenues, net	3,778	3,534	3,375	3,464	3,214
Non-interest financing revenues	295	358	173	14	95
Commissions and other revenues	1,567	1,500	1,439	1,485	1,478
Total revenues	5,640	5,392	4,987	4,963	4,787
Expenses with respect to credit losses	200	211	173	288	276
Operating and other expenses	3,299	3,226	3,039	2,951	2,807
Of which: Payroll and associated expenses	2,071	1,944	1,866	1,823	1,704
Pre-tax profit	2,141	1,955	1,775	1,724	1,704
Provision for taxes on profit	833	761	657	593	594
Net profit(1)	1,266	1,134	1,092	1,083	1,060

Net profit for the Group in 2016 amounted to NIS 1,266 million, compared to NIS 1,134 million in the previous year – an increase of 11.6%, which is higher than growth for the balance sheet as a whole for the period (10.2%).

The following key factors affected Group profit in 2016, compared to 2015:

- Total revenues increased in 2016 by 4.6% compared to 2015.
  The higher revenues were due to business growth, despite the effects of the low interest and inflation environment and various regulatory provisions, primarily with regard to commissions.
- Operating expense level maintained (increased by only 2.3% in 2016 over the previous year).

Multi-period profit data shows:

- Continuous, constant growth in Bank revenues.
- Operating expenses under control, along with high-quality efficiency ratios.
- Consistent growth in Bank net profit year over year.

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

	As of December 31				
	2016	2015	2014	2013	2012
	NIS in millions				
Balance sheet – key items					
Balance sheet total	230,455	209,158	198,513	179,545	162,132
Loans to the public, net	171,341	159,204	147,569	138,565	128,651
Cash and deposits with banks	41,725	30,489	26,798	26,060	16,671
Securities	10,262	11,845	14,259	7,000	9,041
Deposits from the public	178,252	162,380	152,379	141,244	128,081
Debentures and subordinated notes	27,034	23,719	20,580	16,443	14,039
Deposits from banks	1,537	1,166	1,258	2,041	1,694
Shareholders' equity(1)	12,714	11,847	10,797	9,681	8,730

Total assets for the Bank as of December 31, 2016 amounted to NIS 230.5 billion – an increase of NIS 21.3 billion or 10.2%.

Loans to the public, net as of December 31, 2016 amounted to NIS 171.3 billion – an increase of NIS 12.1 billion or 7.6%.

Deposits from the public as of December 31, 2016 amounted to NIS 178.3 billion – an increase of NIS 15.9 billion or 9.8%.

Shareholder equity as of December 31, 2016 amounted to NIS 12.7 billion – an increase of NIS 0.9 billion or 7.3%.

Data from the multi-period balance sheet show constant growth in Bank operations.
Average annual growth between 2012-2016:

Total assets	9.2%
Loans to the public, net	7.4%
Deposits from the public	8.6%
Shareholders' equity	9.9%

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

Key financial ratios (in percent)

	2016	2015	2014	2013	2012
Key performance benchmarks					
Net profit return on equity(1)	10.2	10.0	10.6	11.8	13.0
Net profit return on risk assets(2)	0.97	0.89	0.91	0.98	1.01
Deposits from the public to loans to the public, net	104.0	102.0	103.3	101.9	99.6
Ratio of Tier I equity to risk elements(3)	10.10	9.50	9.05	8.94	8.55
Leverage ratio(4)	5.27	5.32	–	–	–
(Quarterly) liquidity coverage ratio(5)	117	91	–	–	–
Cost income ratio(6)	58.5	59.8	60.9	59.5	58.6
Basic earnings per share (in NIS)	5.46	4.90	4.74	4.74	4.70
Key credit quality benchmarks					
Ratio of provision for credit losses to total loans to the public	0.83	0.87	0.90	0.94	1.22
Ratio of impaired debt or debt in arrears 90 days or longer to total loans to the public	0.98	1.14	1.20	1.70	2.55
Additional information					
Share price (in NIS) as of December 31	56.35	46.50	40.90	45.44	38.49
Dividends per share (in Agorot)	80	37	–	33	–
Number of branches for the Group	184	177	176	177	175
Number of employees for the Group	6,141	6,047	5,864	5,820	5,670

Financial ratios indicate:

- In 2016, net profit return increased compared to 2015, to reach 10.2%.

  Return over the past 5 years was in double digits, given a 46% increase in capital (NIS 12.7 billion in 2016, compared to NIS 8.7 billion in 2012).
- The Bank's cost income ratio improved to 58.5% in 2016. This ratio is in line with best-in-class international standards for operating efficiency.
- The Bank is compliant with regulatory targets required for capital adequacy, liquidity coverage and leverage.
- Dividends per share increased significantly in 2016, with distributions amounting to NIS 186 million, or NIS 0.80 per share. In 2016, the Bank applied the dividend distribution policy set by the Board of Directors and distributed in each quarter 15% of the previous quarter's profit.
- Credit quality benchmarks continue to improve, showing a low level of problematic debts and credit losses.
- The number of Bank branches and employees increased in 2016. This is in line with the Bank's growth strategy with emphasis on the human factor in banking service.

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) Any mention of "net profit" or "equity" in this Board of Directors' Report refers to net profit and equity attributable to shareholders of the Bank.
(2) Net profit to average risk assets.
(3) Calculated in conformity with Basel III directives as from 2014.
(4) Leverage Ratio – ratio of Tier I capital, according to Basel rules, to total exposure. This ratio is calculated in conformity with Proper Banking Conduct Directive 218
(5) Liquidity Coverage Ratio – ratio of total High-Quality Liquid Assets to net cash outflow. This ratio is calculated in conformity with Proper Banking Conduct Directive 221, in terms of simple averages of daily observations during the reported quarter.
(6) Total operating and other expenses to total operating and financing revenues before expenses with respect to credit losses.

Bank Group and its lines of business

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

The Bank Group operates in Israel and overseas. The Bank Group is engaged in commercial banking (business and retail) as well as mortgage activities in Israel, through a nation-wide network of 184 branches and business centers. Furthermore, business clients are supported by business centers and professional departments at Bank headquarters, which specialize by sector. The Bank's overseas operations are conducted via 3 bank affiliates (two branches and a subsidiary) and 3 representative offices in Europe and Latin America.

In addition to its banking activities, the Bank Group is engaged in various activities related to the capital market, including: Consultancy for capital market activities, management of securities portfolios for clients, pension advisory service, trust services, distribution of mutual funds, operation of provident funds and insurance incidental to mortgages. The Bank Group also engages in credit operation and participated in syndication deals.

The Bank is one of the five largest bank groups in Israel. Below is the Bank Group share out of the Top 5 groups (based on financial statements as of September 30, 2016):

Loans to the public	18.2%
Deposits from the public (1)	15.7%
Total assets	15.7%
Shareholders' equity	12.8%

(1) The Bank Group's share of deposits from the public, among the five top bank groups, excluding deposits from institutional investors, as of September 30, 2016 was 14.6%, compared to 13.8% as of December 31, 2015.

Major risks

In its operations, the Bank is exposed to a succession of risks which may potentially impact its financial results and Bank reputation.

The Bank conducts a structured process, at least once a year, for mapping the risks to which the Bank is exposed in the course of its business operations. This list is dynamically updated by new activities by the Bank or due to new or revised regulation. The risks mapping is approved by management and by the Board of Directors and each risk is classified as material or non-material, based on the materiality threshold specified by the Board of Directors. This threshold is given in terms of the Bank's capital. A Risk manager is assigned to each material risk and the framework for handling such risk is incorporated in a specific policies document, approved, at least once a year, by the Bank management and Board of Directors. The policies document stipulates how risk is to be managed, how the risk is to be measured, the required reports with regard to it and its mitigation. In particular, the Board of Directors specifies the risk appetite, i.e. the allowed exposure cap for each risk. During the year, Bank units in the various lines of defense monitor the risk profile, to ensure that risk does not deviate from the specified risk appetite. This monitoring uses a wide range of benchmarks specified, which review how close the risk profile is to the specified risk appetite and is conducted as part of the Bank's quarterly Risks Document, which is approved by management and by the Board of Directors. A report is submitted whenever any risk benchmark is getting close to the risk appetite and, definitely, in case of deviation from the Bank's risk appetite. In general, Bank management has zero risk appetite for deviation from risk restrictions specified by the Board of Directors.

As part of the risk mapping, the Bank reviews the top risks, existing (or new) risks which may materialize over the coming 12 months which potentially may materially impact the Bank's financial results and stability, such as: credit, interest and liquidity risk. The Bank also identifies emerging risks, which may materialize over the longer term and subject to uncertainty with regard to their nature and impact on the organization. Of these risks, one may note the following: information security and cyber risks, IT risk, reputation risk as well as compliance and regulatory risks. As noted, the risks mapping is regularly reviewed to ensure that it encompasses all business operations at the Bank, market conditions and regulatory requirements.

Below are definitions of the major risks to which the Bank is exposed in conjunction with its operations:

Credit risk – the risk that a borrower or counter-party of the Bank would not fulfill its obligations towards the Bank. Credit concentration risk is due to over-exposure to a borrower / borrower group and to economic sectors.

Market risk – This is the risk of loss in 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).

Interest risk – The risk to Bank profit (change in revenues) or 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).

Liquidity risk – The risk to profit and stability of the banking corporation, due to its inability to satisfy its liquidity requirements.

Operating risk – The risk of loss due to inappropriateness or failure of internal processes, people and systems or due to external events. This risk is inherent in all products, activities, processes and systems. The framework for addressing operating risk also includes addressing of legal risk, defined in Proper Banking Conduct Directive 350 concerning "Operating risk" as "including, *inter alia*, exposure to fines or penalties arising from supervisory action, as well as from individual arrangements".

Information security and cyber risk – Information security risk is risk arising from faults in protection of the Bank's computer systems and information stored there. Cyber risk arises from an event including an attack on computer systems by or on behalf of internal or external adversaries of the Bank.

IT risk – the risk of failure in the Bank's information and/or IT and operating systems.

Legal risk – Risk of loss due to exposure to fines, lawsuits and/or punitive action due to breach of contract or disagreements. Legal risk includes risks arising from legal exposure due to Bank conduct with its various interested parties (such as: clients, suppliers and other third parties).

Compliance and regulatory risk – The risk of imposition of legal or regulatory sanctions, material financial loss or damage to reputation, which the Bank may incur due to its failure to comply with compliance provisions (such as: statutory provisions, regulation, standards and conduct commonly expected from a corporation). The Bank is also exposed to business implications of changes to regulatory provisions.

Cross-border risk – The risk of financial loss (including due to legal proceedings, fines or sanctions imposed by statutory authorities or others in Israel and in other countries) and of damage to reputation, arising from the Bank's failure to comply with statutory provisions originating in other countries – whether provisions are binding on the Bank or provisions which are not binding, but failure to comply with them may cause the Bank to incur damage, or from overseas activities of Bank clients in contravention of any statutory provisions.

AML risk – The risk of imposition of legal or regulatory sanctions, of material financial loss or of damage to reputation and image, which the Bank may incur due to non-compliance with AML and terror financing provisions.

Reputation risk – the risk to corporate profit, stability or capacity to achieve its objectives, due to impact to reputation which may arise from practices applied by the corporation, its financial standing or negative publicity (whether true or false).

Strategic business risk – 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.

Business goals and strategy

The strategic plan

On July 23, 2012 the Bank's Board of Directors approved a strategic plan for 2013-2017 (hereinafter: "the original strategic plan").

On December 23, 2014, the Bank's Board of Directors resolved to update the original strategic plan, due to changes to certain underlying assumptions of the original strategic plan, including the effect of new regulations and of macro-economic conditions.

Given the Bank's achievements and changes to the macro-economic environment in Israel, on November 21, 2016 the Bank's Board of Directors approved a new five-year plan for 2017-2021 (hereinafter: "the new strategic plan"). The new strategic plan is designed to achieve the following targets:

- Achieve in 2021, net return on profit attributable to equity holders of 11.5% on average and double-digit return over the term of the new strategic plan; these rates are based on the ratio of Tier I capital to risk elements for the Bank at the minimum set by the Supervisor of Banks plus appropriate margin;
- Further organic growth of core Bank operations, at a higher rate than for the Israeli banking system, so as to increase the Bank's market share in the Israeli banking system.

  The Bank's growth engines are aimed to grow Bank profitability due, inter alia, to average annual revenue growth rate of 8% (though not in linear fashion), while maintaining expenses at a moderate annual growth rate of 6% (also not in linear fashion).
- Maintain high operating efficiency – achieve a cost-income ratio (total expenses to total revenues) lower than 60% over the plan term and even attempt to improve it to below 55% in 2021.

Guidelines for achieving strategic plan targets

The Bank based the new strategic plan on the following targets:

- Increase focus and expand public loans and deposits in the business segments, based on the following supporting steps:
  - Rely on the branch network, further expanding it and the number of business bankers, leveraging the experience, knowledge and expertise accumulated by the Bank in recent years;
  - Develop custom marketing plan and IT systems;
  - Co-operate with institutional investors and leverage mutual funds for businesses;

- Maintain and establish the Bank's leadership position in retail banking, based on the following efforts:
  - Maintain leadership position in the mortgage market and leverage it to intensify commercial operations;
  - Focus on high-quality clients and target specific segments, such as the Arab segment, Jewish Orthodox segment and retirees.
  - Further reinforce the synergy with Bank Yahav for a two-pronged strategy: service-oriented and price-oriented;
  - Provide personal, human service supported by innovative technology and significant improvement in the client service experience;

  For more information about developments in credit risk to individuals (housing and non-housing) and Bank action with regard to such risk, see chapter "Risks Overview" below.
- Turn the Bank into a central operator of financial assets in the banking system, by investing effort in expanding the use of infrastructure so as to utilize the Group's capacity to provide service to other financial institutions, such as operating provident funds, study funds, mutual funds, IT services etc.

- Maintain high operating efficiency by investing effort in the following:
  - Promote an organizational culture supporting efficiency and improved efficiency;
  - Transfer activities from branches to back-office operations while providing more efficient operating solutions;
  - Maintain stable long-term labor relations;

In addition, on November 21, 2016 the Bank’s Board of Directors approved a revised policy on dividend distribution, effective as from 2017. For more information about the revised policy and dividend distributions, see chapter "Analysis of development of assets, liabilities, capital and capital adequacy" below.

The aforementioned new strategic plan is a strategic plan which specifies Bank objectives for 2017-2021 and does not constitute a forecast, estimate or assessment with regard to achievement of these objectives; as such, by its nature, the strategic plan may not materialize.

Moreover and without derogating from the generality of the aforesaid, in as much as this plan includes forward-looking information, as defined in the Securities Act, 1968, this information is based on assumptions, facts and data (hereinafter jointly: "assumptions") brought before the Bank’s Board of Directors, including: Absence of any further changes to legislation and to regulatory provisions which may impact the business environment; absence of developments and changes to the geo-political situation which may impact or harm the business environment; the interest environment in the Israeli economy remaining at its current level with annual inflation at 0.5%; stable economic environment – Israel's economy would grow in the next few years at an average annualized 2.5%.

These assumptions may fail to materialize due to factors other than under the Bank's control, which may affect the aforementioned issues and cause the new strategic plan, as described above, not to materialize.

For more information, see Immediate Reports dated November 22, 2016 (references 2016-01-080631 and 2016-01-080628). These mentions constitute inclusion by way of reference of all information provided in the aforementioned Immediate Reports.

The Bank’s Board of Directors will monitor execution of the new strategic plan, and may make changes to this plan from time to time, as required, including due to changes in factors which may affect the plan, as described above.

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

Significant developments in business activities

The mortgage market continued to expand in 2016, with housing loans in the banking system lower than in 2015 but higher compared to previous years. The Bank is acting to reinforce its leadership position in the mortgage market in terms of market share and in perception and further reinforce the expertise of mortgage bankers. Over the past year, the Bank succeeded in increasing its market share, while maintaining low risk attributes for LTV and repayment ratio out of borrower income.

The household segment is in the midst of growing competition, both from the banking system and from insurance companies and credit card companies – along with increased regulatory effects. On January 27, 2017, the Increased Competition and Reduced Concentration in Israeli Banking Act was enacted. The objective of this Act is to increase competition in retail banking services, with reference to both supply (adding new players) and demand (increasing consumer capacity to compare the costs of financial services). The Committee's vision of competition is defined by creating a more efficient market along with cost cutting for the economy, simplified competition for consumers and more diverse sources of credit and financial services offered to consumers.

The Bank's target is to increase its market share in the household segment, by expanding the client base with a focus on high-quality target audiences. Regulatory steps to increase competition in the household segment and to remove barriers to account transfer between banks – are an opportunity for increased client recruitment, based on the unique, high-quality personal service provided by the Bank. In this context, the Bank used hybrid banking platform and the LIVE branches to recruit new clients and improve service to current clients, while expanding the value proposition.

The mortgage client base at the Bank is potential ground for increasing the client base in commercial activity – and Bank Yahav clients are reinforcement for the retail segment activity of the Group. The Bank also strives to expand in new client segments, including the Arab segment.

The Bank is focusing its effort on getting deposits from retail clients and from business clients, in order to improve the Bank's liquidity coverage ratio and in order to reduce the cost of sources required for its operations, leading to improved profitability. These efforts resulted in the Bank continuing to significantly increase the scope of retail and business deposits in 2016, with a significant increase in the liquidity coverage ratio.

The Bank's business strategy emphasizes significant expansion of the client base and increase of the Bank's market share among small to medium business clients, with regular risk assessment at client level, at sector level and for the economy as a whole. The Bank addresses growing competition in these operating segments by increased marketing activities with clients, with client segmentation by type of occupation and needs and an overall view of their activities, as well as by expanding Bank activity in the State fund for small and medium businesses. In order to expand activity in the commercial banking segment, the Bank reorganized this activity under three business hubs. This infrastructure would support further expansion of operations in this segment in coming years.

Competition for provision of banking and financial services to the business banking segment has been affected in recent years by expanded operations of institutional investors and insurance companies, which are focused on providing large-scale credit for long terms. The Bank is facing competition in this segment by relying on the advantages of its human resources and on their knowledge and experience in providing professional service and in adapting banking solutions for client needs. The Bank's business strategy in this segment is directed toward maximizing the economic potential of the capital by focusing on activities having high profitability relative to the capital needed for them, Concurrently, the Bank is acting to leverage its professional advantage by increased cooperation in consortiums with other entities.

In order to maximize the economic potential of capital, in 2016 the Bank sold loan portfolios to various institutional investors. For more information see chapter "Significant Events in the Bank Group's Business" below.

The Bank continues to maintain high operating efficiency through, *inter alia*, reorganization of assets and optimization of the branch network, including opening new branches in locations with potential for business growth – along with streamlining the existing branch network.

For more information see chapter "Significant developments in management of Bank business" below.

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Developments in capital structure

Investments in Bank Capital and Transactions in Bank Shares

The Bank holds 2,500,000 Bank shares as dormant shares bought back in 2009, as approved by the Bank of Israel.

On June 2, 2014, the Bank applied to the Supervisor of Banks for approval of a potential buy-back of 5 million Bank shares. Buy-back of Bank shares is tantamount to a dividend distribution. See Note 24 to the financial statements for additional information.

For more information about share issuance in conjunction with the employee stock option plan, see statement of changes to shareholder equity.

For more information about changes to the control structure at the Bank, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" (Controlling shareholders) on these financial statements.

Raising of capital sources

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

The plan includes issue of contingent subordinated notes (Contingent Convertibles – CoCo) as needed and should ensure that the overall capital ratio as from 2017 would be at least 13.4%.

Developments in financing sources

Group financing sources include deposits from the public and from other banks, issuance of debentures as well as shareholder equity. The Group selects the mix of financing sources based on its business objectives, including objectives for profitability, return on equity, liquidity, capital adequacy and leverage – subject to statutory limitations applicable to banking corporations and in accordance with the state of the capital market and management forecasts regarding development therein.

Deposits

The Bank distinguishes between different source types by size, client type, individual depositor, number of clients, product and average deposit term. The Bank reviews, on daily basis, the depositor concentration level and in this regard, the Board of Directors and management have set restrictions and guidelines for concentration risk and have defined qualitative and quantitative indicators for on-going monitoring and estimation of the change to concentration risk, as part of the liquidity risk management system.

Total deposits from the public for the Group as of December 31, 2016 amounted to NIS 178.3 billion, compared to NIS 162.4 billion at end of 2015: an increase of 9.8%. Deposits from the public in the NIS-denominated, non-CPI linked segment increased in 2016 by 12.4%; deposits in the CPI-linked segment increased by 1.6%; and deposits denominated in or linked to foreign currency increased by 5.7%. For more information see chapter "Analysis of composition of assets, liabilities, capital and capital adequacy" below.

Bank of Israel

The Bank of Israel serves as a key party for the short-term financing and absorption of money for the entire banking system, and for the Bank in particular. It should be noted that a bank that borrows money from the Bank of Israel must provide collateral, and the Bank takes this parameter into account in its day-to-day management of liquidity.

Another source for raising short-term funds is the inter-bank money market. In 2016, the banking system and the Bank had high excess liquidity and therefore use of this tool was negligible.

Among the factors influencing the scope and types of deposits in the banking system are the monetary policies of the Bank of Israel.

Below is a survey of the monetary tools used by the Bank of Israel for the purpose of implementing its monetary policies:

Bank of Israel interest rate – The Bank of Israel publishes periodically the interest rate for the following period. This interest constitutes the base interest rate for tenders on loans and deposits made available to the banking system, as will be provided below. Note, in this regard, that the Monetary Committee of the Bank of Israel has announced that as from 2017, the frequency of interest rate decisions would be reduced to 8 times a year, instead of 12.

Liquidity requirement – The directives of the Bank of Israel require banks to hold liquid balances for deposits from the public, at varying percentages, according to the period of the deposit. The required liquidity percentages are presently 6% on demand deposits and 3% on time deposits of one week to one year. As to deposits for periods of one year or more, there is no liquidity requirement. For more information about liquidity risks management by the bank, see chapter "Risks overview" below and the Detailed Risks Management Report on the Bank website.

Deposits with Bank of Israel to absorb excess liquidity – When there is excess liquidity in the system, the Bank of Israel absorbs it through tenders on deposits that it makes available to the banking system. The deposit tenders are for a short term of 1or 7 days. The maximum interest rate for these tenders is the stated interest rate of the Bank of Israel. Moreover, there is a window for depositing daily deposits in the Bank of Israel, unlimited in amount, at interest that is 0.10% lower than the Bank of Israel interest rate. In 2016, the banking system – including the Bank – had excess liquidity, and throughout the year, the Bank of Israel offered deposit tenders for terms of one day / week . month in order to absorb this excess.

Short-term Government loans (MAKAM) – The principal financial instrument used to absorb surplus shekel liquidity is the short-term Government loan (MAKAM), through regular issuances to the public and the activity of the Bank of Israel in the secondary market. In 2016, the Bank of Israel issued MAKAM series equal or lower in amount than series reaching maturity, so the total outstanding MAKAM balance held by the public at the end of 2016 was lower by NIS 11 billion compared to the balance at the end of the previous year.

Tools for enhancing system liquidity – For the purpose of injecting liquidity into the banking system, the Bank of Israel makes available short-term credit tenders for 1-7 days, in which the minimum interest is the Bank of Israel interest. Moreover, the Bank of Israel provides a daily credit window at interest that is 0.10% higher than the Bank of Israel interest. Receipt of credit from the Bank of Israel, whether through the credit tender or the credit window, is limited to the collateral amount that each bank has in the Bank of Israel. In 2016, the banking system and the Bank had excess liquidity – and the Bank of Israel had no need to conduct any credit tenders.

Obligatory notes and debentures issued to the public

The Bank is acting to raise long-term sources via issuances, inter alia via Mizrahi Tefahot Issuance Company Ltd. ("Tefahot Issue"), a wholly-owned subsidiary of the Bank. Over the years, Tefahot Issue Company issued subordinated notes to the public under published prospectuses.

As of the balance sheet date, all obligatory notes, including subordinated notes, issued to the public by Tefahot Issuance, amounted to NIS 22.6 billion in total par value (as of December 31, 2015: NIS 19.8 billion), of which NIS 1.9 billion in subordinated notes (included in Tier II capital for maintaining minimum capital ratio and gradually reduced subject to transition provisions).

In 2016, Mizrahi Tefahot Issuance issued debentures amounting to NIS 5.8 billion par value for consideration of NIS 6.1 billion.

For more information about a prospectus to the public issued by Tefahot Issuance on July 4, 2016 (dated July 5, 2016), see chapter "Significant Events in the Bank Group's Business" below.

For more information about a prospectus to the public issued by Bank Mizrahi-Tefahot on September 25, 2016 (dated September 26, 2016), see chapter "Significant Events in the Bank Group's Business" below.

Complex capital instruments

In December 2015 and in January 2016, the Bank issued contingent subordinated notes (Contingent Convertibles – CoCo) with loss-absorption provisions through principal write-off, amounting to NIS 0.6 billion. These notes qualify pursuant to Basel III provisions and recognized by the supervisor of Banks as Tier II capital.

Standard & Poor's Ma'alot rated the contingent subordinated notes ilAA-.

In July 2016, Bank Yahav issued contingent subordinated notes (Contingent Convertibles – Coco) with loss-absorption provisions through principal write-off, amounting to NIS 0.2 billion.

These notes qualify for recognition as Tier II equity pursuant to Basel III provisions.

In November 2006, the Bank raised, in a private placement with institutional investors, NIS 0.5 billion though issuance of subordinated notes. On May 21, 2007 the Bank published a prospectus under which the complex capital instruments were listed for trading in early June 2007. In total, the Bank issued and listed for trading additional complex capital instruments under the prospectus amounting to NIS 1.2 billion.

All of the Bank's complex capital instruments as of December 31, 2016, issued and listed for trading amounted to NIS 1.7 billion.

The complex equity instruments are included in Tier II capital but do not qualify as supervisory capital pursuant to Basel III directives – and are therefore gradually reduced in conformity with transitional provisions.

The revalued balance of the complex capital instruments, including contingent subordinated notes, as of December 31, 2016 was NIS 2.8 billion (of which NIS 0.8 billion in contingent subordinated CoCo notes), compared to NIS 2.4 billion as of December 31, 2015 (of which NIS 0.4 billion in contingent subordinated CoCo notes). See Note 25 to the financial statements for details.

Significant developments in management of business operations

Branch deployment

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

Group branches are located nationwide, consisting of 184 business centers, branches and affiliates, including 45 Bank Yahav branches – as of December 31, 2016.

The Bank continues to expand its branch network in accordance with its strategic plan, with location selection based on considerations such as providing optimal service to clients, economic viability considerations etc.

In 2016, the Bank opened 7 new points of sale and relocated several others to better geographic locations, following the mapping of bank client needs and in order to improve service to clients and expand future recruitment activity. In 2017, the Bank is expected to open 4 more points of sale.

As part of the strategy designed to increase Bank market share in the Arab sector, the Bank opened two branches in Arab towns in 2016. The Bank is reviewing other expansion options.

The Bank operates a unique service – the LIVE branches – which are branches providing full personalized service during extended business hours using a range of communication channels between clients and bankers (via telephone, fax, internet, email, SMS, video conferencing). As of the publication date of these financial statements, the Bank operates 6 LIVE branches.

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Direct channels

The policy applied by the Direct Banking sector concerning direct channels is as follows:

- Apply a multi-channel strategy, at the center of which stands the branch, and direct banking services constitute an integral part thereof.
- Develop Hybrid Banking as a primary channel for contacting your banker by telephone, email and SMS for the commercial banking and mortgage segments.
- Expand the range and diversity of services provided through direct banking channels (telephone, on line, cell phone, self-service stations and ATMs) and expand the use thereof.

Direct channels offered to Bank clients include:

Hybrid Banking services

Hybrid Banking is about integrating personal service accessible to clients with technology – telephone, email and SMS.

Hybrid Banking services are provided by Bank branches and banking centers, as follows:

- Bank branches – phone calls, emails and SMS messages from identified clients are directly routed to that client's banker and are answered by the banker or by the backup staff at the branch.
- Banking center – the branch team at the banking center provides backup to branch bankers, assisting with transactions and providing information to Bank clients, as part of the integrated Hybrid service offered to clients. Service is provided 24 hours a day (on weekdays).

  In 2016, the Bank extended its Hybrid Banking service to business clients at the banking center.
- In 2016, the chat option was launched – correspondence with clients interested in a mortgage and with clients interested in deposits.

  The Bank also established desks in lending operations to initially address references from marketers, purchase groups, specializing in internal refinancing and service to foreign residents.
- In 2017, the Bank is expected to intensify the mortgage refinancing operations for commercial clients, activities designed to prevent churn, reactivation of open but inactive accounts and will improve performance across its operations by better interfacing with Bank branches.

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On line, cell phone, notification box, IVR and fax services

On line service – allows clients to receive banking information and execute transactions in your account for a range of banking products available to Bank clients at a reduced cost.

In 2016, the Bank launched a new website for mortgages and launched the app "Tefahot to Home".

In 2017, the Bank expects it would expand its service to business clients and international operations.

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Self-service at branches

- Service stations – Mizrahi-Tefahot provides clients with service stations which allow them to conduct transactions and obtain information about accounts in the commercial sector and in the mortgage sector – using self-service, 24 hours a day – even when the branch is closed. Some of the service stations also offer immediate checkbook printing.
- In 2017, the Bank would consider the option of cash deposits using service stations.
- ATMs - The Bank owns 197 cash withdrawal machines, some in Bank branches and some are "remote ATMs".

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Expansion of business operations

For more information about the Bank's strategic plan, see chapter "Business goals and strategy" above.

Management of deposit funds for overseas workers

On December 30, 2015, the Bank was informed it was awarded a tender issued by the State of Israel for management of deposit funds for foreign workers. In 2016, the Bank started offering the special deposit in conformity with conditions specified in the agreement. As of December 31, 2016, deposits under management amounted to NIS 343 million. For more information see chapter "Household segment" below.

Small business tender

On January 17, 2016, the Ministry of Finance announced that the financial partnership between Bank Mizrahi Tefahot and other companies was selected as a winning bidder for the tender to provide loans to small and medium businesses, as part of the new fund guaranteed by the State. The new fund started operations in May 2016. For more information see chapter "Micro and small business segment" below.

Savings account for every child

On August 5, 2015, the Government adopted a resolution on "Change in composition of child allowance and launch of long-term savings for every child".

On September 26, 2016, the Comptroller General Division of the Ministry of Finance issued a call for proposals to select banks and provident funds to manage these savings accounts.

The Bank submitted its proposal and on November 9, 2016, the Bank was informed that it was selected to be one of the financial institutions which in future would manage these long-term savings accounts.

In early 2017, the Bank launched the operation and started receiving deposited funds for clients who had chosen the Bank.

Expansion of the operations center

The Bank is acting to develop and expand the banking centers at the operations center in the Technology Center in Lod, along with expanding the branch network and adapting it to changing requirements. This action is part of a multi-annual plan to transition back-office operations from branches to the back-office system and expanding it by diverting simple in-person activities using the telephone channel to telephone service centers, while freeing up time at branches for sales, marketing and complex advisory activities.

This move results in significant operating flexibility, due to economies of scale in operations centers, various reductions in work processes and process automation along with the transition to back-office centers.

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Strategic cooperations

In 2016, the Bank continued to conduct transactions to sell off and share credit risk with institutional investors and financial institutions in Israel and overseas. Further co-operation with institutional investors is part of the Bank's strategic plan for 2017-2021.

As part of this activity, the Bank has significantly expanded service provision for operating financial assets, including management and operation of housing loans purchased from the Bank.

For more information about sale of rights and obligations in the mortgage portfolio (80% of a housing loan portfolio amounting to NIS 1,788 thousand), acquiring an insurance policy to cover 80% of guarantees amounting to NIS 15.5 billion and other cooperations, see above and in chapter "Significant Events in the Bank Group's Business" below.

For more information about business results of the various operating segments, see chapter "Supervisory operating segments" below.

Significant developments in marketing

The Bank's marketing operations and marketing strategy are derived from the Bank's strategic plan. Distribution channels used by the Bank to base the strategic plan, include: the nation-wide branch network, business centers, business hubs, the banking center, professional headquarters units and LIVE branches.

Business strategy and growth targets:

– Increase the Bank's share of the retail market, by expansion of the customer base, growing the total number of customers in the Bank's household segment, while focusing on profitable target groups.
– Increase the Bank's share and the number of small to medium business clients.
– Continue to lead the mortgage market in terms of market share and in perception and further reinforce the expertise of mortgage bankers.
– Recruit new deposits and increase investment activities among existing clients.
– Effectively maximize share of Bank clients and increase total products per client.
– Expand operations to new operating segments – including the Arab segment, Jewish orthodox segment and retirees.
– Improve satisfaction of Bank clients by benefiting from promotions and benefits of "The Card Club", Mizrahi-Tefahot's client loyalty program.
– Expand the "Let us meet at Mizrahi-Tefahot" activity, increase awareness and the number of attendees at this activity. This applies to all the relevant marketing segments.
– Regional marketing – geography-appropriate activity in areas around Bank branches with expansion of the branch network.
– Use LIVE to recruit new clients in relevant segments.

Marketing strategy

The marketing strategy is derived from the business strategy and growth targets, including continued Mizrahi-Tefahot leadership as a differentiated and preferred brand based on better service to clients. The service is based on the Hybrid method, which allows for personal, professional banker service for each client.

As part of the overall service concept and Mizrahi-Tefahot's unique DNA, digital services do not replace human service but are additional, allowing clients to select the most appropriate channel at each point in time.
Services and products are developed and launched in order to improve client satisfaction and to offer a better service experience.
The Bank conducts data-based marketing activities to offer clients the most appropriate service and product for their needs, using a range of marketing and contact channels.
Mizrahi-Tefahot strives to establish the brand as a challenger bank, a differentiated brand in the banking system, offering advanced, human banking to clients, focused on their needs. The brand is reinforced through marketing communications, including advertising campaigns and a distinguishable, likable media language.

Media activities appeal to the public at large, as well as to the aforementioned demographic segments.

In order to achieve business targets, the marketing plan includes activities using diverse media and advanced marketing tools.

Highlights of marketing activities:

– **Brand** – preserve the preference and reinforce the differentiation of the "Mizrahi Tefahot" brand, increase satisfaction and a better service experience.

– **Business** – brand distinction when addressing the business segment, using a sub-brand, differentiated language and products relevant for this segment. Improve the professional capacity and image of the business banker, understand business needs by sector and field of operation. Make channels accessible and develop advanced technology solutions for businesses.

– **Client recruitment** – Focus on recruiting high-quality clients through general campaigns in the media, local recruiting, internal recruiting, regular activities using various on line tools, marketing using databases and checking account offering by distinct segments, such as the "Executive Account" and the "Priority Account".

- **Client experience** – develop client journeys to create a satisfactory, high-quality service experience, a continuous experience customized for the client. Activity based in joy, creating joy among clients. Client journeys are customized by demographic segment, need and contact channel with the Bank. The client experience is based on allowing Bank clients to choose the best and most convenient contact channel for them. As part of the Bank commitment to personal, human service the teller stations remain unchanged in Bank branches, unlike policies applied by competitors.
- **Mortgages** – Further position Tefahot as a leading brand for mortgages, establish the bankers as experts in their field and innovative value propositions for clients. Further improve the client experience by using advanced tools and services, such as the Tefahot app, an advanced website providing comprehensive real estate information (MADLAN), hybrid service to connect client and a regular banker etc. We have also continued to reinforce relations with real estate players forming a bridge between end clients and mortgage bankers, added and developed relevant content to enrich and empower potential and existing clients.
- **Deposits** – Further growth in deposit market share, recruit new clients for deposit accounts and reinforce the image of investment professionals. Image based on offering creative and relevant investment solutions for clients and for the changing economic environment. Media channels are used with a clear, accessible language for clients.
- **Segments**– Continued marketing and media campaign targeted at the Arab and Jewish Orthodox segments.
    - **Arab segment** – Continued opening of branches in Arab towns, further creating and establishing the brand as a differentiated, preferred brand, communication activities in media focused on this segment, using a communication language and products customized for this population. Local activities through "Let us meet at Mizrahi Tefahot" and local marketing communications activity.
    - **Jewish Orthodox segment** – Marketing activity in custom media channels, reinforcing brand preference, recruitment of high-quality individual, business and mortgage clients. Continued support for local tactical activity and expansion of "Let us meet at Mizrahi Tefahot" activities in segment branches.
- **"The Card Club"** – Improve satisfaction of "The Card" clients and increase awareness thereof by expanding the range of suppliers and promotions. Establish "The Card Club" as a unique client loyalty club which provides exclusive, attractive offers to Bank clients.
- **"Let us meet at Mizrahi Tefahot"** – Support for the Bank's marketing strategy and brand values, designed to create a close relationship with the community and the public in areas where branches operate. As part of the "Let us meet at Mizrahi Tefahot" activity, the public is exposed to a wide range of fascinating content, delivered by leading speakers. These activities are open to the general public.
- **Existing clients** – Nurture and preserve existing clients and intensify activities with them. Activities for existing clients are based on the range of unique value propositions listed above; the relationship with existing clients is primarily based on providing high-quality, personal and human service by the banker. In addition, the Bank offers exclusive, innovative products, club benefits and promotions to clients, with a personal, customized contact and positioning which underlines the sense of belonging.
- **Focused marketing activity** – Smart use of information systems for focused marketing campaigns through various distribution channels and through the CRM system and multi-channel systems, constantly developing insights and tools for better knowledge of Bank clients and their needs, thus offering products and services which are relevant for them.
- **Activity on social media** – Create a constant, on-going dialog with clients using social media, monitor activity on social media and blogs and provide a quick response, in as much as possible, to client inquiries by using advanced technological tools:
    - Understanding the clients – Real-time monitoring of consumer calls to assist in improvement of products and services offered to clients.
    - Active involvement in social media – Identify questions and inquiries from clients and provide a rapid, efficient response.
    - Useful insights for new product development.
    - Monitor and measure campaigns.

- **Deploy IT tools** – Reinforce the Bank relations with the client and empower the client's relations with their personal banker, using advanced technological tools to support the strategy, based on a multi-channel perspective and on client data.

Market research conducted by the Bank reveals that these activities reinforce the positioning of Mizrahi Tefahot as a preferred bank:

- Mizrahi Tefahot is the bank perceived as the bank providing the best personal and human service compared to the competition, scoring high on satisfaction.
- The Bank has an image advantage over time, as perceived by the public compared to the competition. Perceived by the public as a different and differentiated bank. Bank clients are perceived by the public to be the best-served clients.
- Mizrahi Tefahot is the only bank (out of the top 5 banks) with a potential market share higher than the reported market share, having the highest growth potential.
- The Bank leads in client satisfaction, regularly over many years.
- Tefahot, the mortgage brand, leads in client satisfaction in the mortgage category – significantly higher than competitors. It also leads the market in all image-related dimensions: Awareness, the bank perceived to be the first one to call – Tefahot is perceived as the number one mortgage bank in Israel.

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Significant developments in human resources and administration

Developments in labor relations

Labor relations with managers and employees are governed by the collective agreement with each sector's representative labor union.

Payroll agreements of employees represented by the Bank's Employee Association

- In late 2015, an economic arbitration process was launched between the Bank and the employee union, to discuss the demands made by the employee union for 2005-2015.

  In 2016, the arbitrators tried to move the discussion of employee union demands to a reconciliation process. This attempt was un-successful and in late 2016, the issue was referred back to arbitration.

  Moreover, concurrently with the economic arbitration, there are negotiations under way to renew the payroll agreement between Bank management and the employee union for 2016-2020.
- Due to disagreement with the employee union with regard to the value per hour for calculating extra time, since the parties failed to reach agreement in the reconciliation process, in 2016 the parties launched an arbitration proceeding on this matter. In December 2016, the arbitration verdict was given and the Bank is acting to implement it.

The Bank made appropriate provisions for these matters.

Payroll agreements for employees represented by the Council of Managers and Authorized Signatories

The labor agreement with the Council of Management is effective through 2017. In 2017, negotiations will start in order to sign a new labor agreement for the coming years.

Labor and payroll agreements at Bank Yahav

Bank Yahav has a collective bargaining agreement with employee representation which governs labor and remuneration at Bank Yahav for 2013-2016. This agreement has been extended through 2017.

Remuneration of officers in financial corporations act

On April 12, 2016, the Remuneration of officers in financial corporations act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 was made public. The Bank has taken the steps required to implement provisions of the Act. For more information see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" (Legislation and Supervision of Bank Group Operations) of these annual financial statements and Note 8 to the financial statements.

Streamlining plan

On December 27, 2016, the Bank's Board of Directors approved a streamlining plan recommended by Bank management. For more information about the streamlining plan, see chapter "Significant Events in the Bank Group's Business" below and Notes 22 and 25 to the financial statements.

Developments in logistics, administration and streamlining

In 2016, the Bank continued the trend of streamlining and utilizing existing resources as follows:

- Streamlining in space used and better deployment of the branch network.
- Leveraging infrastructure through temporary leasing to third parties space used by the Bank as reserve for future growth.
- Expansion of the operations center – For more information see chapter "Significant developments in management of Bank business" above.
- Making Bank branches accessible, in conformity with new accessibility regulations, at a faster pace than required by law. In some cases, decisions were made to relocate to other properties.

The activities and trends described above are expected to continue in 2017.

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For more information about human resources at the Bank, organizational structure and senior officers of the Bank, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" of these financial statements.

Significant developments in IT

Computer services for Bank Yahav

In 2008, Bank Mizrahi-Tefahot acquired a controlling interest in Bank Yahav (50% of shares) from Bank HaPoalim Ltd. (hereinafter: "Bank HaPoalim").

Through December 31, 2016, Bank Yahav received computer and operating services from Bank HaPoalim. These services were provided to Bank Yahav in conformity with approval by the Supervisor of Banks and by the Anti-Trust Supervisor.

In order to disconnect from the Bank Hapoalim systems, in conformity with Bank of Israel directives, Bank Yahav contracted with an international company of the TATA Group, to create a core banking system and receive outsourced IT and operating services.

On January 1, 2017, Bank Yahav started receiving services from this company, as planned. The transition to the new core system was successfully completed after completion of data conversion and internal and external correctness tests (with third parties).

In the first days following the transition, Bank Yahav handled a large volume of client inquiries. As of the reporting date, the volume of inquiries has stabilized and holding times have decreased significantly.

In 2017, Bank Yahav would continue to follow the work plan in order to stabilize the system, make corrections and complete development according to the schedule agreed during system development – and make additional developments as planned.

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For more information about investments and expenses with respect to IT, see chapter "Analysis of composition of assets, liabilities, capital and capital adequacy" below.

For more information about fixed assets and installations see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" of these annual financial statements.

Developments in international geographic deployment

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

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

Details of the affiliates and their business are as follows:

Swiss subsidiary – UMB (Switzerland) Ltd. – specializes in private banking services and in extending loans for purchase of real estate in Israel. The subsidiary operates through one branch and is owned by the wholly-owned Bank holding company incorporated in Holland – UMOHC B.V. (hereinafter: ("the holding company"). The Swiss subsidiary is subject to the regulatory laws in Switzerland.

Bank's overseas branches – Overseas branches offer their customers banking services, in accordance with the local laws and regulations. The branches are subject to the local and Israeli regulation.

– **London Branch:** The branch is engaged mainly in business banking, including participation in loan syndicates, foreign trade, credit, receiving deposits, foreign currency trade and providing private banking services. The branch's clients are local, Israeli and international clients.
– **Los Angeles Branch:** The branch is primarily engaged in commercial banking, participating in syndicated loans and receiving deposits. Deposits with this branch are insured by the Federal Deposit Insurance Corporation(FDIC). The branch's clients are local, Israeli and international clients.

International private banking branches in Israel – The Bank operates four special branches, located in Jerusalem, Tel Aviv, Netanya and Ashdod, serving foreign resident of significant financial means and new immigrant clients. These branches are among 14 specialized Bank branches providing service to foreign resident clients. These four branches provide full banking services to their clients, primarily private banking. The branches are under Israeli supervision and report to the Private Banking and International Operations sector.

Representative offices – The major activities of representative offices are marketing of Bank services and representation of the Bank overseas. The representative office in Panama was closed in 2016. At end of 2016, the Bank operates representative offices in Mexico, Germany and Uruguay. In 2016, the Bank decided to close its representative office in Uruguay. This representative office is in the process of being closed and should be closed in 2017.

Legislation and regulation

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

Subsidiary in Switzerland – Federal Supervisory Authority of Switzerland FINMA.

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

London branch – subject to two authorities: FCA (Financial Conduct Authority) and PRA (Prudential Regulation Authority).

Mexico affiliate – Comision Nacional Bancaria y de Valores (banking regulators).

Germany representative office - Financial Supervisory Authority - (BaFin)

Uruguay representative office - Banking regulation - Banco Central Del Uruguay.

Business goals and strategy

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

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

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

International operations involve several unique risk factors:

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

Each overseas affiliate operates subject to local laws and regulations, and is regularly assisted by local legal counsel who specialize in banking operations applicable for each affiliate.

International operations also involve cross-border risk, for more information see chapter "Risks overview" below.

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

For more information see chapters "Risk overview" and "Supervisory operating segments" below as well as the detailed Risk Management Report on the Bank website.

Significant projects

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

Projects completed in 2016

- For more information about the project to replace the core system at Bank Yahav, see chapter "Significant developments in IT" below.
- Savings for Every Child – management of long-term savings for children. In early 2017, the Bank launched the operation and started receiving deposited funds for clients who had chosen the Bank.
- Mutual fund management system FMR – Operation of back-office system and control over the funds' prospectus policies.
- Advanced models – In conformity with Bank of Israel directives, the Bank developed models to improve decision making when extending credit.
- Loans guaranteed by the State – Providing loans to small and medium businesses in the new fund, guaranteed by the State.
- Credit cards – Support for passive and debit cards.
- Extending loans at service stations – Money Line loans extended by self service at service stations.
- System for management of deposit funds for overseas workers.
- SKY system applications (the Bank's online system) and mobile apps – Operation of a modern mortgage website and app (MortgageApp) for those interested in a mortgage, option for check deposit using the mobile app.

Projects under development

Hybrid Banking – Adding the private banking sector to the hybrid service and operations domain.

Paperless Branch – Signatures and storage on electronic media.

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

Development of IT infrastructure

Investment in infrastructure development forms an important basis, allowing the Bank to support expansion of its business through development of new, state-of-the-art banking systems. Below are major projects which took place in 2016:

- Virtualization – Consolidation of VM servers (virtual server farm).
- Upgrade of the Bank's communication network.
- Storage – New systems installed.
- Consolidation of enterprise cabinets for modern infrastructure.

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Other matters

Significant Agreements

For more information about material agreements, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" of these annual financial statements.

Social involvement and charitable donations

As a business organization whose activities and achievements depend on the community in which it operates, the Bank sees itself as obligated to show involvement and to support all facets of the community's needs.

The Bank is primarily focused on 2 specific social areas, to which it funnels most of the charitable donations and volunteer activity by the Bank and its employees:

- Promoting under-privileged children and youth
- Supporting NGOs and businesses who promote social causes and employ persons with special needs

Most Bank branches and HQ units have connections to different social organizations and institutions working on behalf of disadvantaged children and youth at risk, in communities in which branches are located. “Adoption” of these organizations is reflected by volunteer work by branch and headquarters staff and providing assistance to the populations they treat, and providing financial assistance – Bank donations for purchase of products to benefit the children and youth. In addition, the Bank operates a variety of ventures to benefit populations in need – financial education kits for youngsters, empowerment of youngsters, activities to benefit sick children, scholarships for students in financial need, fair for sale of products by NGOs etc. These activities are carried out with involvement of Bank employees, their families and even Bank clients. In 2016, the Bank expanded its "Let us meet at Mizrahi-Tefahot" program, in which lectures and activities on various topics were offered to the general public at Bank branches – free of charge.

In 2016, the Bank Group allocated NIS 9.7 million to social involvement and charitable donation, compared to NIS 8.5 million last year. In addition, Bank employees and managers invested work hours valued at NIS 4.6 million compared to NIS 4.4 million last year in community work as part of the various activities.

In total in 2016, the Bank Group invested in community social activities NIS 14.3 million, compared to NIS 12.9 million in 2015.

In August 2016, the Bank issued its 2015 Corporate Social Responsibility Report.

This report was also compiled in conformity with reporting guidelines of GRI (the Global Reporting Initiative) and it is compliant with the GRI G4 Sustainability Reporting Guidelines.

All data reported in this issued report was externally audited by the Israeli Corporate Social Responsibility Institute.

The Bank's Corporate Social Responsibility Report is available on its website:
www.mizrahi-tefahot.co.il >> about the bank >> investor relations

Information required by the Anti-Trust Authority

On January 4, 2017, the Bank received a letter from the Anti-Trust Authority, whereby the Bank is required to provide to the Anti-Trust Authority information, documents and data with regard to the state of competition and/or the Bank's competitive situation with regard to mortgages, pricing policy on housing loans, application of regulatory directives with regard to housing loans and Bank policy and procedures with regard to being advised by external mortgage advisors.

According to the letter, this requirement was issued after the Anti-Trust Supervisor found that this should ensure or facilitate compliance with the law.

In January 2017, the Bank provided to the Anti-Trust Authority the great majority of the documents requested.

Changes in legal structure and incorporation of the Bank

In 2016 there was no change to legal structure and incorporation of the Bank.

Explanation and analysis of results and business standing

This chapter includes a description of trends, phenomena, developments and material changes with regard to results and business standing, including analysis of revenues, expenses and profit as well as analysis of developments in assets, liabilities, capital and capital adequacy. It also describes the results of the Bank's supervisory operating segments and operating results for holdings in major investees.

Trends, phenomena and material changes

Significant Events in the Bank Group's Business

New five-year strategic plan for 2017-2021

Given the Bank's achievements and changes to the macro-economic environment in Israel, on November 21, 2016 the Bank's Board of Directors approved a new five-year strategic plan for 2017-2021.

For more information about the new five-year strategic plan, see chapter "Business goals and strategy" above.

Project to replace the core banking system at Bank Yahav

For more information about replacement of the core banking system at Bank Yahav, see chapter "Significant developments in IT" above.

Obtaining a guarantee insurance policy

On December 28, 2016, the Bank acquired an insurance policy for credit exposure due to guarantees provided by the Bank pursuant to the Sale Act (Apartments) (Securing Investments of Home Buyers), 1974 and obligations to issue such guarantees.

The insurance policy covers 80% of the guarantees amounting to NIS 15.5 billion and is effective as from December 31, 2016.

The aforementioned transaction was made through an insurance company which is a wholly-owned subsidiary of the Bank which, concurrently, has contracted with international re-insurers with a high international rating.

The insurance policy provides the Bank with coverage should the Bank be required to pay due to forfeiture of the guarantees; it is primarily intended to reduce risk assets with respect to credit exposure due to these guarantees.

Obtaining this insurance resulted in a reduction of NIS 3.3 billion in the Bank's risk assets and in an increase of 0.25% in the Bank's Tier I capital ratio.

Sale of assets and liabilities in mortgage portfolio

On June 30, 2016, the Bank and institutional investors signed an agreement for sale of 80% of assets and liabilities in a housing loan portfolio valued in total at NIS 882 million. The loan portfolio consists of housing loans extended by the Bank in 2014. The loan portfolio sold includes loans with LTV ratios ranging below 60%.

On September 29, 2016, the Bank and institutional investors signed an agreement for sale of 80% of assets and liabilities in a housing loan portfolio valued in total at NIS 906 million. The loan portfolio consists of housing loans extended by the Bank from January 1, 2014 through February 25, 2015. The loan portfolio sold includes loans with an LTV ratio of up to 60% (in total, the two housing loan portfolios sold in 2016 amount to NIS 1,788 million).

In the two aforementioned transactions, the remainder of this loan portfolio is retained by the Bank, so that rights of the buyer and those of the Bank shall have equal precedence (pari passu).

According to management agreements signed by the parties, the Bank will manage and operate, on behalf of the buyer, the portion of the loan portfolio acquired – in the same manner and based on the same rules used by the Bank to manage and operate its own housing loans, including the portion of the loan portfolio retained by the Bank.

Streamlining plan

On December 27, 2016, the Bank's Board of Directors approved the streamlining plan recommended by Bank management, whereby early retirement would be possible for 300 employees in 2017-2021, at improved conditions.

See also the Bank's Immediate Reports: Dated December 27, 2016 (reference 2016-01-092211); dated December 29, 2016 (reference 2016-01-093738); and dated January 3, 2017 (reference 2017-01-001033).

Bank management is in negotiations with the employee union with regard to the retirement program and as a first step, has started implementation of the plan in the Mizrahi Tefahot Technology Division Ltd., pending agreement with the employee union at the Bank.

The cost of update to the actuarial liability with respect to the streamlining plan, recorded on the financial statements as of December 31, 2016, amounts to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity (under Other Comprehensive Income).

In conformity with the Supervisor of Banks' letter dated January 12, 2016, with regard to operating streamlining of the Israeli banking system, the Supervisor of Banks allowed capital relief with respect to this plan. The Bank applies this capital relief so that supervisory capital used to calculate capital adequacy would be adjusted (increased) and the capital effect of the streamlining (a decrease by 0.14%) would be applied on a straight line basis as from 2017, over a five-year period.

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

See Notes 22 and 25 to the financial statements for further information.

Remuneration Act

On April 12, 2016, the Remuneration of officers in financial corporations act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 was made public. The Act, whose provisions with regard to contracts approved prior to its publication date would apply as from six months after said publication date, contracting with a senior officer or employee of a financial corporation with regard to their terms of office or employment, which include remuneration for which the forecasted expenses, as calculated as of the approval date, in conformity with GAAP, would exceed NIS 2.5 million per year, is subject to special approval proceedings (including approval by the General Meeting of Bank shareholders by a special majority). The Act also stipulates that a pre-condition for approval of contracting with such employee is that the ratio of the aforementioned anticipated expense to the expense for the lowest remuneration of a full-time position paid by the financial corporation, directly or indirectly, to any employee of the corporation, must be less than 35.

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

For more information about the Remuneration Act, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" (Legislation and Supervision of Bank Group Operations) of these annual financial statements.

Issue of prospectus – Mizrahi Tefahot Issue Company Ltd.

On July 4, 2016, Mizrahi Tefahot Issue Company Ltd. (hereinafter: "Mizrahi Tefahot Issue") issued a shelf prospectus (dated July 5, 2016) whereby the company may issue to the public securities of different types subject to statutory provisions – non-convertible debentures, non-convertible subordinated notes and commercial paper – through shelf offering reports in which it would complete all specifics of each offering, including details, terms and conditions of the securities and composition of the offered units, subject to statutory provisions and to bylaws and directives of the Tel Aviv Stock Exchange Ltd., as they may be at that time.

The prospectus is valid for two years from the issue date and may be extended for a further 12 months by the company.

Publication of prospectus – the Bank

On September 25, 2016, the Bank issued a shelf prospectus (dated September 26, 2016) whereby the Bank may issue to the public securities of different types subject to statutory provisions – including Bank ordinary shares in the holder's name of NIS 0.1 par value each, as well as other securities of the Bank (including debentures, subordinated notes (including contingent subordinated notes (CoCo), options exercisable for shares and options exercisable for debentures) – through a shelf offering report in which it would complete all specifics of each offering, including details, terms and conditions of the securities and composition of the offered units, subject to statutory provisions and to bylaws and directives of the Tel Aviv Stock Exchange Ltd., as they may be at that time.

The prospectus is valid for two years from the issue date and may be extended for a further 12 months by the Bank.

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

Major developments in the banking industry in Israel and overseas

The banking system has been facing several key challenges in recent years:

- Moderate economic activity, with a low interest rate and inflation environment over time, which impairs bank profitability.
- More moderate global growth, impacted *inter alia*, by weaker emerging markets and increased uncertainty in the Euro Zone, results in a trend of transition from global multi-national banking to local banking.
- Rapid development of digital banking based on Internet platforms and increased use of mobile devices. The increased digital trend allows for entry of technology companies into the financial brokerage arena (P2P and crowd financing companies), due to the advantages of the on line platform: rapid information flow, rapid cooperation between individuals and low transaction cost.
- Competition in the household segment and in the small and medium business segments has increased in recent years, given the focus of the banking system on these segments, along with increased new entries from institutional investors and credit card companies. These effects are accompanied by increased regulation in the following areas: Supervision of prices of banking services; elimination of barriers to account transfer between banks; promotion of the Credit Information Act and creation of a banking ID for increased transparency for consumers and for reducing information gaps; increased competition in the banking sector by encouraging entry of new competitors – credit associations and cooperative banks.
- Further to the trend of expanding regulatory directives on June 3, 2015 the Finance Minister announced the appointment of the Committee for Increased Competition in Common Financial Banking Services in Israel ("the Shtrum Committee"). On July 6, 2016 the Committee published its final recommendations. Further to the Committee's final recommendations, on January 27, 2017, the Increased Competition and Reduced Concentration in Israeli Banking Act was enacted. The objective of this Act is to increase competition in retail banking services, with reference to both supply (adding new players) and demand (increasing consumer power). Below are key provisions of the Act:

  - Separation of control and ownership by large banks (banks with total balance sheet assets, on consolidated basis, exceeding 20% of total balance sheet assets for the Israeli banking system) from credit card companies.
  - Imposing restrictions on large banks with regard to issue and distribution of credit cards.
  - Launching a technology interface for viewing financial information (Read Only), to make it easier for consumers to choose between various financial alternatives.
  - Financial institutions may acquire IT services from banks.
  - Credit card settlement – Existing clearing houses would be required to contract with a new clearing house, so as to allow them to provide settlement services to merchants.
  - In order to review competition in the credit market, a committee was established, headed by the Director General of the Ministry of Finance and the Manager, Research Division at the Bank of Israel. The committee is tasked with monitoring the implementation of the Act and recommending further steps to increase competition in the credit market.

For more information about the Act, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" (Legislation and Supervision of Bank Group Operations) of these annual financial statements.

- Streamlining steps taken in the banking system, as reflected by several moves: Launch of early retirement programs for employees, merger of subsidiaries into parent banks, reduced branches and real estate area, computer-based teller services and increased use of digital banking.
- On September 28, 2014, the Supervisor of Banks issued a directive, requiring banks to increase the capital buffer against their housing loan portfolio. The directive stipulates, in addition to targets specified by the Supervisor of Banks for Tier I capital ratios for the banking corporations, that banking corporations would be required to increase their Tier I capital ratio by a rate equivalent to 1% of the balance of their housing loan portfolio. The effective start date for compliance with the capital target specified in the directive is January 1, 2017, with gradual implementation over the period from publication of the directive to the effective start date.

For more information see chapter "Analysis of composition of assets, liabilities, capital and capital adequacy" below.

Stricter requirements with regard to maintaining liquidity coverage ratio and leverage ratio, in order to improve stability of the banking system. On the other hand, the Supervisor of Banks allowed Israeli banks to issue debentures with a loss-absorption provision, as is common around the world (contingent conversion debentures – CoCo). Such debentures contribute to stability of the issuing bank and to reduced support required from the Government should the bank be in trouble.

For more information about issue of contingent subordinated notes (Contingent Convertibles – CoCo), see chapter "Developments in financing sources" above.

Stricter international regulation is characterized by increased, cross-border enforcement as well as by local taxation issues.

Increased consumer awareness due, inter alia, to increased use of social networks and to technology which allows for easier access to information and to comparison of financial alternatives. Consequently, the banking world is becoming focused on identifying client needs.

Developments in Israel's Economy and in the global economy in 2016

Israeli economy

Real Developments

Macro-economic data for 2016 show faster growth in the economy, due to faster growth in private consumption and increase in exports of services and in investments in fixed assets.
GDP growth in 2016 was 4.0% in annualized terms, compared to 2.5% in the previous year and compared to 3.2% in 2014.
The average unemployment rate in 2016 was 4.8%, compared to 5.3% in the previous year. The employment rate remained at 64.1%.

Inflation and exchange rates

In 2016, the Consumer Price Index decreased by 0.2%, following a decrease of 1.0% in the previous year. In 2016, the CPI was primarily impacted by lower prices of the following: Transportation and communications, food, furniture and household equipment, fruits and vegetables. Conversely, the CPI was affected by higher housing prices and prices of education, culture and entertainment.

Below is information about official exchange rates and changes there to:

	December 31, 2016	December 31, 2015	Change in %
Exchange rate of:			
USD (in NIS)	3.845	3.902	(1.5)
EUR (in NIS)	4.044	4.247	(4.8)

On March 15, 2017, the USD/NIS exchange rate was 3.658 – a 4.9% revaluation compared to December 31, 2016. The EUR/NIS exchange rate on this date was 3.887 – a revaluation of 3.9% since December 31, 2016.

In support of the exchange rate, the Bank of Israel purchased in 2016 foreign currency valued at USD 5.7 million, after purchasing USD 5.5 billion in the previous year (USD 1.8 billion purchased in 2016 to offset the effect on USD exchange rates of gas production from the Tamar reservoir, compared to USD 3.1 billion in the previous year).

Monetary and fiscal policy

In 2016 there was no change in the Bank of Israel interest rate which was reduced from 0.25% to 0.10% in March 2015. The Bank of Israel monetary policy was affected this year, *inter alia*, by the constantly stronger NIS against the currency basket, continued weakness in exportation of goods, more moderate inflationary expectations and continuing expansive monetary policy in major world economies, against the backdrop of further slow growth in major world economies.

In 2016, the government budget recorded a NIS 25.9 billion cumulative deficit, compared to a NIS 24.5 billion cumulative deficit last year. The deficit rate as percentage of GDP for the 12 months ended in December 2016 was 2.2%, similar to the previous year. Tax revenues increased in 2016 by 5.6% over the previous year, while Government expenditure increased by 8.2% in the same period. Actual revenues collected in 2016 exceeded the expected amount in the original budget proposal by NIS 8.8 billion.

Residential construction and the mortgage market

According to data from the Central Bureau of Statistics, in the first 11 months of 2016 demand for new apartments (apartments sold and apartments constructed not for sale) was 44 thousand apartments, a decrease of 6.6% over the corresponding period last year and an increase of 20.8% over the corresponding period in 2014. The decrease compared to the corresponding period last year, is due, inter alia, to a decrease in demand for apartments from investors. In this period, demand for apartments decreased in most regions: Haifa (-17%), Northern (-16%), Jerusalem (-12%), and Tel Aviv (-5%). On the other hand, the Southern and Central regions recorded increase by 5% and 1%, respectively. Based on the average pace of sales in November 2016, the inventory will account for 13.0 months' sales -higher than in December 2015 (10.7 months) and than in December 2014 (11.2 months). In 2016, housing loans given to the public amounted to NIS 59.1 billion, compared to NIS 65.0 billion in the corresponding period last year and NIS 52.0 billion in 2014.

According to data from the Central Bureau of Statistics, housing prices increased in 2016 by 5.9%, compared to 7.8% in 2015.

Capital market

In 2016, trading on local and global equity markets was volatile, with declines due to concern about China's economy early in the year and the Brexit implications later on replaced by rallies following the UK referendum and the the US elections.

Equity market - The leading benchmarks, Tel Aviv 25 and Tel Aviv 100, were lower in 2016 by 3.8% and 2.5%, respectively, compared to increase of 4.4% and 2.0% in 2015.

The average daily trading volume in shares and convertible securities in 2016 was NIS 1.27 billion, compared to NIS 1.45 billion in 2015.

Debenture market - the Government debenture market was higher in early 2016, but reversed direction in the third quarter. In particular, CPI-linked debentures declined as inflationary expectations declined, after the CPI for August was lower by 0.3%, following three positive CPI readings. Corporate debentures continued to provide positive returns to investors, in absence of alternatives and given the low interest rate environment.

The General Debenture Index rose by 2.1% in 2016, following an increase of 1.8% in 2015. The CPI-Linked Government Debenture Index rose by 0.7%, after rising by 0.2% in 2015. The Non-Linked Government Debenture Index rose in 2016 by 1.2%, after rising by 2.8% in 2015. The Tel Bond 20 Index was up 3.2% in 2016, following a decrease of 1.1% in 2015. The Tel Bond 40 Index was up 1.8% in 2016, following a decrease of 0.2% in 2015.

Global economy

The US economy's growth rate slowed down in 2016, with US GDP increasing by 1.6%, compared to 2.6% in 2015 and to 2.4% in 2014.

On November 9, 2016, Donald Trump was elected the 45th President of the United States. This was in fact of most early polls published prior to the election indicating that Hillary Clinton was likely to be elected. Upon his inauguration, President Trump withdrew the USA from the Trans-Pacific Trade agreement, stating his intention to impose heavy tariffs on US companies which would move their production out of the country, to reduce taxes and to make significant investment in infrastructure. At this stage it is too early to estimate the effect of Trump's economic policy on the US and global economy.

In 2016, GDP in the Euro Zone grew by 1.7%, compared to 2.0% in 2015.

On June 23, 2016, UK citizens decided in a poll to have the UK leave the European Union (Brexit). In early February 2017, the UK parliament voted to activate Section 50 of the EU Bylaws, meaning the start of negotiations between the UK and the EU to agree on departure terms and conditions and to agree on trade agreements, movement of people, capital and taxation. These negotiations are to be completed within two years. Should the parties fail to reach agreement within two years – the UK would have to negotiate trade agreements and other economic agreements with Europe, just like any other country in the world. The agreement to be reached by the parties would have to be ratified by the parliaments of all EU member states. The IMF estimated that the cumulative impact, over several years, to global GDP growth due to the UK leaving the EU should not be significant, at 0.1%-0.3% of GDP. Following the Brexit vote, according to the Bank of Israel, it is more widely believed that major central banks would maintain their expansive monetary policy for a long time.

China's GDP grew in the fourth quarter of 2016 at an annualized 6.8%, slightly higher than the 6.7% growth in each of the previous three quarters. Note that this growth rate is lower compared to growth in China's economy in previous years. This was mostly due to a slowdown in exports and moderate growth in industrial output.

The US election outcome, positive macro-economic indicators and absence of investment alternatives pushed equity indexes around the world higher. In 2016, the Dow Jones and S&P 500 indexes rose by 13.4% and 9.5%, respectively - after declining by 3.0% and 1.5% in 2015. The NASDAQ 100 Index rose in 2016 by 5.9%, compared to 7.5% in 2015.

The German DAX Index and the French CAC Index were up in 2016 by 6.9% and 4%, respectively - after being up by 3.5% and 8.5%, respectively in 2015. The UK's FTSE 100 Index was higher in 2016 by 14.4%, after dropping by 4.9% in 2015. The Japanese Nikkei Index rose in 2016 by 0.4%, compared to 7.8% in 2015.

Risk events

In 2016, there were no material loss events nor any events with a potential for material loss.

For more information, including analysis of major risks to which the Bank is exposed and an overview of their management and evolution in the reported period, see chapter "Risks Overview" as well as the Detailed Risk Management Report on the Bank website

www.mizrahi-tefahot.co.il >> financial reports.

The chapter "Risks Overview" below includes a mapping of various risk factors and their potential impact on the Bank Group. Risk factors whose potential impact on the Bank Group was not classified as Low are: Credit risk, market risk, liquidity risk, operating risk, including , information security and cyber risk, IT risk and legal risk, compliance and regulatory risk, cross-border risk and AML risk.

Below is an overview of top risks and most significant emerging risks.

Therefore, the various risks faced by the Bank may be classified into two risk categories:

Top risk – An existing or new risk which may materialize over the short term (one year) and has potentially material impact on the financial results, reputation and stability of the organization, such as credit risk and market risk.

Emerging risk – Risk which may materialize over the long term (longer than one year) and there is a high degree of uncertainty with regard to the nature and extent of its impact on the organization, such as information security and cyber risk, IT risk, compliance and regulatory risk.

During the year, the Bank monitored the development of its risks profile under normal and stress conditions, using a range of stress tests specified at the Bank. The risk profile is monitored by reviewing a range of risks benchmarks in segments relevant for Bank operations and their remoteness to the risk appetite specified by the Board of Directors. The impact of the aforementioned risk factors is:

Overall effect of credit risk	– Low-medium
Overall effect of market risk	– Low-medium
Liquidity risk	– Intermediate
Overall effect of operating risk	– Intermediate
Compliance and regulatory risk	– Intermediate
Cross-border risk	– Intermediate
Anti-money laundering risk	– Low-medium

Credit risk – The risk profile in the Bank's mortgage portfolio has been decreasing over the past year – a continued trend due to continued decrease in risk factors relevant to this portfolio: LTV, repayment ratio, default rates, probability of default (PD) etc. The Bank has a range of scenarios designed to challenge the potential impact to the mortgage portfolio under extreme macro-economic conditions, including a sharp drop in housing prices or an increase in unemployment. These scenarios indicate that the potential damage to the portfolio as compared to the Bank's core capital is low. During the year, the Bank expanded its retail operations, with the risk level monitored using traditional benchmarks. Concurrently, the Bank completed the development of advanced models in this segment, in order to support regular monitoring and underwriting operations. The new benchmarks, like the old ones, indicate that the risk level of this portfolio is low and stable. During the year there was no material change to the Bank's business credit risk profile, which remained at a low-medium level. During the year, the Bank reduced the credit concentration in its business portfolio, especially with regard to exposure to large borrowers.

For more information about credit risk with respect to individuals (excluding housing loans), credit risk in the construction and real estate economic sector in Israel and housing loan risk, see chapter "Credit risk" below.

Market risk – The market risk profile in the negotiable portfolio is low and interest and inflation risk in the banking portfolio were kept at a low-medium risk profile throughout the year. Note that the interest and inflation environments remained low and the Bank's framework for addressing such risks was reviewed and found to be in line with potential changes to risk factors. At the end of 2016, the interest risk profile benchmarks became stable, under normal life conditions as well as under stress conditions, at a reasonable margin from the specified risk appetite.

Liquidity risk – In 2016, the Bank continued to take action to improve liquidity ratios and source concentration. The Liquidity Coverage Ratio (LCR) increased consistently throughout the year, in line with the outline specified in Proper Banking Conduct Directive 221, for achieving a minimum ratio of 80% in 2016 and a minimum ratio of 100% in early 2017. The average liquidity coverage ratio (consolidated) for the fourth quarter of 2016 and at the end of 2016 were higher than the restrictions specified by the Bank's Board of Directors, which are in turn higher than the Bank of Israel requirements for 2017. Thus, the Bank completed application of the Bank of Israel directives with regard to minimum liquidity coverage ratio. The Bank monitors and manages depositor concentration and source composition using a range of benchmarks and indicators, which also point to improvement in 2016. Given the foregoing, the risk assessment is low-medium. (For details see chapter "Risks overview" below and the detailed Risks Management Report on the Bank website).

Operating risk – Action taken by the Bank to implement principles for addressing operating risk (including information security and cyber risk), training and surveys, designed to map the major risks associated with Bank operations and to take action in order to mitigate them. These risks increase as technology evolves and as Bank business expands; therefore, the risk assessment is medium and concurrently, the Bank expands its on-going activity to improve monitoring, management and control of these risks. The Bank is aware of the importance of business continuity; therefore, this year the Bank continued taking action required to upgrade and exercise this framework and has achieved a high level of readiness for business continuity in case of emergency.

Legal risk – The risk profile did not materially change during the past year and its level was determined to be low-medium.

Compliance and regulatory risk – The compliance and regulatory risk profile of the Bank has been decreasing over the past year, due to many significant actions taken by the Bank and against the backdrop of stricter regulation of Bank operations. These actions include intensive deployment of a compliance culture at Bank branches, other business units and at headquarter units through, *inter alia*, training delivery using various means and engaging compliance entities for professional support and control as part of the first line, including at Bank branches, regions and headquarter units. In addition, the involvement of the Compliance Officer in all processes at the Bank was increased and control activity was significantly expanded – both at the Bank in Israel and at overseas Bank subsidiaries and affiliates.

Cross-border risk – This year, the Bank started monitoring cross-border and FATCA (Foreign Account Tax Compliance Act) risk, which is relatively high due to stricter regulation in this field world-wide and increased proactive steps taken by various regulators around the world. The Bank has put in place a framework for handling such risk, including setting a quantitative and qualitative risk appetite and constant monitoring of the risk profile, *inter alia*, by implementation of a campaign to have all clients who are foreign residents sign certifications, whereby they are in compliance with their obligations towards tax authorities wherever relevant and waivers of confidentiality with respect to foreign authorities. The Bank also maps the countries relevant to its operations, creating Do and Don't rules with regard to various business activities and pools activities of foreign residents in specialized branches to be trained in these rules. The Bank also delivers training to entities operating in areas exposed to cross-border risk.

AML risk – The Bank's AML risk profile has been decreasing over the past year, primarily due to deployment of strict control processes, extensive training and improved compliance culture. *Inter alia*, compliance controllers in the different regions, as part of their regular control activity, apply specific controls to various aspects of implementation of AML and terror financing procedures.

As noted above, the Bank constantly monitors its risk profile using a range of tools, including: The quarterly Risks Document, which reviews a host of benchmarks specified for the various risks and their closeness to the risk appetite, as specified in Bank policy documents, the Bank's annual ICAAP document filed in early 2017 and, in particular, the capital planning process included there, which reviews the capital required by the Bank in order to achieve the targets in the Bank's strategic plan. Concurrently, the Bank conducts diverse stress tests at different severity levels and a self-assessment process, in which Risks Owners and controllers conduct a subjective, qualitative review of the various risks profiles at the Bank, taking into account the expected direction of risk evolution given changes in macro-economic conditions, in the Bank's business targets, in regulatory assumptions and in the work plans.

Review of the Bank's risks profile, as indicated by the risks documents and outcome of the ICAAP process, as well as analysis of the Bank's balance sheet resilience and key financial ratios under the uniform stress scenario specified by the Bank of Israel, indicate that the Bank's risk profile, at the end of 2016, is relatively low; the potential loss due to unexpected events, relative to the Bank's capital and profits, is low; Bank profitability is stable; and the capital cushion available to the Bank is satisfactory under stress scenarios as well. These results are similar to the results in 2015. These quantitative results are in line with the outcome of the internal qualitative review process, which indicate that the quality of risks management at the Bank is good and that an appropriate framework is in place for addressing all risks, given business targets and regulatory requirements.

Assessment of the effect of the aforementioned risk factors takes into account the risk associated with the US DOJ inquiry as well as all action taken by the Bank to defend its position with regard to the inquiry. For more information about the US DOJ inquiry with regard to Bank Group business with its US clients and for more information about a motion for approval of a derivative claim and motion for approval of a class action lawsuit on this matter, see Notes 26.C.12 and 26.C.11(B-C) to the financial statements.

Independent Auditors' reports

The Independent Auditor has drawn attention in their report to Note 26.C.11(A-G) to the financial statements, with regard to claims filed against the Bank, including motions for class action status, as well as to Note 26.C.12 with regard to the US DOJ inquiry with regard to Bank Group business with its US clients.

Events after the date of the financial statements

For more information about a dividend distribution with respect to earnings of the fourth quarter of 2016, see chapter "Analysis of developments in assets, liabilities, equity and capital adequacy" below and the statement of changes to shareholder equity and Note 35 "Events after the balance sheet date" of the financial statements.

Changes to critical accounting policies and to critical accounting estimates

The financial statements are prepared in accordance with generally accepted accounting policies in Israel (Israeli GAAP) and in accordance with directives and guidance from the Supervisor of Banks. The significant accounting policies are detailed in Note 1 to the financial statements.

Below are changes to critical accounting policies and to critical accounting estimates which impact the operating results:

Group provision for credit losses

The group-based provision for credit losses is based, *inter alia*, on historical loss rates in various economic sectors, divided into troubled and non-troubled debt, for the 5 years ended on the report date. In conformity with the Bank of Israel directive, as described in Note 1.D.6.D. On the financial statements for 2016 and 2017, the range of loss rates would be extended to include 2011, with the range being 6 and 7 years long, respectively.

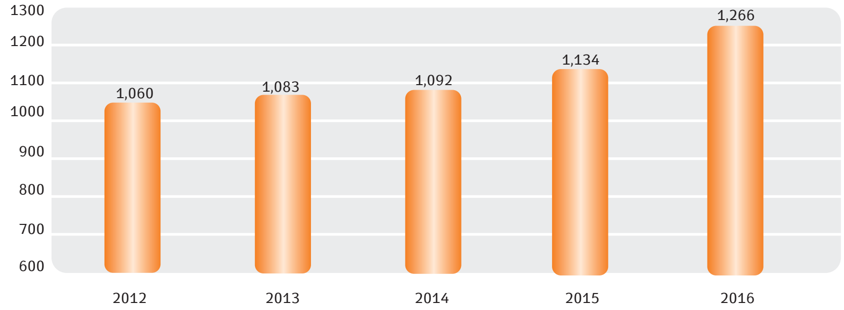
Application of this directive has no material impact on the Bank's financial statements.

Material developments in revenues, expenses and other comprehensive income

Net profit for the Group in 2016 amounted to NIS 1,266 million, compared to NIS 1,134 million in the previous year – an increase of 11.6%. This reflects a return on equity at 10.2%, compared to 10.0% in the corresponding period last year.

Group net profit in the fourth quarter of 2016 amounted to NIS 265 million, compared to NIS 240 million in the corresponding period last year – an increase of 10.4%. This reflects a return on equity at 8.6%, compared to 8.4% in the corresponding period last year.

Net profit
NIS in millions



MIZRAHI TEFAHOT

Analysis of developments in revenues, expenses and other comprehensive income

Net interest revenues and non-interest financing revenues[1] from current operations in 2016 amounted to NIS 3,876 million, as described below, compared to NIS 3,510 million in 2015, an increase of 10.4%.

Net interest revenues and non-interest financing revenues [1] from current operations in the fourth quarter of 2016 amounted to NIS 1,018 million, as described below, compared to NIS 909 million in the corresponding period last year, an increase of 12.0%.

Net interest revenues and non-interest financing revenues[1] in 2016 amounted to NIS 4,073 million, as described on these financial statements, compared to NIS 3,892 million in 2015, an increase of 4.7%.

Net interest revenues and non-interest financing revenues[1] in the fourth quarter of 2016 amounted to NIS 1,067 million, as described on these financial statements, compared to NIS 947 million in the corresponding period last year, an increase of 12.7%.

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

	For the year ended December 31,			For the quarter ended December 31,		
	2016	2015	Change in %	2016	2015	Change in %
Interest revenues, net	3,778	3,534		948	820	
Non-interest financing revenues[1]	295	358		119	127	
Total financing revenues	4,073	3,892	4.7	1,067	947	12.7
Less:						
Effect of CPI	(48)	(130)		(29)	(95)	
Revenues from collection of interest on problematic debts	40	54		7	17	
Gain from realized debentures and from debentures held for trade, net	72	180		1	16	
Effect of accounting treatment of derivatives at fair value and others[2]	133	278		70	100	
Total effects other than current operations	197	382		49	38	
Total financing revenues from current operations	3,876	3,510	10.4	1,018	909	12.0

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

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

Other effects include:

– Following the decrease in early mortgage repayment, in all of 2016 and in the fourth quarter of 2016, revenues decreased by NIS 185 million and NIS 33 million, respectively, compared to the corresponding period last year.

– Other impacts include the effect of Bank coverage against tax exposure with respect to overseas investments, by allocating excess financing sources against such investments.

For definition of supervisory operating segments and differences between supervisory operating segments and operating segments based on management approach – see chapter "Supervisory operating segments" below and chapter "Other Information about the Bank and Management thereof" on the Financial Statements.

Below are total financing revenues by supervisory operating segment (NIS in millions):

	For the year ended December 31,			
Operating segment	2016	2015	Change amount	Change rate (In %)
Individuals:				
Households – housing loans	1,100	992	108	10.9
Households – other	1,084	962	122	12.7
Private banking	47	35	12	34.3
Total – individuals	2,231	1,989	242	12.2
Business operations:				
Small and micro businesses	781	726	55	7.6
Medium businesses	187	169	18	10.7
Large businesses	444	434	10	2.3
Institutional investors	107	112	(5)	(4.5)
Total – business operations	1,519	1,441	78	5.4
Financial management	165	346	(1)(181)	(1)(52.3)
Total activity in Israel	3,915	3,776	(2)139	(1)3.7
Overseas operations	158	116	42	36.2
Total	4,073	3,892	181	4.7

	Fourth Quarter			
Operating segment	2016	2015	Change amount	Change rate (In %)
Individuals:				
Households – housing loans	289	260	29	11.2
Households – other	286	246	40	16.3
Private banking	10	9	1	11.1
Total – individuals	585	515	70	13.6
Business operations:				
Small and micro businesses	199	188	11	5.9
Medium businesses	49	36	13	36.1
Large businesses	113	109	4	3.7
Institutional investors	26	29	(3)	(10.3)
Total – business operations	387	362	25	6.9
Financial management	60	36	24	–
Total activity in Israel	1,032	913	119	13.0
Overseas operations	35	34	1	2.9
Total	1,067	947	120	12.7

(1) The amount of change, excluding the effect of decrease in early mortgage repayment, as noted above and realized debentures held to maturity at Bank Yahav in the third quarter of 2015, is an increase of NIS 56 million, or 51.4%.

(2) The amount of change, excluding the effect of decrease in early mortgage repayment, as noted above and realized debentures held to maturity at Bank Yahav in the third quarter of 2015, is an increase of NIS 376 million, or 10.6%.

Data for supervisory operating segments show that in 2016, revenues grew for both retail and business operations.

Below are average balances of interest-bearing assets attributable to operations in Israel in the various linkage segments (NIS in millions):

	For the year ended December 31,		
Linkage segment	2016	2015	Change in %
Israeli currency – non-linked	138,152	117,783	17.3
Israeli currency – linked to the CPI	50,921	52,518	(3.0)
Foreign currency (including Israeli currency linked to foreign currency)	11,941	13,627	(12.4)
Total	201,014	183,928	9.3

The decrease in average balances of interest-bearing assets in the CPI-linked segment and in the foreign currency segment is primarily due to diversion of uses to the NIS-denominated segment.

Below are interest spreads (difference between interest income on assets and interest expenses on liabilities)(1) based on average balances(2), attributable to operations in Israel in the various linkage segments, in percent:

	For the year ended December 31,		For the quarter ended December 31,	
Linkage segment	2016	2015	2016	2015
Israeli currency – non-linked	1.99	2.28	1.99	2.23
Israeli currency – linked to the CPI	0.52	0.25	0.51	0.21
Foreign currency	1.33	1.39	1.60	1.62
Total	1.57	1.65	1.58	1.61

(1) Revenue and expense rates were calculated relative to interest-bearing assets and liabilities.
(2) Average balances before deduction of provision with respect to credit losses.

The decrease in interest spread for non-linked Israeli currency is primarily due to the effect of decrease in early mortgage repayment, as noted above.

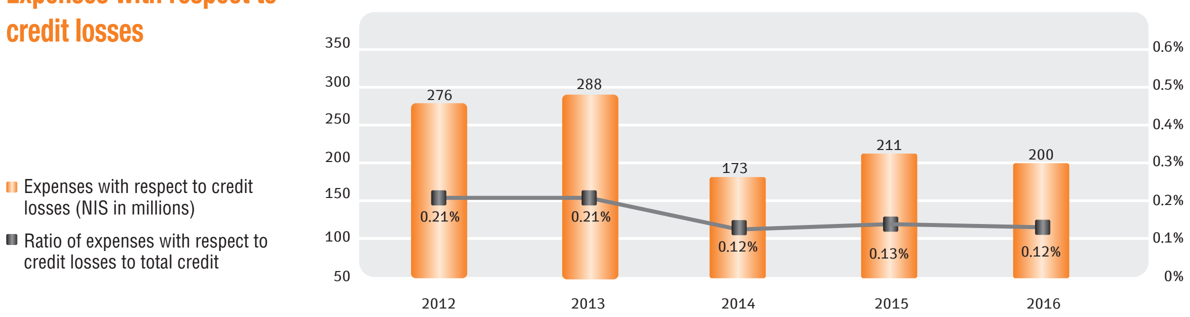
The increase in interest spread in CPI-linked NIS is due to continued improvement in interest spreads and to lower average cost of CPI-linked sources.

For composition of interest spreads by different criteria (activity type, linkage segment and quantity and price analysis), more information about non-interest bearing assets and liabilities and information about overseas activities, see appendix "Interest Revenue and Expense Rates" to the annual financial statements.

Expenses with respect to credit losses for the Group in 2016 amounted to NIS 200 million, or 0.12% of total loans to the public, net compared to NIS 211 million in 2015, or 0.13% of total loans to the public, net), for a total decrease of NIS 11 million.

Expenses with respect to credit losses for the Group amounted to NIS 81 million in the fourth quarter of 2016, or an annualized rate of 0.19% of total loans to the public, net, compared with NIS 75 million in the corresponding period last year – an annualized rate of 0.19% of total loans to the public, net in the corresponding period last year – an increase of NIS 6 million in total.

Expenses with respect to credit losses



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

	For the year ended December 31,		For the quarter ended December 31,	
	2016	2015	2016	2015
Provision for credit losses on individual basis (including accounting write-offs)	150	124	67	73
Provision for credit losses on Group basis:				
By extent of arrears	(20)	(20)	(2)	(11)
Other	70	107	16	13
Total expenses with respect to credit losses	200	211	81	75
Expense with respect to credit losses as percentage of total loans to the public, net (annualized)	0.12%	0.13%	0.19%	0.19%
Of which: With respect to commercial loans other than housing loans	0.33%	0.37%	0.53%	0.60%
Of which: With respect to housing loans	0.01%	0.01%	0.02%	(0.02%)

For information about the Supervisor of Banks' directives with regard to group provision for credit losses, see Note 1.C. 4. to the financial statements.

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

Operating segment	For the year ended December 31,		For the quarter ended December 31,	
	2016	2015	2016	2015
Individuals:				
Households – housing loans	13	9	6	(5)
Households – other	91	55	30	30
Private banking	1	–	–	(1)
Total – individuals	105	64	36	24
Business operations:				
Small and micro businesses	109	88	13	4
Medium businesses	11	13	12	10
Large businesses	(24)	45	19	35
Institutional investors	(1)	(7)	(3)	(2)
Total – business operations	95	139	41	47
Financial management	(1)	(2)	1	(1)
Total activity in Israel	199	201	78	70
Overseas activity	1	10	3	5
Total	200	211	81	75

(1) The increase in expenses with respect to credit losses is due to an increase in Group-based provision, based on the increase in loan volume, as well as to impact of legislation which reduces debt repayment by individual clients who are in difficulties.

For definition of supervisory operating segments and differences between supervisory operating segments and operating segments based on management approach – see chapter "Supervisory operating segments" below and chapter "Other Information about the Bank and Management thereof" on the Financial Statements.

For more information about analysis of development of loans to the public, see chapter "Analysis of composition of assets, liabilities, capital and capital adequacy" below.

For more information about analysis of credit risk, see chapter "Risks overview" below and the detailed Risks Management Report on the Bank website.

Net interest revenues after expenses with respect to credit losses in 2016 amounted to NIS 3,578 million (including non-interest financing revenues – NIS 3,873 million), compared to NIS 3,323 million in 2015 (including non-interest financing revenues – NIS 3,681 million). Interest revenues, net after expenses with respect to credit losses increased in 2016 by 7.7% over the previous year (including non-interest financing revenues: an increase by 5.2%).

Net interest revenues after expenses with respect to credit losses in the fourth quarter of 2016 amounted to NIS 867 million (including non-interest financing revenues – NIS 986 million), compared to NIS 745 million in the corresponding period last year (including non-interest financing revenues – NIS 872 million). Interest revenues, net after expenses with respect to credit losses increased in the fourth quarter of 2016 by 16.4% (including non-interest financing revenues: an increase by 13.1% year-over-year).

See above the analysis of evolution of financing revenues from current operations and analysis of expenses with respect to credit losses.

Non-interest financing revenues include, inter alia, the effect of fair value, gains (losses) from transactions in debentures and expenses (revenues) with respect to linkage differentials on CPI derivatives, where the corresponding revenues (expenses) are recognized as interest revenues, in conformity with accounting rules. For analysis of evolution of financing revenues from current operations, see above.

Commission revenues amounted to NIS 1,433 million in 2016, compared with NIS 1,426 million in 2015, an increase of 0.5%.

Commission revenues in the fourth quarter of 2016 amounted to NIS 356 million, compared to NIS 355 million in the corresponding period last year – an increase of 0.3%.

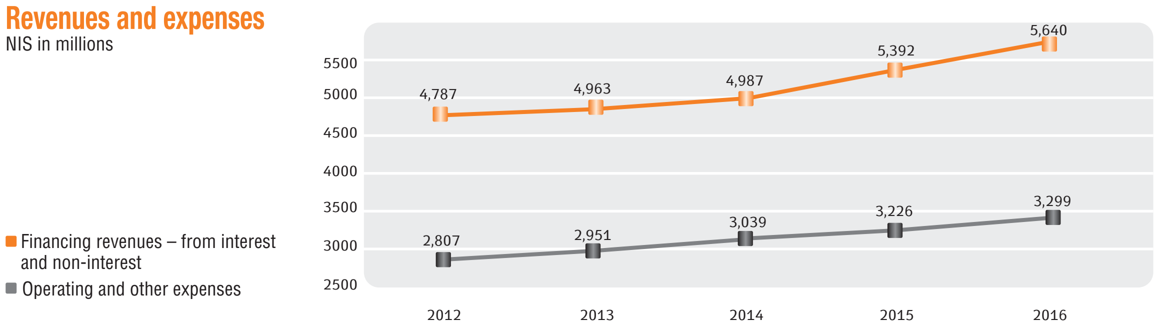
The increase in commissions due to growth in operating volume was significantly offset by the negative impact of various regulatory directives, primarily with regard to management of checking accounts for individual clients.

Other revenues in 2016 amounted to NIS 134 million, compared with NIS 74 million in 2015, an increase of NIS 60 million.
Other revenues in the fourth quarter of 2016, amounted to NIS 14 million, compared with NIS 35 million in the corresponding period last year – a decrease of NIS 21 million.
Changes to other revenues are primarily due to the outcome of Bank activity to realize assets as part of asset reorganization and improvements to the branch network.

Operating and other expenses amounted to NIS 3,299 million in 2016, compared with NIS 3,226 million in 2015, an increase of 2.3%.
Operating and other expenses amounted to NIS 869 million in the fourth quarter of 2016, compared with NIS 819 million in the corresponding period last year – an increase by 6.1%. See explanation below.

Payroll and associated expenses amounted to NIS 2,071 million in 2016, compared with NIS 1,944 million in 2015, an increase of 6.5%.
Payroll and associated expenses amounted to NIS 566 million in the fourth quarter of 2016, compared with NIS 499 million in the corresponding period last year – an increase by 13.4%.
The increase in payroll expenses is primarily due to growth in headcount, to additional provisions with respect to employee rights and a special bonus at Bank Yahav with regard to deployment of a new core banking system.

Maintenance and depreciation expenses for buildings and equipment in 2016 amounted to NIS 693 million, compared to NIS 692 million in 2015, a year-over-year increase of 0.1%.
Maintenance and depreciation expenses for buildings and equipment amounted to NIS 171 million in the fourth quarter of 2016, compared with NIS 169 million in the corresponding period last year – an increase by 1.2%.
Maintaining a stable level of expenses for maintenance and depreciation for buildings and equipment is due to the Bank's efforts in streamlining, utilization of existing resources, asset reorganization and improvements to the branch network.
For more information about expenses with respect to IT, see chapter "Composition and development of assets, liabilities, capital and capital adequacy" below.



Other expenses amounted to NIS 535 million in 2016, compared with NIS 590 million in 2015, a decrease of 9.3%.
Other expenses in the fourth quarter of 2016 amounted to NIS 132 million, compared to NIS 151 million in the corresponding period last year – a decrease of 12.6%.
The decrease in other expenses is due to decrease in mail and communication expenses, advertising and marketing expenses as well as legal and consulting expenses.

Cost-Income ratio information is as follows[(1)] (in percent):

	2016				2015			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Cost-income ratio	60.5	55.2	57.8	60.8	61.3	56.9	58.4	63.4

	For the year ended December 31,	
	2016	2015
Cost-income ratio	58.5	59.8

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

Group profit before taxes amounted to NIS 2,141 million in 2016, compared with NIS 1,955 million in 2015, an increase of 9.5%.
Pre-tax profit for the Group in the fourth quarter of 2016 amounted to NIS 487 million, compared to NIS 443 million in the corresponding period last year – an increase of 9.9%. See detailed explanation above.

Provision for taxes amounted to NIS 833 million in 2016, compared with NIS 761 million in 2015, an increase of 9.5%. In the fourth quarter of this year, the Bank included deferred tax expenses amounting to NIS 40 million, due to the decrease in the statutory tax rate applicable to the Bank Group as from January 1, 2017.
Provision for taxes in the fourth quarter of 2016 amounted to NIS 212 million, compared to NIS 197 million in the corresponding period last year.
See Note 8 to the financial statements for additional information.

Bank share of after-tax profit of associates – in 2016 there was no profit with respect to associates, similar to 2015.
The Bank's share of after-tax profit of associates in the fourth quarter of 2016 amounted to loss of NIS 1 million, compared to no profit with respect to associates in the corresponding period last year.

The share of non-controlling interest in net results of subsidiaries attributable to Bank Yahav in 2016 amounted to NIS 42 million, compared to NIS 60 million in 2015.
In 2015, Bank Yahav profit includes realized gain from debentures, amounting to NIS 68 million before tax (Bank's share of profit: NIS 34 million before tax).
The share of the non-controlling interests in net results of subsidiaries attributable to Bank Yahav in the fourth quarter of 2016 amounted to NIS 9 million, compared to NIS 6 million in the corresponding period last year.

Net profit attributable to shareholders of the Bank amounted to NIS 1,266 million in 2016, compared with NIS 1,134 million in 2015, an increase of 11.6%.
Net profit attributable to shareholders of the Bank amounted to NIS 265 million in the fourth quarter of 2016, compared with NIS 240 million in the corresponding period last year – an increase of 10.4%.

Other comprehensive income attributable to shareholders of the Bank primarily includes changes in adjustments for presentation of securities available for sale at fair value, changes in cash flows hedges and changes in adjustments with respect to employee benefits.
In 2016, other comprehensive income attributable to shareholders of the Bank decreased by NIS 194 million compared to 2015.
In the fourth quarter of 2016, other comprehensive income attributable to shareholders of the Bank decreased by NIS 204 million compared to the corresponding period last year.
The change in Other Comprehensive Income attributable to shareholders of the Bank compared to the corresponding period last year is primarily due to adjustments with respect to employee benefits with respect to the streamlining plan. See chapter "Significant Events in the Bank Group's Business" above and Notes 22 and 25 to the financial statements.

For more information about results of the Bank Group for the interim period, see multi-quarter information for the past two years in Addendums to the financial statements.

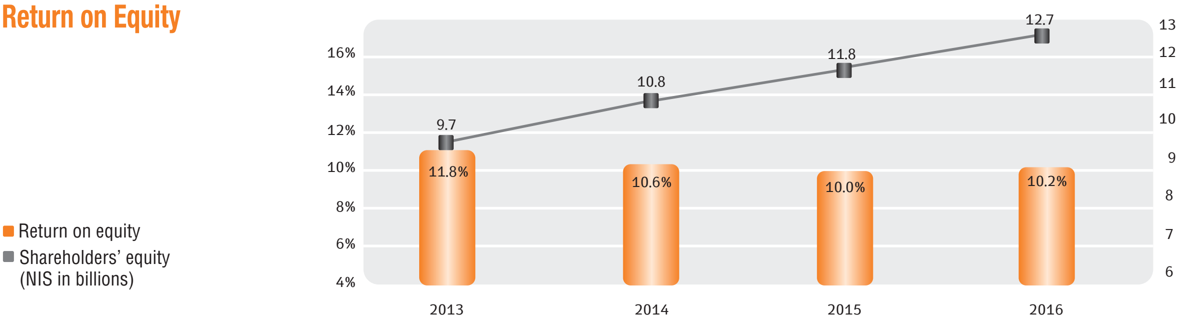
Below is the development of Group return[(1)] on equity[(2)] and ratio of Tier I capital[(3)] to risk elements, liquidity coverage ratio[(4)] and leverage ratio at the end of the quarter[(5)] (in %):

	2016				2015			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Net return on equity	8.6	12.4	11.6	10.0	8.4	11.5	12.4	9.4
Ratio of Tier I capital to risk elements at end of quarter	10.10	9.85	9.72	9.65	9.50	9.30	9.30	9.10
(Quarterly) liquidity coverage ratio	117	105	99	97	91	84	84	–
Leverage ratio at end of quarter	5.27	5.31	5.33	5.23	5.32	5.32	5.24	–

	For the year ended December 31,		
	2016	2015	2014
Net return on equity	10.2	10.0	10.6

(1) Annualized return.
(2) Return on average shareholders' equity, including "total capital resources", as presented in reporting of revenue and expense rates, less average balance of minority interest and less/plus the average balance of unrealized gains/losses from adjustment to fair value of debentures held for trading as well as gains/losses from debentures available for sale.
(3) For more information about Proper Banking Conduct of Directive329 concerning "Restrictions on provision of housing loans" on Tier I equity as from January 1, 2015, see Note 25.M to the financial statements.
(4) Liquidity Coverage Ratio – ratio of total High-Quality Liquid Assets to net cash outflow. This ratio is calculated in conformity with Proper Banking Conduct Directive 221, in terms of simple averages of daily observations during the reported quarter.
(5) Leverage Ratio – ratio of Tier I capital, according to Basel rules, to total exposure. This ratio is calculated in conformity with Proper Banking Conduct Directive 218

Return on Equity



Earnings per share

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

	Fourth Quarte		For the year ended December 31		
	201	201	201	201	201
Basic earnings per share	1.14	1.04	5.46	4.90	4.74
Diluted earnings per share	1.14	1.03	5.46	4.89	4.71
Dividends per share	17.12	15.52	80.25	37.22	–

Analysis of composition of assets, liabilities, capital and capital adequacy

Assets and liabilities

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

	December 31,		
	2016	2015	Change in %
Balance sheet total	230,455	209,158	10.2
Cash and deposits with banks	41,725	30,489	36.9
Loans to the public, net	171,341	159,204	7.6
Securities	10,262	11,845	(13.4)
Buildings and equipment	1,585	1,583	0.1
Deposits from the public	178,252	162,380	9.8
Deposits from banks	1,537	1,166	31.8
Debentures and subordinated notes	27,034	23,719	14.0
Shareholder equity	12,714	11,847	7.3

Cash and deposits with banks – the balance of cash and deposits with banks increased in 2016 by NIS 11.2 billion. The increase in cash balance is part of management of the liquidity coverage ratio.

Loans to the public, net – loans to the public, net on the consolidated balance sheet as of December 31, 2016 accounted for 74% of total assets, compared to 76% at the end of 2015. Loans to the public, net for the Group increased in 2016 by NIS 12.1 billion, an increase of 7.6%.
For more information about on-balance sheet and off-balance sheet credit risk, development of problematic debts and various risk benchmarks with regard to housing loans, see chapter "Risks" below and the Detailed Risks Management Report on the Bank website.

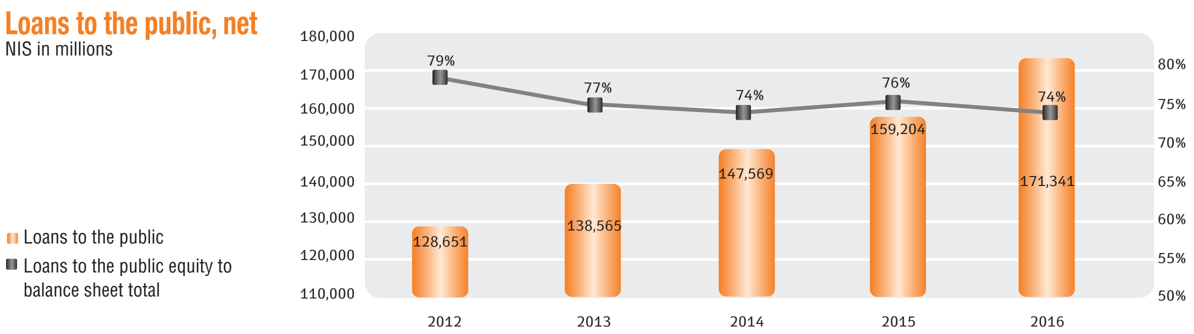
Loans to the public, net by linkage basis (NIS in millions) are as follows:

	Balance as of December 31		Change in %	Percentage of total loans to the public, net as of December 31	
	2016	2015		2016	2015
Israeli currency					
Non-linked	111,144	95,814	16.0	64.9	60.1
CPI-linked	49,369	51,836	(4.8)	28.8	32.6
Foreign currency and foreign currency linked	10,828	11,554	(6.3)	6.3	7.3
Total	171,341	159,204	7.6	100.0	100.0

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

	2016	2015	Change in %
Individuals:			
Households – housing loans	114,070	105,106	8.5
Households – other	18,945	16,816	12.7
Private banking	81	67	20.9
Total – individuals	133,096	121,990	9.1
Business operations:			
Small and micro businesses	15,126	13,909	8.7
Medium businesses	4,786	4,786	-
Large businesses	12,525	13,132	(4.6)
Institutional investors	2,586	2,326	11.2
Total – business operations	35,022	34,153	2.5
Overseas operations	3,223	3,061	5.3
Total	171,341	159,204	7.6

For definition of supervisory operating segments and differences between supervisory operating segments and operating segments based on management approach – see chapter "Supervisory operating segments" below and chapter "Other Information about the Bank and Management thereof" on the Financial Statements.



MIZRAHI TEFAHOT

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

Reported amounts		As of December 31, 2016			As of December 31, 2015	
(NIS in millions)	Credit risk[1]			Credit risk[1]		
	On balance sheet	Off balance sheet	Total	On balance sheet	Off balance sheet	Total
1. Problematic credit risk						
Impaired credit risk	681	212	893	817	169	986
Inferior credit risk	428	–	428	82	–	82
Credit risk under special supervision[2]	1,381	229	1,610	1,318	329	1,647
Total troubled credit risk	2,490	441	2,931	2,217	498	2,715
Of which: Non-impaired debts in arrears 90 days or longer[2]	958			1,012		
2. Non-performing assets[3]	653			774		

(1) On- and off-balance sheet credit is stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.
(2) Including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer, amounting to NIS 853 million (as of December 31, 2015: NIS 956 million).
(3) Assets not accruing interest.

For more information about credit risk with respect to individuals (excluding housing loans), credit risk in the construction and real estate economic sector in Israel and housing loan risk, see chapter "Credit risk".

For more information see Notes 13 and 30 to the financial statements.

Development of Group credit risk distribution by size of borrower (in %) is as follows:

		2016		2015
Credit risk for borrower (NIS in thousands)	Share of total Group credit risk	Share of total Group number of borrowers	Share of total Group credit risk	Share of total Group number of borrowers
Up to 150	10.3	72.1	10.9	72.2
150-600	23.1	17.9	23.4	18.2
600-2,000	34.6	9.2	33.0	8.9
Above 2,000	32.0	0.7	32.7	0.7

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

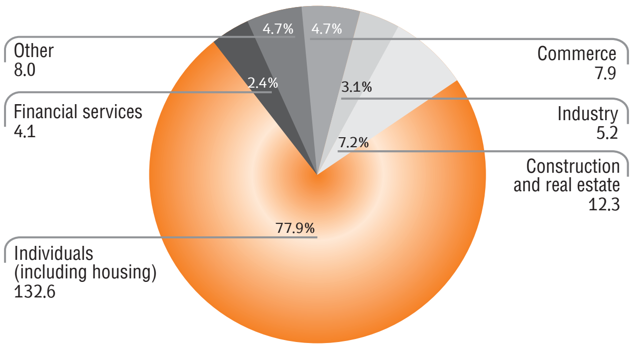
		2016		2015
Sector	Balance sheet credit risk	Percentage of total balance-sheet credit risk	Balance sheet credit risk	Percentage of total balance-sheet credit risk
Private individuals (includes mortgages)	132,618	78.0	121,545	76.9
Construction and real estate	12,250	7.2	11,018	7.0
Financial services	4,136	2.4	4,439	2.8
Industry	5,231	3.1	5,122	3.2
Commerce	7,911	4.7	8,020	5.1
Other	7,969	4.6	8,012	5.0
Total	170,115	100.0	158,156	100.0

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

Credit risk is composed of on-balance-sheet risk and off-balance-sheet credit risk, which are weighted by nature of the borrower and credit type, as per Bank of Israel directives. On-balance-sheet risk includes balances of loans to the public, derivative instruments purchased by the public and Group investment in public debentures. Off-balance-sheet credit risk includes guarantees and transactions in off-balance-sheet instruments, obligations to provide credit and unutilized credit facilities. Total credit risk for the Bank Group as of December 31, 2016 amounted to NIS 207 billion, compared to NIS 217 billion in 2015: a decrease of 4.6%.

Balance sheet credit risk in Israel by economic sector – as of December 31, 2016

NIS in billions



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

	December 31, 2016	December 31, 2015	Change in % over December 31, 2015
Off balance sheet financial instruments other than derivatives [(1)]:			
Unutilized debitory account and other credit facilities in accounts on demand[(1)]	16,688	16,588	0.6
Guarantees to home buyers	12,461	11,597	7.5
Irrevocable commitments for loans approved but not yet granted	10,651	12,901	(17.4)
Unutilized revolving credit card facilities	7,559	7,848	(3.7)
Commitments to issue guarantees	5,797	5,629	3.0
Guarantees and other liabilities	4,869	4,546	7.1
Loan guarantees	2,606	2,245	16.1
Documentary credit	384	472	(18.6)
Derivative financial instruments[(2)]:			
Total par value of derivative financial instruments	233,901	237,147	(1.4)
(On-balance sheet) assets with respect to derivative instruments	3,581	3,527	1.5
(On-balance sheet) liabilities with respect to derivative instruments	3,568	3,634	(1.8)

(1) Contract balances or their stated amounts at the end of the period, before effect of provision for credit losses. For more information see Note 30.E to the financial statements.
(2) Includes forward transactions, swaps, options and credit derivatives.

Securities – investment in securities increased in 2016 by NIS 1.6 billion. The decrease in total investment in securities is in the context of asset and liability management.

Composition of Group securities by portfolio (NIS in millions) is as follows:

					December 31, 2016
	Carrying amount	Amortized cost (for shares – cost)	Unrecognized gains from adjustments to fair value	Unrecognized losses from adjustments to fair value	Fair value(1)
Securities held to maturity	3,236	3,236	75	-	3,311
Securities available for sale	6,678	6,724	(2)30	(2)(76)	6,678
Securities held for trade	348	347	1	-	348
Total securities	10,262	10,307	106	(76)	10,337

					December 31, 2015
	Carrying amount	Amortized cost (for shares – cost)	Unrecognized gains from adjustments to fair value	Unrecognized losses from adjustments to fair value	Fair value(1)
Securities held to maturity	3,320	3,320	71	-	3,391
Securities available for sale	8,303	8,323	20	(40)	8,303
Securities held for trade	222	222	-	-	222
Total securities	11,845	11,865	91	(40)	11,916

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities.
(2) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".

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

	Balance as of December 31		
Linkage segment	2016	2015	Change (in %)
Israeli currency			
Non-linked	5,981	7,002	(14.6)
CPI-linked	146	66	121.2
Foreign currency and foreign currency linked	4,035	4,679	(13.8)
Non-monetary items	100	98	2.0
Total	10,262	11,845	(**13**.4)

Distribution of Group security portfolio by issuer type (NIS in millions) is as follows:

	Carrying amount as of	
	December 31, 2016	December 31, 2015
Government debentures:		
Government of Israel	8,586	9,788
Government of USA	1,479	1,624
South Korea Government	59	40
Total government debentures	10,124	11,452
Debentures of banks in developed nations:		
UK	–	79
Germany	–	117
USA	19	–
Other – Euro Zone	–	78
Total debentures of banks in developed nations	19	274
Corporate debentures (composition by sector):		
Industry and production	–	10
Public and community services	11	11
Financial services	8	–
Total corporate debentures	19	21
Shares	100	98
Total securities	10,262	11,845

For more information about investment in securities and impairment of a temporary nature of securities available for sale, listing the duration of impairment and its share out of the amortized cost, see Note 12 to the financial statements.

Buildings and equipment – The balance of buildings and equipment increased in 2016 by NIS 2 million, or 0.1%. The change in balance of buildings and equipment is due to new investments, primarily investments in technology and conversely, to depreciation and realized assets as part of asset reorganization and improvements to the branch network. See Note 16 to the financial statements for additional information.

Investments and expenses with respect to IT

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

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

	For the year ended December 31 (reported amounts)							
				2016				2015
	Software	Hardware	Other	Total	Software	Hardware	Other	Total
Payroll and associated expenses[1]	196	34	28	258	190	33	25	248
Usage license expenses not capitalized into assets[2]	106	11	2	119	98	11	2	111
Outsourcing expenses[3]	52	2	[6]59	113	42	2	[6]54	98
Depreciation expenses[4]	142	39	2	183	140	38	3	181
Other expenses[5]	10	1	35	46	11	1	35	47
Total expenses	506	87	126	719	481	85	119	685

Total cost with respect to IT recognized as assets on the financial statements in the reported period

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

	For the year ended December 31 (reported amounts)							
				2016				2015
	Software	Hardware	Other	Total	Software	Hardware	Other	Total
Payroll and associated expenses[1]	31	-	-	31	24	-	-	24
Cost of acquisition of usage licenses[2]	56	28	-	84	71	28	1	100
Outsourcing expenses[3]	88	5	-	93	84	7	-	91
Total	175	33	-	208	179	35	1	215

Balance of IT network-related assets at the end of the reported period

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

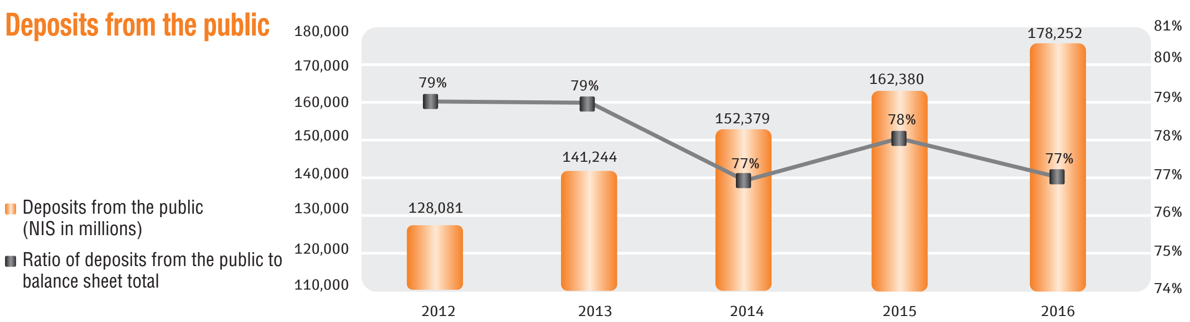
	For the year ended December 31 (reported amounts)							
				2016				2015
	Software	Hardware	Other	Total	Software	Hardware	Other	Total
Total depreciated balance	468	71	7	545	410	77	9	496
Of which: Payroll and associated expenses	61	-	-	61	52	-	-	52

(1) Includes payroll of hardware and software professionals as well as payroll of other IT staff, such as: administrative staff, maintenance staff and operations staff. Payroll costs added to assets include labor costs for development of software for the Bank's own use, capitalized to assets in accordance with generally accepted accounting principles.
(2) These expenses primarily consist of current software maintenance. These expenses are included on the financial statements under "Maintenance and depreciation expenses for buildings and equipment". Additions to assets are with respect to usage licenses and software purchases.
(3) These expenses are with respect to hardware and software maintenance by external employees. These expenses are included on the financial statements under "Maintenance and depreciation expenses for buildings and equipment". Additions to assets with respect to outsourcing include cost of external employees employed by the Bank to develop software for the Bank's own use.
(4) For more information about accounting policies with regard to depreciation expenses, see Notes 1.D.8 and 16 to the financial statements.
(5) Includes expenses with respect to rent and taxes, communication and general & administrative expenses.
(6) In 2016, includes NIS 54 million (In 2015: NIS 53 million) which constitutes payments to banks which provided IT services to Bank Yahav. As from January 1, 2017, Bank Yahav receives IT and operating services from an international Tata Group company. The company specializes, *inter alia*, in providing IT services to financial institutions and banking corporations world-wide. In this regard, Bank Yahav uses a core banking system which includes banking services in various channels, based on the bank's lines of business. Bank Yahav also receives operating services from the company with respect to IT systems it provides, as well as additional outsourced services.

Deposits from the public - these account for 77% of total consolidated balance sheet as of December 31, 2016, compared with 78% at the end of 2015. In 2016, deposits from the public for the Bank Group increased by NIS 15.9 billion, an increase of 9.8%. Deposits from the public include deposits from retail clients, corporations, financial entities and others.

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

	Balance as of December 31		Change rate (In %)	Share of total deposits from the public as of December 31 (in %)	
Linkage segment	2016	2015		2016	2015
Israeli currency					
Non-linked	122,611	109,091	12.4	68.8	67.2
CPI-linked	17,039	16,764	1.6	9.6	10.3
Foreign currency and foreign currency linked	38,602	36,525	5.7	21.6	22.5
Total	178,252	162,380	9.8	100.0	100.0



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

	As of December 31		Change rate
	2016	2015	(In %)
Individuals:			
Households – other	71,334	65,225	9.4
Private banking	11,167	10,242	9.0
Total – individuals	82,501	75,467	9.3
Business operations:			
Small and micro businesses	15,738	13,959	12.7
Medium businesses	7,378	6,098	21.0
Large businesses	31,422	26,688	17.7
Institutional investors	35,964	36,127	(0.5)
Total – business operations	90,502	82,872	9.2
Overseas operations	5,249	4,041	29.9
Total	178,252	162,380	9.8

Evolution of deposits from the public for the Group by depositor size (NIS in millions) is as follows:

	As of December 31	
	2016	(1)2015
Maximum deposit		
Up to 1	59,606	55,229
Over 1 to 10	38,805	35,229
Over 10 to 100	25,042	22,301
Over 100 to 500	24,120	25,616
Above 500	30,679	24,005
Total	178,252	162,380

(1) Reclassified. Reclassification was due to adjustment of deposit composition by size, to also take into consideration the independent legal entity of depositors. Previously, some deposits have been classified as a single depositor group with no such distinction.

Deposits from banks – The balance of deposits from banks increased in 2016 by NIS 0.4 billion.

For more information on the evolution of the composition of deposits from the public and the evolution of the composition of deposits from banks, see Notes 18 and 19 to the financial statements.

Debentures and subordinated notes – The balance of debentures and subordinated notes increased in 2016 by NIS 3.3 billion. See also chapter "Developments in financing sources" above.

For more information about balances of assets and liabilities for the Bank Group for interim periods, see multi-period and multi-quarter information for the past two years in Addendums to the annual financial statements.

Capital, capital adequacy and leverage

Shareholder equity attributable to shareholders of the Bank – Shareholder equity attributable to shareholders of the Bank increased in 2016 by NIS 0.9 billion, to NIS 12.7 billion.

Below is the composition of shareholders' equity (NIS in millions):

	As of December 31		Rate of change
	2016	2015	(In %)
Share capital and premium[1]	2,239	2,222	3.3
Capital reserve from benefit from share-based payment transactions	58	68	11.8
Treasury shares	(76)	(76)	–
Cumulative other comprehensive income (loss)[2]	[3](317)	(97)	–
Retained earnings[4]	10,810	9,730	11.1
Total	12,714	11,847	6.7

(1) For more information about share issuance, see statement of changes to shareholders' equity.
(2) For more information about other comprehensive income (loss), see Note 10 to the financial statements.
(3) Includes adjustments with respect to employee benefits. For more information about the effect of the streamlining plan, see chapter "Significant Events in the Bank Group's Business" above and Notes 22 and 25 to the financial statements.
(4) For more information about developments in revenues and expenses accumulated to retained earnings in the reported period, see chapter "Material developments in revenues, expenses and other comprehensive income" above.

The ratio of shareholders' equity to total assets for the Group as of December 31, 2016 was 5.52%, compared to 5.66% as of the end of 2015.

Capital adequacy

Supervisory capital

The Bank assesses its capital adequacy in accordance with Basel rules, as prescribed by Proper Banking Conduct Directives 201-211. The Bank applies the standard approach in assessing exposure to credit risk, operating risk and market risk.

The Bank regularly monitors its capital adequacy ratio, in order to ensure compliance with requirements of the Supervisor of Banks and with restrictions set by the Board of Directors, as well as to prepare in advance to respond to evolution of risk assets and capital requirements at the Bank. For this purpose, the Board of Directors has created a policy document which specifies the measurement frequency of capital adequacy, the required reporting and actions to be taken if the capital ratio drops below the minimum levels specified; a capital planning and management forum has been operating for several years, attended by the Manager, Finance Division - CFO (chair), Risk Control Division - CRO, and the Manager, Accounting and Financial Reporting Division - the Chief Accountant, the Manager, Business Banking Division, Manager, Retail Division and Manager, Planning, Operations and Client Assets Division. This policy document is an annex to the Bank's master policies on risks management, capital planning and internal control.

As part of implementation of Basel II Pillar 2, the Bank annually files its ICAAR document - which is a report highlighting action taken by the Bank during the year as part of the ICAAP process, which is included in Basel II Pillar 2. On January 31, 2017, the Bank sent its ICAAP document for 2016 to the Bank of Israel. This document consists of several chapters which describe corporate governance for risks management at the Bank, the capital targets and targets of the strategic plan, as well as developments during the year in management of various risks identified and mapped by the Bank, as well as processes for improvement and usability planned for the coming year.

At the core of this document is the capital planning process, conducted across a planning horizon of three years to come, in which the Bank challenges its strategic plan and its overall capital targets, using a long, diverse range of hypothetical stress tests which significantly impact Bank profitability and erode its capital. The outcome of the Bank's current capital planning indicates that the Bank has sufficient general capital to fulfill its strategic plan and capital targets specified by the Board of Directors.

Below is information about supervisory capital and risk assets on the consolidated report:

	As of December 31	
	2016	2015
Capital for purpose of calculating minimum capital ratio		
Tier I capital	13,318	12,299
Tier I capital	13,318	12,299
Tier II capital	4,888	4,916
Total capital	18,206	17,215
Weighted risk asset balances		
Credit risk	122,605	120,793
Market risks	1,184	950
Operating risk	8,113	7,743
Total weighted risk asset balances	131,902	129,486

Ratio of capital to risk elements

As from January 1, 2014, the Bank applies provisions for capital measurement and adequacy, based on Basel III provisions, as published by the Supervisor of Banks and as incorporated in Proper Banking Conduct Directives 201-211. Pursuant to directives of the Supervisor of Banks, as per instructions of the Supervisor of Banks, as from January 1, 2015 the Bank is required to maintain a minimum Tier I equity ratio of no less than 9% and a minimum total equity ratio of no less than 12.5% of weighted total of risk elements of its balance sheet assets and off-balance-sheet items. The Supervisor of Banks' instructions specifies the manner of calculation of total capital and total risk elements

As from January 1, 2015, an additional capital requirement was added to these ratios at 1% of the housing loan balance as of the reporting date.

This requirement is gradually being implemented through January 1, 2017. Accordingly, the minimum Tier I equity ratio and the minimum total equity ratio required by the Supervisor of Banks, as of January 1, 2017, on a consolidated basis, in conformity with data as of the reporting date, are 9.87% and 13.37%, respectively.

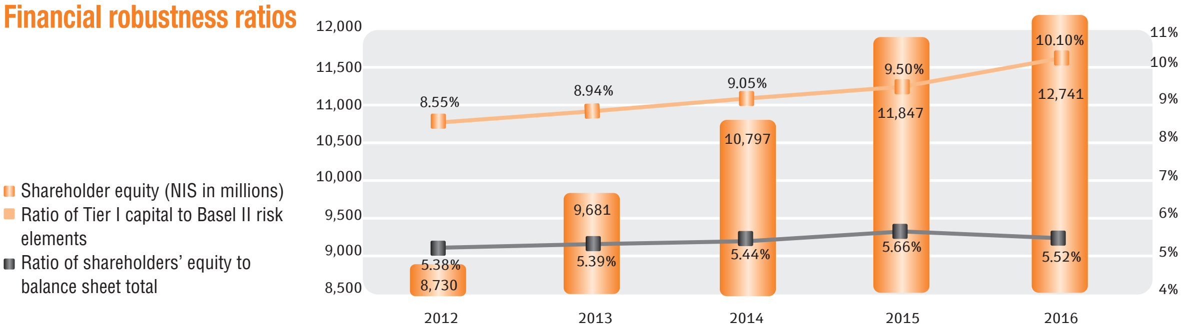
For more information about the Board of Directors resolutions with regard to capital to risk elements ratio and to dividend distribution policy, see Note 25 to the financial statements and chapter "Analysis of composition of assets, liabilities, capital and capital adequacy" (Dividend distribution policy) below.

Development of Group ratio of capital to risk elements is as follows (in %):

	December 31, 2016	December 31, 2015
Ratio of Tier I capital to risk elements	10.10	9.50
Ratio of total capital to risk elements	13.80	13.29
Minimum Tier I capital ratio required by Supervisor of Banks(1)	9.76	9.30
Total minimum capital ratio required by the directives of the Supervisor of Banks(1)	13.26	12.80

(1) Capital ratios required by the Supervisor of Banks as from January 1, 2015.
To these ratios, as from January 1, 2015, an additional capital requirement would be added expressed as 1% of the housing loan balance as of the reporting date. This requirement is applied gradually through January 1, 2017. Accordingly, the minimum Tier I equity ratio and the minimum total equity ratio required by the Supervisor of Banks, as of January 1, 2017, on a consolidated basis, in conformity with data as of the reporting date, are 9.87% and 13.37%, respectively.

Financial robustness ratios



Leverage ratio

On April 28, 2015, the Supervisor of Banks issued a new Proper Banking Conduct Directive 218 concerning "Leverage ratio". This directive 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 shall maintain a leverage ratio of 5% or higher on consolidated basis, as from January 1, 2018. Banking corporations which comply with the requirement upon publication of the directive may not drop below the threshold stated in the regulation. Any banking corporation which does not meet the requirements of this directive is required to increase its leverage ratio at fixed quarterly steps by January 1, 2018.

The Bank's leverage ratio as of December 31, 2016 is 5.27%, compared to 5.32% as of December 31, 2015.

The minimum leverage ratio required by the Supervisor of Banks is 5.00%.

For more information see Note 25 to the financial statements and the Detailed Risk Management Report on the Bank website.

Dividends

Dividend distribution policies

2015-2016

On December 23, 2014, the Bank Board of Directors resolved to approve the dividend distribution policy for 2015-2016.

The dividends policy calls for dividends to be distributed with respect to quarterly earnings in 2015 and 2016 (as from the first quarter of 2015), at a rate of up to 15% of net profit attributable to shareholders.

This dividends policies are subject to the Bank’s maintaining proper safety margins so that Tier I capital ratio would not be lower than the ratio required by the Supervisor of Banks' directives, as adopted by the Board of Directors.

On this date, it was resolved that in 2017 the dividends policy would continue to be annual distribution of 40% of net operating profit and 80% from extraordinary items.

2017-2021

On November 21, 2016, the Bank’s Board of Directors approved a new five-year strategic plan for 2017-2021 and resolved to approve a revised dividends policy as from 2017.

The Bank's revised dividends policy is to distribute dividends with respect to quarterly earnings, at 30% of net profit attributable to equity holders of the Bank.

The Bank has received approval from the Supervisor of Banks for the aforementioned outline of its revised dividends policies.

The Bank’s Board of Directors would monitor execution of the new strategic plan in order to consider optional increase of the aforementioned dividends rate by a further step as from 2018. This would be subject to approval by the Supervisor of Banks.

The revised dividends policy is subject to the Bank achieving a ratio of Tier I capital to risk elements as required by the Supervisor of Banks and maintaining appropriate safety margins.

Below is a summary of previous Board resolutions with regard to dividend distribution policies:

- On April 3, 2006, the Board decided on annual dividend distribution at 40% of net operating profit and 80% of net profit from extraordinary items.
- On July 23, 2012, the Board decided that during the five-year plan for 2013-2017, the Bank would retain its dividend distribution policies.
- On August 14, 2013, a guideline was stipulated whereby, through December 31, 2014, the Bank would distribute dividends equal to up to 30% of annual operating net profit and 80% of annual profit from extraordinary items.

Dividend distribution

Below are details of dividends distributed by the Bank since 2015 (in reported amounts):

Declaration date	Payment date	Dividends per share (Agorot)	Total dividends paid (NIS in millions)
May 18, 2015	June 14, 2015	15.84	36.6
August 16, 2015	September 17, 2015	21.35	49.5
Total dividends distributed in 2015			86.1
February 24, 2016	March 21, 2016	15.52	36.0
May 18, 2016	June 21, 2016	18.62	43.2
August 10, 2016	September 11, 2016	21.99	51.0
November 14, 2016	December 12, 2016	24.12	56.0
Total dividends distributed in 2016			186.2

On March 20, 2017, the Bank's Board of Directors resolved to distribute dividends amounting to NIS 39.8 million, or 15% of earnings in the fourth quarter of 2016.

The dividends amount is 171.2% of issued share capital, i.e. NIS 0.1712 per NIS 0.1 par value share. The effective date for dividends payment is April 9, 2017 and the payment date is April 26, 2017. The final dividends per share is subject to changes due to realized convertible securities of the Bank.

Other Off Balance Sheet Activity

Below is the development of off balance sheet monetary assets held on behalf of Bank Group clients, for which the Bank Group provides management, operating and/or custodial services (NIS in millions):

	As of December 31		Change rate
	2016	2015	(In %)
Securities(1)	217,310	208,514	4.2
Assets of provident funds for which the Group provides operating services	75,515	74,269	1.7
Assets held in trust by the Bank Group	71,564	72,977	(1.9)
Assets of mutual funds for which the Bank provides operating services	13,896	16,219	(14.3)
Other assets under management(2)	11,055	9,964	10.9

(1) Value of securities portfolios in Bank custody, held by clients, including balance of securities of provident funds and mutual funds to which the Bank provides operating services. Note that the balance of client operations presented includes, in addition to the balance of securities for mutual funds as noted above, also the value of participation units in such funds held by Bank clients. The increase in 2016 is primarily due to increase in activity of current and new clients.

(2) Includes:

– Loan balances secured by deposits whose repayment to the depositor is contingent upon collection of the loan balance. With respect to these balances, the Bank receives margin revenues or commissions.

– Other loans managed by the Bank, including housing loans managed and operated by the Bank on behalf of others.

Description of Businesses of the Bank Group by Supervisory Operating Segment

Supervisory operating segments

On November 3, 2014, the Supervisor of Banks issued an update to the Public Reporting Directives concerning supervisory operating segments. According to the directive, the Bank is required to provide, on its financial statements, disclosure with regard to supervisory operating segments in conformity with a uniform, comparable layout specified by the Supervisor of Banks; attribution to supervisory operating segments is typically determined by the client's turnover (annual sales or annual revenues).

Supervisory operating segments include operating segments for individuals and operating segments for business clients other than individuals (including institutional investors and financial management of the Bank).

Individuals are defined as persons with no indebtedness to the Bank or whose indebtedness is classified as indebtedness of "individuals – housing loans and others", in conformity with definitions of credit risk classification by economic sector.

Below are the supervisory operating segments and a brief definition of each one:

Households – individuals, other than private banking clients, as noted below.

Private banking – individuals who manage a financial asset portfolio in excess of NIS 3 million.

Small and micro businesses – businesses with turnover amounting up to NIS 50 million.

Medium businesses – businesses with turnover higher than NIS 50 million and lower than NIS 250 million.

Large businesses – businesses with turnover higher than NIS 250 million

Institutional investors – Primarily provident funds, pension funds, study funds, mutual funds, ETFs, insurance companies and stock exchange members who manage client portfolios.

Financial management – includes trading operations, asset and liability management and non-banking investments.

Overseas operations – presented separately from operations in Israel, divided into individuals and business operations.

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

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

For more information about principles for attribution of balances, revenues and expenses to clients in the system, see Note 29 to the financial statements.

The Bank's operating segments by "management approach" are based on client attribution to the organizational structure responsible in the past period.

However, client attribution to supervisory operating segments is based on uniform definitions specified by the Supervisor of Banks, as noted above.

There is a strong correlation between attributes specified by management for client attribution to the responsible division and the supervisory definitions.

However, according to "management approach", in some cases the final client attribution may be based on other parameters, such as: specialization of a certain unit in activity types of clients or past experience working with the client, which result in business and service-related advantages to client attribution to the specific division.

Given the Supervisor of Banks' requirement to discuss and analyze the supervisory operating segments in the Report of the Board of Directors and Management and given the correlation between supervisory operating segments and "management approach", the segment information (both quantitative and qualitative) is briefly presented below for each segment, as follows:

- Supervisory definition of the segment
- Brief qualitative description of the segment (using "management approach")
- Explanation of differences between the "supervisory" definition and how business is actually managed (using "management approach")
- Financial results of the segment (using "supervisory approach")

For more information and detailed description of the segments, see chapter "Other Information about the Bank and Management thereof" on the Financial Statements.

Financial results using "management approach" are presented in Note 29 to the financial statements.

Below is a summary of financial results by supervisory operating segment (NIS in millions):

	Net profit		Share of total net profit (in %)	
	For the year ended December 31,		For the year ended December 31,	
	2016	2015	2016	2015
Individuals:				
Households – housing loans	474	444	37.4	39.2
Households – other	20	21	1.6	1.9
Private banking	7	5	0.6	0.4
Total – individuals	501	470	39.6	41.4
Business operations:				
Small and micro businesses	255	241	20.1	21.3
Medium businesses	90	81	7.1	7.1
Large businesses	289	248	22.8	21.9
Institutional investors	31	41	2.5	3.6
Total – business operations	665	611	52.5	53.9
Financial management	30	17	2.4	1.5
Total activity in Israel	1,196	1,098	94.5	96.8
Overseas operations	70	36	5.5	3.2
Total	1,266	1,134	100.0	100.0

For more information about operating results in conformity with management approach, see Note 29 to the financial statements.

Household segment

Supervisory definition

In conformity with the supervisory definition, the household segment includes individuals, other than those clients included in the private banking segment. Thus, this segment excludes individuals with financial assets in excess of NIS 3 million. Individuals are defined as persons with no indebtedness to the Bank or whose indebtedness is classified as indebtedness of "individuals – housing loans and others", in conformity with definitions of credit risk classification by economic sector.

Brief description of segment attributes (using "management approach")

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

Differences between management approach and supervisory definition

- Some individual clients attributed to the private banking segment using "management approach" are classified to the household segment using supervisory segments. The difference is primarily due to clients' financial assets used for client classification – the Bank threshold for client classification according to "management approach" is NIS 2.5 million, lower than the supervisory definition.
- As a rule, individual clients are attributed to the household segment. According to the supervisory approach, individual clients with high indebtedness or with business attributes are classified to the business operating segments, rather than to the household segment.

Products and services

Below are key products in the household segment and the primary services offered within the scope of these products.

- Mortgages.
- Banking and finance – includes credit and checking accounts, investments, loans and auto financing.
- Insurance marketing (insurance incidental to mortgages).
- Capital market (transactions involving securities).
- Credit cards.

Major markets and distribution channels

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

The Bank has mortgage marketers operating across Israel, based on geography. The role of these marketers is to identify target audiences in their geographic territory, to increase the exposure of such audiences to Bank products and services and to maximize the marketing potential of such audiences. Marketers give the Bank an edge in the market while making the client the focal point, in line with the Bank's strategy in recent years.

Marketers operate in four major areas:

- Direct activity with real estate players – to obtain potential clients.
- Activity with end clients – proactive contract with potential mortgage and checking account clients.
- Synergetic activity with individual clients – to realize the potential synergy of mortgage clients.
- Synergetic activity with business clients and MM clients – businesses, plants, employee unions etc.

Bank branches – the Group operates 184 business centers, branches, affiliates and representative offices across the country, including 45 Yahav branches. In conformity with the Bank's growth strategy, the expansion of the branch network continues, primarily in business-rich environments and in towns of two distinct demographics where the Bank seeks growth – the Arab segment and the Jewish Orthodox segment.

Direct channels – Direct banking at Mizrahi Tefahot supports the Bank's personal and hybrid service strategy, aiming to use best-in-class technology tools in order to connect the client with their personal banker, based on the understanding that the client requires professional and human assistance for their financial management. The various direct banking channels offer clients most of the information and transactions required to manage their day-to-day finances and the client may contact their personal banker on any matter using digital tools.

In the mortgage segment, the Bank operates a website and application for existing clients. Data for the mortgage segment is presented using an advanced, convenient interface for clients. Clients who enroll in this service can now obtain valuable information, including: detailed information about the mortgage loan (including graphics), details of properties pledged to secure the loan, loan repayment history, details of life and property insurance as entered in the Bank's system, comprehensive environmental information, apartment price lists and market analysis from the MADLAN website. Clients can also produce for themselves useful documents and forms, directly from the website.

Clients interested in obtaining a mortgage may use the "Tefahot to Home" app. This app provides: assistance in creating a financing plan to buy your home, comprehensive, current information about different neighborhoods, including recent transactions, data about apartment prices, rental yields, social benchmarks, education quality etc., an option for clients to photograph and document apartments, a user-friendly mortgage calculator and a service offering correspondence with a mortgage banker.

Business Strategy

Service strategy at Bank Mizrahi Tefahot is based on the understanding that personal, human contact with a banker offering a high level of professional service is at the core of client needs. The Bank's branch network is a key component in creating that personal contact with the banker – and must be supported by a current, efficient digital technology environment.

The Bank sees the importance of further development of the household segment and intends to maintain and establish its leadership position in the retail sector, by investing efforts in the following areas:

- Maintain leadership position in the mortgage market and leverage it to intensify commercial operations;
- Focus on high-quality clients and target specific segments, such as the Arab segment, Jewish Orthodox segment and retirees.
- Further reinforce the synergy with Bank Yahav for a two-pronged strategy: service-oriented and price-oriented;
- Provide personal, human service supported by innovative technology and significant improvement in the client service experience.

Developments in the household segment during the reported period

- In 2016, public moves continued, designed to encourage non-bank entities to enter the competition in the household segment and to increase competition in consumer credit. In January 2017, the Knesset enacted the Increased Competition and Reduced Concentration in Israeli Banking Act. This legislation includes separation of control over credit card companies by the two top banks, including provisions and fledgling protection for the credit card companies to be separated; provisions with regard to creating IT infrastructure and mandatory sale of IT services and operation thereof, as well as leasing of real estate used for IT services and operation thereof, used primarily by the bank; provisions whereby a clearing house would be required to allow settlement by a guest clearing house, in conformity with rules to be specified by the Governor of the Bank of Israel with consent of the Minister of Finance and provisions with regard to guest clearing house and bundled clearing house. Additional provisions enacted relate to a service for comparison of financial costs.
- In 2016, branch closures and elimination of teller positions at branches of some banks continued, with clients referred to digital solutions. Consequently, in August 2016 the Knesset enacted the Banking Act (Licensing) (Amendment no. 22), 2016, whereby any banking corporation seeking to close a permanent branch would be required to obtain permission from the Supervisor of Banks after filing a written justification and application to do so.
- Savings account for every child - On August 5, 2015, the Government adopted a resolution on "Change in composition of child allowance and launch of long-term savings for every child". On September 26, 2016, the Comptroller General Division of the Ministry of Finance issued a call for proposals to select banks and provident funds to manage these savings accounts. The Bank submitted its proposal and on November 9, 2016, the Bank was informed that it was selected to be one of the financial institutions which in future would manage these long-term savings accounts. In early 2017, the Bank launched the operation and started receiving deposited funds for clients who had chosen the Bank.

Analysis of operating results in the household segment

	For the year ended December 31,					
	2016			2015		
	NIS in millions					
	Other	Housing loans	Total	Other	Housing loans	Total
Profit and profitability						
Total interest revenues, net	1,084	1,100	2,184	962	992	1,954
Non-interest financing revenues	-	-	-	-	-	-
Commissions and other revenues	523	154	677	527	170	697
Total revenues	1,607	1,254	2,861	1,489	1,162	2,651
Expenses with respect to credit losses	91	13	104	55	9	64
Operating and other expenses	1,415	465	1,880	1,338	441	1,779
Profit before provision for taxes	101	776	877	96	712	808
Provision for taxes	39	302	341	36	268	304
After-tax profit	62	474	536	60	444	504
Net profit:						
Attributable to non-controlling interests	(42)	-	(42)	(39)	-	(39)
Attributable to shareholders of the banking corporation	20	474	494	21	444	465
Balance sheet – key items:						
Loans to the public (end balance)	19,140	114,691	133,831	16,994	105,719	122,713
Loans to the public, net (end balance)	18,945	114,070	133,015	16,816	105,106	121,922
Deposits from the public, net (ending balance)	71,334	-	71,334	65,225	-	65,225
Average balance of loans to the public	17,961	110,612	128,573	16,034	102,194	118,228
Average balance of deposits from the public	69,137	-	69,137	63,108	-	63,108
Average balance of risk assets	15,935	60,850	76,785	14,964	55,922	70,886
Credit margins and deposit margins:						
Margin from credit granting operations	760	1,073	1,833	699	946	1,645
Margin from activities of receiving deposits	322	-	322	258	-	258
Other	2	27	29	5	46	51
Total interest revenues, net	1,084	1,100	2,184	962	992	1,954

Contribution of the household segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to NIS 494 million, compared to NIS 465 million in the corresponding period last year.

Below are key factors affecting the change in segment contribution:

Contribution of housing loans (including general-purpose loans secured by a lien on a residential apartment) in 2016 amounted to NIS 474 million, compared to NIS 444 million in the corresponding period last year. Total interest revenues, net amounted to NIS 1,100 million, compared to NIS 992 million in the corresponding period last year, an increase of 10.9% - primarily due to an increase in mortgage business volume - reflected in an increase of NIS 8.4 billion in the average loan balance.

Expenses with respect to credit losses increased by NIS 4 million compared to the corresponding period last year. Commission and other revenues decreased by NIS 16 million, due to regulatory effects and current decrease in net revenues from credit portfolio service, due to the decrease in the housing loan portfolio guaranteed by the State.

Operating expenses amounted to NIS 465 million, compared to NIS 441 million in the corresponding period last year - an increase of 5.4%, lower than the 7.9% increase in total revenues.

Contribution of households - other operations (other than housing loans) in 2016 amounted to NIS 20 million, compared to NIS 21 million in the corresponding period last year - an increase of NIS 1 million. Interest revenues, net increased by NIS 122 million. The increase is due to increase in lending margins and to increase in margin from deposit operations, due to higher volumes of both lending and deposits. Commission and other revenues decreased by NIS 4 million, due to regulatory effects.

Expenses with respect to credit losses increased by NIS 36 million. Given the risk attributes of this segment, the Bank increases its qualitative group-based provision for individuals, as directed by the Supervisor of Banks.

Moreover, the increase in expenses with respect to credit losses is due, *inter alia*, to the impact of legislation which reduces debt repayment by individual clients who are in difficulties. For more information about credit risk to individuals, see chapter "Risks" below for detailed analysis of risk evolution.

Operating expenses amounted to NIS 1,415 million, compared to NIS 1,338 million in the corresponding period last year - an increase of 5.8%, lower than the 7.9% increase in total revenues.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.

Private Banking Segment

Supervisory definition

According to the supervisory definition, the private banking segment consists of individuals whose financial assets with the bank (including deposits, securities portfolios and other financial assets) exceed NIS 3 million.

Brief description of segment attributes (using "management approach")

The private banking segment provides banking services in Israel to both Israeli clients and foreign resident clients. Private banking is the concept of banking services geared to clients with high financial wealth, with a considerable part of their activity executed in the management of financial assets. Private banking segment clients are individual clients with liquid deposits and investments in securities in excess of NIS 3 million.

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

This segment has potential for expanding business relationships with clients from a high socio-economic standing, who demand personal, professional service which is highly available.

Differences between management approach and supervisory definition

- Some individual clients attributed to the private banking segment using "management approach" are classified to the household segment using supervisory segments. The difference is primarily due to clients' financial assets used for client classification – the Bank threshold for client classification according to "management approach" is NIS 2.5 million, lower than the supervisory definition.
- The private banking segment according to management approach also includes businesses with liquid assets in excess of NIS 8 million. These clients are classified to the business operating segments under the supervisory approach.

Products and services

Below are key products in the private banking segment and the primary services offered within the scope of these products.

- Banking and finance – including offering of advanced investment products to each client, based on their unique attributes and needs.
- Capital market – services such as buying, selling and custodial services for securities, including financial advice provided to clients who signed advisory agreements and services provided to qualified clients.
- Credit cards – issuing a range of high-end credit cards.

Major markets and distribution channels

The markets addressed by this segment are clients with high financial wealth (both Israelis and foreign residents).

Business Strategy

The Bank intends to further develop the private banking segment, based on professional support centers, focusing on high-quality clients and unique approach to custom segments.

Developments in the private banking segment during the reported period

Over the past year there were no material market developments nor material changes in client attributes in the private banking segment.

Analysis of operating results of the private banking segment

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest revenues, net	47	35
Non-interest financing revenues	-	-
Commissions and other revenues	10	12
Total revenues	57	47
Expenses with respect to credit losses	1	-
Operating and other expenses	45	39
Profit before provision for taxes	11	8
Provision for taxes	4	3
Net profit	7	5
Balance sheet – key items:		
Loans to the public (end balance)	82	68
Loans to the public, net (end balance)	81	67
Deposits from the public, net (ending balance)	11,167	10,242
Average balance of loans to the public	73	74
Average balance of deposits from the public	10,637	9,828
Average balance of risk assets	27	34
Credit margins and deposit margins:		
Margin from credit granting operations	1	1
Margin from activities of receiving deposits	46	34
Other	-	-
Total interest revenues, net	47	35

Contribution of the private banking segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to NIS 7 million, compared to NIS 5 million in the corresponding period last year.

Total interest revenues, net increased by NIS 12 million, primarily due to increase in deposits from the public. Commissions and other revenues decreased by NIS 2 million.

Operating expenses increased by NIS 6 million, attributed to an increase in segment business.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.

For more information about the effect of attribution of expenses related to the US DOJ inquiry on this segment, see Note 29.C to the financial statements.

Micro and Small Business Segment

Supervisory definition

The micro and small business segment includes businesses with annual turnover below NIS 50 million.

Brief description of segment attributes (using "management approach")

The micro and small business segment operates within the retail division, and mainly includes small companies and small business clients with relatively low turnover and total indebtedness of up to NIS 6 million.

This segment is characterized by large client diversification. In view of the fact that the availability of data and their quality regarding the clients of this segment is relatively lower than for major business clients, there is a need for professional service and appropriate means of control, in order to assess the quality of the client for the purpose of issuing credit. Additionally, this segment is characterized by a high percentage of collateral required from the clients to ensure credit repayment.

Differences between management approach and supervisory definition

- Business clients with liquid assets in excess of NIS 8 million are attributed to the private banking segment according to management approach. According to the supervisory segment approach, these clients are classified to the micro and small business segment, based on their annual turnover.
- Business clients currently attributed to commercial banking using management approach and whose annual turnover is lower than NIS 50 million, are classified to the micro and small business segment using the supervisory approach.

Products and services

Below is a description of key products in the micro and small business segment:

- Banking and finance – including loans for various business uses, foreign trade operations, investments and management of debitory facilities.
- Capital market.
- Credit cards.
- Loans for small businesses, guaranteed by the State.

Major markets and distribution channels

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

Business Strategy

Increasing focus and expanding operations in business segments, including the micro and small business segment is at the heart of the Bank's business strategy. This is done while constantly assessing risk and controls at the client, segment and economy levels.

Developments in the micro and small business segment during the reported period

Growing competition among banks in the small business segment continued to accelerate over the past year. In addition, public actions were taken to encourage entry of non-bank entities into the market for credit to small business.

In May 2016, Bank Mizrahi Tefahot launched its financial partnership with HaPhoenix and with Altshuler Shacham, selected as one of the winning bidders in a tender to provide loans to small and medium businesses, guaranteed by the State, by providing loans in a range of tracks under this heading.

Changes to client attributes in this segment

During the year, there was no significant change in attributes of segment clients – this segment is highly diversified as for clients, with strong collateral requirements from clients to secure repayment of credit.

Analysis of operating results of micro and small business segment

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest revenues, net	781	726
Non-interest financing revenues	–	–
Commissions and other revenues	313	301
Total revenues	1,094	1,027
Expenses with respect to credit losses	109	88
Operating and other expenses	567	553
Profit before provision for taxes	418	386
Provision for taxes	163	145
Net profit	255	241
Balance sheet – key items:		
Loans to the public (end balance)	15,387	14,452
Loans to the public, net (end balance)	15,126	13,909
Deposits from the public, net (ending balance)	15,738	13,959
Average balance of loans to the public	14,772	14,360
Average balance of deposits from the public	14,955	13,661
Average balance of risk assets	13,345	12,098
Credit margins and deposit margins:		
Margin from credit granting operations	709	677
Margin from activities of receiving deposits	54	36
Other	18	13
Total interest revenues, net	781	726

Contribution of the micro and small business segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to NIS 255 million, compared to NIS 241 million in the corresponding period last year.

Below are key factors affecting the change in segment contribution:

Interest revenues, net amounted to NIS 781 million, compared to NIS 726 million in the corresponding period last year – an increase of 7.6%, attributed to significant increase in lending and deposit volume.

Expenses with respect to credit losses amounted to NIS 109 million, compared to NIS 88 million in the corresponding period last year, an increase of NIS 21 million – due to increase in the loan portfolio in this segment.

Operating expenses amounted to NIS 567 million, compared to NIS 553 million in the corresponding period last year – an increase of 2.5%.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.

Medium business segment

Supervisory definition

The medium business segment includes businesses with annual turnover higher than NIS 50 million and lower than NIS 250 million.

Brief description of segment attributes (using "management approach")

The medium business segment primarily includes medium-sized private and public companies (Middle Market), with total indebtedness between NIS 6 and 25 million.

Clients in this segment are primarily served by the Bank's Business Division, primarily by the Business Sector, operating three business centers nation-wide.

Segment clients primarily operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

Clients in this segment use a range of banking services, associated with a relatively high ratio of required collateral compared to Business Banking segment clients.

Differences between management approach and supervisory definition

- The commercial banking segment, according to management approach, includes businesses with turnover between NIS 30 and 120 million, and total indebtedness between NIS 6 and 25 million. This means that some commercial banking clients (under management approach) whose turnover is below NIS 50 million are classified to the micro and small business segment using the supervisory operating segments.
- On the other hand, business clients attributed to the business banking segment using management approach and whose annual turnover is lower than NIS 250 million, are attributed to the medium business segment using the supervisory approach.

Products and services

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

Major markets and distribution channels

The segment primarily engages in marketing and distribution using three business hubs operating under the Business Division, as well as business centers and Bank branches throughout Israel.

Operations in this segment include development of marketing and business operations based on understanding client needs and customizing comprehensive banking solutions to these needs; providing professional, rapid and efficient service; offering a range of products and solutions customized for client needs with controlled management of risk arising from segment operations, including by specifying financial covenants to monitor clients' financial robustness.

Business Strategy

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

The Bank intends to continue significantly expanding operations in this segment, primarily by recruiting new clients and expanding banking services to current clients and to clients for which the Bank is a secondary bank.

Developments in the medium business segment during the reported period

In 2016 there was no material change to markets and to segment attributes.

Analysis of operating results in the medium business segment

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest revenues, net	187	169
Non-interest financing revenues	–	–
Commissions and other revenues	68	64
Total revenues	255	233
Expenses with respect to credit losses	11	13
Operating and other expenses	96	90
Profit before provision for taxes	148	130
Provision for taxes	58	49
Net profit	90	81
Balance sheet – key items:		
Loans to the public (end balance)	4,869	4,857
Loans to the public, net (end balance)	4,786	4,786
Deposits from the public, net (ending balance)	7,378	6,098
Average balance of loans to the public	4,862	4,849
Average balance of deposits from the public	6,549	5,927
Average balance of risk assets	6,306	6,077
Credit margins and deposit margins:		
Margin from credit granting operations	161	158
Margin from activities of receiving deposits	23	8
Other	3	3
Total interest revenues, net	187	169

Contribution of the medium business segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to NIS 90 million, compared to NIS 81 million in the corresponding period last year.

Below are key factors affecting the change in segment contribution:

Interest revenues, net increased by NIS 18 million, primarily due to increase in credit spreads in this segment. Commissions and other revenues increased by NIS 4 million.

Expenses with respect to credit losses amounted to expenses of NIS 11 million, compared to expenses of NIS 13 million in the corresponding period last year.

Operating expenses amounted to NIS 96 million, compared to NIS 90 million in the corresponding period last year – an increase of 6.6%.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.

Large business segment

Supervisory definition

The large business segment includes businesses with annual turnover higher than NIS 250 million.

Brief description of segment attributes (using "management approach")

The segment specializes in providing complete banking and financing services to the largest companies, in a range of sectors, with total indebtedness exceeding NIS 25 million per client.

Segment clients are served under responsibility of the Bank's Business Division, primarily by the Large Corporation Sector.

Segment clients operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

In its activities in this segment, the Bank emphasizes expansion of the current client base and improved profitability through expansion of activity in financing areas with very high profitability relative to capital, such as trading room transactions, including transactions in derivatives and other products provided to clients by the trading room.

Differences between management approach and supervisory definition

- The business banking segment, according to management approach, includes businesses with turnover higher than NIS 120 million, and total indebtedness higher than NIS 25 million. This means that some business banking clients (under management approach) whose turnover is below NIS 250 million are classified to the medium business segment using the supervisory approach.
- Institutional investors served, under management approach, by business banking are presented as a separate segment under supervisory operating segments.

Products and services

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

Major markets and distribution channels

The main marketing and distribution parties in this segment are the managers and client managers in the Business Banking Division, supported by the Bank's branches and business centers.

In order to provide an optimal response to segment client needs, the servicing of major business banking clients in this segment was placed under the Corporation Sector of the Bank's Business Division, divided into departments and teams having specific industry specialization. The teams work in cooperation with professional Bank departments involved in factoring, foreign trade, capital market, trading room operations etc. – in order to provide a comprehensive solution for client needs.

Business Strategy

The Bank's business strategy for the large business segment is designed to increase the number of clients and to expand business with existing clients. This is to be done while maximizing the economic potential of the capital by focusing on activities having high profitability relative to the capital needed for them, through, inter alia, the following activities:

- Implement an approach based on total outlook on the business client, leveraging credit products and offering other products to establish a comprehensive client relationship.
- Segment business clients by size, sector of operation and other attributes in order to optimally specify their business needs and to provide an appropriate, professional solution.
- Given the legal complexity of transactions in recent years, *inter alia* in combination projects and in urban renewal projects (evacuation-construction schemes and National Zoning Plan 38), these require custom legal specialization.
- Emphasis on profitability and return on uses.

Analysis of operating results in the large business segment

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest revenues, net	444	434
Non-interest financing revenues	–	–
Commissions and other revenues	147	150
Total revenues	591	584
Expenses with respect to credit losses	(24)	45
Operating and other expenses	142	142
Profit before provision for taxes	473	397
Provision for taxes	184	149
Net profit	289	248
Balance sheet – key items:		
Loans to the public (end balance)	12,731	13,359
Loans to the public, net (end balance)	12,525	13,132
Deposits from the public, net (ending balance)	31,422	26,688
Average balance of loans to the public	13,071	14,189
Average balance of deposits from the public	28,061	21,286
Average balance of risk assets	22,731	26,726
Credit margins and deposit margins:		
Margin from credit granting operations	378	404
Margin from activities of receiving deposits	55	24
Other	11	6
Total interest revenues, net	444	434

Contribution of the large business segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to NIS 289 million, compared to NIS 248 million in the corresponding period last year increase of 16.5%.

Total interest revenues, net amounted to NIS 444 million, compared to NIS 434 million in the corresponding period last year.

Expenses with respect to credit losses amounted to revenues of NIS 24 million, compared to expenses of NIS 45 million in the corresponding period last year. Revenues in the current period are due to collection from previously written-off clients.

Operating expenses amounted to NIS 142 million, similar to the corresponding period last year.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach - see Note 29 to the financial statements.

Institutional investor segment

Supervisory definition

This segment includes provident funds, pension funds, study funds, mutual funds, ETFs, insurance companies and stock exchange members who manage client portfolios.

Brief description of segment attributes (using "management approach")

This segment provides service to financial asset managers, incorporating activities involving providing services to financial asset managers:

insurance companies, managers of provident funds, study funds and pension funds, managers of mutual funds and ETFs, stock exchange members and investment portfolio managers.

Segment operations includes operating these financial assets and providing banking services to their managers.

Services include: asset valuation, generating control reports, reporting to authorities, accounting, administration of accounts and rights of provident fund members and calculation of returns.

Banking services also include credit of various types and transactions involving derivatives.

The Bank has agreements in place to provide operating services to provident fund management companies, some of which are associated with the sale of provident funds previously owned by the Bank. As for mutual funds, the Bank has agreements in place to provide services to mutual fund management companies.

The segment also provides comprehensive service to management companies of provident funds and mutual funds.

Differences between management approach and supervisory definition

Under management approach, institutional investors are served by business banking and by the financial management segment, but are presented as a separate segment under supervisory operating segments.

Products and services

The Bank has agreements in place to provide operating services to provident fund management companies, some of which are associated with the sale of provident funds previously owned by the Bank. As for mutual funds, the Bank has agreements in place to provide services to mutual fund management companies.

The segment also provides comprehensive service to management companies of provident funds and mutual funds.

Banking services also include credit of various types and transactions involving derivatives.

Major markets and distribution channels

The key marketing and distribution agents for this segment are managers and account managers at the Business Banking Division, the Finance Division and the Planning and Operations Division. In order to provide an optimal response to segment client needs, the servicing of major business banking clients in this segment was placed under the Corporation Sector of the Bank's Business Division, the Commercial Sector of the Finance Division and the Provident Fund Operations Sector of the Planning and Operations Division, teams work in cooperation with professional Bank departments involved in capital market, trading room operations etc. - in order to provide a comprehensive solution for client needs.

Business Strategy

The Bank's business strategy for this segment is designed to increase the number of clients and to expand business with existing clients. This is to be done while maximizing the economic potential of the capital by focusing on activities having high profitability relative to the capital needed for them,

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

Analysis of operating results of institutional investor segment

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest revenues, net	107	112
Non-interest financing revenues	-	-
Commissions and other revenues	82	77
Total revenues	189	189
Expenses with respect to credit losses	(1)	(7)
Operating and other expenses	139	131
Profit before provision for taxes	51	65
Provision for taxes	20	24
Net profit	31	41
Balance sheet – key items:		
Loans to the public (end balance)	2,629	2,063
Loans to the public, net (end balance)	2,586	2,326
Deposits from the public, net (ending balance)	35,964	36,127
Average balance of loans to the public	2,858	2,176
Average balance of deposits from the public	35,337	37,447
Average balance of risk assets	2,964	3,437
Credit margins and deposit margins:		
Margin from credit granting operations	46	47
Margin from activities of receiving deposits	61	60
Other	-	5
Total interest revenues, net	107	112

Contribution of the institutional investor segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to NIS 31 million, compared to NIS 41 million in the corresponding period last year.

Below are key factors affecting the change in segment contribution:

Interest revenues, net, amounted to NIS 107 million, compared to NIS 112 million in the corresponding period last year. Commission and other revenues increased by NIS 5 million compared to the corresponding period last year. There was no significant change in margin from credit granting operations and in margin from receiving deposits.

Expenses with respect to credit losses amounted to revenues of NIS 1 million, compared to revenues of NIS 7 million in the corresponding period last year, an increase due to the effect of group-based provision in this segment.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.

Financial Management Segment

Supervisory definition

The financial management segment includes trading operations, asset and liability management and non-banking investments.

Trade operations – Investment in securities held for trade, market making operations for securities, operations involving derivatives not designated as hedges and which are not part of asset and liability management for the Bank, borrowing of securities for trading, short selling of securities, underwriting services for securities.

Asset and liability management – including investment in debentures available for sale and in debentures held to maturity, hedging using derivatives, ALM hedging, currency hedging of investments overseas.

Real investments – Investment in shares available for sale and in associates of businesses.

Other financial management operations – management, operation, trust and custody services for banks, sale and management of loan portfolios.

Brief description of segment attributes (using "management approach")

Financial management at the Bank is conducted by the Finance Division. The financial management segment segment operates in Israel and overseas in several key areas: Management of Bank assets and liabilities, management of the debenture portfolio, management of exposure to market risk and liquidity management as well as trading room operations in the financial and capital markets, in conformity with management's viewpoint as to management of these activities.

Asset and liability management operations are managed by the Financial Management Sector, including management of sources and uses, exposures to market risk – including management of liquidity, basis and interest risk, management of transfer prices ("shadow prices"), pricing of special financial transactions and management of the debenture portfolio.

Trading operations are carried out by the Trading Room, including the Bank's activity in foreign currency, options, interest derivatives, securities in Israel and overseas and financial assets, with local and overseas entities as counter-parties.

The Division also includes a unit dedicated to managing relations with financial institutions and investors. This unit is in charge of all activities with overseas banks, including management of correspondent accounts, obtaining and providing service and developing activities in support of Bank client needs.

Business in this segment is subject to the relevant risk management policy and to restrictions imposed by the Board of Directors and by management on various exposure levels.

Differences between management approach and supervisory definition

Under management approach, institutional investors are served by the financial management segment, but are presented as a separate segment under supervisory operating segments.

Products and services

The trading room provides trading services to Bank clients in OTC (mostly: foreign currency, interest, options) and in brokerage of foreign and local securities, with local and overseas entities as counter-parties.

OTC trading – the transactions which may be conducted through the trading room: buy / sell foreign currency, options and interest derivatives. The Bank is licensed for market making in USD/NIS and in Israeli Government debentures.

Securities trading – trading securities to provide a solution for Bank clients' activity on the local market and on world markets. The Trading Department consists of two parts – trading of Israeli securities and trading of foreign securities; both provide execution services for equities, debentures, options and negotiable futures and mutual funds.

Major markets and distribution channels

The trading room provides services for global currencies and securities, primarily in developed nations. The trading room includes a Client Marketing Unit, which provides distribution services for trading room products.

Business Strategy

Key targets for trading room operations are:

Maintain the Bank's position and positioning as a leader in the OTC market in Israel, while maintaining the risk level specified in Bank policy.

Increase OTC business volume.

Increase business volume in trading of securities on the local and foreign markets.

Align operations with local and global regulation.

Achieve appropriate return on equity.

Asset and liability management operations have the key objective of active management of exposure to market risk and of the debenture portfolio, aimed at optimal management of financing profitability, while maintaining appropriate, controlled exposure to market- and liquidity risk, which reflects the Bank's risk appetite, subject to limits specified by decisions of the Board of Directors and management.

Developments in the financial management segment during the reported period

In 2016, operations in this segment were affected by:

- Growing competition in the banking sector, along with a downward trend in commissions and spreads.
- Regulatory changes in the global and local markets.
- Lower trading volumes on the Tel Aviv Stock Exchange.

Analysis of operating results of the financial management segment

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest expenses, net	(126)	(7)
Non-interest financing revenues	291	353
Commissions and other revenues	239	167
Total revenues	404	513
Expenses with respect to credit losses	(1)	(2)
Operating and other expenses	356	412
Profit before provision for taxes	49	103
Provision for taxes	19	65
After-tax profit	30	38
Share of banking corporation in earnings of associates	-	-
Net profit before attribution to non-controlling interests	30	38
Net profit attributed to non-controlling interests	-	(21)
Net profit attributable to shareholders of the banking corporation	30	17
Balance sheet – key items:		
Average balance of risk assets	5,414	5,224
Credit margins and deposit margins:		
Margin from credit granting operations	-	-
Margin from activities of receiving deposits	-	-
Other	(126)	(7)
Total interest expenses, net	(126)	(7)

Contribution of the financial management segment (in conformity with supervisory definitions) to Group profit in 2016 amounted to a profit of NIS 30 million, compared to a profit of NIS 17 million in the corresponding period last year.

Below are key factors affecting the change in segment contribution:

Total financing revenues (net interest revenues and non-interest financing revenues) decreased by NIS 181 million compared to the corresponding period last year, primarily due to lower early mortgage repayments, resulting in lower early repayment fees. Moreover, in the corresponding period last year the Bank recognized revenues from realized debentures held to maturity at Bank Yahav. See analysis of evolution of financing revenues in chapter "Material developments in revenues, expenses and other comprehensive income".

Commissions and other revenues increased by NIS 72 million, due to results of the Bank's continued effort to re-organize assets and to improve the branch network.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.
For more information about the effect of attribution of expenses related to the US DOJ inquiry on this segment, see Note 29.C to the financial statements.

Operating results of overseas operations

Supervisory definition
The Bank's overseas operations are presented separately, divided into operations involving individuals and business operations.

Brief description of segment attributes (using "management approach")
The Bank Group's international operations include providing banking services to businesses and private banking services to individuals, through subsidiaries and branches overseas. The Group's international operations include: private banking services, foreign trade financing; local credit for purchase of real estate; commercial financing and participation in syndicated lending. International operations, in Israel and overseas, report to the Private Banking and International Operations sector in the Bank's Financial Division.

Differences between management approach and supervisory definition
Business and individual clients at overseas branches classified into the various operating segments in conformity with management approach, are classified into the overseas operations segment in the disclosure of supervisory operating segments.
Business and individual clients at overseas branches are presented as a separate segment under supervisory operating segments and under management approach are managed by the various operating segments – mostly private and business banking.

Products and services
Services offered to clients of the overseas operations segment are:
- Private banking services for clients with high financial wealth. These services include management of client deposits and providing financial advice on management of client securities portfolio.
- Credit solutions for needs of individual and business clients, both locally and Israelis operating overseas.

Major markets and distribution channels
The major markets are local clients, mostly from the Jewish community, located in countries where the Bank's overseas affiliates do business, as well as clients resident in Israel whose financial and business needs include banking services provided overseas.
Major distribution channels include participation in professional conferences in countries where the affiliates are located, local advertising to the Jewish community, marketing of the Bank by Bank representatives among the local Jewish community and referrals from current clients.

Business Strategy

The Bank's overseas affiliates operate in a competitive environment of local and international banks operating in the same country, but are focused on providing banking services on a more limited scale, compared to local and international banks. Competition is focused on service quality, response time and maximizing the client-Bank relationship. Each international operations affiliate has a unique target audience. Critical success factors are based on providing fast, personal service at an international level. Service provided to clients is based on understanding their personal needs and providing individual solutions based on intensive knowledge of local markets in order to find the appropriate range of products.

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

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

Developments in the overseas operations segment during the reported period

In recent years, competition with affiliates of Israeli banks overseas has diminished. Furthermore, global regulatory changes have resulted in a change in business focus and changes to client preferences.

Analysis of operating results of overseas operations

	For the year ended December 31,	
	2016	2015
		NIS in millions
Profit and profitability		
Total interest revenues, net	154	111
Non-interest financing revenues	4	5
Commissions and other revenues	31	32
Total revenues	189	148
Expenses with respect to credit losses	1	10
Operating and other expenses	74	80
Profit before provision for taxes	114	58
Provision for taxes	44	22
Net profit	70	36
Balance sheet – key items:		
Loans to the public (end balance)	3,250	3,092
Loans to the public, net (end balance)	3,223	3,061
Deposits from the public, net (ending balance)	5,249	4,041
Average balance of loans to the public	3,195	2,665
Average balance of deposits from the public	4,770	2,974
Average balance of risk assets	3,594	3,018
Credit margins and deposit margins:		
Margin from credit granting operations	92	78
Margin from activities of receiving deposits	11	7
Other	51	26
Total interest revenues, net	154	111

Contribution of overseas operations to Group profit in 2016 amounted to NIS 68 million, compared to NIS 36 million in the corresponding period last year.

Below are key factors affecting the change in segment contribution:

Interest revenues, net amounted to NIS 154 million, compared to NIS 111 million in the corresponding period last year – an increase of 38.7%, attributed to significant increase in lending and deposit volume.

Operating expenses amounted to NIS 74 million, compared to NIS 70 million in the corresponding period last year.

For more details and extensive information about supervisory operating segments and operating results in conformity with management approach – see Note 29 to the financial statements.

For more information about the effect of attribution of expenses related to the US DOJ inquiry on overseas operations, see Note 29.C to the financial statements.

Major Investees

The contribution of investees to net operating profit in 2016 amounted to NIS 132 million, compared with NIS 149 million last year. These data include impact of changes in exchange rates on the balance of investment in overseas investees, covered by the Bank's own sources. Therefore, exchange rates have no impact on Group net profit.

Excluding the aforementioned effect of exchange rates, contribution of investees amounted to NIS 142 million, compared to NIS 148 million in the corresponding period last year – see explanation under Investees below.

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

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

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

Bank Yahav's contribution to Group net profit in 2016 amounted to NIS 42 million, compared with NIS 60 million in 2015. Net profit return on equity for Bank Yahav (average equity, as defined in the Supervisor of Banks' Public Reporting Directives) amounted in 2016 to 7.2%, compared to 11.3% in 2015. Bank Yahav's balance sheet total as of December 31, 2016 amounted to NIS 23,854 million, compared to NIS 22,651 million as of December 31, 2015, an increase of 5%. The balance of loans to the public, net as of December 31, 2016 amounted to NIS 8,931 million, compared to NIS 7,943 million as of December 31, 2015, an increase of 12%.

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

Tefahot Insurance is an insurance agency wholly owned by the Bank, which sells life insurance policies and property insurance policies of clients obtaining mortgages from the Bank. Tefahot Insurance's contribution to Group net profit in 2016 amounted to NIS 72 million, compared with NIS 68 million in 2015.

Other investees operating in Israel

Other investees operating in Israel, wholly controlled by the Bank and supported by Bank infrastructure, contributed NIS 23 million to the Bank's profit in 2016, net, compared with net profit of NIS 18 million in 2015.

United Mizrahi Bank (Switzerland) Ltd.

United Mizrahi Bank (Switzerland) Ltd. ("Mizrahi Bank Switzerland") is focused on international private banking services. The Swiss bank is held by a wholly-owned Bank subsidiary, UMOHC B.V. ("United Mizrahi Overseas Holding Company"), incorporated in Holland.

Net profit of Mizrahi Bank Switzerland in 2016 amounted to CHF 1.0 million, compared to CHF 0.9 million in 2015. Mizrahi Bank Switzerland's balance sheet total as of December 31, 2016 amounted to CHF 193 million, compared to CHF 196 million at the end of 2015.

The balance of loans to the public as of December 31, 2016 amounted to CHF 69 million, compared to CHF 72 million at end of 2015. On December 31, 2016, the Bank had no investments in securities, compared to CHF 3 million at end of 2015. The deposits with banks as of December 31, 2016 amounted to CHF 121 million, compared to CHF 119 million at end of 2015. Deposits from the public as of December 31, 2016 amounted to CHF 131 million, compared to CHF 124 million at end of 2015. On December 31, 2016, the Bank had no deposits from banks, compared to CHF 10 million at end of 2015.

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

The contribution of Mizrahi Overseas Holdings to Group net profit in 2016, net of exchange rate effects, amounted to net profit of NIS 4 million, compared with NIS 2 million in 2015.

Actual net profit results of Mizrahi Overseas Holdings include the effect of changes in exchange rates, which is covered by the Bank's own resources.

For more information about an investigation by the US Department of Justice concerning Bank Group business with its US clients, see Note 26.C.12 to the financial statements.

Investment in non-banking corporations

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

Bank investments in non-banking corporations as of December 31, 2016 amounted to NIS 101 million, similar to the end of 2015, as set forth below:

	For the year ended December 31,	
	2016	2015
	NIS in millions	
Under "securities available for sale"		
Participation units in equity funds	63	61
Negotiable investments	3	2
Investments in corporations presented on cost basis	1	1
Total under "securities available for sale"	67	64
Under "investment in associates":		
Investment in Psagot Jerusalem(1)	19	19
Investments in mezzanine funds(2)	13	16
Investment in Rosario Capital(3)	2	2
Total investment in associates	34	37
Total investment in non-banking corporations	101	101

(1) Psagot Jerusalem is a private company which acquired land in the Jerusalem area to be developed for residential construction. The carrying amount of Bank investments as of December 31, 2016 amounted to NIS 35 million, (same as of end of 2015). For more information about investment in Psagot Jerusalem, see Note 15 to the financial statements.

(2) A mezzanine fund is a fund for interim financing, providing companies in various sectors with financing complementary to bank credit. This financing is typically extended in return for interest, stock options and other equity instruments.

(3) Rosario Capital is a private company engaged in underwriting, assistance and advisory services for private and public issuances, mergers and acquisitions, investment in securities and distribution of securities.

Bank net gain from investments in non-banking corporations, after provision for impairment, in 2016 amounted to NIS 9 million, compared with gain amounting to NIS 6 million in 2015.

Risks overview

Overview of risks and manner of managing them

Day-to-day activities in a variety of balance sheet and off-balance-sheet financial instruments expose the Group to different risks, mainly – market, interest in the Bank portfolio, liquidity, credit and operating risks. The risks management and control policies, in various aspects, is designated to support achievement of the Group's business goals while limiting exposure to such risks.

Risks description

The Bank is engaged in commercial banking operations (business and retail) and in mortgage operations, where the Bank is a leader in the Israeli banking system.

Credit risk is the primary risk faced by banking corporations in the course of their business. At the Bank, this risk is weighted towards retail lending operations, primarily housing loans, which is why the Bank strongly emphasizes risk monitoring in the housing loan portfolio, which is at the core of the Bank's business. For more details see chapter "Credit risk" below.

The Supervisor's directive with regard to additional capital at 1% of the mortgage portfolio, which increased the capital targets gradually from January 1, 2015 to January 1, 2017, impacted the Bank to a more significant extent than was the case for other banks in the system. The Bank has completed application of this directive and as of the end of 2016, has achieved the required capital targets with additional safety margins.

In the business sector, the Bank operates while regularly assessing risk at client level, at sector level and for the economy as a whole (sector concentration). Operations in this have been affected in recent years by expanded operations of institutional investors and insurance companies, which are focused on providing large-scale credit for long terms. Improving liquidity ratios, in conformity with Bank of Israel directives to gradually increase the liquidity coverage ratio (LCR) were a challenge in 2015 and in 2016; at the end of 2016, the Bank has achieved high liquidity ratios with an appropriate safety margin and stable source composition.

The Bank has low exposure to overseas operations, as are its operations in nostro investments, primarily designed for investment of excess liquidity in high-quality assets with minimal credit risk.

Developments in technology and ever increasing sophistication of those involved in cyber attacks result in higher risk, as well as more intense management and monitoring of operating risk, IT risk and information security risk.

The Bank Group is exposed to the effect of regulatory changes on its business, in conformity with the strategic plan outline. The Bank reviews, monitors and prepares for these effects as part of its regular operations.

The Bank is also exposed to macro-economic changes in Israel and overseas, which may affect Bank operations, revenues and capital. The Bank reviews its capital stability under various macro-economic scenarios, as part of the risk management process.

The Bank has in place an extensive framework for management and control of the risks to which the Bank is exposed, including an organizational structure to support management and control of such risks. Risks are is managed at the Group in conformity with Bank of Israel's Proper Business Conduct Directive 310 "Risks management" and in conformity with the framework specified in Basel II, Pillar 2 – including required changes upon Basel III coming into effect. The Bank's Board of Directors and the Board's Risks Management Committee are responsible for setting the required guidelines for management and control of the various risks to which the Bank is exposed in its operations, including setting the risk appetite (maximum allowed exposure) and supervision of Bank compliance with the specified guidelines and risk appetite.

Bank management is responsible for application of these guidelines, using three lines of defense: first line – risks takers or business lines; second line – control line; third line – Internal Audit and by application of diverse processes, tools, supporting IT systems and reporting – designed to ensure Bank compliance with the guidelines specified by the Board of Directors.

The Bank has a structured process in place for mapping and identification of risk associated with Bank operations. The list of material risks is determined based on materiality threshold, reflected in terms of

Bank capital and principles for addressing the various material risks as identified and mapped, including risk appetite and measurement.

Management and mitigation of each risk are included in specific policy documents, which are approved annually bu the Board of Directors. The Bank has also specified the required reporting chain, under normal conditions and under emergency conditions, as well as on-going monitoring of the Bank's risk profile, given the risk appetite specified by the Board of Directors.

Description of risk appetite and risk management

The Bank's risk appetite is specified for all material risks using quantitative and qualitative restrictions; the quantitative restrictions are mostly specified as percentage of Tier I capital at the Bank. The Bank specified restrictions, under normal market conditions and under stress conditions, for most risks – based on the outcome of various stress tests conducted by the Bank. Each year, the risk appetite is challenged by the Chief Risks Officer, management and the Board of Directors, in view of the business targets specified in work plans, in conformity with the strategic plan, the risk profile and outcome of the qualitative process conducted by Bank managers. This process is designed to review the level of various risks and their development over the coming year. Consequently, the Bank's business strategy is supported by an appropriate risk appetite framework with constant monitoring of the risk profile and with alerts issued if the risk profile reaches the specified limits for risk appetite.

Stress testing

The Bank has extensive methodology for conducting diverse stress tests. This methodology and the use of the stress testing results are incorporated in a specific policy document. The Bank extensively uses the stress testing results in the capital planning process, which is part of the ICAAP document. This process reviews whether the Bank has sufficient capital to fulfill the strategic plan, which is challenged by a range of stress tests at various severity levels. These stress tests impact Bank profitability by causing potential loss due to material risks for Bank operations: credit risk, credit concentration risk, market risk, interest risk in the bank portfolio, operating risk etc. Stress tests strongly emphasize the Bank's mortgage portfolio, it's business lending operations, potential impact of information security and cyber events, operational failure events etc. The outcome of capital planning by the Bank, as resulting from the 2016 ICAAP process, indicates that the Bank has sufficient capital to achieve the targets in its strategic plan, even given stress tests at various severity levels. Furthermore, the Bank applies a Uniform Stress Scenario, a stress test based on macro-economic conditions specified by the Bank of Israel for the banking system. The results of the Uniform Scenario support the results of various stress tests conducted by the Bank, showing that the potential impact on Bank performance under such scenario is low relative to the Bank's capital and annual profit.

The Bank's quarterly risks document, which is discussed by management, by the Board Risk Management Committee and by the Bank Board of Directors, provides an extensive view of the different risks at the Bank, with emphasis on the risk profile given the risk appetite specified in all policy documents. Thus, this document complements and reinforces the view of the risk profile provided in the Bank's annual ICAAP document, as noted above.

For more information see the Detailed Risks Management Report on the Bank website.

Credit risk

Risk description

Credit risk is the risk that a borrower or counter-party of the Bank would not fulfill its obligations towards the Bank. 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, overseas credit risk and operating risk which, should they materialize, would have implications for credit risk. Moreover, such risk is interrelated to multiple other risks, such as market and interest risk, liquidity risk, compliance risk etc.

Description of risk appetite and risk management guidelines

Credit risk management at the Bank is carried out in conformity with Directive 311 "Credit risk management" of the Bank of Israel.

The Bank’s Board of Directors has set credit policy, based upon the Bank's objectives and business strategy, emphasizing macro-economic changes in Israel and overseas and their implications on credit risk. The credit policy includes other policy documents which discuss the relevant risks to the Bank's credit operations, including: Credit concentration policy, which ensures that the credit concentration level at the Bank is regularly managed and monitored; derivatives policy, which stipulates the principles for management and monitoring of Bank clients with derivatives activity; collateral policy, which stipulates the principles required for management of client collateral, safety factors required by transaction type and risk factor; and the environmental risks policy.

Risk appetite consists of a long list of benchmarks and risk factors relevant to the Bank's credit operations, including: Economic sectors, borrower groups, risk factors in the mortgage portfolio, unique activity types, quality of credit portfolio, overseas operations etc. and other risk factors relevant for the Bank's credit risk profile and its business operations. Credit risk is also monitored using a range of stress tests, which estimate the potential impact of stress events on the Bank's credit portfolio. This is done, *inter alia*, in order to review Bank resilience to various stress events and as part of the ICAAP process.

Monitoring of the risk profile, in view of the specified risk appetite, is made at the frequency specified under the credit policies, and compliance with these limitations is reported to Bank’s Board of Directors and management. The Bank’s credit policies prescribe principles and rules for making credit available and for the management and control over the loan portfolio, in order to preserve its quality and reduce the inherent risk. These principles and rules enable controlled management of the risk involved in granting loans to borrowers, at the level of the individual borrower, group of borrowers and the level of economic and business sectors. The credit policies are reviewed during the year, in view of developments in the business environment in which the Bank and Bank clients operate and the policy is revised as needed.

The three lines of defense for credit risk are defined as follows:

First line of defense – credit-related business lines at the Bank

The structure of lines of business with regard to credit is based on three divisions, reporting to the President & CEO, as follows:

Retail Division

This division consolidates most of the bank credit activity of individual clients, including mortgages and the activity of small business clients. Bank branches and business centers operate under this division in eight geographic regions.

Business Banking Division

This division handles most banking activity of business clients (including from the real estate and construction sector) of medium to large business operations.

Finance Division

With regard to credit, the Finance Division serves private banking and international operations through private banking units in Israel and through overseas subsidiaries and affiliates.

For more information about client attributes in each segment, see chapter "Explanation and analysis of results and business standing" (Description of Bank Group business by operating segment) above.

The professional units in each of these client segments are responsible for regularly verification, monitoring and control of exposure to clients and operating segments for which they are responsible. This line of defense includes specific control units, such as division controllers and other control functions. These operations are incorporated in specific procedures, which ensure implementation of the specified principles for risk management.

- **Second line of defense – Risks Control** – The Risks Control Division acts as the Bank's independent risks management function, thus serving as the second line of defense within corporate governance for risk management. Its activities include *post-factum* assessment, independent of Bank entities which approve credit, of borrower quality and quality of the Bank's credit portfolio, as well as producing an independent opinion for credit to material clients, as part of the credit approval process.
- **Second line of defense – Chief Accountant** – The Chief Accountant is responsible for credit classification and for determination of provisions for credit losses.
- **Third line of defense – Internal Audit** – Internal Audit serves as the third line of defense within corporate governance for risks management, operating in line with the work plan for auditing the Bank's credit operations.

The Bank operates on multiple levels to monitor and mitigate credit risk in as much as possible, from the credit approval stage, emphasizing the required collateral and financial covenants specified in accordance with procedures, authorization and diversification policies specified by the Bank, through to regular control by business units and dedicated control units operating within the lines of business. This is done with constant effort invested in improving the professional expertise of those involved with credit, by means of banking courses and training, as well as professional seminars at all levels. Concurrently, the Bank invests extensive resources in improving its control mechanisms and IT systems available to decision makers in the credit sector.

In 2016, the Retail Division started using a new computer system which is being gradually put into use, designed to allow the Division to manage its clients by different criteria, including client rating, and to use the new models for underwriting and client pricing. The Bank continues to deploy and expand use of this system while concurrently further developing and upgrading these models.

In 2016, the Amot system was implemented, a new and improved system for management and monitoring of financial covenants. The system is connected to Bank infrastructure systems and supersedes an older system.

For more information about key processes involved in management and control of credit risk at the Bank, see the Detailed Risks Report on the Bank website.

Environmental risks

Environmental risk to the Bank is the risk of loss which may be incurred due to deterioration in the borrower's financial position due to high costs incurred as a result of environmental hazard and regulation concerning environmental protection, or due to impairment of collateral exposed to environmental risk or to the Bank being indirectly liable for an environmental hazard caused by a project funded by the Bank. Environmental risk also includes other risks derived from this risk (goodwill, third party liability etc.) In recent years, global awareness of the potential financial exposure arising from regulations related to environmental protection has grown.

The Bank has a structured methodology for identification, assessment and handling of environmental risk and acts to incorporate management of exposure to environmental risk within all risks at the Bank, including specification of work processes for identification of significant risk when granting credit and inclusion of risk assessment, if any, within periodic assessment of quality of credit extended.

For more information see the Bank's Corporate Social Responsibility Report on the Bank website:

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

Handling of non-performing loans and collection of debts - The handling of problem loans requires special focus and professionalism, other than the level that approved or processed the credit extended and collateral received. Initial identification is typically computer-based by designated departments for identification and control. Identified clients are handled by the Special Client Sector of the Business Division.

In order to identify credit risk materializing, or which may materialize, at the Bank, the Bank regularly conducts a process to review and identify debts, based on specified criteria. Some of these criteria require debt to be classified as problematic debt, while others provide a warning and allow the professional entity to exercise discretion. Debts are reviewed by a ranking of authorizations specified in Bank procedures. This authorization ranking includes individual authorizations, from branch and headquarters staff, to authorizations at higher levels with regard to classifications and provisions granted to regional management and to special headquarter units, to conduct a structured, independent control process. The Chief Accountant forms a second line in the classification and provision setting process; they are responsible, in conformity with Proper Conduct of Banking Business Directive 311, for being the independent entity in charge of classification and setting the provision for credit losses.

A computer system which supports application of measurement and disclosure provisions for impaired debts, credit risk and provision for credit losses, including in identification and control processes, carries out logical, criteria-based testing and determines defaults for debts classification as debts under special supervision, inferior debt, impaired debt or debt in restructuring, as required.

Identification of housing loans (mortgages) with risk attributes is automated by identifying criteria for arrears and other qualitative criteria. In early stages of arrears, the Bank mostly applies automated collection processes. Later on, the Bank applies proactive processes, both internal and external, including legal proceedings, if needed.

For more information about impaired debt, credit risk and provision for credit losses, see Note 1.D. 6 to the financial statements and the Detailed Risk Management Report on the Bank website.

Analysis of credit quality and problematic credit risk

Significant exposure to groups of borrowers

Disclosure of credit risk with respect to significant exposure to borrower groups is provided with regard to each group of borrowers whose net indebtedness, on a consolidated basis, after allowed deductions pursuant to Proper Conduct of Banking Business Directive 313, exceeds 15% of the banking corporation's capital (as defined in Directive 313), NIS in millions:

As of December 31, 2016, the Bank had no borrower group which meets the aforementioned criteria.

Bank business with major borrower groups is conducted subject to several guidelines designed to mitigate risk associated with such activity:

- Activity with borrower groups is primarily done with established, leading public companies.
- Credit is mostly provided for short- and medium term, to be used in current operations of these companies.
- Credit is diversified among Group companies operating in different segments and economic sectors.
- Credit is provided, in as much as possible, to companies which are not mutually dependent or which are subject to mutual covenants or guarantees.

The Bank takes the following steps in order to manage exposure to groups of borrowers:

- Set financial covenants as needed.
- Provide credit against collateral, in as much as possible, and closely monitor exposure not secured by collateral.
- Closely monitor company operations and financial results.
- Closely monitor compliance of borrower group companies with financial covenants, if and when specified.

Major borrowers

Below is the sector composition of the top 6 borrowers for the Group as of December 31, 2016 (NIS in millions):

Borrower no.	Sector	Balance sheet credit risk	Off-balance sheet credit risk	Total credit risk
1.	Construction and real estate	121	908	1,029
2.	Construction and real estate	42	940	982
3.	Construction and real estate	67	708	775
4.	Construction and real estate	417	277	694
5.	Construction and real estate	-	626	626
6	Transport and storage	200	400	600

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

Leveraged financing

Leveraged financing is credit financing provided to customers which fulfills one of the following criteria:

1. **Credit for an equity transaction would be classified according to one of the following rules:**
   - Credit for an equity transaction (as defined below), provided that the balance of such credit exceeds 0.5% of Bank capital or NIS 35 million, whichever is higher.
   - For credit financing acquisition of equity interests in another banking corporation, or in a banking holding corporation, provided that the balance of such credit exceeds NIS 35 million.
   - Additional credit extended to the borrower after the financing for the equity transaction, with repayment primarily based on the cash flows derived from the equity interests whose purchase was financed by the banking corporation.

   "Equity transaction": A transaction with one of the following goals:
   - Buyout – purchase or buyback, by the borrower, of the borrower's issued capital (including an employee stock ownership plan).
   - Acquisition of another corporation – the purchase of any capital rights in another corporation, or the purchase of all, or a significant share, of the assets of another corporation.
   - Capital distribution – the payment of dividends or other transaction whose goal is to increase shareholder value.

   An equity transaction, with regard to leveraged financing, is one where the loan balance exceeds 0.5% of Bank capital and where the LTV ratio exceeds 50%.

2. **Financing for leveraged companies**, which is credit extended to companies with attributes which indicate that an adverse change in the global economic environment or in the specific environment of the sector in which they do business, may significantly impact their capacity to repay the bank. The Bank has specified criteria for defining credit included in this category, based on the business client's credit risk rating, as reflected by the Bank's rating model; it also specified benchmarks for leveraging (i.e. for significantly high deviation from typical norms for the sector), determined based on generally accepted financial ratios among Bank clients with material credit in major sectors in which the Bank operates. Leverage benchmarks and economic sectors are reviewed based on changes to the business environment and are modified as necessary. Borrowers flagged for one or more of the criteria specified are individually reviewed by a forum which includes representatives from the Business Division, the Risks Control Division and the Accounting and Financial Reporting Division, which reviews changes to financial parameters of the company and the economic environment in which it operates.

As from January 1, 2016, amendments became effective with regard to limits on financing of equity transactions in conformity with Proper Conduct of Banking Business Directive 323 and Proper Conduct of Banking Business Directive 327 with regard to management of leveraged loans. These regulations specify the overall risks framework for leveraged loans.

Details of Bank exposure to credit constituting leveraged financing are as follows:

Credit for equity transactions (NIS in millions):

	December 31, 2016				December 31, 2015			
Economic sector of acquired company	On-balance sheet credit risk	Off-balance sheet credit risk	Total credit risk	Individual provision for credit losses	On-balance sheet credit risk	Off-balance sheet credit risk	Total credit risk	Individual provision for credit losses
Construction and real estate	-	-	-	-	178	-	178	-
Commerce	81	15	96	-	112	1	113	-
Total	81	15	96	-	290	1	291	-

Credit to leveraged companies (NIS in millions):

	December 31, 2016				December 31, 2015			
Economic sector of borrower	On-balance sheet credit risk	Off-balance sheet credit risk	Total credit risk	Individual provision for credit losses	On-balance sheet credit risk	Off-balance sheet credit risk	Total credit risk	Individual provision for credit losses
Construction and real estate	64	210	274	-	193	280	473	-
Commerce	404	161	565	-	128	38	166	-
Financial services	309	-	309	-	-	-	-	-
Information and communications	-	95	95	-	61	96	157	-
Total	777	466	1,243	-	382	414	796	-

Developments in problematic credit risk

Below is a summary of overall problematic credit risk and non-performing assets before provision for credit losses, in accordance with provisions for measurement and disclosure of impaired debt, credit risk and provision for credit loss (NIS in millions):

	Total credit risk	
	December 31, 2016	December 31, 2015
Troubled credit risk:		
Impaired credit risk	893	986
Inferior credit risk	428	82
Credit risk under special supervision – housing	853	957
Credit risk under special supervision – other	757	690
Total troubled credit risk	2,931	2,715

Major risk benchmarks related to credit quality (in percent):

	December 31, 2016	December 31, 2015
Ratio of impaired loans to the public to total loans to the public	0.4	0.5
Ratio of impaired loans to the public to total non-housing loans	1.2	1.6
Ratio of problematic loans to the public to total non-housing loans	2.8	2.4
Ratio of housing loans in arrears 90 days or longer to total loans to the public (1)(2)	0.5	0.5
Ratio of problematic credit risk to total credit risk with respect to the public	1.3	1.2

(1) This non-housing rate is negligible.
(2) Balance of credit in arrears before provision by extent of arrears.

For more information see chapter "Explanation and analysis of results and business standing" above.

Below is a summary of impaired debt under restructuring made or in default (NIS in millions):

	December 31, 2016		December 31, 2015	
	Recorded debt balance before restructuring	Recorded debt balance after restructuring	Recorded debt balance before restructuring	Recorded debt balance after restructuring
Restructurings made	52	48	53	41

	December 31, 2016	December 31, 2015
	Recorded debt balance	Recorded debt balance
Restructurings made which are in default	5	5

For more information see Note 30.B.2.C to the financial statements.

Analysis of change to impaired debts

Movement in impaired debts and impaired debt under restructuring (NIS in millions):

	Impaired debts not under restructuring				Impaired debts under restructuring			
	Commercial	Housing	Individual – other	Total	Commercial	Housing	Individual – other	Total
Balance of impaired debts as of December 31, 2015	537	24	27	588	175	-	54	229
Impaired debts and/or restructured debts for the period	238	3	10	251	13	-	8	21
Impaired debt classified as debt in good standing or as problematic, non-impaired debt	(26)	-	(3)	(29)	(14)	-	(1)	(15)
Write-offs for the period	(44)	-	(5)	(49)	(6)	-	(5)	(11)
Recovery of debts written off for accounting purposes in previous years	19	-	4	23	4	-	4	8
Other changes	(242)	-	(9)	(251)	(70)	-	(14)	(84)
Balance of impaired debts as of December 31, 2016	482	27	24	533	102	-	46	148

	Impaired debts not under restructuring				Impaired debts under restructuring			
	Commercial	Housing	Individual – other	Total	Commercial	Housing	Individual – other	Total
Balance of impaired debts as of December 31, 2014	338	3	15	356	367	-	58	425
Impaired debts and/or restructured debts for the period	392	21	15	428	6	-	7	13
Impaired debt classified as debt in good standing or as problematic, non-impaired debt	(66)	-	(1)	(67)	(6)	-	(2)	(8)
Write-offs for the period	(44)	-	(4)	(48)	(9)	-	(4)	(13)
Recovery of debts written off for accounting purposes in previous years	18	-	7	25	22	-	6	28
Other changes	(101)	-	(5)	(106)	(205)	-	(11)	(216)
Balance of impaired debts as of December 31, 2015	537	24	27	588	175	-	54	229

For more information about problematic credit risk, see Notes 13 and 30 to the financial statements.

Analysis of provision for credit losses

Analysis of movement in balance of provision for credit losses (NIS in millions):

	Commercial	Housing	Individual – other	Total	Banks and governments	Total
Balance of provision as of December 31, 2015	700	614	192	1,506	3	1,509
Expenses with respect to credit losses	96	13	92	201	(1)	200
Accounting write-offs	(191)	(12)	(133)	(336)	-	(336)
Recovery of debts written off for accounting purposes in previous years	119	-	57	176	-	176
Net accounting write-offs	(72)	(12)	(76)	(160)	-	(160)
Balance of provision as of December 31, 2016	724	615	208	1,547	2	1,549

	Commercial	Housing	Individual – other	Total	Banks and governments	Total
Balance of provision as of December 31, 2014	635	624	186	1,445	5	1,450
Expenses with respect to credit losses	149	9	55	213	(2)	211
Accounting write-offs	(211)	(20)	(114)	(345)	-	(345)
Recovery of debts written off for accounting purposes in previous years	127	1	65	193	-	193
Net accounting write-offs	(84)	(19)	(49)	(152)	-	(152)
Balance of provision as of December 31, 2015	700	614	192	1,506	3	1,509

For more information about provision for credit losses see Notes 13 and 30 to the financial statements.

Major risk benchmarks related to provision for credit losses (in percent):

	December 31, 2016	December 31, 2015
Ratio of provision for credit losses to total loans to the public	0.9	0.9
Ratio of provision for credit losses to total credit risk with respect to the public	0.7	0.7
Ratio of expenses with respect to credit losses to average balance of loans to the public, gross	0.1	0.1
Ratio of net write-offs to average balance of loans to the public, gross	0.1	0.1
Ratio of expenses with respect to credit losses to average balance of loans to the public, net	0.1	0.1
Of which: With respect to commercial loans other than housing loans(1)	0.3	0.4
Ratio of net write-offs to average balance of loans to the public, net	0.1	0.1

(1) The rate with respect to housing loans with respect to credit is negligible.

For more information about changes to components of the provision for credit losses, see chapter "Material developments in revenues, expenses and other comprehensive income" above.

For information about the Supervisor of Banks' directives with regard to group provision for credit losses, see Note 1.C. 4. to the financial statements.

Credit risk to individuals (excluding housing loans)[1]

The household segment is a key growth engine and a significant component of the Bank's strategic plan for 2017-2021.

The individual client segment is 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. A recession in non-banking operations is a major risk factor for household activity and higher unemployment may increase the number of clients who face difficulties.

Credit policy and work procedures with regard to extending credit, including to individual clients, include directives and guidelines with regard to proper credit underwriting and adapting credit to client needs and repayment capacity: Review of credit objective, requested LTV, loan term, analysis of client's repayment capacity and repayment sources, for all of their indebtedness. This is done along with review of various economic parameters of the client and based on familiarity with the client and the cumulative experience working with the client.

The Bank regularly monitors the risk level in the loan portfolio to individuals, including by using an internal model for credit rating of individual clients, monitoring and analysis of expenses with respect to credit losses and by conducting various stress tests, including stress tests in conformity with Bank of Israel directives, which include scenarios such as: economic recession, significant increase in unemployment and higher interest rates.

Below is information about credit risk to individuals – balances and various risk attributes as of December 31 (NIS in millions):

	December 31,	
	2016	2015
Debts		
Checking accounts and credit cards	5,553	5,427
Auto loans	1,883	1,600
Other loans and credit	10,477	8,850
Total debt (on-balance sheet credit)	17,913	15,877
Unutilized facilities, guarantees and other commitments		
Checking account and credit cards – unutilized facilities	10,097	10,811
Guarantees	195	193
Other liabilities	61	93
Total unutilized facilities, guarantees and other commitments (off-balance sheet credit)	10,353	11,097
Total credit risk to individuals	28,266	26,974
Of which:		
Part of loans maturing in over 5 years[2]	1,911	1,291
On-balance sheet credit over NIS 300 thousand	1,114	914
Financial asset portfolio and other collateral against credit risk[4]		
Financial assets portfolio	3,443	3,197
Other collateral[3]	1,201	1,125
Total financial asset portfolio and other collateral against credit risk	4,644	4,322

(1) As defined in Proper Banking Conduct Directive 451.
(2) Primarily loans to salaried Government employees, where loan repayment is directly deducted from the client's pay check and which bear significantly lower risk than similar loans for the same term.
(3) Collateral is after applying the safety factor, in conformity with Bank factors accounted for when extending credit.
(4) Amounts presented are the financial assets portfolio and other collateral, only up to client indebtedness amount.

Troubled credit risk before provision for credit losses (NIS in millions):

	As of December 31, 2016			As of December 31, 2015		
	Credit risk(1)			Credit risk(1)		
	On balance sheet	Off balance sheet	Total	On balance sheet	Off balance sheet	Total
Balance of problematic credit risk	183	3	186	187	5	192
Problematic credit risk rate(2)	1.02%	0.03%	0.66%	1.18%	0.05%	0.72%

(1) On- and off-balance sheet credit before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(2) The ratio of problematic credit risk to total credit risk before provision for credit losses.

Below is the expense rate with respect to credit losses to individuals (annualized)

	For the year ended December 31,	
	2016	2015
Expense with respect to credit losses as percentage of total loans to the public to individuals	0.51%	0.35%

Data for credit risk to individuals show that:

- Total debts by individuals (on-balance sheet credit) increased by 12.8%, primarily due to increase in loans and other credit.
- There was no significant change to composition of debts by individuals in 2016.
  As of December 31, 2016:
  Checking accounts and credit cards - 31%
  Auto loans - 11%
  Other loans and credit - 58%
- Of all debts (on-balance sheet credit) as of December 31, 2016, 26% is secured by financial assets and other collateral in the client's account (essentially unchanged from the year-ago period).

Given the risk attributes of this segment, the Bank increases its qualitative group-based provision for individuals, as directed by the Supervisor of Banks.

Moreover, the increase in expenses with respect to credit losses is due, *inter alia*, to the impact of legislation which reduces debt repayment by individual clients who are in difficulties.

Credit risk in construction and real estate economic sector in Israel

Credit operations in this sector account for a significant component of credit operations of the Business Division. In financing the construction and real estate industry, specific analysis and monitoring tools are used to assist the Bank in reaching decisions on the granting of financial support to the various projects. Construction financing in this industry is focused mainly on residential construction in areas with strong demand in central Israel at mid-level prices. In addition, the financing is allocated between geographic regions, based inter alia on relevant demand. In providing credit for construction, the Bank focuses on the financial support method (closed assistance). The application of this method is designed to reduce the exposure to risks in the granting of the loans, because it incorporates current and close monitoring of the progress of the financed project, both before the loans are provided, and as the project receives the financial support, while maintaining a distinction between the financed projects and the business risk inherent in the other activities of the developer-borrower. The Bank is assisted by outside construction supervisors, and also relies on liens on the land in the project, to secure the loans. Loans are issued for financed projects only by branches with professional knowledge of the subject, and under the supervision of the construction and real estate sector. The Bank also sets policies and rules for financing other real estate transactions, such as financing for rental properties, purchase groups, National Zoning Plan 38 etc. In 2016, the Business Division and the Retail Division created units aimed at providing a response to smaller-scale projects.

For more information about the Bank acquiring an insurance policy for guarantees on December 28, 2016, see chapter "Significant events in the Bank Group's business".

Below is information about credit risk in the construction and real estate economic sector in Israel, by real estate collateral type (NIS in millions)

							December 31, 2016
	Credit risk to the public(1)						
	Credit risk			Total problematic credit risk		Balance of provision for credit losses	
	On balance sheet(2)	Off balance sheet(3)	Total	Impaired	Other problematic(4)	Balance sheet credit risk	Off-balance sheet credit risk
Secured by real estate in Israel:							
Housing	6,144	14,445	20,589	170	211	48	32
Commercial and industrial	3,667	977	4,644	63	8	60	4
Total secured by real estate in Israel:	9,811	15,422	25,233	233	219	108	36
Not secured by real estate in Israel	2,435	2,322	4,757	159	39	42	13
Total for construction and real estate economic sector in Israel	12,246	17,744	29,990	392	258	150	49
Of which: Designated for project assistance	5,740	13,309	19,049	78	271	48	33

							December 31, 2015
	Credit risk to the public(1)						
	Credit risk			Total problematic credit risk		Balance of provision for credit losses	
	On balance sheet(2)	Off balance sheet(3)	Total	Impaired	Other problematic(4)	Balance sheet credit risk	Off-balance sheet credit risk
Secured by real estate in Israel:							
Housing	4,827	13,930	18,757	29	306	47	32
Commercial and industrial	3,522	901	4,423	48	4	55	3
Total secured by real estate in Israel:	8,349	14,831	23,180	77	310	102	35
Not secured by real estate in Israel	2,666	2,499	5,165	280	76	73	11
Total for construction and real estate economic sector in Israel	11,015	17,330	28,345	357	386	175	47
Of which: Designated for project assistance	4,220	13,077	17,297	6	283	27	29

(1) On- and off-balance sheet credit risk, problematic credit risk and impaired credit to the public are stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower.

(2) Loans to the public, investment in debentures by the public, other debt by the public and other assets with respect to derivative instruments against the public.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits.

(4) On- and off-balance sheet credit risk with respect to the public, which is inferior or under special supervision.

Below is information about credit risk in the construction and real estate economic sector in Israel, by asset status (NIS in millions):

						December 31,
			2016			2015
			Credit risk[1]		Credit risk[1]	
	On balance sheet	Off balance sheet	Total	On balance sheet	Off balance sheet	Total
Real estate collateral in Israel						
Real estate yet to be constructed:						
Raw land	3,860	1,074	4,934	2,572	904	3,476
Real estate under construction	3,870	13,828	17,698	3,517	13,410	16,927
Real estate constructed	2,081	520	2,601	2,260	517	2,777
Total credit secured by real estate in Israel	9,811	15,422	25,233	8,349	14,831	23,180
Not secured by real estate in Israel	2,435	2,322	4,757	2,666	2,499	5,165
Total credit risk for construction and real estate	12,246	17,744	29,990	11,015	17,330	28,345

(1) On- and off-balance sheet credit risk, problematic credit risk and impaired credit to the public are stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower.

Credit risk data for the construction and real estate clients sector show that 47% of the on-balance sheet credit risk and 75% of the off-balance sheet credit risk is associated with closed assistance to real estate projects, mostly for residential construction in areas of strong demand in Central Israel and in Jerusalem. Most of the off-balance sheet credit is due to guarantees provided to home buyers pursuant to the Sale Act.

Most of the credit risk in the construction and real estate sector is backed by real estate fully pledged to secure loan repayment. Note that for credit not secured by real estate collateral, there is other collateral in place, such as: deposits, securities etc.

The share of the construction and real estate sector in Israel out of total credit risk to the public at the Bank as of December 31, 2016, as presented in chapter "Risks" below (Credit Risk by Economic Sector) is 13.4%.

Note that proper Banking Conduct Directive 315, the rate of indebtedness of the construction and real estate sector (for calculation of sector concentration) is 9.13% (excluding liabilities, including contingent liabilities to extend credit or to provide guarantees and amounts of Sales Act guarantees for which the Bank has obtained an insurance policy).

Credit Risk by Economic Sector - Consolidated
As of December 31, 2016
Reported amounts (NIS in millions)

	Debts[1]	Off balance sheet debts[1] and credit risk (other than derivatives)[2]: Guarantees and other commitments on account of clients	Total credit risk: Total	Debentures[4]	Fair value of derivatives
Public – commercial					
Agriculture, forestry and fishing	594	184	778	-	–
Mining and excavation	336	252	588	-	18
Industry and production	5,153	3,050	8,203	-	78
Construction and real estate - construction[7]	10,150	17,400	27,550	-	2
Construction and real estate – real estate operations	2,096	344	2,440	-	2
Electricity and water delivery	524	558	1,082	-	331
Commerce	7,848	2,297	10,145	-	63
Hotels, dining and food services	807	229	1,036	-	-
Transport and storage	1,107	710	1,817	-	5
Information and communications	502	578	1,080	-	-
Financial services	3,484	6,327	9,811	-	652
Other business services	2,369	1,103	3,472	-	12
Public and community services	1,356	385	1,741	-	8
Total commercial credit	36,326	33,417	69,743	-	1,171
Private individuals – housing loans	114,691	5,659	120,350	-	-
Private individuals – other	17,913	10,353	28,266	-	14
Total	168,930	49,429	218,359	-	1,185
For borrowers' activities overseas	3,849	1,371	5,220	19	135
Total loans to the public	172,779	50,800	223,579	19	1,320
Banking corporations	2,509	281	2,790	19	2,264
Governments	330	–	330	10,133	–
Total credit	175,618	51,081	226,699	10,171	3,584

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements.
(2) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits, except for derivatives.
(3) Includes with respect to off-balance sheet credit instruments (included on balance sheet under Other Liabilities).
(4) Includes borrowed securities amounting to NIS 9 million.
(5) Credit risk whose credit rating as of the report date matches the credit rating for new credit performance, in conformity with Bank policy. In conformity with the Supervisor of Banks' directives, the directive is to be applied prospectively as from the 2014 financial statements.
(6) On- and off-balance sheet credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer.
(7) Includes on-balance sheet credit risk amounting to NIS 1,544 million and off-balance sheet credit risk amounting to NIS 1,646 million, provided to certain purchase groups in the process of construction and includes off-balance sheet credit risk amounting to NIS 6,111 million for which insurance has been acquired to cover the Sales Act guarantee portfolio from international re-insurers.

			Total problematic credit risk		Problematic off balance sheet debts[1] and credit risk (other than derivatives)		
					Credit losses[3]		
Futures transactions	Total	Credit performance rating[5]	Problematic[6]	Impaired	Expenses with respect to credit losses	Net accounting write-off	Balance of provision for credit losses
-	778	767	11	7	4	2	8
9	615	615	-	-	(2)	-	4
135	8,416	8,228	188	91	20	15	92
1	27,553	26,984	569	314	7	11	140
3	2,445	2,364	81	78	(19)	-	59
95	1,508	1,503	5	3	3	2	4
52	10,260	9,725	535	211	61	21	200
-	1,036	1,011	25	11	9	7	19
5	1,827	1,810	17	11	7	4	9
4	1,084	1,075	9	3	(15)	1	7
1,519	11,982	11,653	329	17	(4)	(16)	96
53	3,537	3,468	69	27	23	15	41
41	1,790	1,767	23	18	6	8	8
1,917	72,831	70,970	1,861	791	100	70	687
–	120,350	119,470	880	27	13	12	614
37	28,317	27,893	186	71	92	76	208
1,954	221,498	218,333	2,927	889	205	158	1,509
30	5,404	5,400	4	4	(4)	2	38
1,984	226,902	223,733	2,931	893	201	160	1,547
786	5,859	5,859	-	-	(1)	-	2
–	10,463	10,463	-	-	-	-	-
2,770	243,224	240,055	2,931	893	200	160	1,549

Credit Risk by Economic Sector - Consolidated - continued

As of December 31, 2015

Reported amounts (NIS in millions)

	Off balance sheet debts[1] and credit risk (other than derivatives)[2]			Total credit risk	
	Debts[1]	Guarantees and other commitments on account of clients	Total	Debentures[4]	Fair value of derivatives
Public – commercial					
Agriculture, forestry and fishing	617	185	802	-	–
Mining and excavation	505	314	819	-	29
Industry and production	5,059	3,277	8,336	-	63
Construction and real estate - construction[7]	8,866	17,146	26,012	-	1
Construction and real estate – real estate operations	2,149	184	2,333	-	2
Electricity and water delivery	674	543	1,217	-	280
Commerce	7,978	2,054	10,032	-	42
Hotels, dining and food services	752	229	981	-	-
Transport and storage	968	404	1,372	-	1
Information and communications	902	462	1,364	-	7
Financial services	3,398	6,534	9,932	-	1,041
Other business services	2,224[8]	914	3,138[8]	-	7
Public and community services	1,037	317	1,354	-	9
Total commercial credit	35,129[8]	32,563	67,692[8]	-	1,482
Private individuals – housing loans	105,635	7,352	112,987	-	-
Private individuals – other	15,877[8]	11,097	26,974[8]	-	33
Total	156,641	51,012	207,653	-	1,515
For borrowers' activities overseas	3,963	1,269	5,232	21	57
Total loans to the public	160,604	52,281	212,885	21	1,572
Banking corporations	3,096	262	3,358	274	1,955
Governments	316	16	332	11,523	–
Total credit	164,016	52,559	216,575	11,818	3,527

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements.
(2) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower lending limits, except for derivatives.
(3) Includes with respect to off-balance sheet credit instruments (included on balance sheet under Other Liabilities).
(4) Includes borrowed securities amounting to NIS 71 million.
(5) Credit risk whose credit rating as of the report date matches the credit rating for new credit performance, in conformity with Bank policy. In conformity with the Supervisor of Banks' directives, the directive is to be applied prospectively as from the 2014 financial statements.
(6) On- and off-balance sheet credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer.
(7) Includes on-balance sheet credit risk amounting to NIS 1,285 million and off-balance sheet credit risk amounting to NIS 1,467 million, extended to certain purchase groups which are in the process of construction.
(8) Reclassified.

			Total problematic credit risk			Problematic off balance sheet debts[1] and credit risk (other than derivatives)	
							Credit losses[3]
Futures transactions	Total	Credit performance rating[5]	Problematic[6]	Impaired	Expenses with respect to credit losses	Net accounting write-off	Balance of provision for credit losses
-	802	794	8	7	1	2	6
11	859	859	-	-	2	-	6
121	8,520	8,369	151	84	23	17	87
1	26,014	25,397	617	233	(5)	(2)	144
2	2,337	2,211	126	124	37	52	78
80	1,577	1,575	2	1	-	-	3
29	10,103	9,684	419	338	78	27	160
-	981	951	30	20	10	7	17
2	1,375	1,357	18	5	(2)	(1)	6
2	1,373	1,301	72	3	17	-	23
2,564	13,537	13,519	18	15	(35)	(30)	84
46	3,191[8]	3,151[8]	40	19	6	11	33[8]
45	1,408	1,384	24	18	1	-	10
2,903	72,077[8]	70,552	1,525	867	133	83	657
-	112,987	112,007	980	24	9	19	613
60	27,067[8]	26,565[8]	195	81	55	49	192[8]
2,963	212,131	209,124	2,700	972	197	151	1,462
28	5,338	5,323	15	14	16	1	44
2,991	217,469	214,447	2,715	986	213	152	1,506
599	6,186	6,186	-	-	(2)	-	3
-	11,855	11,855	-	-	-	-	-
3,590	235,510	232,488	2,715	986	211	152	1,509

Exposure to Foreign Countries – Consolidated[1]

Reported amounts (NIS in millions)

Part A – Information regarding total exposure to foreign countries and exposure to countries for which total exposure to each country exceeds 1% of total consolidated assets or 20% of capital, whichever is lower:

As of December 31, 2016													
	Balance sheet exposure[2]									Off-balance sheet exposure[2][3][6]			
Country	Cross-border balance sheet exposure			Balance sheet exposure of Bank affiliates in foreign country to local residents								Cross-border balance sheet exposure	
	To governments[4]	To banks	To others	Balance sheet exposure before deduction of local liabilities	Deduction with respect to local liabilities	Net balance sheet exposure after deduction of local liabilities	Total balance sheet exposure	On-balance sheet problematic credit risk	Impaired debts	Total off-balance sheet exposure	Of which: Off-balance sheet problematic credit risk	Maturing in under 1 year	Maturing in over 1 year
USA	2,660	413	1,208	405	405	-	4,281	9	-	1,268	-	1,646	2,635
UK	-	159	422	978	551	427	1,008	6	-	3,411	-	201	380
France	-	126	1,304	-	-	-	1,430	19	-	916	-	200	1,230
Others [5]	121	515	2,122	-	-	-	2,758	4	-	3,054	-	1,248	1,510
Total exposure to foreign countries	2,781	1,213	5,056	1,383	956	427	9,477	38	-	8,649	-	3,295	5,755
Of which: Total exposure to LDC countries	-	1	509	-	-	-	510	1	-	151	-	147	363
Of which: Total exposure to Greece, Portugal, Spain, Italy and Ireland	-	2	51	-	-	-	53	-	-	837[6]	-	14	39

(1) Based on final risk, after effect of guarantees, liquid collateral and credit derivatives.
(2) On- and off-balance sheet credit risk, troubled commercial credit risk and impaired debt are stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.
(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limits, in conformity with Proper Conduct of Banking Business Directive 313.
(4) Governments, official institutions and central banks.
(5) The Bank closely monitors events in the financial markets which started after the balance sheet date and adjusts its current operations as required. The Bank informs the Supervisor of Banks of its exposure to foreign financial institutions and of steps taken to mitigate the risk associated with its operations.
(6) The balance of off-balance sheet exposure includes NIS 6,111 million with respect to acquiring insurance from international re-insurers for the portfolio of Sales Act guarantees for borrowers in the real estate sector in Israel. Includes NIS 767 million for international re-insurers from Ireland, rated A.

Exposure to Foreign Countries – Consolidated[(1)] – continued

Reported amounts (NIS in millions)

	As of December 31, 2015												
	Balance sheet exposure[(2)]							Off-balance sheet exposure[(2)(3)]					
Country	Cross-border balance sheet exposure			Balance sheet exposure of Bank affiliates in foreign country to local residents								Cross-border balance sheet exposure	
	To governments[(4)]	To banks	To others	Balance sheet exposure before deduction of local liabilities	Deduction with respect to local liabilities	Net balance sheet exposure after deduction of local liabilities	Total balance sheet exposure	On-balance sheet problematic credit risk	Impaired debts	Total off-balance sheet exposure	Of which: Off-balance sheet problematic credit risk	Maturing in under 1 year	Maturing in over 1 year
USA	2,635	945	1,297	405	405	–	4,877	13	1	407	-	2,083	2,794
Others [(5)]	46	750	3,685	1,063	370	693	5,174	34	1	1,012	-	1,215	3,266
Total exposure to foreign countries	2,681	1,695	4,982	1,468	775	693	10,051	47	2	1,419	-	3,298	6,060
Of which: Total exposure to LDC countries	6	1	550	-	-	-	557	1	-	80	-	177	380
Of which: Total exposure to Greece, Portugal, Spain, Italy and Ireland	-	5	49	-	-	-	54	-	-	14	-	18	36

The exposure presented above represents, in accordance with directives of the Supervisor of Banks, exposure based on final risk. The party bearing the final risk is an individual, business, institution or instrument which provides "credit reinforcement" to the Bank, such as guarantees, collateral, insurance contracts or credit derivatives. When no "credit reinforcement" exists, the party bearing the final risk is the debtor.

The row "Total exposure to LDC countries" includes total exposure to countries classified as "Less Developed Countries" (LDC) in Proper Conduct of Bank Businesses Directive 315 "Supplementary provision for doubtful debts".

Balance sheet exposure to such country includes cross-border balance sheet exposure and balance sheet exposure of affiliates of the banking corporation in foreign country to local residents. Cross-border balance sheet exposure includes balance sheet exposure of Israeli offices of the banking corporation to residents of the foreign country and balance sheet exposure of overseas affiliates of the banking corporation to non-residents of the country where the affiliate is located.

Balance sheet exposure of affiliates of the banking corporation in a foreign country to local residents includes balance sheet exposure of affiliates of the banking corporation in that foreign country to local residents, less liabilities of these affiliates (deducted up to the exposure amount).

(1) Based on final risk, after effect of guarantees, liquid collateral and credit derivatives.
(2) On- and off-balance sheet credit risk, troubled commercial credit risk and impaired debt are stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.
(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limits, in conformity with Proper Conduct of Banking Business Directive 313.
(4) Governments, official institutions and central banks.

Exposure to Foreign Countries – Consolidated[1] – continued

Reported amounts (NIS in millions)

Part B – Information regarding countries for which total exposure to each country is between 0.75%-1% of total consolidated assets or between 15%-20% of capital, whichever is lower:

	December 31, 2016		December 31, 2015	
	Balance sheet exposure	Off-balance sheet exposure	Balance sheet exposure	Off-balance sheet exposure
France	-	-	1,727	138
UK	-	-	1,588	250

Part C – Information regarding balance sheet exposure to foreign countries facing liquidity issues

Movement in balance sheet exposure to foreign countries facing liquidity issues:

	For the year ended December 31, 2016		For the year ended December 31, 2015	
	Ireland		Ireland	
Exposure at start of reported period	16	-	14	-
Net change in short-term exposure	(1)	-	2	-
Exposure at end of reported period	15	-	16	-

(1) Based on final risk, after effect of guarantees, liquid collateral and credit derivatives.

Credit exposure to foreign financial institutions

Below is information on the Bank's exposure to foreign financial institutions[(1)(2)] (NIS in millions):

External credit rating	On-balance sheet credit risk[(3)]		Off balance sheet credit risk[(4)]	Current credit exposure	
	Before offset of deposits with respect to master netting agreements[(5)]	After offset of deposits with respect to master netting agreements[(6)]		Before offset of deposits with respect to master netting agreements	After offset of deposits with respect to master netting agreements[(5)]
	As of December 31, 2016				
AAA to AA-	597	409	1,698	2,295	2,107
A+ to A-	628	419	5,425	6,053	5,844
BBB+ to BBB-	25	7	-	25	7
BB+ to B-	-	-	18	18	18
Lower than B-	-	-	-	-	-
Unrated	1	1	-	1	1
Total credit exposure to foreign financial institutions	1,251	836	7,141	8,392	7,977
	As of December 31, 2015				
AAA to AA-	629	572	1	630	573
A+ to A-	558	551	77	635	628
BBB+ to BBB-	9	6	-	9	6
BB+ to B-	-	-	14	14	14
Lower than B-	-	-	-	-	-
Unrated	34	34	-	34	34
Total credit exposure to foreign financial institutions	1,230	1,163	92	1,322	1,255

As of December 31, 2016 and December 31, 2015 there was no problematic commercial credit risk, net. Problematic credit risk – credit risk for impaired, inferior credit or credit under special supervision.

(1) Foreign financial institutions include: banks, investment banks, brokers/dealers, insurance companies, institutional entities and entities controlled by the former. Bank exposure is almost entirely to banks and investment banks primarily incorporated in the UK, USA, Germany, Switzerland and France.
(2) After deduction of provision for credit losses.
(3) Bank deposits, credit to the public, investment in debentures, securities borrowed or acquired in conjunction with resale agreements and other assets with respect to derivative instruments.
(4) Primarily guarantees and commitments to grant credit, including guarantees to secure indebtedness of third parties. (6) The balance of off-balance sheet exposure to financial institutions includes NIS 6,111 million with respect to acquiring insurance from international re-insurers for the portfolio of Sales Act guarantees for borrowers in the real estate sector in Israel.
(5) Presented net of fair value of liabilities with respect to derivative instruments for counter-parties which have signed master netting agreements. Comparative figures were reclassified.
(6) With respect to offset of cash deposits used as collateral for transactions with regard to financial derivatives.

The aforementioned credit exposure excludes exposure to financial institutions for which complete, explicit government guarantees are in place, and exclude investments in asset-backed securities. For further information with regard to credit exposure composition with respect to derivative instruments vis-à-vis banks and dealers/brokers (domestic and foreign), see Note 28.C to the financial statements.

Some of the exposures listed in the above table are included under "Credit Risk by Economic Sector", under "Financial services". This includes deposits with banks, credit to the public, public investment in debentures and other assets with respect to derivative instruments. Futures transactions, weighted in accordance with rules stated in Proper Business Conduct Directive 313, are included as part of off-balance sheet credit risk, and are excluded from the above table.

In conjunction with its policies regarding management of exposure to foreign financial institutions, the Bank's Board of Directors sets, *inter alia*, the risk appetite – i.e. the maximum exposure limit for states and foreign financial institutions, while adjusting the exposure limit to the risk assessment for each state and financial institution. Exposure limits are set based, inter alia, on rating of the various nations and financial institutions and on Bank assessment of the risk level in a manner which diversifies exposure.

The Bank determines the exposure limit to each financial institution based on the most recent rating available for said institution, provided by one of the leading international rating agencies are used – based on financial information for the institution under review. Exposure limits per institution include maximum exposure amount and maximum time to maturity for different types of activities and transactions. To this end, the existence (or absence) of an offset agreement for derivative operations with these financial institution is also taken into consideration. The policies also specify a hierarchy of authority for approval of specific transactions within the exposure limits.

The Bank monitors current ratings published for financial institutions to which it has exposure, and adjusts the exposure limits and actual exposure, as required, to the current rating. The Bank also reviews on a regular basis any additional information available with regard to these institutions in order to monitor exposure even where the credit rating may not reflect the complete picture.

The Bank takes into consideration the maturity dates of its credit exposure in conjunction with the Bank's liquidity requirements. Deposits are normally deposited for short terms, whereas exposure with respect to derivatives and investments in securities are for longer terms.

Ratings – Bank activity with overseas entities generates exposure to sovereigns and to financial institutions. The Bank has set policies with regard to review and routing of risk arising from this exposure. For credit risk exposure management, as stated above, the Bank uses ratings by independent rating agencies, primarily: Fitch, Standard & Poor's, and Moody's. These ratings are accounted for as part of the considerations in setting limits on the Bank's exposure to nations and banks, intended primarily for derivatives operations, financing and guarantees for foreign trade and various investments. External ratings form a basis for in-house analysis of a country or counter-party, conducted by the Bank. Other data from various sources used for this analysis are also taken into account. The Bank's assessment of the counter-party may differ from that of the rating agency.

The Bank acquires the ratings, and analysis underlying such ratings, from Fitch and Moody's. Ratings and analysis are periodically updated by the rating agencies and the Bank uses the most current information available when setting facilities or when reviewing a counter-party.

Housing credit risk

In conjunction with credit risks management, the Bank takes various actions to manage, control and mitigate risk associated with provision of housing loans. The Bank estimates the risk profile associated with provision of housing loans as low, relative to the inherent risk in the Bank's overall loan portfolio, due to the high level of client diversification, geographic diversification of borrowers, relatively low leverage, which recently has decreased even further due to Bank of Israel directives, intensive review procedures of borrower quality and their repayment capacity, and securing credit with property as collateral.

The Bank acts regularly to control and manage the risk associated with housing loans, for which the Retail Division, the Risks Control Division and other Bank entities are responsible. This activity includes portfolio analysis by inherent risk factors (LTV, repayment ratio, geographic location, loan age, income decile etc.) and carrying out a variety of stress tests to review the impact of macro-economic factors on portfolio risk – primarily the impact of unemployment and interest rates. The Bank has developed an advanced model for rating housing loans, which includes a rating for each loan and calculation of potential loss in case of failure. This model is in addition to the Bank's existing monitoring tools.

Risk appetite and risk profile in mortgage segment

As part of its credit risk policies, the Bank has set various restrictions on housing loan operations, to account for major risk factors. These factors are reviewed from time to time and additional restrictions are imposed as needed, i.e. based on the actual risk profile of the mortgage portfolio and its trend, as well as on regulatory directives from the Bank of Israel.

The risk appetite for mortgages is defined using multiple risk benchmarks, which apply to credit risk and concentration risk aspects at regular performance level. These benchmarks include: differential risk premium (reflecting the risk of the mortgagee), the LTV ratio, property location (geographic risk), credit quality benchmark (see below under Credit Control), loan repayment to income ratio, loan purpose, loan term, loan track mix, property type, document quality, normative interest rate, financial wealth and cross restrictions on combinations of multiple parameters.

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 the Board of Directors and its Risks Management Committee. Such monitoring reveals that the leading risk benchmarks are relatively low and continuously improving. These benchmarks include: LTV ratios, repayment ratio, rate of obligo in default and, in particular, the rate of arrears for new loans (one year since origination), which is constantly dropping to very low rates, 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 December 2016) was 54.7% (reflecting the LTV ratio upon loan origination – see more details below). 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 significantly lower than the original LTV ratio due to the constantly higher housing prices. 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.

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

	Loans granted (NIS in millions)			Change in %	
	2016	2015	2014	2015-2016	2014-2015
Mortgages issued (for housing and any purpose)					
From the Bank's funds	23,627	23,804	18,280	(0.7)	30.2
From the Treasury's funds					
Directed loans	103	65	108	58.5	(39.8)
Standing loans and grants	116	125	173	(7.2)	(27.7)
Total new loans	23,846	23,994	18,561	(0.6)	29.3
Refinanced loans	2,103	4,795	3,309	(56.1)	44.9
Total loans originated	25,949	28,789	21,870	(9.9)	31.6
Number of borrowers (includes refinanced loans)	48,450	59,468	46,529	(18.5)	27.8

Attributes of the Bank's housing loan portfolio

The Bank's policies with regard to mortgages are based on a conservative approach, limiting specific risk for each loan by reviewing various attributes. These attributes include: LTV ratio, ratio of repayment to regular borrower income, and borrower capacity to make current repayments even under scenarios involving a change in interest rates. Whenever loans are granted with attributes which do not meet one or more of the standards set by the Bank for these attributes, the Bank requires additional bolstering for the loan, such as guarantors for the loan, proven repayment capacity not based on regular borrower income etc. In recent years, due to expansion of the housing market and relatively low interest environment, the Bank has enhanced measures taken to monitor and mitigate risk, as reflected by a significant decrease in loan risk factors, as detailed below (all data below as of December 31, 2016).

LTV ratio

One of the key parameters used by the Bank in minimizing risk in its housing loan portfolio is the LTV ratio (ratio of loan amount to value of the property pledged as collateral).

The average loan-to-value ratio for the Bank's mortgage portfolio as of December 31, 2016 was 54.7%, compared to 55.0% on December 31, 2015 and to 55.8% on December 31, 2014. Out of the total loan portfolio of the Bank, amounting to NIS 116.0 million, some 95% were granted with an original LTV ratio under 75%, which secures the loan even in case of an extreme 25% decrease in value of the property pledged as collateral.

The LTV ratio in this report is the historical LTV ratio calculated upon loan approval, and does not account for any current repayments which reduce the loan balance nor any changes in value of properties pledged as collateral. The significant increase in housing prices, as from late 2008 and, conversely, reduced loan balances due to current repayments result in a decrease in the current "actual" LTV ratio and, as noted above, based on changes to property values as estimated by the Central Bureau of Statistics, against current portfolio balances. This ratio is significantly lower than the historical LTV ratio. Total loans granted at LTV ratios over 75% in the past two years amounted to NIS 0.2 billion, or only 0.2% of the total housing loan portfolio.

Note, in this regard, that the Bank's average LTV ratio as of December 31, 2016, based on current outstanding balances (with no change to property value due to changes in housing prices) would have decreased as follows: For loans originated up to one year ago – by 4%. For loans originated one to 5 years ago – by 8%; and for loans originated over 5 years ago – by 18%. For all loans – by 9%.

On November 1, 2012, the Supervisor of Banks issued directives which restrict the loan-to-value ratio for housing loans (these directives were grouped, together with other directives, in a directive with regard to housing loans dated July 15, 2014.

These directives stipulate that the LTV ratio may not exceed:

Up to 75% – for borrowers who are Israeli citizens buying a single apartment (as defined in Section 9(c) of the Real Estate Taxation Act)

Up to 70% – for second home buyers buying an alternative apartment (an apartment bought by an Israeli citizen who owns a residential apartment which would be a single apartment if not for the apartment being purchased, where the borrower commits to sell their existing apartment as stated in Section 9(c1a)(2)(a)(2) of the Real Estate Taxation Act)

Up to 50% – for buyers of a rental property, for general-purpose loans and for loans to foreign residents.

Loans granted with LTV ratio higher than 75% (cases which are exceptions to the directive on limitation of LTV ratio) are usually secured by credit insurance, which significantly reduces risk for the Bank, although it does not affect the LTV, capital allocation required for such loan or the repayment ratio calculation. Out of the balance of loans granted with an original LTV ratio higher than 75%, a total of NIS 2.3 billion is insured by credit insurance – 42.3%.

In recent years, due to measures taken by the Bank to mitigate risk in the mortgage portfolio and the aforementioned restrictions imposed by the Bank of Israel, the percentage of loans granted with a high LTV ratio out of total housing loan portfolio of the Bank decreased to 0.6% for loans granted 1-2 years ago, 0.6% for loans granted 3-12 months ago and 0.7% for loans granted in the fourth quarter of 2016.

Repayment as percentage of regular income

The LTV ratio of a housing loan is a benchmark of loan security, regardless of borrower attributes. Therefore, in addition, when a mortgage is approved, the Bank requires borrowers to show their capacity to make current loan repayments on schedule, primarily by calculating the ratio of monthly repayment to regular borrower income.

The average repayment ratio for the Bank's housing loan portfolio is 27.6%. Some 80.3% of the Bank's mortgage portfolio were granted to borrowers with a repayment ratio under 35% (the average repayment ratio for these borrowers is 23.6%). Some 16.2% of the mortgage portfolio were granted to borrowers with a repayment ratio of 35% to 50% (the average repayment ratio for these borrowers is 39.9%). Some 3.1% of mortgages were granted to borrowers with a repayment ratio of 50% to 80% (the average repayment ratio for these borrowers is 59.7%), and only 0.4% were granted to borrowers with a repayment ratio over 80% (the average repayment ratio for these borrowers is 92.5%).

The loans with a high repayment ratio are loans granted to borrowers with significant other assets, whose repayment capacity is not necessarily based on current income, to borrowers with very high income where the repayment ratio is less significant, or where additional bolstering of the loan is in place, in addition to the pledged property and repayment capacity of the borrower, such as financially robust guarantors.

On August 29, 2013, the Supervisor of Banks issued directives with regard to restrictions on provision of housing loans, which stipulated restrictions on the ratio of monthly loan repayment to income.

On July 15, 2014, the Supervisor of Banks issued Directive 329 concerning restrictions on provision of housing loans, which incorporates, *inter alia*, the directives described above, dated August 29, 2013. This also redefines the term "repayment ratio".

Loans bearing variable interest

The Bank offers clients housing loans which in part bear adjustable interest and in part are linked (to CPI, foreign currency) or non-linked (NIS-denominated loans).

The directive by the Supervisor of Banks dated May 3, 2011, restricted the portion of loans extended bearing interest which may vary within a 5-year term to 33% of total loan amount. The Supervisor's letter dated August 29, 2013 stipulates that in addition, a banking corporation may not approve a housing loan where the ratio of the loan portion bearing variable interest to total loan amount exceeds 67% – regardless of the frequency of interest rate change.

The aforementioned directives by the Supervisor of Banks, dated May 3, 2011 and dated August 29, 2013, were incorporated in a circular concerning restrictions on provision of housing loans dated May 15, 2014.

The Bank provides clients with the knowledge and expertise of its staff in order for clients to understand the risk involved with a loan bearing adjustable interest and how this risk may be mitigated or avoided. The Bank advises clients to attribute appropriate weighting to this risk, and to be cautious when deciding upon the loan composition.

Total loans linked to the prime lending rate granted over the past two years, which constitute the major portion of risk associated with such mortgages, is NIS 10.7 billion, or only 9.2% of the housing loan portfolio.

Note however that before approving a loan linked to the prime lending rate, similar to loan approvals for other variable interest tracks, the Bank reviews the repayment capacity of the borrower under scenarios where the prime lending rate would increase based on "normative interest".

Loan amount

Loans granted by the Bank with an original amount over NIS 2 million amounted in total to NIS 5.2 billion, or only 4.4% of the Bank's housing loan portfolio.

Below are details of various risk attributes of the housing loan portfolio[1] as of December 31, 2016 (NIS in millions):

LTV ratio	Repayment as percentage of regular income	Loan age[2] (time elapsed since loan grant) Up to 3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
Up to 60%	Up to 35%	2,455	9,273	10,808	17,799	13,530	4,080	57,945
	35%-50%	356	1,428	1,435	4,608	3,458	828	12,113
	50%-80%	-	-	1	914	1,246	311	2,472
	Over 80%	-	-	-	84	141	63	288
60%-75%	Up to 35%	982	5,592	6,498	10,956	6,286	973	31,287
	35%-50%	129	769	752	1,969	1,644	257	5,520
	50%-80%	-	-	1	266	512	101	880
	Over 80%	-	-	-	8	51	14	73
Over 75%	Up to 35%	28	82	97	861	1,748	1,242	4,058
	35%-50%	1	15	13	200	400	429	1,058
	50%-80%	-	-	-	11	110	145	266
	Over 80%	-	-	-	3	19	28	50
Total		3,951	17,159	19,605	37,679	29,145	8,471	116,010
Of which:								
Loans granted with original amount over NIS 2 million		167	981	900	1,738	1,318	59	5,163
Percentage of total housing loans		4.2%	5.7%	4.6%	4.6%	4.5%	0.7%	4.5%
Loans bearing variable interest:								
Non-linked, at prime lending rate		829	4,486	5,358	10,511	12,425	1,783	35,392
CPI-linked[3]		5	18	44	431	4,577	1,523	6,598
In foreign currency[3]		68	236	422	1,569	1,352	334	3,981
Total		902	4,740	5,824	12,511	18,354	3,640	45,971
Non-linked loans at prime lending rate, as percentage of total housing loans		21.0%	26.1%	27.3%	27.9%	42.6%	21.0%	30.5%
CPI-linked loans bearing variable interest as percentage of total housing loans		0.1%	0.1%	0.2%	1.1%	15.7%	18.0%	5.7%
Loans with LTV over 75% as percentage of total housing loans		0.7%	0.6%	0.6%	2.9%	7.8%	21.8%	4.7%

(1) Balance of housing loans after provision by extent of arrears.
(2) The loan balances presented above are aged based on the date of loan origination, and include under the same age group any loan balances actually provided at a later date.
Furthermore, loan refinancing does not modify the loan age, i.e. the loan balance is attributed to the original loan origination date.
This treatment also applies to refinancing of "directed" loans originally guaranteed by the State and refinanced to loans for which the Bank is responsible.
(3) Pursuant to directives by the Supervisor of Banks, these include loans for which the interest rate is adjusted up to once every 5 years.

Provision by extent of arrears

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 Banking Conduct Directive 314, as of December 31, 2016 (NIS in millions):

	Extent of arrears							
	In arrears 90 days or longer						Balance with respect to refinanced loans in arrears[(4)]	Total
	In arrears 30 to 89 days[(3)]	90 days to 6 months	6-15 months	15-33 months	Over 33 months	Total over 90 days		
Amount in arrears	6	10	10	10	200	230	53	289
Of which: Balance of provision for interest[(1)]	-	-	-	-	101	101	6	107
Recorded debt balance	407	357	165	58	138	718	138	1,263
Balance of provision for credit losses [(2)]	-	-	24	31	101	156	64	220
Debt balance, net	407	357	141	27	37	562	74	1,043

(1) With respect to interest on amounts in arrears.
(2) Excludes balance of provision for interest.
(3) In conformity with Public Reporting Directives, excludes the balance of housing loans in arrears up to 2 months.
(4) 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.

For more information about housing credit risk, see the Detailed Risks Management Report on the Bank website.

Means for risk management in housing loans

Underwriting process

Criteria for loan approval

The Bank has specified uniform, quantitative criteria for review and approval of housing loan applications. Along with the uniform criteria, decision makers at the Bank exercise their judgment. The guiding criteria for granting housing loans have been determined, inter alia, based on the following:

- Accumulated experience at the Bank with regard to housing loans, including lessons learned over time with regard to parameters which determine borrower quality and quality of loan collateral.
- Results of current credit reviews which include, inter alia, review of changes to credit quality in certain sectors.
- Review of loan portfolios carried out by a special-purpose nation-wide review center.
- Assessment of credit risks in different areas of the country, due to security-related and other events.
- During evaluation of the loan application, three key parameters are assessed: Borrower quality and repayment capacity, proposed collateral and nature of the transaction. For commercial banking, prime importance is usually assigned to the loan purpose. In the mortgage business, the main weighting in making credit decisions lies in assessment of borrower quality, because practically all of the loans are extended for purchase of real estate by households. However, for general-purpose loans, self-construction loans and non-standard loans, a weighting is assigned to the nature and quality of the transaction when making a decision.
- Collateral and guarantors form a safety net for the Bank in a specific transaction, in case the monthly repayment does not go according to plan.
- Decision making by the Bank involves a process of review of transaction data against predetermined criteria. Decision making with regard to credit is hierarchical and, to a large extent, corresponds to the Bank's management ranking. There are multiple approval levels and the application is routed to the required level based on application data.

These criteria are regularly updated in line with market developments and the portfolio's risk profile.

Credit authority

The Bank has created a ranking of authority for approval of housing loans (at branch, region and headquarters level). The authorized entity to approve the loan is determined based on data in the loan application and on its inherent risk (data about borrowers, LTV ratio, risk premium and nature of the transaction). To enhance control over approval of complex, high-risk loans and loans to specific populations (such as: large loans, transactions between family members, acquisition through a Trust, loans with pledged collateral being a property in high-risk locations etc.), such applications are sent for approval by the Underwriting and Control Department operating in the mortgage headquarters sector.

In addition, a major part of the loan origination process is conducted by the National Review Center. This Center controls the appropriateness of the loan origination process, including compliance with Bank procedures and various directives.

Model for determination of differential risk premium

The Bank has developed a model for calculation of differential risk premium, based on past empirical data, for rating transaction risk at the loan application stage. For each application, an individual risk premium is calculated based on all risk factors identifiable in client information and attributes of the desired transaction.

This premium reflects an estimate of overall transaction risk, allowing for assessment of client odds of being in arrears on the loan or becoming insolvent – at the outset of the application stage. This premium is used for both credit decision making and for pricing of client interest rate. The Bank is currently reviewing potential improvement of this model. The Bank is currently in the process of upgrading the model, expected to be deployed in 2017.

Built-in controls in loan origination system

The Bank manages its mortgage operations using a dedicated computer system developed for this purpose, which includes the following built-in real-time controls:

- Ensure information completeness required for loan and activities required in preparation of the material, review and approval of the loan.
- Rigid, real-time control over transactions by authorizations. Use of this preventive control methodology significantly reduces the need for discovery controls after loan origination.
- Work flow process with real-time control over execution of all required tasks at each stage of the loan origination process, sending the application to the authorized entity for performing the required actions at each stage of the loan approval process.

Use of this system has resulted in improved control in different stages of the loan origination process, while achieving uniformity among different Bank branches.

Mortgage-related training

The Bank's Training Center delivers courses for training, development and improvement of all those involved in provision of housing loans. Training content is determined in cooperation with the Mortgage Headquarters Sector, and staff at headquarters participates in training delivery to bankers. These courses include, inter alia, special emphasis on risks management. In addition, the mortgage operations are included within the Bank-specified framework for handling operating risk and staff at the mortgage headquarters take part in training designated for this area.

Professional conferences

The Retail Division regularly holds professional conferences for managers and bankers. In these conferences, extensive reviews of developments in the mortgage market are presented, along with steps to be taken to handle the risks associated with such developments.

Regular monitoring of borrower condition and of the housing loan portfolio

Credit control is a key factor in maintaining quality of credit provided by the Bank to its clients. Control over housing loans is exercised at the individual loan level as well as for the entire mortgage portfolio.

At the individual loan level, the Bank acts to identify as early as possible any symptoms indicating a decline in borrower repayment capacity, in order to identify as soon as possible any credit failure situation. The Bank operates various controls, including regular internal controls at branches, regions and headquarters, as well as additional controls by the second and third line of defense of the Bank's credit risk management system – the Risks Control Division and Internal Audit.

The Bank maintains control over quality of new credit provided by branches, by means of a monthly Credit Quality report, which includes all loans originated by the Bank between 6-18 months prior to the reported date which are over 3 months in arrears. This report is designed to assist branches in reducing the extent of arrears, and to increase awareness of troubled loans by those originating and approving loans in order to learn lessons for future credit approval. Along with the individual report, listing loans, details of arrears etc., a statistical report is also produced, showing the extent of arrears at each branch, compared to the region and to the Bank as a whole, and compared to previous months. Management of the Retail Division regularly monitors handling of debts in arrears, using this report.

For the entire mortgage portfolio, control is maintained of restrictions imposed by the Bank's risk appetite, both at the Retail Division and at the Risks Control Department of the Risks Control Division.

In addition, a credit control report is produced semi-annually by the Risk Control Division, containing an extensive review of the development of the housing loan portfolio's risk profile over the reviewed period, with reference to the following:

- Risk appetite.
- Analysis of major risks and attributes.
- Review of state of arrears and credit quality
- Client debts collection
- Housing loan portfolio for special populations
- Stress testing
- Purchase groups.

Entities participating in risk management and control for housing loans

Mortgage Management Department of the Retail Division

Handles different events which occur during the loan term, whether initiated by the Bank or by the borrower.

The National Review Center of the Retail Division

Reviews loan files prior to origination.

Collection Department

Handles debts collection from borrowers in arrears and realization of properties.

Arrears Forum

Headed by the Manager, Business Division, reviews the current state of affairs with regard to collection, implications on the financial statements and on the provision for credit losses.

Legal Division

Responsible for review of collateral in non-standard cases (such as: transactions involving family members) and for high-value loans, as part of the underwriting process.

Risks Control Division

Responsible for monitoring the quality of the Bank's loan portfolio, including risk measurement using advanced models developed by the Bank, review of the evolution of the Bank portfolio risk profile, in view of the specified risk appetite. In addition, conducting detailed analysis of the mortgage portfolio, including stress testing.

Credit risks and credit concentration monitoring forum

Headed by the Manager, Risks Control Division.

Internal Audit

The work plan for Internal Audit with regard to loans includes, inter alia, reference to review of entities involved in loan approval, origination, administration and control.

For more information about operations of these entities, see the Detailed Risk Report on the Bank website.

Tools for risk mitigation in housing loans

Collateral

In accordance with Bank procedures for mortgages, loans are only provided if secured by property collateral. In some cases, the Bank demands guarantors for the debt, in addition to property collateral.

For verification of information about the property offered to the Bank as collateral and to determine its value, an assessor visit to the property is normally required, providing a report which describes the property, its location, physical condition and market value. Assessors are party to an agreement with the Bank and act in accordance with Bank guidance, including a structured procedure for conducting assessments, identifying exceptions etc.

The common practice for assessment in the mortgage sector is to use an abbreviated assessment. However, since 2006, the Bank has required assessors to conduct extended assessment for some of the loans for purchase of existing apartments, self-construction or general-purpose loans with high-risk property types, which includes additional tests subject to criteria set for this matter.

Insurance

According to Bank procedures, all properties serving as collateral must be insured under property insurance. In addition, the borrowers are insured by life insurance assigned to the Bank in case of death prior to complete repayment of the loan.

For some loans (usually loans with LTV ratio higher than 75%), the Bank contracted with EMI Corp., which provides credit insurance in case the proceeds from realization of the property collateral for the loan should fail to cover the outstanding loan amount. This credit insurance process is a key risk mitigator.

As from November 1, 2012, the Bank of Israel restricted origination of housing loans with LTV over 75%, so that as of this date the Bank no longer approves new loans with credit insurance and LTV over 75% (except for loans exempted from this directive, such as refinancing loans).

Loan to Value (LTV) ratio

The maximum LTV ratio approved by the Bank is determined by the credit policies and is periodically reviewed. Generally, the Bank requires borrowers to contribute part of the financing for the acquisition. This equity payment forms a safety cushion in case the property is realized during a down-turn in the real estate market. Furthermore, borrower equity is a further indication of the borrower's financial robustness. As from November 1, 2012, the Bank restricted the LTV ratio for approval of applications for housing loans, pursuant to the Bank of Israel directive on this matter. The LTV ratio for loans to acquire rights to real estate constituting a "single apartment" (as defined in the directive) shall not exceed 75%, for an "alternative apartment" (as defined in the directive), the LTV ratio shall not exceed 70%, and for acquisition of an investment property, general-purpose loan or loan extended to foreign residents – the LTV ratio shall not exceed 50%. For more information about the Supervisor of Banks' directives with regard to capital adequacy, see Note 25.H to the financial statements.

Market risk and interest risk

Risk description

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).

Interest rate risk in the banking book is the risk to Bank profit (change in revenues) or to the Bank's economic value, primarily due to changes in the structure of interest rate curves relevant for Bank operations, non-identical fluctuations of various curves used by the Bank for pricing and management of its exposures, 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.

Overview of market and interest risk and guidelines for management thereof

The Bank has no exposure to commodities and its exposure to equities is not material; thus, the Bank's major exposure to market risk is due to basis risk – which is due to Bank assets and liabilities being denominated in different currencies or linkage segments – and to interest risk in the banking book. Changes in interest rates impact Bank profits (change in revenues) and the value of Bank assets (change in fair value). The Bank manages its market risk and interest risk in integrated fashion, under the same organizational structure and using similar tools, data structures, methodology and systems.

Market risk and interest risk form an integral part of banking business and of management of Bank assets and liabilities. However, excessive market risk and/or interest risk may expose the Bank to loss and may pose a threat to Bank capital. Therefore, the Bank’s Board of Directors and management have specified, in the Bank's structured process for risks mapping and identification, that market risk and interest risk are material risks and that management of these risks is critical for stability of the Bank, especially in view of the low interest rate environment and the potential for change in market interest trend. Management of these risks is designed to maintain a reasonable risk level, in conformity with the exposure caps, i.e. the risk appetite specified for these risks, while taking advantage of opportunities and constant monitoring of the risk profile, so that the Bank would not be exposed to significant loss.

Management of market risk and interest risk at the Bank consists of two main risk concentrations: the bank portfolio and the negotiable portfolio. The negotiable portfolio is small relative to activity in the bank portfolio and is associated with low risk. The bank portfolio, which accounts for most of the Bank's operations, is primarily exposed to interest risk.

Market risk and interest risk are managed at Group level, including the Bank's overseas affiliates and subsidiaries. Operations vis-à-vis Bank Yahav are regularly coordinated, in particular for setting the Group risk appetite, which requires monitoring of the Group-level risk profile. Policy principles were specified in line with Bank strategy and with regulatory requirements, i.e. Proper Banking Conduct Directives of the Bank of Israel, relevant Basel Committee directives and in line with globally accepted best practice.

As part of risk management, the Bank is required to allocate capital, as part of Basel II, Pillar 1, against risk in the negotiable portfolio, in conformity with Proper Conduct of Banking Business Directive 208 "Capital measurement and adequacy – market risk" which includes the Basel II directives with regard to definition, management and revaluation of the negotiable portfolio.

Bank operations in the negotiable portfolio are subject to restrictions which reflect low risk appetite and therefore, the Bank's capital allocation with respect to market risk is very low.

The bank portfolio includes the positions not classified as negotiable positions in the negotiable portfolio. The Bank handles interest risk in the bank portfolio and overall additional capital allocation with respect there to, in conformity with Basel Pillar 2. Capital allocation in conformity with Basel Pillar 2 is reviewed both under scenarios which reflect the normal life state and under stress scenarios, including systemic scenarios and threat scenarios. This is done as part of the ICAAP process, as described in chapter "Capital adequacy".

The Bank structure, which is weighted towards the mortgage portfolio, produces long-term uses for which the Bank requires sources. Due to incomplete alignment of the average duration of uses and the average duration of sources, the Bank's economic value is exposed to increase in interest rate curves.

This risk is monitored on a regular basis, both in managing interest risk for the overall portfolio in VaR terms, and in EVE (Economic Value of Equity) terms, as well as another range of scenarios which mostly reflect stress conditions. The risk level was set at low-medium, reflecting the Bank's policy and actions to raise sources of relatively long durations, both in negotiable issues and in deposits from the public – unique deposits which provide a solution for client needs and provide sources for medium and long terms to hedge interest rate exposure.

For more information about these models, their use and their limitations, see the Detailed Risk Report on the Bank website.

Means of supervision over and implementation of the policy

The Bank has put in place an organizational structure for management of market risk and interest risk in the bank portfolio, which includes the Board of Directors, management and the three lines of defense. This structure is supported by special committees and forums, created for such risks management and in order to create an internal controls system, designed to prevent deviation from Bank policy in its activity in the negotiable portfolio and in the bank portfolio.

For more information about market and interest risk, see the Detailed Risk Management Report on the Bank website.

Hedging and risks mitigation policy

A major tool for management and mitigation of interest risk is setting shadow prices at the Bank (transfer pricing). Shadow prices are determined daily at the Bank by the Asset and Liability Management Department of the Financial Management Sector and reflect the needs for management of various exposures under the policy on risk / reward management.

Another tool is buying / selling government debentures. The Asset and Liability Management Department also manages the interest and/or basis position through forward contracts, swap transactions and options. The advantages of using these tools stem from rapid execution at large amounts, which allows the Bank to "move positions" within a reasonable time frame for asset and liability management. In addition, these transactions are unfunded, are highly liquid and are conducted through the Bank's trading room.

Derivatives transactions, which are identified as hedging balance sheet positions in accordance with accounting rules, are to be specified as hedge accounting transactions, in accordance with the Bank's hedging procedure. Hedge effectiveness is the degree of correlation between changes in fair value or between cash flows of the hedged item and of the hedging derivative. The hedge is considered highly effective if the changes in fair value or cash flows of the hedged item, are nearly fully set off by changes in fair value or cash flows of the hedging instrument. When hedging instruments and hedged items are not fully identical, hedge effectiveness is tested quarterly.

At least once a year, the Bank reviews the underlying assumptions of models used to manage market and interest risk, including behavioral assumptions made in order to determine forecasting of certain instruments.

The Bank reviews the concentration of interest risk by linkage segment and by major instrument type. The concentration map is discussed annually by risks management committees.

The Bank constantly acts to increase awareness of market and interest risks in the bank portfolio at Group level, both at headquarter units, at branches and at overseas units of the Bank, through operating procedures, training and seminars on this topic. Furthermore, constant contact is maintained with all relevant units for management of market and interest risk. Coordination between units is designed to achieve a uniform methodology for management of market and interest risk in the bank portfolio.

Measurement of market and credit risk exposure and their management using models for risks management

Measurement of market and interest risks is supported by a wide range of information systems, models, processes, risk benchmarks and stress tests. The information systems involved in the calculation are regularly reviewed, through internal controls processes at the Bank, including specific surveys for monitoring activities and information and continuous validation processes, in order to ensure completeness and accuracy of data and calculations.

The Bank has two major models for managing its market and interest risks: The VaR model and the EVE model. The Bank calculates these benchmarks, as well as other benchmarks used for management of such risks, at least once per day.

The VAR model is a statistical model that estimates the loss expected for the Bank in a certain investment period and at a predetermined statistical level of assurance. This model measures risk level in terms of money, where the Bank aligns the investment horizon for the portfolios reviewed using this benchmark. The Bank uses a combination of multiple methods for VaR calculation, commonly used around the world. The VaR calculation is in addition to a back testing calculation, designed to review the quality of its calculation estimates, i.e. review the model forecast, compared to actual results. The Bank has specified a risk appetite in VaR terms, for the entire Bank portfolio and for its activities in various options portfolios (for various underlying assets). VaR calculations for the Bank's overall portfolio are made daily, while calculations for the option portfolios are made hourly.

EVE (Economic Value of Equity) is a model which reflects the economic value approach. This is the Bank's main model for estimating interest risk in the bank portfolio, which reviews changes in economic value of the portfolio under various assumptions of changes to interest rate curves, under normal conditions and under stress conditions, including a concurrent increase / decrease in the interest rate curve. In addition, the Bank has various stress tests at different severity levels, designed to review its risk profile under stress conditions, in view of the risk appetite determined by the Board of Directors. The Bank also applies innovative methods to review interest risk in the bank portfolio under emergency conditions, including under stress scenarios of an economic outline. This scenario is based on the Bank's understanding as to development under stress conditions of macro-economic conditions relevant for these risks. The Bank also performs a scenario where the interest rate curve moves in non-parallel fashion. Such scenario complements the EVE approach, which is based on parallel move of interest rate curves.

Below is the VAR for the Bank Group (NIS in millions):

	All of 2016	All of 2015
At end of period	386	195
Maximum value during period	386 (Dec.)	379 (May)
Minimum value during period	235 (JAN)	193 (OCT)

Back-testing of the historical-analytic VaR model shows one case in which the daily loss exceeded the forecast VaR value. This deviation, of a small amount, was primarily due to an increase in the NIS-denominated curve (for longer terms). This number of cases is within the criteria specified by the Basel Committee for review of the VaR model quality.

Analysis of interest risk in bank portfolio

Below is the impact of a parallel shift of the curve by 2% on the economic value of the Bank's portfolio in EVE terms (NIS in millions):

						December 31, 2016
						Change in fair value
		Israeli currency				Foreign currency
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total
2% increase	(1,221)	421	(55)	(25)	5	(875)
Decrease of 2%	1,710	(574)	75	29	(5)	1,235

						December 31, 2015
						Change in fair value
		Israeli currency				Foreign currency
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total
2% increase	(631)	83	(72)	(37)	(11)	(668)
Decrease of 2%	875	(198)	91	39	12	819

Exposure of the Bank and its subsidiaries to changes in interest rates

Reported amounts (NIS in millions)

	As of December 31, 2016					
	On Call to 1 month	Over 1 month to 3 months	Over 3 months to 1 year	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years to 10 years
Israeli currency – non-linked						
Financial assets, amounts receivable with respect to derivative instruments and to complex financial assets						
Financial assets(1)	121,301	1,747	3,996	11,073	7,816	6,809
Financial derivative instruments (other than options)	5,569	12,549	21,420	11,643	9,214	7,487
Options (in terms of underlying asset)	709	841	1,390	260	172	94
Total fair value	127,579	15,137	26,806	22,976	17,202	14,390
Financial liabilities, amounts payable with respect to derivative instruments and to complex financial liabilities						
Financial liabilities(1)	77,865	10,841	21,012	9,122	6,892	8,033
Financial derivative instruments (other than options)	22,374	22,642	15,284	8,479	8,968	7,726
Options (in terms of underlying asset)	595	525	1,539	269	141	35
Total fair value	100,834	34,008	37,835	17,870	16,001	15,794
Financial instruments, net						
Exposure to interest rate fluctuations in the sector	26,745	(18,871)	(11,029)	5,106	1,201	(1,404)
Cumulative exposure in sector	26,745	7,874	(3,155)	1,951	3,152	1,748

Specific remarks:

(1) Excludes balance sheet balances of financial derivative instruments, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Weighted average by fair value of average effective duration.

			As of December 31, 2016			As of December 31, 2015		
Over 10 to 20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective duration(2)	Total fair value	Internal rate of return	Average effective duration(2)
				In %	in years		In %	in years
3,675	325	303	157,045	3.99	1.25	131,739	3.19	1.04
87	–	–	67,969		1.06	66,214		1.23
–	–	–	3,466		1.56	2,763		0.73
3,762	325	303	228,480		1.20	200,716		1.10
665	100	2	134,532	0.93	0.90	119,611	1.18	0.82
49	–	–	85,522		0.90	77,724		1.42
–	–	–	3,104		1.39	3,729		0.85
714	100	2	223,158		0.91	201,084		1.05
3,048	225	301	5,322			(348)		
4,796	5,021	5,322	5,322					

Exposure of the Bank and its subsidiaries to changes in interest rates – continued

Reported amounts (NIS in millions)

	As of December 31, 2016					
	On Call to 1 month	Over 1 month to 3 months	Over 3 months to 1 year	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years to 10 years
Israeli currency – linked to the CPI						
Financial assets, amounts receivable with respect to derivative instruments and to complex financial assets						
Financial assets[(1)]	1,536	2,688	11,990	18,502	10,872	2,804
Financial derivative instruments (other than options)	105	199	309	1,289	1,372	295
Total fair value	1,641	2,887	12,299	19,791	12,244	3,099
Financial liabilities, amounts payable with respect to derivative instruments and to complex financial liabilities						
Financial liabilities[(1)]	678	919	6,834	12,381	8,638	8,240
Financial derivative instruments (other than options)	359	1,535	1,166	4,118	1,317	456
Total fair value	1,037	2,454	8,000	16,499	9,955	8,696
Financial instruments, net						
Exposure to interest rate fluctuations in the sector	604	433	4,299	3,292	2,289	(5,597)
Cumulative exposure in sector	604	1,037	5,336	8,628	10,917	5,320

Specific remarks:

(1) Excludes balance sheet balances of financial derivative instruments, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Weighted average by fair value of average effective duration.

			As of December 31, 2016			As of December 31, 2015		
Over 10 to 20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective duration[(2)]	Total fair value	Internal rate of return	Average effective duration[(2)]
				In %	in years		In %	in years
497	25	21	48,935	2.80	2.35	52,284	2.64	2.64
–	–	–	3,569		2.75	3,221		3.08
497	25	21	52,504		2.38	55,505		2.67
2,497	–	(2)	40,185	1.33	3.58	37,438	1.59	3.54
44	–	–	8,995		1.80	8,958		1.61
2,541	–	(2)	49,180		3.25	46,396		3.17
(2,044)	25	23	3,324			9,109		
3,276	3,301	3,324	3,324					

Exposure of the Bank and its subsidiaries to changes in interest rates – continued

Reported amounts (NIS in millions)

	As of December 31, 2016					
	On Call to 1 month	Over 1 month to 3 months	Over 3 months to 1 year	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years to 10 years
Foreign currency[1]						
Financial assets, amounts receivable with respect to derivative instruments and to complex financial assets						
Financial assets[2]	7,301	4,751	1,175	773	405	908
Financial derivative instruments (other than options)	34,155	28,215	17,342	5,056	4,555	2,569
Options (in terms of underlying asset)	841	669	1,752	253	126	30
Total fair value	42,297	33,635	20,269	6,082	5,086	3,507
Financial liabilities, amounts payable with respect to derivative instruments and to complex financial liabilities						
Financial liabilities[2]	21,690	7,103	9,498	724	102	134
Financial derivative instruments (other than options)	17,336	16,679	22,421	5,509	4,876	2,170
Options (in terms of underlying asset)	938	907	1,612	245	153	82
Total fair value	39,964	24,689	33,531	6,478	5,131	2,386
Financial instruments, net						
Exposure to interest rate fluctuations in the sector	2,333	8,946	(13,262)	(396)	(45)	1,121
Cumulative exposure in sector	2,333	11,279	(1,983)	(2,379)	(2,424)	(1,303)

Specific remarks:

(1) Includes Israeli currency linked to foreign currency.
(2) Excludes balance sheet balances of financial derivative instruments, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.
(3) Weighted average by fair value of average effective duration.

				As of December 31, 2016				As of December 31, 2015
Over 10 to 20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective duration(2)	Total fair value	Internal rate of return	Average effective duration(2)
				In %	in years		In %	in years
1,713	–	461	17,487	1.20	1.23	19,218	1.66	1.53
–	–	–	91,892		0.41	81,065		1.50
–	–	–	3,671		0.08	4,215		0.42
1,713	–	461	113,050		0.53	104,498		1.46
3	–	653	39,907	0.68	0.32	37,401	0.63	0.34
–	–	–	68,991		0.59	64,073		0.94
–	–	–	3,937		0.32	3,101		0.44
3	–	653	112,835		0.49	104,575		0.71
1,710	–	(192)	215			(77)		
407	407	215	215					

Exposure of the Bank and its subsidiaries to changes in interest rates – continued

Reported amounts (NIS in millions)

	As of December 31, 2016					
	On Call to 1 month	Over 1 month to 3 months	Over 3 months to 1 year	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years to 10 years
Total exposure to interest rate fluctuations						
Financial assets, amounts receivable with respect to derivative instruments and to complex financial assets						
Financial assets(1)	130,138	9,186	17,161	30,348	19,093	10,521
Financial derivative instruments (other than options)	39,829	40,963	39,071	17,988	15,141	10,351
Options (in terms of underlying asset)	1,550	1,510	3,142	513	298	124
Total fair value	171,517	51,659	59,374	48,849	34,532	20,996
Financial liabilities, amounts payable with respect to derivative instruments and to complex financial liabilities						
Financial liabilities(1)	100,233	18,863	37,344	22,227	15,632	16,407
Financial derivative instruments (other than options)	40,069	40,856	38,871	18,106	15,161	10,352
Options (in terms of underlying asset)	1,533	1,432	3,151	514	294	117
Total fair value	141,835	61,151	79,366	40,847	31,087	26,876
Financial instruments, net						
Total exposure to interest rate fluctuations	29,682	(9,492)	(19,992)	8,002	3,445	(5,880)
Total cumulative exposure	29,682	20,190	198	8,200	11,645	5,765

Specific remarks:

(1) Excludes balance sheet balances of financial derivative instruments, fair value of off-balance sheet financial instruments and fair value of complex financial instruments.

(2) Weighted average by fair value of average effective duration.

General remarks:

- In this table, data by term represents the present value of future cash flows from each financial instrument, discounted using the interest rate which discounts them to the fair value recognized for the financial instruments in Note 33.2) to the financial statements.
- Internal rate of return is the interest rate which discounts the expected cash flows from a financial instrument to its fair value recognized under Note 33.3) to the financial statements.
- Average effective duration of a group of financial instruments is an approximation of the change, in percent, in fair value of the group of financial instruments which would be caused by a minor change (0.1% increase) in the internal rate of return of each of the financial instruments.
- Certain transactions conducted by the Bank constitute complex financial instruments, which include embedded derivatives not detached, in accordance with Public Reporting Directives. These transactions include, inter alia, loans with exit points, deposits bearing gradual interest rates with withdrawal dates, credit and deposits with guaranteed minimum and deposits with optional linkage. The Bank reflects the interest rate risk with respect to these instruments in a reasonable manner, by spreading maturities of the cash flows in accordance with contract dates, and with various assumptions based on past experience.

				As of December 31, 2016			As of December 31, 2015	
Over 10 to 20 years	Over 20 years	Without maturity	Total fair value	Internal rate of return	Average effective duration(2)	Total fair value	Internal rate of return	Average effective duration(2)
				In %	in years		In %	in years
5,885	350	785	223,467	3.40	1.49	203,241	2.79	1.50
87	–	–	163,430		0.73	150,500		1.42
–	–	–	7,137		0.80	6,978		0.54
5,972	350	785	394,034		1.16	360,719		1.45
3,165	100	653	214,624	1.13	1.29	194,450	1.38	1.25
93	–	–	163,508		0.82	150,755		1.23
–	–	–	7,041		0.80	6,830		0.66
3,258	100	653	385,173		1.08	352,035		1.23
2,714	250	132	8,861			8,664		
8,479	8,729	8,861	8,861					

Below is the average effective duration of assets and liabilities as of December 31, 2016:

	Including early repayment assumptions[1]					Excluding early repayment assumptions				
	Assets		Liabilities		Average effective duration difference	Assets		Liabilities		Average effective duration difference
	Average effective duration	Fair value	Average effective duration	Fair value		Average effective duration	Fair value	Average effective duration	Fair value	
Non-linked	1.20	228,480	0.91	223,158	0.29	1.31	228,737	0.91	223,276	0.40
Linked to CPI	2.38	52,504	3.25	49,180	(0.87)	3.38	52,192	3.26	49,229	0.12
Foreign currency and linked to foreign currency	0.53	113,050	0.49	112,835	0.04	0.53	113,050	0.49	112,835	0.04
Total	1.16	394,034	1.09	385,173	0.07	1.37	393,979	1.10	385,340	0.27

(1) For details about fair value calculations and early maturity assumptions, see Note 33 to the financial statements.

In the non-linked NIS segment, the effective duration of assets exceeds that of liabilities by 0.29 years. The effective duration calculation is based on early mortgage repayment assumptions and on deposit withdrawals prior to final maturity at exit points, in conformity with terms of the different deposits. Excluding these early maturity assumptions, the effective duration of assets exceeds that of liabilities by 0.4 years.

The difference between internal rate of return (IRR) of financial assets and IRR of financial liabilities is 3.06%. Excluding these early maturity assumptions, the IRR for financial assets exceeds the IRR for financial liabilities by 2.93%.

In the CPI-linked segment, the effective duration of liabilities exceeds that of assets by 0.87 years. The effective duration calculation is based on early mortgage repayment assumptions and on deposit withdrawals prior to final maturity at exit points, in conformity with terms of the different deposits. Excluding these assumptions, the effective duration of liabilities exceeds that of assets by 0.12 years.

The difference between IRR of financial assets and IRR of financial liabilities is 1.47%. Excluding the early maturity assumptions, the difference is 0.40%.

In the foreign currency sector, the duration to maturity of assets exceeds that of liabilities by 0.04 of a year. In this sector, most of the activity is in variable interest, linked to the LIBOR rate, and, therefore the duration to maturity in this sector is low. The assumption concerning early redemption of deposits and loans in this sector has no effect on differences in duration or internal rate of return.

The difference between IRR of financial assets and IRR of financial liabilities is 0.52%.

Impact of hypothetical changes in interest rates on fair value of financial instruments of the Bank and its subsidiaries

Fair value of financial instruments before impact of hypothetical changes in interest rates (NIS in millions):

	Israeli currency		Foreign currency[2]			
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total
December 31, 2016						
Financial assets[1]	157,045	48,935	12,728	2,877	1,882	223,467
Amounts receivable with respect to financial derivative instruments[3]	71,435	3,569	76,490	13,753	5,320	170,567
Financial liabilities[1]	(134,532)	(40,185)	(29,860)	(7,376)	(2,671)	(214,624)
Amounts payable with respect to financial derivative instruments[3]	(88,626)	(8,995)	(59,188)	(9,217)	(4,523)	(170,549)
Total	5,322	3,324	170	37	8	8,861
December 31, 2015						
Financial assets[1]	131,739	52,284	13,604	3,507	2,107	203,241
Amounts receivable with respect to financial derivative instruments[3]	68,977	3,221	66,514	13,217	5,549	157,478
Financial liabilities[1]	(119,611)	(37,438)	(28,490)	(6,113)	(2,798)	(194,450)
Amounts payable with respect to financial derivative instruments[3]	(81,453)	(8,958)	(51,657)	(10,499)	(5,018)	(157,585)
Total	(348)	9,109	(29)	112	(160)	8,684

Net fair value of financial instruments, after impact of changes in interest rates (NIS in millions)[4]:

	Israeli currency		Foreign currency[2]				Change in fair value	
	Non-linked	Linked to CPI	Dollar	Euro	Other	Total	NIS in millions	In %
December 31, 2016								
Change in interest rates:								
Concurrent immediate increase of 1%	5,021	4,033	(88)	(145)	–	8,821	(40)	(0.5)
Concurrent immediate increase of 0.1%	5,290	3,686	142	27	7	9,152	291	3.3
Concurrent immediate decrease of 1%	5,670	3,210	495	155	16	9,546	685	7.7
December 31, 2015								
Change in interest rates:								
Concurrent immediate increase of 1%	(590)	9,188	(96)	105	(162)	8,445	(239)	(2.8)
Concurrent immediate increase of 0.1%	(318)	9,118	(36)	111	(160)	8,715	31	0.4
Concurrent immediate decrease of 1%	(88)	9,005	46	119	(157)	8,925	241	2.8

(1) Includes Israeli currency linked to foreign currency.

(2) Includes complex financial instruments. Excludes balance sheet balances of financial derivative instruments and fair value of off-balance sheet financial instruments.

Note that in calculation of the fair value of financial instruments, as stated in Note 10 to the financial instruments, the discount rate for financial assets reflects the inherent credit risk and the discount rate for financial liabilities also reflects the Bank's premium on raising resources. This differs from calculation of the effect of interest risk in the banking portfolio, in EVE (Economic Value of Equity) terms, which only includes the effect of exposure to risk-free interest.

(3) Amounts receivable (and payable) with respect to financial derivatives, discounted using interest rates used for calculation of the fair value.

(4) Net fair value of financial instruments presented in each linkage segment is the net fair value for this segment, assuming the indicated change in all interest rates in the linkage segment. Total net fair value of financial instruments is the net fair value of all financial instruments (excluding non-monetary items), assuming the indicated change in all interest rates in all linkage segments.

For further details of assumptions used in calculation of the fair value of financial instruments, see Note 33 to the financial statements.

CPI and exchange rate

Overview of inflation and currency risks and guidelines for management thereof

Inflation exposure – The risk appetite varies with expected profit from holding a position and the Bank's capacity to reduce the exposure within a reasonable time frame. This exposure is included among the risk appetite benchmarks and models applied by the Bank to all market risks.

Currency exposures – It is Bank policy to maintain minimal (operating) currency positions, except for specific strategic positions approved by the different committees and/or Trading Room positions, in conformity with approved risk restrictions. Foreign currency strategic positions are capped by a Stop Loss mechanism to restrict and reduce risk.

Derivatives in the bank portfolio used for economic hedging of balance sheet activity, or which cannot be defined as an accounting hedge, impact accounting profit and loss. The gap derives from difference in accounting treatment between balance sheet items and derivatives other than accounting hedges. This effect is regularly monitored and managed subject to guidelines specified by management, by the Financial Management Sector and is reported and discussed by various risks management committees.

Presented below are major data reflecting CPI and exchange rate exposures, as reflected in the financial statements, while relating to the difference between the accounting presentation and measurement of economic exposure:

Financial capital – As of December 31, 2016, the Group capital exceeded its non-monetary items by NIS 11,664 million. Group free capital, which includes financial capital, was used in 2016 to finance uses in the CPI-linked NIS segment, in line with current policies on resource and use management in the bank portfolio.

Linkage status – Details on the assets and liabilities in the various linkage segments at December 31, 2016 and 2015 are presented in Note 31 to the financial statements. However, the extent of the Bank's economic exposure is not fully reflected in the positions included in this note because of differences between the accounting approach and the economic approach with regard to capital items, non-monetary items and investments in investees, as explained below.

Surplus CPI-linked assets of the Group, which include balance sheet and off-balance-sheet items as of December 31, 2016 as presented in Note 31 to the financial statements, amounts to NIS 4.9 billion, representing the economic exposure. In December 2015, excess assets in this segment amounted to NIS 10.0 billion.

Excess assets in foreign currency for the Group as of December 31, 2016 amounted to NIS 47 million. After adjustment of the economic reference to deposits used to cover investments in overseas subsidiaries, which are presented as non-monetary items, and to temporary impairment of investments in securities, the position in this segment amounts to surplus sources of NIS 53 million. As of December 31, 2015, the foreign currency position for the Group, after the aforementioned adjustments and after attribution of the general and supplementary provision for doubtful debts to free capital, amounted to surplus resources amounting to NIS 40 million.

The position in the non-linked NIS segment balances the open economic positions in the CPI-linked and foreign currency segments.

The Bank has CPI-linked uses due to current operations in the mortgage portfolio linked to the CPI, for which the Bank raises CPI-linked sources, including debenture issues and deposits from the public. The Bank uses financial derivatives to actively manage this exposure, in line with the specified exposure policy.

The Report of the Board of Directors and Management presents the Group's exposure to interest on a consolidated basis is presented in terms of average effective duration and in terms of fair value. Cash flows used in calculating exposure are based on assumptions with regard to withdrawal rates at exit points for deposits and early mortgage repayment rates. The percentage of withdrawals is based on empirical data.

For further details of assumptions used in calculation of cash flows and fair value of financial instruments, see Note 33 to the financial statements.

Below is an analysis of the sensitivity of Bank Group capital to changes in major exchange rates and in the CPI (before tax effect) as of December 31, 2016:

Capital increase (erosion), NIS in millions:

	Scenarios				Historical stress scenario(1)	
	10% increase	5% increase	Decrease of 5%	Decrease of 10%	Maximum increase	Maximum decrease
CPI	502.6	251.3	(251.3)	(502.6)	73.4	(38.7)
Dollar	8.2	11.0	4.0	14.2	(6.4)	(0.4)
Pound Sterling	1.1	0.4	(0.4)	(1.1)	0.2	(0.6)
Yen	(0.5)	0.1	0.6	0.9	0.1	0.4
Euro	3.0	2.9	1.0	0.5	2.4	0.4
Swiss Franc	(0.4)	(0.1)	0.1	0.1	(0.6)	0.1

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

Share price risk

Bank policy with regard to investment in non-banking corporations is to realize the current portfolio and individually review any new investments. Shares of non-banking corporations in which the Bank invested were acquired for the purpose of earning capital gains, and are listed at fair value in the available-for-sale security portfolio and under investment in associates, where the Bank has a material investment in such entity. Investments in non-banking corporations are managed by the Business Banking Division. The steering committee for investments in non-banking corporations convenes quarterly and advises Bank management on investments in non-banking corporations. The steering committee is responsible for management and maintenance of the existing portfolio, trying to improve it so as to allow for rational realization of this portfolio within a reasonable time frame but with no specified schedule, in order to allow for maximum returns. Quarterly reports are provided to the Risk Control Division and to other divisions.

About 2% of these investments in non-banking corporations are negotiable and presented at their market value. The remainder of these investments are presented at cost or at their carrying amount. In case of impairment of a non-temporary nature, in accordance with management assessment, a provision for impairment of the investment is made by the Bank.

For more information about equity investments in the bank portfolio, see chapter "Major investees" above, the Detailed Risk Report on the Bank website and Notes 12 and 15.A to the financial statements.

Operating risk

Risk description

Operating risk is defined by the Bank of Israel as the risk of loss due to inappropriateness or failure of internal procedures, people, systems or due to external events.

The Bank adopts a wider definition of operating risk. The definition would turn the framework for addressing operating risk into an active one, designed to support operations of the business units, to improve major business processes associated with their operations and thus, to increase business value, rather than only reducing the expected loss due to operating risk. The definition does not supersede the definition which is supported by Basel and by the Bank of Israel, but rather expands it in order to create a framework for operating risk management, which analyzes processes, systems and other risks which may impact the business viability of the Bank.

Information security and cyber risk – Information security risk is risk arising from faults in protection of the Bank's computer systems and information stored there. Cyber risk arises from an event including an attack on computer systems by or on behalf of internal or external adversaries of the Bank.

IT risk – IT risk is risk of failure of the Bank's systems.

Legal risk – Risk of loss due to exposure to fines, lawsuits and/or punitive action due to breach of contract or disagreements. Legal risk includes risks arising from legal exposure due to Bank conduct with its various interested parties (such as: clients, suppliers and other third parties).

Overview of operating risk and guidelines for management thereof

With the developments in global markets and the higher complexity of financial activity and supporting technological infrastructure, an understanding has emerged, that Bank exposure to potential loss due to failures in regular operating activity may impact the business activity. Operating failure events which occurred at financial institutions in recent years have increased legislator awareness and financial institutions' awareness of operating failure events, to the large potential for damage which may be caused by such operating risk event and to their main attributes, as follows:

Operating events may occur throughout the organization and are inherent to financial institution operations.

Operating risk may potentially impact earnings, revenues, value and reputation of the Bank.

Operating risk has inter-relationships with other risks, such as market risk, credit risk, liquidity risk, reputation risk and other risks. Thus, for example, an operating risk event may cause reputation risk to materialize, after which the Bank may face a liquidity event.

A significant share of operating failures has very low probability but relatively large damage potential – which may even threaten Bank stability.

Operating risk has diverse instances, from human error, malfunction in technological systems, fraud, embezzlement, war, fire, robbery etc.

Operating events sometimes occur which are not under control of the financial institution, and may develop as a result of external events, some of which are unforeseen, with chances of occurring which cannot be estimated in advance, such as: natural disaster (earthquake, flooding) or security event.

Bank management and the Board of Directors attach great importance to managing operating risk, due to its materiality, as part of the Bank's overall framework for risk management and control. The Board of Directors and management have determined that management of operating risk requires creation of an appropriate culture within the organization, by means of training, dissemination of related content and application of elevated standards of internal control at all levels.

The Bank has a special policies document for addressing operating risk. The operating Risk Owner at the Bank is the Manager, Risks Control Division – who is also the Bank's Chief Risks Officer. The framework stipulated for handling this risk includes the framework required for handling fraud and embezzlement, which are part of the operating risk categories according to Bank of Israel directives. Recently, the Bank has deployed a framework for addressing operating risk which is not only defensive, i.e. acting only to minimize potential loss due to operating risk events, but also actively strives to regulate aspects of operating risk in systems, processes and controls applied by the Bank, in order to support achievement of its business targets.

Bank policies specify the Bank's operating risk appetite at 1% of the Bank's core capital. This appetite is constantly monitored by follow up on any default events which caused a loss, managed by category of operating risk, in conformity with Bank of Israel directives and also includes loss due to legal risk, information security and cyber risk, including fraud and embezzlement. The policies also stipulates the risk appetite for potential loss upon occurrence of a stress event. The Bank acts to specify a high-quality risk appetite, primarily by creating forward-looking risk indicators which can indicate a potential for development of operating risk, in addition to collection of actual losses, i.e. losses which have already occurred.

The framework for handling operating risk is based on three lines of defense:

- **First line of defense** The Bank's approach is that risk management is based, first and foremost, on the business units, which review the major business processes and put in a continuous effort of self-assessment of the risk associated there with.
- **Second line of defense** The Risks Control Division is tasked with overview and monitoring of the framework for addressing operating risk through a range of processes, tools and methods: Locating major risk hubs in business operations of the first line, through collection of actual operating failure data and conducting specific surveys for identification of potential future failures, as well as adapting the operating risk handling framework to Bank needs, in line with business development at the Bank and with regulatory requirements.
- **Third line of defense:** Internal Audit conducts audits of operating risk management in order to ascertain the effectiveness of handling such risk, in accordance with the work plan.

The Bank allocates capital with respect to operating risk using the standard approach. According to this approach, the Bank was segmented into eight lines of business, as stipulated by the Bank of Israel, with a standard risk weighting assigned to each line of business, reflecting its sensitivity to loss with respect to operating risk. This segmentation and addressing the required capital allocation are incorporated in a specific policy document which governs the aspects required for capital allocation using the standard approach and, in particular, specified the lines of business in Bank operations.

The Bank framework for handling operating risk is reviewed quarterly, as part of the Bank's Risks Document. The risk profile is presented in this context, i.e. the actual loss level, in view of the risk appetite and the most material events which occurred during the quarter are also presented and analyzed.

The Bank has prepared to put in place comprehensive infrastructure for addressing fraud and embezzlement risk. As part of this effort, the Bank operates a range of laws designed to identify anomalies. Handling of fraud and embezzlement is in conformity with a specific policy document, using a framework which integrates several entities at the Bank: Risks Controls, information security and cyber, human resources and the Technology Division.

Operating risk mitigation

Due to the significance of operating risk, the Bank takes different steps to mitigate this risk. The most important step is to instill a corporate culture which promotes strong awareness of operating risk, and of deployment of risk-mitigating processes. The internal controls trustees, across the entire organization, are the long arm of the operating Risk Manager in this process. The Bank initiates delivery of in-person and technology-based training about operating risk to new employees and to units and populations within such units which were identified as being associated with high operating risk.

Changes to revised processes and new processes with potential for materialization of operating risk undergo a structured process of approval by business entities and by control entities, prior to launch, using a checklist – and are sent for approval by the Steering Committee. This mechanism is used to review all aspects of the change, ensuring a professional review of the root risk and how to mitigate it.

One of the tools used by the Bank is debriefing and lesson learning flowing internal and/or external events. Conclusions formulated by this process are incorporated into work processes, systems, training content and procedures – and are also disseminated using the operating risk system to internal controls trustees for deployment at their units.

The Bank has established policies and operating plans for case of emergency, for backup, recovery and business continuity in case of physical damage to Bank infrastructure. This plan, supported by emergency procedures and pre-appointed officers, is exercised annually and the conclusions from such exercises is incorporated into the action plan.

Mitigating operating risk via insurance – the Bank is insured under a banking insurance policies, against damage which may be incurred in the course of normal operations, as a result of human error, fraud, embezzlement etc. The Bank obtains an officers' insurance policies, which applies to all officers at the Bank and at the different Bank Group companies, which provides insurance coverage for personal claims which may be filed against officers with respect to their actions in the course of their position with Group companies. Obtaining such an officer liability insurance policy is subject to approval by the General Meeting of Bank shareholders.

The Bank has obtained specific insurance policies for property damage and liability, which provide insurance coverage of Bank property and liability. The Bank has a specific policy document which governs insurance aspects related to Bank operations.

Business continuity

The Bank applies Proper Banking Conduct Directive 355. In implementing the directive, the Bank maintains a management and reporting framework, including a steering committee which supervises implementation of the plan and a manager responsible for actual implementation. Once every six months, a status report is provided to management and to the Board of Directors' Risks Committee. The Bank implements a multi-annual exercise program, which includes drills and technology trials, in order to review and improve readiness and awareness of Bank management and employees to handling disaster scenarios; this included exercise of the secondary computer site (DRP).

In the second half of 2016, progress was made on implementation and management of the business continuity plan, including better technology survivability and improved readiness of DRP sites. Highlights of activities:

Training and drilling:
- In-person training at Bank branches, including core branches.
- Regular training on business continuity in banking courses at the Training Center.
- Comprehensive annual exercise using national reference scenarios and internal scenarios, including exercise of in-depth scenarios of the business continuity plan, with participation of the business divisions and the Situation Room.
- Exercise of alternate Trading Room, involving employees of the Trading Room and the Finance Division, including system operation and conducting transactions.
- Exercise of select branches in operating the business continuity plan and how the branch is to be operated under various emergency scenarios.
- Conducting technology exercises, operating systems at DRP site, including review of the recovery time of computer systems, in conformity with the Bank's recovery plan.
- Taking part in exercises conducted by the Bank of Israel.

Refreshers on basic procedures and BIA:
- In conformity with the maintenance procedure for the business continuity plan, the Bank conducts a refresher of emergency services, once every two years.
- In late 2016, the Bank completed a refresher of emergency services, including the business divisions, and accordingly updated the emergency files of the divisions and the business continuity plan.
- In conformity with the maintenance plan, the Bank recently refreshed the basic procedures of the business continuity plan, including: the policy document, the reference scenario document, the recovery document, the Bank's master procedure etc.

Information security and cyber security

Directive 361 with regard to Cyber Defense Management provides guidelines for proper management of cyber risk, which require expansion and adjustment of the IT risk management framework with regard to the threat space perception and the required defensive capabilities. Accordingly, the Bank has an approved strategy and comprehensive cyber defense policy and has specified the defense lines for implementation thereof, has appointed an Information Security and Cyber Defense Manager, reporting to the Manager, Risks Control Division – responsible, *inter alia*, for setting policy on information security and cyber defense at the Bank, development of a cyber defense work plan, monitoring the implementation of this work plan and review of the effectiveness of systems and processes for information security and cyber defense.

The relationships and information flow between these units have been specified in procedures, including reference to: information security, physical security, IT governance, IT operations, risk management, fraud, human resource management, business continuity, client relationship management, spokesperson operations and legal counsel.

Information security and cyber defense policies at the Bank is implemented, inter alia, by the Mizrahi Tefahot Technology Division Ltd. As part of this effort, the management concept applied includes guidelines for management of cyber security. Application of these guidelines and ensuring that they are current while incorporating them into strategic decisions and business and operational activity at the Bank – would ensure the consistency and integrity of the cyber security management concept over time.

The information security and cyber security policy is based on the following principles:

- Mapping and identifying cyber risks.
- Establishing an effective set of controls with cross-organizational integration of technology, human resources, processes and procedures.
- Specifying mechanisms to protect client and business activities in the online domain, in conformity with Proper Banking Conduct Directive 367.
- Proactive cyber security implemented through mapping and knowledge of the environment, forecasting and study of threats, weighting of the current situation report, development of responsiveness processes, use of techniques for deception, diversion and delay, cyber resilience and recovery capacity, conducting processes of inquiry, debriefing and execution of judgment.
- Implementation of multi-layer security in several circles and disciplines (both logical and physical), from the external system accessible to clients and through to internal systems, information and intelligence sharing.
- Using a system for monitoring, control and response for management of cyber events with integrated, corporate-wide view of components such as human resources, means of communications and procedures.
- Periodic and current reporting of risks management as a whole.
- Current analysis and assessment of cyber threats and exercising all those involved in handling cyber events.
- Development of stress scenarios related to information security and cyber.

In addition, the Bank's On line Banking sector is certified under the information security management standard ISO 27001.

In 2016, the Bank prepared for implementation of Proper Banking Conduct Directive no. 367 with regard to online banking systems and to risk management in this area as from January 1, 2017.

In 2016, the Bank conducted multiple attempts to introduce viruses and ransomware. The existing defense systems blocked these attempts. The appropriate reports have been duly delivered to the various entities involved.

In 2016 there were no significant cyber events which caused damage to the Bank.

Information technology risk

In recent years, the risk associated with IT management has 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. This is also intended to ensure that the Bank maintain business continuity during an alert or emergency. This may mitigate reputation risk and business risk which may arise under such conditions.

The Technology Division Manager is responsible for management of IT assets and the management framework is specified in a special policy document, in line with principles specified in policy documents on risk management and control at the Bank. The IT asset management policy is in line with requirements of the Supervisor of Banks and, in particular, with the principles stipulated in Proper Conduct of Banking Business Directive 357 "IT management"; Proper Conduct of Banking Business Directive 350 "Operating risk management"; Proper Conduct of Banking Business Directive 355 "Business continuity management" and Proper Conduct of Banking Business Directive 361 "Cyber security management". The Bank has minimal risk appetite for this risk, which is included, as noted above, under management of risk appetite under routine conditions and under stress conditions, for operating risk.

For more information about the project to replace the core banking system at Bank Yahav, see chapter "Significant developments in IT" above.

Legal risk

Proper Banking Conduct Directive no. 350 concerning "Operating risks" defines legal risk to include, inter alia, exposure to fines or penalties arising from supervisory action, as well as from individual arrangements.

The Bank regards legal risk in its wider definition, with regard to Bank conduct in its relationships with various stake holders (clients, suppliers, other third parties etc.) Legal risk includes risks arising from legislative and regulatory provisions, rulings by judiciary or quasi-judiciary authorities as well as legal risks arising from regular Bank operations. The Chief Legal Counsel for the Bank has been appointed Chief Legal Risks Manager. The Bank constantly strives to minimize as much as possible the legal risks associated with its current operations, and acts to disseminate a practical culture leading to identification and mitigation of legal risk in all its different aspects.

The Bank's Legal Division regularly analyzes the legal risk components, the risk boundaries (arising, for example, from the counter-party identity, from creation of collateral etc.) as well as specific risk attributes while reviewing its risk level and exposure with attention to the different lines of business at the Bank. For more information about an investigation by the US Department of Justice concerning Bank Group business with its US clients, see Note 26.C.12 to the financial statements.

The Bank's Legal Division applies internal processes to ensure regular monitoring of developments in legislation, rulings and other regulatory provisions which could have implications for the day-to-day activities of the Bank Group. In this context, the Legal Division provides guidance to relevant Bank entities with regard to implementation of the implications arising from these developments. The Legal Division provides regular counsel to different Bank units, including to some subsidiaries. This is done, *inter alia*, by providing opinions, editing and updating legal documents, support for updates to procedures etc.

The Bank has specified procedures to help in minimizing legal risk, including regulating the interface between the Legal Division and different Bank departments. The Legal Division is also involved in training delivered to branches, at the Bank's Training Center and in compiling professional eLearning kits for imparting the legal knowledge required for regular Bank operations.

Similar reference is made for Bank affiliates overseas (branches and subsidiaries), with these affiliates receiving assistance from local external attorneys approved by the Bank's Legal Division. The Bank's overseas subsidiaries and affiliates have adopted similar procedures with regard to management of legal risk, and provide immediate and quarterly reports to the Legal Risk Manager of the Bank with regard to any legal risks identified in these entities.

For more information about operating risk, see also the Detailed Risk Management Report on the Bank website.

Liquidity and financing risk

Risk description

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.

Financing risk – risk resulting from shortage of financing sources or too high costs for such sources.

Overview of liquidity risk and guidelines for management thereof

Liquidity risk is managed in conjunction with Proper Conduct of Banking Business Directive 310 "Risks management", Directive 342 "Liquidity risk management" and Directive 221 "Liquidity coverage ratio". The risk is managed subject to the limitations of the Board of Directors and Executive Management in an effort to minimize the losses deriving from an investment of surplus liquidity in assets that are highly liquid, but have a low yield.

Liquidity risk management is governed by a policies document submitted annually or more frequently for approval by the Board of Directors. The policies document covers how risk is managed, including roles and responsibilities of the various organs, the regular management of liquidity risk, all parameters used for risk measurement in the normal course of business and under various stress scenarios, restrictions specified by the Board of Directors and by management, including restrictions on source concentration and composition, as well as a detailed emergency plan for handling a liquidity crisis, including various states of alert for liquidity risk management and potential means under each scenario type and the estimated time for execution.

The Bank’s Board of Directors sets strategy for liquidity risk management and the risk appetite in conformity with regulatory requirements, using a range of restrictions on three risk dimensions: Normal course of business, scenarios (liquidity coverage ratio and minimum liquidity ratio – internal model) and concentration. Bank management has specified a further set of restrictions to serve as management guidelines – beyond those specified by the Board of Directors. In 2016 there were no recorded deviations from the Board of Directors’ restrictions.

In September 2016, the Bank of Israel issued a Q&A File with regard to Directive 221 "Liquidity coverage ratio". The update stipulated that banking corporations would not be required, as of January 1, 2017, to maintain a minimum liquidity ratio (as specified in Proper Banking Conduct Directive 342) equal to or higher than 1. Therefore, as from the start of 2017, the Board of Directors restrictions with regard to minimum liquidity ratio (internal model) were replaced by management restrictions.

The Bank applies tools for monitoring liquidity risk using endogenous and exogenous indicators, which may point to an increase in risk up to crisis status. The Bank developed an integrated benchmark for monitoring financial markets in Israel, in order to identify any instability in the financial system in Israel – this benchmark is a decision-support tool for declaring a state of alert due to systemic failure.

In 2016, the Bank raised its state of alert to Elevated Alert on multiple occasions; in all cases, the cause was external-systemic, such as: sharp declines in equity indexes in Europe in the first quarter of 2016 due to severe concern about stability of European banks and the Brexit event (the UK leaving the EU) in the second quarter of 2016. In actual fact, in all cases there was no impact to the Bank's liquidity situation.

For more information about liquidity risk, see also the Detailed Risks Management Report on the Bank website.

Overview of financing risk and guidelines for management thereof

Financing risk is managed, as part of the liquidity risk, using Board and management restrictions on concentration of financing sources and through reduced dependence on material counter-parties.

Concentration of financing sources is monitored through a wide range of restrictions set by the Board of Directors, management as well as by key risk indicators, classified into several sub-categories: Size, client type, individual depositor, number of clients, product and average deposit term. A "super-benchmark" was defined, which averages all indicators related to concentration of financing sources. Current management of source composition includes setting policy on source diversification and financing terms as well as setting specific targets for risk benchmarks. Concentration is monitored daily and is regularly managed and reported.

The Bank's main financing sources are stable and diverse sources for different time horizons – retail and business deposits, long-term deposits from financial institutions and debenture issues. The Bank acts proactively to identify sources for longer terms, including through a wide range of deposits offered by the Bank to its clients, deposits with unique attributes, which allow clients to benefit from relatively high interest over the long term with optional liquidity during the deposit term. In the fourth quarter of 2016, concentration risk for financing sources remained low.

Furthermore, exposure to derivatives is regularly managed, in line with the exposure to each counter-party, counter-party collateral is immediately increased or collateral is immediately demanded from the counter-party.

For more information about financing sources, see chapter "Developments in financing sources" above.

For more information about financing risk, see also the Detailed Risk Management Report on the Bank website.

Liquidity coverage ratio

As from April 1, 2015, the Bank applies Directive 221 "Liquidity coverage ratio" which became effective on that date. This Directive stipulates minimum liquidity ratios for a one-month term (regulatory LCR), calculated based on uniform multipliers for the banking system, specified by the Bank of Israel based on Basel III directives. In conformity with transitional provisions, the minimum requirement increased in 2016 to 80% and as from January 1, 2017, the minimum requirement is 100%. The Bank’s Board of Directors specified a further safety cushion beyond the minimum ratio. This ratio is managed and reported for all currencies in aggregate and for NIS separately, both at Bank level and on Group basis. The ratio for the bank solo and the consolidated ratio are calculated daily and reported as the average of daily observations over 90 days prior to the report date. This regulation is in addition to liquidity risk management using internal models, as stipulated by Directive 342, as described above.

In 2016, the Bank continued to maintain appropriate liquidity by investing excess liquidity in liquid assets of very high quality – Level 1 assets. The average (consolidated) liquidity coverage ratio for the fourth quarter of 2016 was 117% (the minimum ratio required by the Supervisor of Banks was 80%), compared to 105% in the third quarter. The increase in the average ratio compared to the previous quarter is due to continued increase in retail and other deposits and continued improvement in the structure of Bank resources, which resulted in increase in liquid assets. In 2016 there were no recorded deviations from the restrictions on this ratio.

For more information about liquidity risk, see also the Detailed Risk Management Report on the Bank website.

As of December 31, 2016, the balance of the three largest depositor groups at the Bank Group amounted to NIS 10.5 billion.

Term to maturity – Below is evolution of Bank cash flow by term to maturity, as presented in detail in Note 32 to the financial statements.

The Bank consistently acts, as part of its strategy on resource and use management, to raise long-term sources.

The Bank's NIS-denominated balance sheet sources for terms longer than 1 month, as percentage of total NIS-denominated sources as of December 31, 2016, was 52% (similar to the previous year), of which balance sheet sources for terms longer than 1 year – 57% (as of December 31, 2015: 52%).

Most of the Bank's balance sheet sources in foreign currency as of December 31, 2016 are for terms of up to 1 year, constituting 97% of total foreign currency-denominated sources (last year: similar), of which 22% are sources for terms longer than 3 months (as of December 31, 2015: 23%).

The NIS-denominated sources have longer terms than foreign currency-denominated sources, in line with the longer term use of NIS-denominated funds, primarily for mortgages denominated in NIS.

The Bank also conducts a significant volume of futures transactions to divert excess liquidity between NIS and foreign currency and by term, as part of dynamic management of sources and uses.

Soliciting sources and Bank liquidity status – During 2016, there was an increase in the Bank’s balance of deposits from the public. The balance of deposits from the public rose from NIS 162.4 billion on December 31, 2015 to NIS 178.3 billion on December 31, 2016, an increase of 9.8%.

In the non-linked segment, total deposits from the public amounted to NIS 122.6 billion, an increase of 12.4% compared to end of 2015. In the CPI-linked sector, deposits from the public amounted to NIS 17.0 million, an increase of 1.6%, and in the foreign currency sector – to NIS 38.6 billion, an increase of 5.7% compared to end of 2015.

Other risks

Compliance and regulatory risk

Risk description

Compliance risk is the risk of imposition of legal or regulatory sanctions, material financial loss or impact to reputation, which the Bank may incur due to its failure to comply with compliance provisions.

Compliance risk includes cross-border risk, which is presented separately below.

Overview of compliance and regulatory risk and guidelines for management thereof

As from January 1, 2016, when the new Proper Banking Conduct Directive 308 became effective, the scope of responsibility within compliance risk management was expanded; therefore, the compliance provisions include laws, rules and regulations (including positions stated by the Supervisor of Banks in conjunction with handling public inquiries), internal procedures and the Code of Ethics which apply to banking operations at the Bank.

The Bank has minimal risk appetite for compliance and regulatory risk, with regard to compliance with statutory provisions applicable to the Bank. Therefore, the Bank has specified that any faults discovered in compliance with statutory provisions would be addressed by Bank units as a top priority. The Bank has specified a multi-annual work plan for the Compliance Function, which includes qualitative targets for reducing compliance risk across the Bank.

The compliance and regulatory Risk Manager for the Bank is the Manager, Risks Control Division. The Compliance Officer is responsible for continuous management of this risk.

The Bank operates in conformity with policies on compliance and regulation risk management, approved by the Bank Board of Directors. The Compliance Officer acts in conformity with a letter of appointment approved by the Board of Directors, to deploy a compliance culture at the Bank, its subsidiaries and overseas affiliates by implementing a Group policy and supervising the implementation of appropriate compliance processes at subsidiaries and affiliates. Compliance risk is managed by identification, documentation and assessment of compliance risk associated with business operations of the Bank, including developments related to new products, business conduct, lines of business or new clients, or to material changes to any of the above, through various measurement methods.

In 2016, the risk level for compliance and regulation decreased, in our opinion. The decrease is due to continued addressing of risk classified as High and continued reinforcement of control in both First Line and Second Line units. This is against the backdrop of increased regulation and frequently issued new directives.

For more information see the Detailed Risks Management Report on the Bank website.

Cross-border and AML risk

Risk description

Cross-border risk is the risk of financial loss (including due to legal proceedings, fines or sanctions imposed by statutory authorities or others in Israel and in other countries) and of impact to reputation, arising from the Bank's failure to comply with statutory provisions originating in other countries – whether provisions binding on the Bank or provisions which are not binding, but failure to comply with them may cause the Bank to incur damage, or from overseas activities of Bank clients in contravention of any statutory provisions.

Cross-border risk includes, *inter alia*, risk of damage, including impact to reputation, due to lawsuits or other enforcement proceedings brought by authorities in other countries, with regard to foreign tax laws applicable to certain Bank clients, AML and terror financing laws, sanctions imposed by international bodies and foreign authorities or other laws. Cross-border risk applies primarily at the Bank's overseas affiliates; in transactions with clients who are foreign residents; in business operations conducted by Bank representatives in foreign countries; and with regard to funds of individual Israeli clients invested overseas.

Cross-border risk includes the risk arising from obligations arising from US tax laws applicable to Bank Group operations outside of the USA (the Foreign Account Tax Compliance Act – "FATCA"). For more information about FATCA, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" (Legislation and Supervision of Bank Group Operations) of these annual financial statements.

AML risk – The risk of imposition of legal or regulatory sanctions, of material financial loss or of damage to reputation and image, which the Bank may incur due to non-compliance with AML and terror financing provisions.

Overview of cross-border risk and guidelines for management thereof

The Bank has zero appetite for cross-border risk. Therefore, the Bank has specified that any faults discovered with regard to cross-border risk would be addressed by Bank units as a top priority. The Bank has specified a multi-annual work plan for the Compliance Function, which includes qualitative targets for reducing compliance risk across the Bank.

In 2016, the Bank has trained 15 branches specialized in management of foreign-resident client accounts and only allows foreign residents to open accounts in these branches. Current foreign-resident clients with a significant balance were relocated from other Bank branches to these specialized branches.

After an increase in risk intensity last year, cross-border risk continued to moderately decrease in 2016, due to continued preparation for risk management.

For more information see the Detailed Risks Management Report on the Bank website.

Overview of AML risk and guidelines for management thereof

The Bank has zero risk appetite with regard to AML risk.

The AML Risk Owner for the Bank is the Manager, Risks Control Division.

The Chief Compliance Officer for the Bank Group, appointed in the Risks Control Division, is also in charge of implementation of the Prohibition of Money Laundering Act, and of the Prohibition of Financing Terrorism Act for the Bank Group, including Bank affiliates overseas.

Following the amendment of the Prohibition of Money Laundering Act, which adds serious tax offenses to the list of original violations, making them subject to all requirements with regard to AML, the Bank is preparing to adjust work processes and infrastructure for compliance with this requirement.

AML risk increased in 2016, primarily due to addition of serious tax offenses, as noted, to the Prohibition of Money Laundering Act.

For more information see the Detailed Risks Management Report on the Bank website.

Reputation risk

Risk description

The Bank has mapped reputation risk as a material risk, because past events indicate that impact to the reputation of a financial institution may result in significant loss of value. Reputation risk is a stand-alone risk, but may also arise from materialization of other risks at the Bank, such as materialization of an operating risk event. Furthermore, impact to Bank reputation may bring about the materialization of other risks, in particular liquidity risk – with growing demand by clients to withdraw deposits.

Overview of reputation risk and guidelines for management thereof

The Bank has defined its risk appetite for reputation risk as minimal. In recent years, the Bank took action to put in place a framework for handling reputation risk. The Bank considers that this risk should be addressed based on similar principles to those used to address other risks, such as credit risk or market risk – even though this risk is considered harder to quantify.

The Reputation Risk Owner is the Manager, Marketing, Promotion and Business Development Division at the Bank.

Reputation risk is managed in conformity with the policy on three levels: In advance (under normal conditions), in real time (alert condition) and in retrospect.

In 2016, there were no events which negatively impacted the Bank's reputation.

For more information see the Detailed Risks Management Report on the Bank website.

Strategic risk

Risk description

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 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.

Overview of strategic risk and guidelines for management thereof

The Bank operates in conformity with the outline of a five-year strategic plan, most recently approved by the Bank Board of Directors in November 2016, whose principles have been made public. Deviation from Bank strategy is subject to approval by the Bank’s Board of Directors. This risk is monitored by the Planning, Operations and Client Asset Division (hereinafter: "the Planning and Operations Division") and is challenged by the Risks Control Division.

The Strategic Risk Owner is the President & CEO; based on their guidance, management periodically reviews the implementation of the strategy, monitoring of regulatory, economic or technology developments which affect the strategy and initiating annual work plans derived from and in conformity with the strategic plan.

For more information see the Detailed Risks Management Report on the Bank website.

For more information about environmental risk, see the chapter "Credit risk" above.

Risk factor assessment

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[1]	Risk factor impact	Risk Owner
Overall effect of credit risk	Low-medium	Manager, Business Division
Risk from quality of borrowers and collateral	Low-medium	
Risk from industry concentration	Low-medium	
Risk from concentration of borrowers/ borrower groups	Low	
Risk with respect to mortgage portfolio	Low	
Overall effect of market risk	Low-medium	Manager, Financial Division
Interest risk	Low-medium	
Inflation risk	Low-medium	
Exchange rate risk	Low	
Share price risk	Low	
Liquidity risk	Low-medium	Manager, Financial Division
Overall effect of operating risk	Intermediate	Manager, Risk Control Division
Cyber and information security	Intermediate	Manager, Risk Control Division
Information technology risk	Intermediate	Manager, Mizrahi-Tefahot Technology Division Ltd.
Legal risk	Low-medium	Chief Legal Counsel
Compliance and regulatory risk	Intermediate	Manager, Risk Control Division
Cross-border and AML risk	Low-medium	Manager, Risk Control Division
Reputation risk[2]	Low	Manager, Marketing, Promotion and Business Development Division
Strategic-business risk	Low	President & CEO

(1) Assessment of the effect of the aforementioned risk factors takes into account the risk associated with the US DOJ inquiry as well as all action taken by the Bank to defend its position with regard to that inquiry. For more information about the US DOJ inquiry with regard to Bank Group business with its US clients and for more information about a motion for approval of a derivative claim and motion for approval of a class action lawsuit on this matter, see Notes 26.C.10.J, 26.C.11.A and 26.C.12 to the financial statements.
(2) The risk of impairment of the Bank's results due to negative reports about the Bank.

The impact of the various risk factors in the table above have been determined based on management assessment, as provided from time to time. These assessments, based on monitoring of various quantitative risk benchmarks specified by the Bank, includes the direction of their development and are based on qualitative assessment of risk management and the effectiveness of control circles, in coordination with the Bank's ICAAP process and results thereof, led by the Bank's risk managers.

The ICAAP process accounts for both qualitative and quantitative aspects, including the Bank's risk profile, outcome of various scenarios at the Bank and the capital planning process. In the fourth quarter of 2016, as an integral part of the ICAAP process as part of the work plan discussions at the Bank for 2017, the Bank conducted self-assessment of the quality of risk management for risk mapped by the Bank. This process was based on rating the risk level and management quality, conducted independently by teams on behalf of Risk Owners and teams on behalf of risk controllers.

Policies and critical accounting estimates

The Bank's financial statements are prepared in conformity with generally accepted accounting policies in Israel (Israeli GAAP) and in accordance with Public Reporting Directives of the Supervisor of Banks.

For most topics, these directives are based on generally acceptable accounting practices by US banks. For other, less material topics, these directives are based on International Financial Reporting Standards (IFRS) and on generally accepted accounting principles in Israel (Israeli GAAP). When International Financial Reporting Standards (IFRS) allow multiple alternatives, or do not specifically refer to a certain situation, these directives prescribe specific implementation guidelines, mostly based on generally acceptable accounting practices by US banks.

The significant accounting policies are detailed in Note 1 to the financial statements.

The application of generally accepted accounting principles by management at the time that the financial statements are prepared occasionally involves various assumptions, assessments and estimates that affect the amounts and business results reported in the financial statements. Some of the assumptions, assessments and estimates are critical to the financial position or the results of operations reflected in the Group's financial statements, because of the materiality of the matter, complexity of calculations or the extent of the probability that matters shrouded in uncertainty will be realized.

Provided below are accounting policies on critical matters:

Provision for credit losses

The Bank has put in place procedures for classification of credit and for measurement of provision for credit losses, in order to maintain an appropriate provision to cover expected credit losses with regard to the Bank's loan portfolio. Further, the Bank has put in place procedures to be followed, an appropriate provision to cover expected credit losses with regard to off-balance sheet credit instruments (such as: commitments to provide credit, unutilized credit facilities and guarantees).

The required provision to cover expected credit losses from the credit portfolio is estimated under one of the following tracks: "individual provision" or "group provision". Further, the Bank reviews the overall appropriateness of the provision for credit losses.

Such review of debts in order to determine the provision and debt handling is consistently applied to all debts in excess of NIS 700 thousand and in conformity with the Bank's credit management policy – and no transition is made, during the debt term, between the individual review track and the group-based review track – unless in case of restructuring of troubled debt.

Individual provision for credit losses – According to Bank policy, this is applied for any debts determined to be impaired, whose contractual balance (including accounting write-offs, unrecognized interest, provisions for credit losses and collateral) is NIS 700 thousand or higher.

Individual provision is also applied to any debt whose terms and conditions have been changed in conjunction with restructuring of problematic debt, unless this debt is subject to provision by extent of arrears. The individual provision for credit losses is estimated based on expected future cash flows, discounted using the effective interest rate of the original debt. When debt collection is contingent on collateral, or when the Bank has determined that seizure of an asset is expected, the individual provision for credit loss is evaluated based on the fair value of the collateral pledged to secure such debt, after application of consistent, conservative multipliers to reflect, *inter alia*, the volatility in fair value of such collateral, the time it would take until actual realization and the expected cost for selling the collateral. For this matter, the Bank defines debt as debt contingent upon collateral, when it is expected to be entirely repaid by pledged collateral, or when the Bank expects repayment from an asset even with no specific pledge on such asset, provided that the borrower has no other reliable sources available for repayment.

The Bank regularly reviews the forecasted expected credit losses, based on actual cash flows, and adjusts the individual provision to the current forecast. Actual credit losses may differ from the Bank's original estimates upon classification of the debt as impaired.

Group provision for credit losses – This is applied for large, homogeneous groups of small debts (whose balance is below NIS 700 thousand, according to Bank policy) (such as: credit card debts, housing loans and consumer debts repaid by installments) as well as for large, non-impaired debts. The provision for credit losses with respect to debts based on group estimate, other than housing loans for which the provision has been calculated based on a formula specified by the Supervisor of Banks based on extent of arrears, is based on rules specified in FAS 5 (ASC 450) "Accounting treatment of contingencies" and in conformity with the directives of the Supervisor of Banks, based on historical loss rates in various economic sectors, divided into troubled and non-troubled debt, for the period from January 1, 2011 through the report date. For more information about the Supervisor of Banks' directive with regard to group provision for credit losses, see Note 1.C. 4) to the financial statements.

Application of this directive has no material impact on the Bank's financial statements.

In addition to calculating the average range of historic loss rates for various economic sectors, as per the above, for determining the appropriate rate of provision, the Bank also accounts for relevant environmental factors, including trends in credit volume for each sector as well as sector condition, macro-economic data, general quality assessment of credit to each economic sector, changes in volume and in trend of balances in arrears and impaired balances and the effect of changes in credit concentration.

In conformity with directives of the Supervisor of Banks, the Bank has formulated a methodology for measuring the group provision, which takes into account both past loss rates and adjustments with respect to relevant environmental factors.

Furthermore, the rate of adjustment with respect to relevant environmental factors for group provision for credit losses with respect to individuals is not less than 0.75% of the non-impaired consumer credit balance (excluding credit due to receivables for bank credit cards without interest charge).

This is based on a specific directive by the Supervisor of Banks, dated January 19, 2015.

Pursuant to provisions stated in the interim directive, as from January 1, 2011 the Bank is not required to maintain general and supplementary provisions, but continued to calculate the supplementary provision and to verify that in any case, the amount of group provision at the end of each reporting period shall be no less than the sum of general and supplementary provisions which would have been calculated as of the same date, gross of tax.

Housing loans – A minimum provision with respect to housing loans is calculated based on the formula stipulated by the Supervisor of Banks, by extent of arrears, such that the provision rate is higher the longer the arrears. This directive applies to all housing loans, other than loans not repaid by periodic installments and loans used to finance activity of a business nature.

The Bank also applies Proper Banking Conduct Directive no. 329, as per the Supervisor of Banks' letter dated March 21, 2013 "Update to guidelines with regard to residential real estate".

In conformity with these directives, the Bank has set policies designed to ensure that the Bank would be in compliance with stipulations of this directive and that, as from June 30, 2013, the balance of group provision for credit losses with respect to housing loans shall be at least 0.35% of the outstanding balance of such loans as of the report date.

Off-balance sheet credit – The required provision with regard to off-balance sheet credit instruments is assessed as per rules stated in FAS 5. The provision estimated on group basis for off-balance sheet credit instruments is based on provision rates specified for total credit exposure (as stated above), accounting for expected credit realization rate for the off-balance sheet credit risk. The credit realization rate is calculated by the Bank based on credit conversion factors, as specified in Proper Banking Conduct Directive 203 "Measurement and capital adequacy – Credit risk – Standard approach" with certain adjustments.

Derivatives

are treated and presented based on US accounting standards codification ASC 815 and ASC 820. According to the guidelines, all derivatives are stated in the balance sheet at fair value. FAS 157 (ASC 820) defines fair value, and sets forth a consistent work framework for fair value measurement, by defining valuation techniques and a fair value ranking. The ranking divides instruments measured at fair value into three levels:

Level 1 – fair value measured using prices quoted for identical instruments on an active market accessible by the bank upon the measurement date.

Level 2 – fair value measured using observed data, either direct or indirect, which are not quoted prices as set forth under Level 1. Level 2 data include quoted market data on active markets, or on non-active markets, if they exist, or data derived from or based upon such observed market data.

Level 3 – fair value measured by using non-observed data.

The Bank evaluates whether markets on which financial instruments are traded are active, based on the following parameters: Volume and value of transactions conducted on the market, current bid/ask spread and alignment of prices for similar transactions on the same market.

According to the standard, the non-performance risk should be reflected in estimating the fair value of debt, including derivatives, measured at fair value. The Bank estimates credit risk for derivatives using a model based on indications of credit quality of the counter-party, derived from prices of debt instruments of the counter-party traded on an active market, and from prices of credit derivatives based on the counter-party's credit quality. In the absence of such indications, the Bank calculates the adjustments based on internal ratings. The Bank reviews the materiality of the credit risk element compared to fair value as a whole, in conjunction with review of instrument classification under fair value ranking levels.

In accordance with Bank of Israel directives, fair value measurement of a derivative instrument, when no quoted prices, liquid collateral or offset agreements exist which adequately secure the derivative's credit quality, and when no market information exists as to the credit quality of the counter-party (such as CDS or negotiable debentures of the counter-party) – shall be classified as a Level 3 fair value measurement.

For more information, see Note 1.D. 16) to the financial statements. For details of derivatives measured at fair value by different fair value levels – see Note 33 to the financial statements.

Securities

in the portfolio held for trading and in the portfolio of available for sale securities are stated at fair value, in accordance with the public reporting directives of the Supervisor of Banks. Securities classified in the portfolio held to maturity are measured at amortized cost. The fair value of the securities is determined based on quoted market prices in active markets for the securities or for securities with similar terms, i.e. stock market price, quotes from recognized data services, such as Bloomberg, or quotes from banks acceptable to the Bank. The Bank uses internal models for reviewing the fair value of financial instruments for which there is no quote on a stock exchange, and does not rely entirely on prices obtained from counter-parties or from quoting firms. The fair value calculation was validated by the Bank's Risks Control Department, which does not participate in the fair value calculation process, assisted by an external professional consultant specializing in models for calculating fair value of financial instruments. Validation is conducted by reviewing the model assumptions and parameters; reviewing the model methodology and its application thereof; and independently reviewing the model in comparison with other models, to the extent possible.

For details of securities measured at fair value by different fair value levels – see Note 33 to the financial statements.

The financial statements as of December 31, 2016 include critical estimates with regard to other-then-temporary impairment of investment in securities, with a total original investment cost of USD 25 million (NIS 96 million). Total impairment recognized as other-than-temporary in nature as amounted to USD 25 million (NIS 96 million). For estimating such impairment, the fair value of investment was calculated based on market prices quoted on the major market. In conformity with regulations and directives of the Supervisor of Banks, the Bank periodically reviews whether impairment of the fair value of such securities is other-than-temporary in nature. It is assumed that impairment compared to deviation of the original investment is not of a temporary nature, primarily in view of the significant decrease, the duration in which the quoted value has not increased, and the erosion of investment's safety cushions. The investment has been fully written-off on the financial statements as of December 31, 2016.

The actual investment value may turn out in future to be materially different from the aforementioned estimate. The future effect on the financial statements may result in recognition of revenues amounting to USD 25 million (NIS 96 million), should it emerge that the impairment is temporary in whole.

The Bank has specified a validation procedure for fair value of instruments measured at fair value on a recurring basis on the financial statements (continued validation), conducted by the Bank's Validation Department. The validation process includes review of the process for determination of fair value, of the assumptions included in this process, of the models used for calculation (including their review, as needed, vs. calculations made by other generally accepted calculation engines) and of input/output data used for calculations and reports.

Liabilities with respect to employee rights

are calculated using actuarial models, based on a discount rate determined based on the yield of Government debentures in Israel plus the average yield spread for corporate debentures rated AA (international rating scale) or higher upon the report date. For practical reasons, the spread would be determined by the difference between yields to maturity, by term to maturity, for corporate debentures rated AA or higher in the USA – and yields to maturity, for the same term to maturity, for US government debentures, all as of the report date. The actuarial models include assumptions related to the mortality tables, disability rates, departure rates and wage hike rates. A change in any of the parameters could lead to a change in the amount of the Bank's liabilities for employee rights.

Group liabilities for employee rights calculated based on an actuarial model amount to NIS 1,231 million. (Including provision for employee retirement at beneficial terms).

The Bank has revised the underlying assumptions of actuarial estimates with regard to liabilities with respect to employee rights. For more information about the streamlining plan and revised assumptions with regard to employee rights, see Notes 1 and 22 to the financial statements.

The following is a sensitivity analysis of total provision for employee rights to changes in key assumptions used as basis for the actuarial estimate, as of the transition date (NIS in millions):

	A 1% increase in discount rate	A 1% change in annual payroll increase		A 1% change in departure rate before retirement age	
		Increase	Decrease	Increase	Decrease
Severance pay provision	(68)	66	(60)	58	(80)
Budgetary pension	(6)	–	–	–	–
Bonuses	(24)	1	(1)	(6)	5

Share-based payment transactions

The financial statements include the benefit value of the stock option plan for the Bank President & CEO and for Bank managers, estimated based on the opinion of an expert external consultant, using generally accepted models, including the Black & Scholes model, the binomial model and the Monte Carlo model, based on various assumptions, mainly with regard to expected exercise date of the options and standard deviation of Bank share price. Changes in the price of the Bank's share, the standard deviation for the Bank's shares and other factors which could affect the economic value of the benefit.

The benefit value is recognized by the Bank over the vesting term of the options using accelerated amortization. For more information see also Note 23 to the financial statements.

The actual benefit value upon exercise of the options is a deductible expense by the Bank for tax purposes, and is subject to payroll tax. The total allowed expense for tax purposes, for which the Bank would record a tax benefit on the profit & loss statement shall not exceed the original benefit value upon option grant. Any tax benefit exceeding this amount would be charged directly to equity.

Some of the Bank's stock option plans include multiple lots which vest on specified dates. The number of options which the offerees may actually exercise, will be primarily based on the net operating profit return on the Bank's average shareholders' equity, up to an annual rate of return equal to 14.5%, as well as on other parameters (for more information see Note 23 to the financial statements), based on the exercise eligibility formula, as stated in the option plan. As of December 31, 2016, the number of options which each offeree may exercise have been adjusted based on actual parameters for each year of the plan.

As of December 31, 2016, the option plans have been fully amortized, hence there is no effect due to changes in management estimates or actual return on equity or other such parameters on the number of options to be awarded.

Provisions for legal claims

The financial statements include appropriate provisions to cover possible damages, where, in the estimation of the Bank's management, based on the opinion of its legal counsel, a provision is required.

In accordance with the directives of the Supervisor of Banks, claims have been classified according to the range of probability of realization of the risk exposure, as follows:

1) Probable risk: there is a probability of more than 70% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Probable, an appropriate provision was made in the financial statements.
2) Reasonably Possible risk: there is a probability of between 20% and 70% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Reasonably Possible, an appropriate provision is sometimes made on the financial statements, at the discretion of Bank management and based on the opinion of legal counsel.
3) Remote risk: there is a probability of less than 20% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Remote, no provision was made in the financial statements.

See Note 26.C for disclosure of material claims (whose amount, excluding interest and expenses, is over 1% of equity attributable to equity holders of the Bank).

Likewise, disclosure is given to motions for recognition as class actions, when the amount claimed in them is material, when, in the estimation of the Bank's management, based on the opinion of its legal counsel, it is not possible, on the date of preparing these financial statements, to estimate their possible outcome, and therefore, no provision was recorded for them.

In accordance with the directives of the Supervisor of Banks, the Bank is permitted to determine for class actions that it is not possible to estimate the prospects for realization of the exposure to risk in the four financial statements published since the claim was filed, or in case of delay of proceedings by decision of the Court. Beyond this, only in rare cases is the Bank permitted to determine that the prospects for realizing the exposure cannot be determined.

Note that the provision for legal claims and contingent liabilities depends on multiple factors and involves a high degree of uncertainty. New information to be received by the Bank in future with regard to existing exposures as of the approval date of the financial statements may materially impact the exposure amount or the provision required with respect to such exposure. For more information about an investigation by the US Department of Justice concerning Bank Group business with its US clients, see Note 26.C.12 to the financial statements.

Provision for impairment of non-financial assets

Recorded in conformity with IAS 36 "Impairment of Assets". Provision for impairment, if needed, is based on assessor valuations updated by the assessor or valuator as required.

Deferred taxes

Deferred taxes are recognized with respect to temporary difference between the carrying amount of asset and liabilities for the purpose of financial reporting, and their value for tax purposes.

Deferred tax are measured so as to reflect the tax implications expected to arise from the manner in which the Bank, at the end of the reported period, anticipates recovering or discharging the carrying amount of assets and liabilities.

Deferred taxes are measured using tax rates expected to apply to temporary differences when realized, based on statutes enacted, or essentially enacted, as of the balance sheet date.

Deferred tax assets are recognized with respect to carry-forward loss, tax credits and deductible temporary differences, when taxable revenue is more likely than not in future, which may enable utilization of these deferred tax assets.

Uncertain tax positions

The Bank applies the rules for recognition and measurement stipulated in FASB Interpretation No. 48 "Accounting for Uncertainty In Income Taxes". In this context, the Bank only recognizes the effect of tax positions if it is more likely than not that those positions would be accepted by the Tax Authority or by the Court. Tax positions recognized are measured at the maximum amount whose likelihood of realization exceeds 50%. Changes in recognition or measurement are reflected in the period in which a change in circumstances resulted in a change in judgment.

The consolidated balance sheet as of December 31, 2016 includes deferred taxes, net amounting to NIS 1,004 million (excludes deferred taxes with respect to securities, which do not affect the provision for taxes). An increase of 1% in tax rates would cause a decrease of NIS 24 million in the provision for taxes.

Controls and Procedures

In accordance with the Public Reporting Directives of the Supervisor of Banks, based on requirements stipulated in Sections 302 and 404 of the American Sarbanes Oxley Act, the Bank President & CEO and the Chief Accountant of the Bank have each separately signed a Certification attached to the financial statements on "Disclosure Controls and Procedures ("Disclosure Certification").

The Disclosure Certification relates to the controls and procedures that were designed to assure that the information that the Bank requires for disclosure in accordance with the Public Reporting Regulations of the Supervisor of Banks, is accumulated, processed and sent to the Bank's Executive Management in a manner that enables decisions to be reached at an appropriate time, with respect to disclosure requirements. The certification also refers to setting of internal controls over financial reporting intended to provide a reasonable degree of certainty with regard to the reliability of financial reporting and to the fact that the financial statements for external use are prepared in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks.

Controls and procedures with regard to disclosure

At the end of the period covered by this Report, the Bank's management, together with the Bank President & CEO and the Chief Accountant of the Bank, evaluated the effectiveness of the Bank's disclosure controls and procedures. Based on this evaluation, the Bank President & CEO and Chief Accountant of the Bank concluded that at the end of this period, the disclosure controls and procedures are effective for recording, processing, summarizing and reporting the information that the Bank is required to disclose in the annual report, in accordance with the Public Reporting Directives of the Supervisor of Banks, on the date stipulated in these Directives.

Developments in internal control

In the quarter ended December 31, 2016, no change occurred in the Bank's internal controls over financial reporting that had a material effect, or can reasonably be expected to have an effect on the Bank's internal controls over financial reporting.

In accordance with the directive by the Supervisor of Banks with regard to adoption of provisions of Section 404 of the Sarbanes-Oxley Act, starting with financial statements as of December 31, 2008, this report includes a declaration concerning the responsibility of management and the Board of Directors for setting and maintaining proper internal controls over financial reporting and management's assessment of the effectiveness of internal controls over financial reporting as of the date of the financial statements. Concurrently, the opinion of the Bank's independent auditors with regard to appropriateness of the Bank's internal controls over financial reporting in accordance with the applicable standards of the Public Company Accounting Oversight Board (PCAOB) is also provided.

Moshe Vidman	**Eldad Fresher**
Chairman of the Board of Directors	President & CEO

Approval date:
Ramat Gan
March 20, 2017

Certification

I, ELDAD FRESHER, certify that:

1. I have reviewed the annual report of Bank Mizrahi Tefahot Ltd. ("the Bank") for 2016 ("the Report").
2. Based on my knowledge, this Report does not contain any untrue statement of a material fact nor omit to state any material fact necessary so that the statements included therein, in light of the circumstances under which such statements were made, would not be misleading with respect to the period covered by the Report.
3. Based on my knowledge, the financial statements and other financial information included in the Report fairly present, in all material respects, the financial condition, results of operations, and changes in shareholders' equity and cash flows of the Bank as of the dates and for the periods presented in this Report.
4. I and others at the Bank who provide this certification, are responsible for determining and maintaining controls and procedures with regard to disclosure(1) and to the Bank's internal controls over financial reporting(1) as well as:

A. We have determined such controls and procedures, or caused these controls and procedures to be determined under our supervision, for the purpose of ensuring that material information relating to the Bank, including its subsidiaries, is made known to us by others in the Bank and in those entities, particularly during the period in which the Report is being prepared;

B. We have set such internal controls over financial reporting, or had them set under our supervision, intended to provide a reasonable degree of certainty with regard to the reliability of financial reporting and to the fact that the financial statements for external use are prepared in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks.

C. We have evaluated the effectiveness of the Bank's disclosure controls and procedures and have presented in this report our conclusions about the effectiveness of the disclosure controls and procedures in this Report, as of the end of the period covered by this Report based on our evaluation; and

D. We have disclosed in this Report any change in the Bank's internal controls over financial reporting that occurred during the fourth quarter, that has materially affected, or is reasonably likely to materially affect, the Bank's internal controls over financial reporting; and

5. I and others in the Bank who are declaring this certification, have disclosed, based on our most recent evaluation of the internal controls over financial reporting, to the Bank's independent auditors, the Board of Directors and the Audit Committee of the Board of Directors of the Bank:

A. All significant deficiencies and material weaknesses in the determination or operation of internal controls over financial reporting which are reasonably likely to impair the Bank's ability to record, process, summarize and report financial information; and

B. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank's internal controls over financial reporting.

The aforesaid does not derogate from my responsibility or the responsibility of any other person according to the law.

Eldad Fresher
President & CEO

Ramat Gan,
March 20, 2017

(1) As defined in Public Reporting Directives with regard to "Report of the Board of Directors and Management".

Certification

I, MENAHEM AVIV, certify that:

1. I have reviewed the annual report of Bank Mizrahi Tefahot Ltd. (“the Bank”) for 2016 (“the Report”).
2. Based on my knowledge, this Report does not contain any untrue statement of a material fact nor omit to state any material fact necessary so that the statements included therein, in light of the circumstances under which such statements were made, would not be misleading with respect to the period covered by the Report.
3. Based on my knowledge, the financial statements and other financial information included in the Report fairly present, in all material respects, the financial condition, results of operations, and changes in shareholders’ equity and cash flows of the Bank as of and for the periods presented in this Report.
4. I and others at the Bank who provide this certification, are responsible for determining and maintaining controls and procedures with regard to disclosure[(1)] and to the Bank's internal controls over financial reporting[(1)] as well as:

A. We have determined such controls and procedures, or caused these controls and procedures to be determined under our supervision, for the purpose of ensuring that material information relating to the Bank, including its subsidiaries, is made known to us by others in the Bank and in those entities, particularly during the period in which the Report is being prepared;

B. We have set such internal controls over financial reporting, or had them set under our supervision, intended to provide a reasonable degree of certainty with regard to the reliability of financial reporting and to the fact that the financial statements for external use are prepared in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks.

C. We have evaluated the effectiveness of the Bank’s disclosure controls and procedures and have presented in this report our conclusions about the effectiveness of the disclosure controls and procedures in this Report, as of the end of the period covered by this Report based on our evaluation; and

D. We have disclosed in this Report any change in the Bank’s internal controls over financial reporting that occurred during the fourth quarter, that has materially affected, or is reasonably likely to materially affect, the Bank’s internal controls over financial reporting; and

5. I and others in the Bank who are declaring this certification, have disclosed, based on our most recent evaluation of the internal controls over financial reporting, to the Bank’s independent auditors, the Board of Directors and the Audit Committee of the Board of Directors of the Bank:

A. All significant deficiencies and material weaknesses in the determination or operation of internal controls over financial reporting which are reasonably likely to impair the Bank’s ability to record, process, summarize and report financial information; and

B. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank’s internal controls over financial reporting.

The aforesaid does not derogate from my responsibility or the responsibility of any other person according to the law.

Menahem Aviv
Vice-president,
Chief Accountant

Ramat Gan,
March 20, 2017

(1) As defined in Public Reporting Directives with regard to "Report of the Board of Directors and Management".

Report of the Board of Directors and Management as to Internal Controls over Financial Reporting

The Board of Directors and Management of Mizrahi Tefahot Bank Ltd. (hereinafter: "the Bank") are responsible for establishing and maintaining proper internal controls over financial reporting (as defined in Public Reporting Directives with regard to "Report of the Board of Directors and Management"). The Bank's internal controls system has been designed to provide the Bank's Board of Directors and management a reasonable degree of certainty as to proper preparation and presentation of financial statements published in accordance with generally accepted accounting principles and with directives and guidelines of the Supervisor of Banks. Regardless of the quality of the design there of, all internal controls systems have inherent limitations. Therefore, even should it be determined that these systems are effective, they may only provide a reasonable degree of certainty with regard to preparation and presentation of financial statements.

The management, under supervision of the Board of Directors, maintains a comprehensive system of controls intended to ensure that transactions are executed in line with management authorization, that assets are protected, and that accounting records are reliable. Furthermore, management under supervision of the Board of Directors, takes steps to ensure that information and communication channels are effective and monitor execution, including execution of internal control procedures.

The Bank's management, under supervision of the Board of Directors, has evaluated the effectiveness of the Bank's internal controls system over financial reporting as of December 31, 2016 based on criteria stipulated in the internal control model of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on the aforementioned evaluation, management believes that as of December 31, 2016, the Bank's internal controls over financial reporting are effective.

The effectiveness of the Bank's internal controls over financial reporting as of December 31, 2016 was audited by the Bank's independent auditors, Brightman Almagor Zohar & Co. as noted in their report, . 151 בעמוד, which includes their unqualified opinion as to the effectiveness of the Bank's internal controls over financial reporting as of December 31, 2016.

Moshe Vidman	**Eldad Fresher**	**Menahem Aviv**
Chairman of the Board of Directors	President & CEO	Vice-president, Chief Accountant

Approval date:
Ramat Gan, March 20, 2017

Deloitte.

Independent Auditors' Report to Shareholders of Bank Mizrahi-Tefahot Limited Pursuant to Public Reporting Directives of the Supervisor of Banks Concerning Internal Controls over financial Reporting

We have audited the internal controls over financial reporting at Bank Mizrahi-Tefahot Ltd. and subsidiaries (hereinafter jointly: "the Bank") as of December 31, 2016 based on criteria set forth under the integrated framework for internal control (1992) published by the Committee of Sponsoring Organizations of the Tread way Commission ("COSO"). The Bank's Board of Directors and management are responsible for maintaining effective internal controls over financial reporting, and for evaluating the effectiveness of said internal controls over financial reporting which is included in the attached report of the Board of Directors and management with regard to internal controls over financial reporting, enclosed herewith. We are responsible for our opinion on the Bank's internal controls over financial reporting, based on our audit.

We have not audited the effectiveness of internal controls over financial reporting at subsidiaries whose assets and whose net interest revenues before provision for credit losses included in consolidation account for 6.31% and 9.53%, respectively of the related amounts on the consolidated financial statements as of December 31, 2016 and for the year then ended. The effectiveness of internal controls over financial reporting at these companies was audited by other independent auditors whose reports have been provided to us and our opinion, in as much as it refers to effectiveness of internal controls over financial reporting at these companies, Is based on the reports of these other independent auditors.

We have conducted our audit in accordance with standards of the Public Company Accounting Oversight Board (PCAOB) in the USA with regard to audit of internal controls over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel. In accordance with these standards, we are required to plan and perform the audit and obtain a reasonable degree of assurance as to the maintenance of effective internal controls over financial reporting, in all material aspects. Our audit included: obtaining an understanding of the internal controls over financial reporting, assessing the risk of existence of a material weakness, and also testing and evaluating of the design and operating effectiveness of internal controls based on the assessed risk. Our audit also included performing such other procedures which we considered necessary under the circumstances. We believe that our audits and the reports of the other independent auditors provide a reasonable basis for our opinion.

A bank's internal controls over financial reporting is a process designed to provide a reasonable degree of certainty as to the reliability of financial reporting and preparation of financial statements for external use in accordance with Israeli GAAP, directives and guidelines of the Supervisor of Banks. A bank's internal controls over financial reporting include policies and procedures which: (1) refer to record keeping which, with reasonable detail, accurately and properly reflects transactions and transfers of Bank assets (including their removal from Bank ownership); (2) provide a reasonable degree of certainty that transactions are properly recorded so as to allow for preparation of financial statements in accordance with Israeli GAAP and directives and guidelines of the Supervisor of Banks, and that the Bank's receipts and expenditures are made exclusively in line with authorizations of the Bank's management and Board members; and (3) provide a reasonable degree of certainty with regard to avoidance or timely discovery of any unauthorized acquisition, use or transfer of Bank assets (including removal from Bank ownership) which may materially impact the financial statements.

Due to structural limitations, internal controls over financial reporting may not prevent or disclose misleading presentation. Also, reaching conclusions about the future on the basis of any current assessment of effectiveness is exposed to the risk that controls will become unsuitable due to changes in circumstances or that the extent of observance of the policies or procedures will change adversely

In our opinion, the Bank maintained, in all material aspects, effective internal controls over financial reporting as of December 31, 2016 based on criteria set forth in the integrated framework for internal controls (1992) published by COSO.

We have also audited, in accordance with generally accepted auditing standards in Israel and certain audit standards whose application to audits of banking corporations was stipulated in directives of and guidance from the Supervisor of Banks, the Bank's consolidated balance sheet as of December 31, 2016 and 2015 and the consolidated statements of profit and loss, consolidated statements of comprehensive income, consolidated statements of changes to equity and consolidates statements of cash flows for each of the three years ended December 31, 2016, and our report dated March 20, 2017 includes an unqualified opinion on the aforementioned financial statements, based upon our audit and on the reports of other independent auditors, as well as a referral with regard to claims filed against the Bank, including requests to recognize them as class actions, status with regard to the US Department of Justice investigation concerning Bank Group business with its US clients.

Brightman Almagor Zohar & Co.
Certified Public Accountants
Brightman Almagor Zohar & Co.
Ramat Gan, March 20, 2017

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Deloitte.

Independent Auditors' Report to Shareholders of Bank Mizrahi-Tefahot Limited

We have audited the accompanying consolidated balance sheets of Mizrahi Tefahot Limited and its subsidiaries ("the Bank") as of December 31, 2016 and 2015, and the statements of profit and loss, consolidated statements of comprehensive income, consolidated statements of changes to equity and consolidated statements of cash flows – for each of the three years in the period ended December 31, 2016. The Bank Board of Directors and management are responsible for these financial statements. Our responsibility is to express an opinion of these financial statements based on our audit.

We have not audited the financial statements of subsidiaries whose assets included in consolidation account for 6.31% and 6.87% of total consolidated assets as of December 31, 2016 and 2015, respectively and whose net interest revenues before expenses with respect to credit losses, included on the consolidated statements of profit and loss, account for 9.53%, 8.46% and 8.74%, respectively of total consolidated net interest revenues before expenses with respect to credit losses for the years ended December 31, 2015, 2015 and 2014, respectively. Furthermore, we have not audited the financial statements of an associate, the investment in which amounts to NIS 19 million as of December 31, 2016 and 2015. The financial statements of this company were audited by another auditor, whose reports were furnished to us, and our opinion, insofar as it relates to amounts included with respect to these companies, is based on the reports of the other auditor.

We conducted our audits in accordance with generally accepted auditing standards in Israel, including those prescribed by the Auditors' Regulations (Mode of Performance), 1973 and certain auditing standards, the application of which was mandated by the directives of the Supervisor of Banks. These regulations require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditor provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditor, the above financial statements present fairly, in all material respects, the financial position of the Bank – as of December 31, 2016 and 2015, and the results of operations, changes in shareholders' equity and cash flows of the Bank – for each of the three years in the period ended December 31, 2016, in conformity with generally accepted accounting principles in Israel (Israeli GAAP). Moreover, in our opinion the aforementioned financial statements have been prepared in accordance with the directives and guidelines of the Supervisor of Banks.

Without qualifying our aforementioned opinion, we draw your attention to:

A. Note 26.C. section 11(A-G) with regard to lawsuits filed against the Bank and its subsidiary, including requests to recognize them as class actions

B. Note 26.C. Section 12 with regard to an investigation by the US Department of Justice concerning Bank Group business with its US clients.

We have also audited in accordance with PCAOB standards in the USA (Public Company Accounting Oversight Board) with regard to audit of internal controls over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel, the internal controls of the Bank over financial reporting as of December 31, 2016, based on criteria specified in the integrated framework for internal control published by COSO (the Committee of Sponsoring Organizations Commission of the Treadway), and our report dated March 20, 2017 included an unqualified opinion on the effectiveness of internal controls over financial reporting at the Bank.

Brightman Almagor Zohar & Co.
Certified Public Accountants

Brightman Almagor Zohar & Co.

Ramat Gan, March 20, 2017

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Annual financial statements

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Consolidated statement of profit and loss

For the year ended December 31,

Reported amounts (NIS in millions)

	Note	2016	2015	2014
Interest revenues	2	5,311	4,906	5,347
Interest expenses	2	1,533	1,372	1,972
Interest revenues, net		3,778	3,534	3,375
Expenses with respect to credit losses	13,30	200	211	173
Interest revenues, net after expenses with respect to credit losses		3,578	3,323	3,202
Non-interest revenues				
Non-interest financing revenues	3	295	358	173
Fees	4	1,433	1,426	1,395
Other revenues	5	134	74	44
Total non-interest revenues		1,862	1,858	1,612
Operating and other expenses				
Payroll and associated expenses	6	2,071	1,944	1,866
Maintenance and depreciation of buildings and equipment	16	693	692	715
Other expenses	7	535	590	458
Total operating and other expenses		3,299	3,226	3,039
Pre-tax profit		2,141	1,955	1,775
Provision for taxes on profit	8	833	761	657
After-tax profit		1,308	1,194	1,118
Share in profits of associates, after tax	15	–	–	5
Net profit:				
Before attribution to non-controlling interests		1,308	1,194	1,123
Attributable to non-controlling interests		(42)	(60)	(31)
Attributable to shareholders of the Bank		1,266	1,134	1,092

Moshe Vidman
Chairman of the Board of Directors

Eldad Fresher
President & CEO

Menahem Aviv
Vice-president, Chief Accountant

Approval date:
Ramat Gan, March 20, 2017

Consolidated statement of profit and loss – Continued

For the year ended December 31,

(Reported amounts)

	Note	2016	2015	2014
Earnings per share[1]	9			
Basic earnings per share (in NIS)				
Net profit attributable to shareholders of the Bank		5.46	4.90	4.74
Diluted earnings per share (in NIS)				
Net profit attributable to shareholders of the Bank		5.46	4.89	4.71

(1) Share of NIS 0.1 par value each.

The accompanying notes are an integral part of the financial statements.

Consolidated statement of comprehensive income

For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
Net profit:			
Before attribution to non-controlling interests	1,308	1,194	1,123
Attributable to non-controlling interests	(42)	(60)	(31)
Net profit attributable to shareholders of the Bank	1,266	1,134	1,092
Other comprehensive income (loss) before taxes			
Adjustments for presentation of available-for-sale securities at fair value, net	(26)	(27)	(10)
Adjustments from translation of financial statements of investments in associates[1]	1	(1)	6
Net gains (losses) with respect to cash flows hedging	(9)	(6)	23
Adjustment of liabilities with respect to employee benefits[2]	[3] (294)	(3)	(46)
Total other comprehensive income (loss), before tax	(328)	(37)	(27)
Related tax effect	108	13	10
Other comprehensive income (loss) after taxes[4]			
Other comprehensive income (loss), before attribution to non-controlling interest	(220)	(24)	(17)
Less other comprehensive income (loss) attributable to non-controlling interest	–	(1)	2
Other comprehensive income (loss) attributable to equity holders of the Bank, after taxes	(220)	(25)	(15)
Comprehensive income:			
Before attribution to non-controlling interests	1,088	1,170	1,106
Attributable to non-controlling interests	(42)	(61)	(29)
Comprehensive income attributable to shareholders of the Bank	1,046	1,109	1,077

(1) Adjustments from translation of financial statements of associates.
(2) Includes adjustments with respect to actuarial estimates included in the reported period for defined-benefit pension plans and current amortization of adjustments with respect to liabilities to profit and loss.
(3) Includes the cost of update to the actuarial liability with respect to the streamlining plan, amounting to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity.
(4) For details see Note 10 to the financial statements – Cumulative Other Comprehensive Income (Loss).

The accompanying notes are an integral part of the financial statements.

Consolidated balance sheet

As of December 31

Reported amounts (NIS in millions)

	Note	2016	2015
Assets			
Cash and deposits with banks	11	41,725	30,489
Securities[2][1]	12	10,262	11,845
Securities loaned or purchased in resale agreements	27	9	71
Loans to the public	13,30	172,779	160,604
Provision for credit losses	13,30	(1,438)	(1,400)
Loans to the public, net		171,341	159,204
Loans to Governments	14	330	316
Investments in associates	15	34	36
Buildings and equipment	16	1,585	1,583
Intangible assets and goodwill	15.D	87	87
Assets with respect to derivative instruments	28	3,584	3,527
Other assets	17	1,498	2,000
Total assets		230,455	209,158
Liabilities and Equity			
Deposits from the public	18	178,252	162,380
Deposits from banks	19	1,537	1,166
Deposits from the Government		50	58
Debentures and subordinated notes	20	27,034	23,719
Liabilities with respect to derivative instruments	28	3,566	3,634
Other liabilities[3]	30.E, 21	6,692	5,786
Total liabilities		217,131	196,743
Shareholders' equity attributable to shareholders of the Bank		12,714	11,847
Non-controlling interests		610	568
Total equity	**24**	13,324	12,415
Total liabilities and equity		230,455	209,158

(1) Includes: NIS 6,928 million at fair value (December 31, 2015: NIS 8,429 million).
(2) For more information with regard to securities pledged to lenders, see Note 27 to the financial statements.
(3) Includes: Provision for credit losses with respect to off balance sheet credit instruments amounting to NIS 109 million (on December 31, 2015: NIS 106 million).

The accompanying notes are an integral part of the financial statements.

Statement of Changes in Shareholders' Equity

For the year ended December 31,

Reported amounts (NIS in millions)

	Share capital and premium[1]	Capital reserve from benefit from share-based payment transactions	Treasury shares	Total paid-up share capital and capital reserves
Balance as of December 31, 2013	2,108	116	(76)	2,148
Net profit for the period	-	–	–	–
Benefit from share-based payment transactions	-	40	–	40
Related tax effect	–	(1)	–	(1)
Realization of share-based payment transactions[2]	89	(89)	–	–
Other comprehensive income (loss), net, after tax	–	–	–	–
Balance as of December 31, 2014	2,197	66	(76)	2,187
Net profit for the period	–	–	–	–
Dividends paid[6]	–	–	–	–
Benefit from share-based payment transactions	–	20	–	20
Related tax effect	–	7	–	7
Realization of share-based payment transactions[2]	25	(25)	–	–
Other comprehensive income (loss), net, after tax	–	–	–	–
Balance as of December 31, 2015	2,222	68	(76)	2,214
Net profit for the period	–	–	–	–
Dividends paid[6]	–	–	–	–
Benefit from share-based payment transactions	–	8	–	8
Related tax effect	–	(1)	–	(1)
Realization of share-based payment transactions[2]	17	(17)	–	–
Other comprehensive income (loss), net, after tax	–	–	–	–
Balance as of December 31, 2016	2,239	58	(76)	2,221

(1) Share premium generated prior to March 31, 1986.

(2) In 2016, the Bank issued 157,119 ordinary shares of NIS 0.1 par value each, for exercise of options pursuant to the Employee Stock Option Plan, and issued to the President 31,065 ordinary shares of NIS 0.1 par value each.
In 2015, the Bank issued 1,086,264 ordinary shares of NIS 0.1 par value each, for exercise of options pursuant to the Employee Stock Option Plan, and issued to the President 74,647 ordinary shares of NIS 0.1 par value each.
In 2014, the Bank issued 1,240,933 ordinary shares of NIS 0.1 par value each, for exercise of options in conjunction with the Employee Stock Option Plan.

(3) For details see Note 10 – Cumulative Other Comprehensive Income (Loss).

(4) Includes the cost of update to the actuarial liability with respect to the streamlining plan, amounting to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity.

(5) For more information about various limitations on dividend distributions, see Note 24 to the financial statements.

(6) On March 21, 2016, June 21, 2016, September 11, 2016 and November 14, 2016, the Bank paid dividends amounting to NIS 36.0, 43.2, 51.0 and 56.0 million, respectively, in conformity with a decision by the Bank/s Board of Directors.
On March 20, 2017, after the balance sheet date, the Bank's Board of Directors resolved to distribute dividends amounting to NIS 39.8 million, or 15% of earnings in the fourth quarter of 2016. According to accounting rules, this amount will be deducted from retained earnings in the first quarter of 2017.

The accompanying notes are an integral part of the financial statements.

Cumulative other comprehensive income (loss)[3]	Retained earnings[5]	Total shareholder equity	Non-controlling interests	Total equity
(57)	7,590	9,681	478	10,159
–	1,092	1,092	31	1,123
–	–	40	–	40
–	–	(1)	–	(1)
–	–	–	–	–
(15)	–	(15)	(2)	(17)
(72)	8,682	10,797	507	11,304
–	1,134	1,134	60	1,194
–	(86)	(86)	–	(86)
–	–	20	–	20
–	–	7	–	7
–	–	–	–	–
(25)	–	(25)	1	(24)
(97)	9,730	11,847	568	12,415
–	1,266	1,266	42	1,308
–	(186)	(186)	–	(186)
–	–	8	–	8
–	–	(1)	–	(1)
–	–	–	–	–
(220)[4]	–	(220)		(220)
(317)	10,810	12,714	610	13,324

Statement of cash flows – consolidated

For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
Cash flows provided by current operations			
Net profit	1,308	1,194	1,123
Adjustments			
Share of the Bank in un-distributed earnings of associates	–	–	(5)
Depreciation of buildings and equipment	223	223	246
Expenses with respect to credit losses	200	211	173
Gain from sale of securities available for sale	(58)	(118)	(110)
Gain from sale of securities held to maturity(1)	–	(67)	–
Impairment of securities held for sale	–	–	2
Realized and unrealized loss (gain) from adjustment to fair value of securities held for trading	(14)	5	(4)
Gain from sale of buildings and equipment	(92)	(36)	(10)
Expenses arising from share-based payment transactions	8	20	40
Deferred taxes, net	(3)	27	21
Change in employee provisions and liabilities	307	(10)	(21)
Effect of changes in exchange rate on cash balances	195	183	(545)
Proceeds from sale of loan portfolios	(45)	(1)	–
Net change in current assets			
Deposits with banks	(50)	2,967	346
Loans to the public	(14,935)	(12,453)	(9,177)
Loans to Governments	(14)	(9)	(2)
Securities loaned or purchased in resale agreements	62	36	(37)
Assets with respect to derivative instruments	(66)	2,069	(1,973)
Securities held for trade	(112)	807	522
Other assets, net	613	191	90
Net change in current liabilities			
Deposits from banks	371	(92)	(783)
Deposits from the public	15,872	10,001	11,135
Deposits from the Government	(8)	3	(7)
Securities loaned or sold in conjunction with repurchase agreements	–	(223)	223
Liabilities with respect to derivative instruments	(68)	(2,863)	2,959
Other liabilities	273	(464)	123
Accrual differences included with investment and financing operations	107	(399)	(181)
Net cash provided by current operations	4,074	1,202	4,148

(1) Proceeds from sale of debentures held to maturity at Bank Yahav.

The accompanying notes are an integral part of the financial statements.

Statement of cash flows – consolidated – continued

For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
Cash flows provided by investment operations			
Acquisition of debentures held to maturity	–	–	(3,477)
Proceeds from sale of debentures held to maturity(1)	–	1,917	–
Acquisition of securities available for sale	(6,902)	(10,497)	(12,930)
Proceeds from sale of securities available for sale	7,546	9,603	8,658
Proceeds from redemption of securities available for sale	1,083	761	153
Proceeds from sale of loan portfolios	2,662	590	–
Acquisition of buildings and equipment	(245)	(233)	(286)
Proceeds from sale of buildings and equipment	125	55	21
Proceeds from realized investment in associates	2	15	17
Net cash provided by investment operations	4,271	2,211	(7,844)
Cash flows provided by financing operations			
Issuance of debentures and subordinated notes	6,318	7,502	5,809
Redemption of debentures and subordinated notes	(3,096)	(3,988)	(1,574)
Dividends paid to shareholders	(186)	(86)	–
Net cash provided by financing operations	3,036	3,428	4,235
Increase (decrease) in cash	11,381	6,841	539
Cash balance at beginning of year	30,309	23,651	25,105
Effect of changes in exchange rate on cash balances	(195)	(183)	545
Cash balance at end of year	41,495	30,309	26,189
Interest and taxes paid / received			
Interest received	5,204	5,080	5,929
Interest paid	1,676	1,591	1,760
Dividends received	35	10	8
Taxes on income received	81	69	80
Taxes on income paid	800	738	800
Appendix A – Non-cash Transactions			
Acquisition of buildings and equipment	13	22	10

(1) Proceeds from sale of debentures held to maturity at Bank Yahav.

Notes to financial statements as of December 31, 2016

Note 1 – Reporting Principles and Accounting Policies

A. Overview

1) The Bank's Board of Directors authorized publication of these consolidated financial statements on March 20, 2017.

2) The Bank's financial statements are prepared in conformity with generally accepted accounting policies in Israel (Israeli GAAP) and in accordance with Public Reporting Directives of the Supervisor of Banks.
For most topics, these directives are based on generally acceptable accounting practices by US banks. For other, less material topics, these directives are based on International Financial Reporting Standards (IFRS) and on generally accepted accounting principles in Israel (Israeli GAAP). When International Financial Reporting Standards (IFRS) allow multiple alternatives, or do not specifically refer to a certain situation, these directives prescribe specific implementation guidelines, mostly based on generally acceptable accounting practices by US banks.

3) In conformity with the Supervisor of Banks' Public Reporting Directives, the Bank may – under certain circumstances listed in the regulations – present annual financial statements on consolidated basis only.
On February 12, the Supervisor of Banks allowed the Bank to present its annual financial statements on a consolidated basis only.
For more information about the condensed financial statements of the Bank solo, including balance sheet, statement of profit and loss and statement of cash flows, see Note 36 to the financial statements.
Data for the Bank solo is available on the Bank website:
www.mizrahi-tefahot.co.il >> about the bank >> investor relations >> financial statements.

4) Definitions

"Generally accepted accounting principles"	Accounting rules which US banks traded in the USA are required to apply. These principles are specified by banking supervisory authorities in the USA, the US SEC, the US Financial Accounting Standards Board and other US entities; they are applied in conformity with the hierarchy specified in (ASC 105) FAS 168 – Codification of accounting standards of the US Financial Accounting Standards Board and US GAAP hierarchy. In addition, as stipulated by the Supervisor of Banks, notwithstanding the hierarchy specified in FAS 168, it has been clarified that any position made public by US banking supervision authorities or by the team thereof, with regard to application of generally accepted accounting principles in the USA, is a Generally Accepted Accounting Principle for Banks in the USA.
"International Financial Reporting Standards"	Standards and interpretations adopted by the International Accounting Standards Board (hereinafter: "IASB"), which include international financial reporting standards (hereinafter: "IFRS") and International Accounting Standards (hereinafter: "IAS"), including interpretations of these standards by the International Financial Reporting Interpretations Committee (IFRIC) or interpretations by the Standing Interpretations Committee (SIC), respectively.
"FASB"	Financial Accounting Standards Board in the USA.
"The Bank"	Mizrahi-Tefahot Bank Ltd.
"Subsidiaries"	entities whose financial statements are fully consolidated with those of the Bank, directly or indirectly.
"Bank Group"	The Bank and its subsidiaries.

Note 1 – Reporting Principles and Accounting Policies – continued

"Associates"	Entities in which the Group has material influence over financial and operational policies, but over which it has no control. Investment in associates is included in the financial statements using the equity method.
"Investees"	Subsidiaries and associates.
"Overseas affiliates"	Representatives, branches or subsidiaries of the Bank outside Israel.
"Functional currency"	The currency in the primary economic environment in which the Bank operates. This is typically the currency of the environment in which the corporation generates and expends most of its cash.
"Presentation currency"	The currency in which the financial statements are presented.
"Adjusted amount"	Historical nominal amount, adjusted for changes in the economic purchase power of Israeli currency.
"Reported amount"	An amount adjusted as of December 31, 2003 (hereinafter: "the transition date"), plus amounts in nominal values that were added after the transition date, minus amounts deducted after the transition date.
"Cost"	Cost in reported amount.
"Related parties" and "Interested parties"	As defined in Section 80 of the Public Reporting Regulations.

B. Preparation basis of the financial statements

1) Principles of financial reporting

The Bank's financial statements are prepared in conformity with generally accepted accounting policies in Israel (Israeli GAAP) and in accordance with Public Reporting Directives of the Supervisor of Banks. See above in section A.

2) Functional currency and reporting currency

The consolidated financial statements are presented in NIS, which is the Bank's functional currency, rounded to the nearest one million, unless otherwise indicated. NIS is the currency which reflects the primary economic environment in which the Bank does business. For information about the functional currency of overseas banking affiliates, see section 1.D. below.

3) Measurement basis

The financial statements were prepared based on historical cost, except for the following items:

- Financial derivatives and other financial instruments measured at fair value on the statement of profit and loss (such as: investments in securities in the held-for-trade portfolio or instruments for which the fair value option was selected);
- Financial instruments classified as available for sale;
- Share-based payments;
- Non-current assets held for sale and asset group held for sale;
- Deferred tax assets and liabilities
- Various provisions, such as provisions for credit losses and provision for legal claims;
- Assets and liabilities with respect to employee benefits;
- Investments in associates.

The value of non-monetary assets and capital items measured based on historical cost was adjusted for changes in the Consumer Price Index through December 31, 2003. Through this date, the Israeli economy was considered a hyper-inflationary economy. As from January 1, 2004, the Bank prepares its financial statements in reported amounts.

4) Use of estimates

In preparing the consolidated financial statements in accordance with Israeli GAAP and with directives and guidelines of the Supervisor of Banks, Bank management is required to use judgment, assessments, estimates and assumptions which impact policies implementation and amounts of assets and liabilities, revenues and expenses. Note that actual results may differ from these estimates.

When making accounting estimates during preparation of the financial statements, Bank management is required to make assumptions with regard to circumstances and events involving significant uncertainty. In exercising its judgment when making these estimates, Bank management relies on past experience, various facts, external factors and reasonable assumptions in accordance with the appropriate circumstances for each estimate.

These estimates and assumptions are regularly reviewed, and changes to accounting estimates are recognized in the period in which these estimates were revised and in any affected future period.

5) Change to estimates

- For more information about the Supervisor of Banks' directive with regard to group provision for credit losses, see section C. 4) below.
- The Bank has revised the underlying assumptions of actuarial estimates with regard to liabilities with respect to employee rights. For more information about the streamlining plan and revised assumptions, see section D. 13) below and Note 22 to the financial statements.

C. Initial application of accounting standards, accounting standard updates and directives of the Supervisor of Banks

As from reporting periods starting on January 1, 2016 (unless otherwise noted), the Bank initially applies the following new accounting standards and directives:

1. Supervisory operating segments and reporting of operating segments in conformity with management approach.
2. Application of US GAAP with regard to business combinations, consolidation of financial statements and investment in investees.
3. Application of US GAAP with regard to intangible assets.
4. Supervisor of Banks' directive on group-based provision for credit losses.
5. Restructuring of troubled debt.

Below is a description of the substance of changes in accounting policies on the consolidated financial statements and description of the effect of their initial application, if any:

1) Supervisory operating segments and reporting of operating segments in conformity with management approach

Supervisory operating segments

On November 3, 2014, the Supervisor of Banks issued a circular which includes changes to the Public Reporting Directives with regard to supervisory operating segments, as well as a Q&A file on this topic. The circular revised the Public Reporting Directives with regard to required reporting of supervisory operating segments and modified certain definitions and directives, whereby banks are required to classify clients into supervisory segments.

Note 1 – Reporting Principles and Accounting Policies – continued

The major changes to the Public Reporting Directives according to this Q&A file are as follows:

- Added was a requirement for disclosure of "supervisory operating segments", based on definitions by the Supervisor of Banks. The disclosure layout includes the following segments: private banking, households, very small and small business, mid-size business, large business, institutional entities and financial management.
- Additional definitions clarify which clients are to be included in each segment.
- An additional requirement stipulates separate disclosure of the "Financial management" segment.
- It has been clarified that a banking corporation where, according to its management approach, the operating segments differ materially from the supervisory operating segments – should also provide disclosure of the operating segments based on its management approach.
- It has been clarified that the disclosure requirements in the Board of Directors' report and in the interim directive with regard to "Description of the banking corporation's business and forward-looking information in the Board of Directors' report" shall refer to disclosure of supervisory operating segments.

On September 10, 2015, the Supervisor of Banks issued an updated Q&A file, which includes certain relief with regard to client categorization by operating segments based on the volume of their revenues – when this data is not typical or is unavailable to the Bank. According to the Q&A file, in such cases the Bank may categorize clients into operating segments based on other parameters, in line with total client indebtedness. Thus, in some cases listed in the Q&A file, clients may be categorized based on the number of employees or total assets on their balance sheet. If this information is not available either, clients may be categorized, in such cases, based on their total financial assets with the bank, multiplied by a specified factor.

Operating segments in conformity with management approach.

In addition to uniform reporting by supervisory operating segments, the circular stipulates that disclosure of "Operating segments in conformity with management approach" should be provided in conformity with generally acceptable accounting practices by US banks with regard to operating segments (included in ASC 280), if there is a material difference between management approach and supervisory reportable segments.
An operating segment in conformity with management approach pursuant to ASC 280-10 is a Bank component with operations which may derive revenues and incur expenses which meet the following criteria:

- Its operating results are regularly reviewed by chief decision makers at the Bank for the purpose of making decisions about resource allocation and performance evaluation, and
- Separate financial information is available with regard to it.

In fact, there is a correlation between supervisory operating segments and "operating segments in conformity with management approach" but nevertheless, there are some differences in client attribution to segments and in decision making. Therefore, the financial statements also include reporting of operating results in conformity with "management approach", as noted above.
For more information about criteria for client classification into supervisory segments and into segments in conformity with management approach and for differences between them and additional extensive segment information, see Note 29 to the financial statements.

Note 1 – Reporting Principles and Accounting Policies – continued

Scope

The directives are applicable, with regard to balance sheet data, as from the 2015 financial statements. The other requirements, except for the required detailed disclosure for the financial management segment, apply as from the financial statements for the first quarter of 2016. Provisions of the circular, including the required detailed disclosure for the financial management segment, would apply in full as from the first quarter of 2017. In conformity with the circular, the Bank presents comparative figures for only one year, based on client classification to supervisory operating segments as of January 1, 2016.

2) Application of US GAAP with regard to business combinations, consolidation of financial statements and investment in investees

On June 10, 2015, the Supervisor of Banks issued a circular concerning reporting by banking corporations and credit card companies in Israel in conformity with US GAAP with regard to business combinations, consolidation of financial statements and investment in investees. According to the circular, US GAAP should be applied to these matters as follows:

- Presentation, measurement and disclosure rules stated in provisions of ASC 805 "Business combinations".
- Provisions of ASC 810 "Consolidation".
- Provisions of ASC 350-20 "Intangibles – Goodwill and Other Assets" with regard to accounting treatment of impairment of goodwill acquired in a business combination. According to the directive, should the Bank believe that the fair value is lower than the carrying amount, the carrying amount of the reporting unit, including goodwill should be compared to its fair value. If the fair value is lower than the carrying amount, goodwill impairment would be measured at the excess of the carrying amount over the difference between the fair value of the reporting unit and the fair value of assets and liabilities included in the reporting unit. No loss may be recognized in excess of the carrying amount of goodwill.
- US GAAP with regard to investees, including presentation, measurement and disclosure rules as well as provisions with regard to impairment specified in ASC 323 "Investments – Equity Method and Joint Ventures".

The new provisions cover a variety of topics, including non-material changes to the old provisions on these topics: Recognition of non-controlling interests, subsequent measurement of contingent liabilities, revaluation of assets and liabilities by subsidiaries in a business combination ("Push Down Accounting"), investments held for sale, impairment of investment in associate, transition from cost method to equity method and other topics.

The provisions of the circular would apply as from January 1, 2016. Upon initial application, action should be taken in conformity with transitional provisions included in US GAAP for these issues, *mutatis mutandis*, including retroactive amendment of comparative figures, if required by US GAAP for these issues.

Provisions with regard to Push Down Accounting apply to business combinations made as from January 1, 2016.

Application of this circular has no material impact on the Bank's financial statements.

Note 1 – Reporting Principles and Accounting Policies – continued

3) US GAAP with regard to intangible assets

On October 22, 2015, the Supervisor of Banks issued a circular containing amendments to Public Reporting Directives concerning reporting by banking corporations and credit card companies in Israel, in conformity with US GAAP with regard to intangible assets.

According to this circular, banking corporations are required to adopt US GAAP with regard to intangible assets including the presentation, measurement and disclosure rules specified in provisions of ASC 350 "Intangible assets – Goodwill and other".

In this regard, accounting treatment of goodwill, including review of its impairment, was revised in conformity with the circular dated June 10, 2015 concerning "Reporting by banking corporations and credit card companies in Israel in conformity with US GAAP with regard to business combinations and consolidation of financial statements". ASC 350 also discusses treatment of intangible assets from in-house development, including capitalization of software costs (including treatment of and review for impairment) and revaluation of intangible assets.

According to the directive, intangible assets of un-specified useful life are reviewed if there are indicators of impairment at the Asset Group level. An asset group is the smallest group of assets and liabilities which generates a separate cash flow. First is a review of whether the carrying amount of the asset group is higher than the non-discounted cash flow amount expected there from. If so, impairment is to be recognized equal to the difference between the carrying amount and the fair value of the asset group. Impairment is to be proportionately attributed to assets in the asset group, provided that the value of any individual asset does not drop below its fair value.

Assets of unspecified useful life are reviewed for impairment at least once per year. They are reviewed as to whether the carrying amount of the asset exceeds its fair value. If so, impairment is to be recognized, equal to the difference between the carrying amount and the fair value.

Banks are required to apply the provisions of the Public Reporting Directives in conformity with the circular, as from January 1, 2016.

Application of this circular has no material impact on the Bank's financial statements.

4) Group provision for credit losses

The group-based provision for credit losses is based, *inter alia*, on historical loss rates in various economic sectors, divided into troubled and non-troubled debt.

On February 20, 2017, the Supervisor of Banks issued a circular concerning provision for credit losses, whereby the "range of years" used as a component in determining the group-based provision for credit losses, should continue to include 2011 on the financial statements for 2016 and 2017.

Application of this circular has no material impact on the Bank's financial statements.

5) Re-structuring of troubled debt

On May 22 2016, the Supervisor of Banks issued a circular concerning restructuring of problematic debt. This circular revises the Public Reporting Regulations given update no. 2011-20 to the codification issued by FASB and given new directives by regulators in the USA. These directives include, *inter alia*, clarifications with regard to criteria for award of waivers and for determination whether a debtor is facing financial difficulties, requirements for comprehensive documentation for renewal, extension or changes to debt of borrowers facing financial difficulties and whose debt is classified as inferior, where a decision has been made that they do not constitute restructuring of problematic debt, as well as performance of credit analysis for restructured debt.

Furthermore, they specify that in case of a subsequent restructuring. the banking corporation is no longer required to treat the debt as a restructuring of problematic debt if both of the following conditions are met:

- The debtor is no longer facing financial difficulties upon the date of the subsequent restructuring.
- According to terms of the subsequent restructuring, the banking corporation did not give the debtor any waiver.

In order to meet these conditions, the restructuring agreement is required, *inter alia*, to be at market terms.

The provisions specified in conformity with the circular apply as from December 31, 2016 to any restructuring to be carried out or renewed.

Application of this circular has no material impact on the Bank's financial statements.

For more information see section D. 6) below.

D. Accounting policies applied in preparing the financial statements

1) Foreign currency and linkage:

A. Foreign currency transactions

Foreign currency transactions are translated into the functional currency of the Bank and its affiliates (NIS) using the exchange rate as of the transaction date. Monetary assets and liabilities denominated in foreign currency as of the reporting date are translated into the functional currency at the exchange rate as of that date.

Exchange rate differences with respect to monetary items are the differences between the amortized cost in the functional currency as of the start of the year, adjusted for the effective interest and installments during the year, and the amortized cost in foreign currency, translated at the exchange rate as of the end of the year.

Non-monetary assets and liabilities denominated in foreign currency and measured at fair value, are translated into the functional currency using the exchange rate as of the date on which the fair value is determined. Exchange rate differences arising from translation into the functional currency are recognized in the statement of profit and loss, other than differences arising from translation into the functional currency of cash flow hedges, as well as adjustments to fair value of investments of certain funds accounted for using the equity method, which are recognized in the statement of Other Comprehensive Income.

Non-monetary items denominated in foreign currency and measured at historical cost, are translated at the exchange rate as of the transaction date.

For more information about application of US GAAP with regard to topic 830 of the codification "Foreign currency matters", applicable as from January 1, 2017, see section E. 3) below.

B. Overseas banking affiliates

Pursuant to IAS 21 and to the Supervisor of Banks' circular on this matter, dated February 14, 2012, in order to determine the functional currency of the affiliate, the banking corporation is required to consider, inter alia, the following:

- The currency which primarily affects the selling price of goods and services (usually this would be the currency in which selling prices of goods and services are denominated and settled), and the currency of the country whose competitive forces and regulation primarily determine the selling prices of goods and services.
- The currency which primarily affects labor costs, material and other costs for delivery of goods or services (usually, this would be the currency in which these costs are denominated and settled).

Note 1 – Reporting Principles and Accounting Policies – continued

- Other factors which may serve as evidence of the entity's functional currency, such as: The currency in which monetary resources are generated by financing operations, and the currency in which receipts from current operations are usually kept.
- Relations of the affiliate with the Bank – is the foreign operation significantly independent, do transactions between the affiliate and the Bank constitute a large or small percentage of the foreign operation, do cash flows from the foreign operation directly affect the cash flows of the Bank and are readily available to be transferred to it, and are cash flows from the foreign operation sufficient to fund its current and anticipated liabilities in the normal course of business of the entity, without resources being provided by the Bank.
- Does the affiliate recruit clients on an autonomous basis and is affiliate business with Bank clients (not recruited by the affiliate) not significant.
- Affiliate operations with the Bank, such as asset and liability balances or revenues and expenses, are not significant.
- Affiliate operations are essentially independent, stand alone and are not an extension of or complementary to the Group's domestic operations. Furthermore, the affiliate conducts its operations with significant autonomy.

Based on review of these criteria, the Bank treats its overseas banking affiliates as operations whose functional currency is the same as the Bank's (NIS).

Assets and Liabilities linked to the CPI which are not measured at fair value, are included based on the linkage terms specified for each balance.

Below is information about major official exchange rates, the Consumer Price Index and changes there to:

	As of December 31			Change in %		
	2016	2015	2014	2016	2015	2014
Consumer Price Index:						
CPI for December (points)	106.1	106.3	107.4	(0.2)	(1.0)	(0.2)
Known CPI for November (points)	106.1	106.4	107.4	(0.3)	(0.9)	(0.1)
Exchange rate of:						
USD (in NIS)	3.845	3.902	3.889	(1.5)	0.3	12.0
EUR (in NIS)	4.044	4.247	4.725	(4.8)	(10.1)	(1.2)

2) Consolidation basis

א. Subsidiaries in which the Bank holds less than 50%

The Bank holds 50% of the issued and paid-in share capital of Bank Yahav for Government Employees Ltd. (hereinafter: "Bank Yahav"). The balance of the issued and paid-in share capital is held by a single shareholder and the Bank has no excess legal rights. The Supervisor of Banks has allowed the Bank to consolidate the financial statements of Bank Yahav under the circumstances concerning the Bank's influence over management of Bank Yahav business and in conformity with Section 9G of the Public Reporting Regulations.

For more information about the balance of investment in investees and contribution to net profit attributable to equity holders of the Bank, see Note 15 to the financial statements.

B. Business combinations

The Bank applies the acquisition method to all business combinations.

The acquisition date is the date on which the acquiring entity achieves control over the acquired entity. The acquiring entity has control over the acquired entity when it is able to direct policy and management of the acquired entity, including by way of ownership or agreement. The test for control does not take into account potential rights.

The Bank recognizes goodwill as of the acquisition date at fair value of the consideration, including amounts recognized with respect to any non-controlling interest in the acquired entity, and the fair value as of the acquisition date of equity interest in the acquired entity previously held by the Bank, less the net amount attributed upon acquisition to identifiable assets acquired and liabilities assumed.

The Bank recognizes upon acquisition a contingent liability assumed upon business combination, if its fair value may be reliably measured.

Acquisition-related cost incurred by the Bank with respect to business combination, such as: brokerage fees, consulting fees, legal fees, valuations and other fees with respect to professional services or consulting services – are recognized as expenses in the period when such cost is incurred and services are rendered. Issuance cost of equity or debt instruments are accounted for in conformity with relevant provisions of the Public Reporting Directives.

For more information about adoption of US GAAP for business combinations, see section C. 2) above.

C. Subsidiaries

Financial statements of subsidiaries are included on the consolidated financial statements as from the date control is achieved.

For more information about adoption of US GAAP with regard to consolidation of financial statements and investment in investees, see section C. 2) above.

D. Non-controlling interests

Non-controlling interest is any shareholders' equity in a subsidiary which is not attributable, directly or indirectly, to the parent company.

Attribution of Comprehensive Income to shareholders

Profit or loss and any Other Comprehensive Income item are attributed to the controlling shareholder of the Bank and to non-controlling interests. Total profit, loss and other comprehensive income is attributed to equity holders of the Bank and to non-controlling interest.

E. Investments in associates

In reviewing the existence of material influence, the assumption is that a holding stake of 20%-50% in an investee confers material influence.

Investment in associates is accounted for using the equity method and is initially recognized at cost. The investment cost includes transaction costs. The consolidated financial statements include the Group's share of revenues and expenses, profit or loss and other comprehensive income of equity-accounted investees.

When the Group's share of loss exceeds the value of Group interest in an entity accounted for using the equity method, the carrying amount of these rights (including any long-term investment) is completely written-off.

For more information about adoption of US GAAP with regard to investment in investees as from January 1, 2016, see section C. 2) above.

F. Transactions canceled upon consolidation

Mutual balances within the Group and unrealized revenues and expenses arising from inter-company transactions have been canceled in the course of preparing the consolidated financial statements.

Note 1 – Reporting Principles and Accounting Policies – continued

3) Offset of assets and liabilities

The Bank applies the rules specified in the Supervisor of Banks' circular dated December 12, 2012.

In conformity with the directives, a banking corporation should offset assets and liabilities arising from the same counter-party and present their net balance on the balance sheet, when all of the following conditions are fulfilled:

- The banking corporation has an enforceable legal right to offset assets against liabilities with regard to said liabilities
- The banking corporation intends to repay the liabilities and realize the assets on net basis or concurrently;
- Both the banking corporation and the counter-party owe each other amounts which may be determined.

According to the directives, a banking corporation should offset assets and liabilities with two different counter-parties and present the net amount on the balance sheet when all of the aforementioned conditions are fulfilled, and provided that the three parties have an agreement which clearly stipulates the banking corporation's set-off rights with regard to those liabilities.

It was further stipulated that a banking corporation should offset deposits whose repayment to the depositor is contingent on the extent of collection of borrowing against those deposits, when the banking corporation has no risk of credit losses.

A banking corporation should not offset assets with respect to derivatives against liabilities with respect to derivatives, unless all of the aforementioned conditions are fulfilled. However, the directives stipulate that under certain conditions, a banking corporation may offset fair value amounts recognized with respect to derivative instruments and fair value amounts recognized with respect to the right to call cash collateral (receivables) or the commitment to reimburse cash collateral (payables) arising from derivative instruments transacted with the same counter-party in accordance with a master netting arrangement - even if there is no intention to repay on net basis or concurrently.

Moreover, a banking corporation may offset securities purchased in conjunction with repurchase agreements against securities sold in conjunction with repurchase agreements, if certain conditions specified in US GAAP on this matter are fulfilled.

However, the banking corporation may not offset amounts on the balance sheet without prior approval of the Supervisor of Banks.

Currently, it is Bank policy to present exposures with transactions on gross basis, except for deposits whose repayment to the depositor is contingent on the extent of collection of borrowing, as described above. Accordingly, designated deposits for which repayment to the depositor is contingent upon the collection of the loan (when the Bank Group is not at risk of credit loss) were set off against the loans issued out of these deposits. The interest margins from this activity are presented in the statement of profit and loss under “commissions”.

Note 1 – Reporting Principles and Accounting Policies – continued

4) Basis of recognition of revenues and expenses

A. Interest revenues and expenses are included on an accrual basis, except as follows:

1) Interest accrued on problematic debt classified as non-performing debt is recognized as revenue on a cash basis when there is no doubt about collection of the outstanding recorded balance of the non-performing debt. In such cases, the amount collected on account of interest to be recognized as interest revenues, is limited to the amount which would have accrued in the reported period for the outstanding recorded debt balance at the contractual interest rate. Interest revenues on cash basis are classified as interest revenue under the relevant item on the statement of profit and loss.

   When collection of the outstanding recorded balance is doubtful, all payments collected serve to decrease the loan principal, until such doubt has been eliminated. Moreover, interest on amounts in arrears with respect to housing loans are recognized in the statement of profit and loss based on actual collection.

   For more information about interest accrual for impaired debt under restructuring, see section 6)C. below.
2) Securities – see section 5 below.
3) Financial derivative instruments – see section 15 below.

B. Commission revenues with respect to services rendered (such as: activities in securities and derivative instruments, credit cards, account management, handling of credit, conversion differences and foreign trade activities) are recognized in the statement of profit and loss when the Bank becomes eligible to receive them. Certain commissions, such as commissions with respect to guarantees and certain commissions with respect to project assistance, are recognized gradually over the transaction term.

C. Other revenues and expenses – are recognized on accrual basis.

D. Measuring interest revenues

As from January 1, 2014, the Bank applies the Supervisor of Banks' directives with regard to adoption of adoption of generally accepted accounting principles for banks in the USA with regard to measuring interest revenues (ACS 310-20). These principles stipulate that commissions from loan origination would not be recognized on the statement of profit and loss, but rather would be accounted for in calculating the effective interest for the loan.

Changes to terms and conditions of debt

In case of refinancing or restructuring of non-problematic debt, the Bank reviews whether a material change was made to terms and conditions of the loan. Accordingly, the Bank reviews whether the present value of cash flows under the new terms and conditions of the loan differs by at least 10% from the present value of remaining cash flows under the current terms and conditions (plus early repayment fee), or whether this involves a change in loan currency. In such cases, all unamortized commissions and early repayment commissions collected from the client with respect to changes to the terms and conditions of the loan are recognized in profit & loss. Otherwise, these commissions are included as part of net investment in the new loan and are recognized as adjustments to returns, as described above.

Note 1 – Reporting Principles and Accounting Policies – continued

Early repayment commissions

Early repayment commissions charged with respect to early repayment made prior to January 1, 2014 and yet to be amortized, are recognized over a three-year period or the remaining term of the loan, whichever is shorter. Commissions charged with respect to early repayment made after January 1, 2014, are immediately recognized under Interest Revenues.

Given that initial application of the standard hence forward started on January 1, 2014, in 2014, 2015 and 2016 the revenues from continued accounting under the accounting method applied prior to the new standard's start date are included concurrently with immediate revenue recognition with respect to collection of early repayment commissions, in conformity with the stipulated rules. In 2017, only current revenues would be included under "Revenues from early repayment commissions".

In 2016, the Bank charged NIS 37 million to interest revenues due to continued spreading of commissions, compared to NIS 78 million and NIS 94 million in 2015 and 2014, respectively.

5) Securities

A. Investments in securities were classified into three categories, as follows:

1) Debentures held to maturity – debentures that the Bank has the intention and ability to hold until maturity date. These debentures are presented at their amortized cost, i.e. at par value plus accrued interest and linkage or exchange rate differentials, plus or minus the discount or premium component generated upon acquisition and not yet amortized and minus loss with respect to other-than-temporary impairment. Income from debentures held to maturity is charged accordingly to the statement of profit and loss on the accrual basis.
2) Securities held for trade – securities acquired or held in order to be sold in the near term, or securities which the Bank has elected to measure at fair value through profit & loss using the fair value option, except for shares for which no fair value is available. These securities are included in the balance sheet at their fair value on the reporting date. Unrealized gains or losses from the adjustment to fair value are charged to the statement of profit and loss.
3) Securities available for sale – securities not classified as debentures held to maturity or as securities held for trade. Securities available for sale are presented on the balance sheet at fair value. Shares having no available fair value are presented at fair value as of the date they were received – which does not exceed their cost – and net of provision for impairment which is not of a temporary nature, which is charged to the statement of profit and loss, as are dividends received from investment in shares available for sale, originating from earnings of a company which are distributed after the investment date.

   Any unrealized gain or loss from adjustment to fair value is not included in the statement of profit and loss and is reported net of the appropriate tax reserve, under a separate equity item under Cumulative Other Comprehensive Income. For securities which include embedded derivatives – see section 15.C below.

B. For more information about realization of the debenture portfolio held to maturity by Bank Yahav, see Note 25 to the financial statements.

C. Bank investments in other funds not accounted for using the equity method, are stated at cost net of any other-than-temporary impairment loss. Gain from these investments are recognized in the Statement of Profit and Loss upon realization of the investment. Dividends received from Bank investments in these funds are charged to profit & loss when the Bank has the right to receive them, up to the amount of accumulated gain since this investment was acquired.

D. The cost of realized securities is calculated on FIFO basis, except for securities acquired as part of a hedge, or in conjunction with creating a strategic position or for any other specific purpose, which is separately identified.

Note 1 – Reporting Principles and Accounting Policies – continued

E. With regard to calculation of fair value, see section 16 below.

F. Impairment:

Pursuant to directives and guidelines of the Supervisor of Banks, the Bank periodically reviews whether impairment of the fair value of securities classified under the available-for-sale portfolio or the held-to-maturity portfolio, below their cost f (or the amortized cost for debentures held to maturity), is of an other-than-temporary nature.

To this end, the following indicators, inter alia, are reviewed:

- Intent and capacity of the Bank to hold the securities for a sufficient period which would allow the security to recover its original cost.
- The time period during which the value of the security was lower than its cost.
- The ratio of impairment to total cost.
- Adverse change in conditions of the issuer or of the economy as a whole.
- Review of conditions reflecting the financial standing of the issuer, including whether or not the impairment is due to individual reasons related to the issuer, or to any macro-economic conditions.

Furthermore, in any of the following situations, the Bank recognizes other-than-temporary impairment:

- The security was sold prior to publication of the report to the public for that period.
- The Bank intends, as of the publication of the report to the public for that period, to sell the security within a short time.
- Debenture is significantly impaired between its rating upon acquisition by the Bank and its rating upon publication of the report to the public for that period.
- Debenture classified by the Bank as problematical after its acquisition.
- Debenture which is in payment default after its acquisition.
- Security where, in general, its fair value as of the end of the reported period and soon prior to publication of the financial statements, is significantly lower than its cost (amortized cost), or where any payment failure has occurred after its acquisition, unless proven with a high degree of confidence and based on objective evidence, that the impairment is merely of a temporary nature.

If the impairment of fair value is deemed to be other-than-temporary in nature, the cost of the security is written-off to its fair value, so that any loss amounts referring to securities classified as available for sale, accrued in equity under Other Comprehensive Income, would be classified upon impairment to the statement of profit and loss. This value would serve as the new cost basis. Appreciation in subsequent reported periods (for securities classified in the available-for-sale portfolio) are charged to a separate item under shareholders' equity under Cumulative Other Comprehensive Income, and are not recognized in the Statement of Profit and Loss.

6) Impaired debt, credit risk and provision for credit losses

A. Pursuant to the Supervisor of Banks' directive on measurement and disclosure of impaired debt, credit risk and provision for credit losses, the Bank applies as from January 1, 2011 the rules stipulated by codification of US accounting standards ASC 310 and the opinion of the US banking supervision authorities and of the US SEC, as adopted in the Public Reporting Directives, in position statements and directives of the Supervisor of Banks. Moreover, as from the aforementioned date, the Bank applies the Supervisor of Banks' directive with regard to treatment of problematic debt. Moreover, as from January 1, 2013, the Bank applies the Supervisor of Banks' directive with regard to updated disclosure of credit quality of debt and of provision for credit losses.

B. Scope of the directives

The regulation is applied for all debt balances, such as: deposits with banks, debentures, securities borrowed or purchased in resale agreements, loans to the public and loans to the government. Loans to the public and other debt balances for which no specific rules on measurement of provision for credit losses were specified in the Public Reporting Regulations (such as: loans to the government, deposits with banks and other assets) are reported on the Bank's accounts at their recorded debt balance.

The recorded debt balance is defined as the debt balance after accounting write-offs but before deduction of the provision for credit losses for that debt. The recorded debt balance does not include any accrued interest not recognized, or previously recognized and then reversed.

As for other debt balances, for which there are specific rules in place with regard to measurement and recognition of a provision for impairment (such as debentures), the Bank continues to apply the measurement rules as specified in section 5 above.

C. Identification and classification of problematic debt

The Bank classifies all problematic debt and problematic off-balance sheet credit items under: special supervision, inferior or impaired. Debt under special supervision is debt with potential weaknesses, which require special attention by Bank management. Should these weaknesses not be addressed, the likelihood of debt repayment may deteriorate. Inferior debt is debt insufficiently secured by collateral or by debtor repayment capacity, and for which the Bank may incur a loss if faults are not corrected.

In conformity with Bank policy, debt in excess of NIS 700 thousand is classified as impaired when, based on current information and events, it is expected that the Bank would be unable to collect all amounts due pursuant to contractual terms of the debt contract. In any case, debt in excess of NIS 700 thousand 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 Banking Conduct Directive 314 on problematic debt in housing loans.

Debt under NIS 700 thousand in arrears 90 days is assessed on Group basis and in such case, is classified as inferior debt.

Decisions with regard to debt classification are made based, *inter alia*, on assessment of the borrower's financial standing and repayment capacity, any collateral and its status, the financial standing of guarantors, if any and their commitment to support the debt and the borrower's capacity to obtain financing from third parties.

Debt restructuring and treatment of problematic debt in restructuring – In general, when it is possible to reach agreement on debt repayment with no impact to collateral available to the Bank and without any legal action, the Bank gives preference to reaching agreement on debt repayment.

In order to improve collection and to avoid, in as much as possible, debt collection default – the Bank makes attempts to reach agreements on debt repayment prior to taking legal action or even during and after taking such action, which may include: Delay of repayment, restructuring of debt repayment, reduced interest rates, changes to repayment schedule, changes to terms and conditions of the debt in order to align it with the borrower's financing structure, debt consolidation for the borrower, transfer of debt to other borrowers in a borrower group under joint control, review of financial covenants imposed on the borrower etc.

Debt which has been formally restructured as problematic debt is defined as debt for which, for economic or legal reasons related to financial difficulties of the debtor, the Bank has made a concession by way of modification to terms and conditions of the debt, designed to make it easier for the debtor to make cash payments in the near term (reduction or postponement of cash payments due from the debtor), or by way of receiving other assets as debt repayment (in whole or in part).

Note 1 – Reporting Principles and Accounting Policies – continued

In order to determine whether a debt arrangement executed by the Bank constitutes problematic debt restructuring, the Bank conducts a qualitative review of all terms of the arrangement and the circumstances under which it was made in order to determine whether: (1) the creditor is in financial duress; and (2) the Bank made a concession to the debtor in conjunction with the arrangement.

In order to determine whether the creditor is in financial duress, the Bank reviews for indications of the creditor being in financial duress at the time of the arrangement, or for reasonable likelihood that the borrower would be in financial duress if not for the restructuring. *Inter alia*, the Bank reviews the existence of one or more of the following circumstances:

- The debtor is currently in payment default for any of their debts. Moreover, the Bank estimates whether it is expected that the debtor would be in payment default for any of their debts in the foreseeable future, if the change is not made. This means that the Bank may conclude that the debtor is in financial difficulties, even if the debtor is not currently in payment default.
- The debtor has declared bankruptcy or is in Receivership or any in any other bankruptcy or Receivership proceedings.
- There is significant doubt about the debtor continuing as a going concern.
- The debtor had securities delisted, being delisted or being threatened with delisting from the stock exchange.
- According to estimates and projections which only include the debtor's current capabilities, the Bank expects specific cash flows for the debtor entity would be insufficient to service any of its debt (principal and interest) in conformity with contractual terms and conditions of the existing agreement in the foreseeable future.
- Without the existing change, the debtor would be unable to obtain cash from sources other than the current lenders, at effective interest rates equal to the prevailing market interest rates for similar debt of a non-problematic debtor.

The Bank concludes that a concession was made to the creditor in conjunction with the restructuring, even if the contractual interest rate was increased in the restructuring – if one or more of the following exists: Due to the restructuring, the Bank does not expect to collect all debt amounts (including accrued interest pursuant to contractual terms); the current fair value of collateral, for debt contingent on collateral, does not cover the contractual debt balance and indicates inability to collect all debt amounts; the debtor is unable to raise funds at market rates for debt with similar terms and conditions to debt determined in the context of the arrangement; If a the Bank does not perform such additional underwriting upon renewal of inferior debt, or if there is no change in debt pricing or if pricing has not been adjusted to align with the risk prior to renewal, or the debtor does not provide additional means to offset the increase in risk due to the borrower's financial difficulties, it is presumed that such renewal is restructuring of troubled debt.

The Bank does not classify debt as restructured problematic debt, if in conjunction with the arrangement, it granted to the creditor a delay in payments which is not material considering the payment frequency, the contractual term to maturity and the expected effective maturity of the original debt. For this matter, if multiple restructurings took place involving changes to debt terms, the Bank accounts for the accumulated effect of previous restructurings in order to determine whether the delay in payments is not material.

Handling of debt under restructuring and subsequent restructuring – restructured debt, including debt assessed on group basis prior to restructuring, shall be classified as impaired debt and shall be individually assessed for making a provision for credit losses. In general, reorganized problematic debt would continue to be measured and classified as impaired debt until fully repaid.

However, under certain circumstances, when debt is restructured as troubled debt restructuring and later on, the Bank and the debtor have signed an additional restructuring agreement, the Bank is no longer required to treat the debt as restructured problematic debt if the following conditions are fulfilled:

- The debtor is no longer facing financial difficulties upon the date of the subsequent restructuring.
- According to terms of the subsequent restructuring, the banking corporation did not give the debtor any waiver.

Such debt which has been subsequently restructured and from which the Impaired classification has been removed, is to be evaluated on group basis in order to quantify the provision for credit losses and the recorded debt balance will not change during subsequent restructuring (unless cash has been received or paid).

If, in subsequent periods, such debt has been individually reviewed and it was found that impairment should be recognized with respect to it, or if it undergoes problematic debt restructuring, the Bank would reclassify it as Impaired Debt and would treat it as reorganization of problematic debt.

Reinstatement of impaired debt to non-impaired status – impaired debt is reclassified as non-impaired debt upon one of these conditions occurring:

1. It includes no principal or interest components which are past due, and the Bank anticipates payment of the outstanding principal and interest in full according to contractual terms (includes amounts subject to accounting write-off or provision).
2. When the debt has become well-secured and is in collection proceedings.

Rules governing reinstatement from the Impaired classification, as noted above, shall not apply to debt classified as impaired due to restructuring of problematic debt.

Reinstatement of impaired debt to impaired and accruing status – debt which has been formally restructured, so that after restructuring all of the following cumulative conditions are fulfilled::

- There is reasonable certainty that the debt would be repaid and will perform according to its new terms and conditions, based on a current, well-documented credit evaluation of the debtor's financial situation and repayment schedule according to its new terms and conditions.
- The debtor has made cash and cash equivalent payments over a reasonable period of at least six months for loans repaid (principal and interest) by monthly installments, or has repaid 20% of the restructured debt for loans with longer maturities.
- The loan, after restructuring, is not in arrears of 90 days or more.

D. Provision for credit losses

The Bank has put in place procedures for classification of credit and for measurement of provision for credit losses, in order to maintain an appropriate provision to cover expected credit losses with regard to the Bank's loan portfolio. Further, the Bank has put in place procedures to be followed, an appropriate provision to cover expected credit losses with regard to off-balance sheet credit instruments (such as: commitments to provide credit, unutilized credit facilities and guarantees).

The required provision to cover expected credit losses from the credit portfolio is estimated under one of the following tracks: "individual provision" or "group provision". Further, the Bank reviews the overall appropriateness of the provision for credit losses.

Such review of debts in order to determine the provision and debt handling is consistently applied to all debts in excess of NIS 700 thousand and in conformity with the Bank's credit management policy – and no transition is made, during the debt term, between the individual review track and the group-based review track – unless in case of restructuring of problematic debt, as noted above.

Individual provision for credit losses – According to Bank policies, this is applied for any debts determined to be impaired, whose contractual balance (including accounting write-offs, unrecognized interest, provisions for credit losses and collateral) is NIS 700 thousand or higher.

Individual provision is also applied to any debt whose terms and conditions have been changed in conjunction with restructuring of problematic debt, unless this debt is subject to provision by extent of arrears. The individual provision for credit losses is estimated based on expected future cash flows, discounted using the effective interest rate of the original debt. When debt is contingent on collateral, or when the Bank has determined that seizure of an asset is expected, the individual provision for credit loss is evaluated based on the fair value of the collateral pledged to secure such debt, after application of consistent, conservative factors to reflect, *inter alia*, the volatility in fair value of such collateral, the time it would take until actual realization and the expected cost for selling the collateral. For this matter, the Bank defines debt as debt contingent upon collateral, when it is expected to be entirely repaid by pledged collateral, or when the Bank expects repayment from an asset even with no specific pledge on such asset, provided that the borrower has no other reliable sources available for repayment.

The Bank regularly reviews the forecasted expected credit losses, based on actual cash flows, and adjusts the individual provision to the current forecast. Actual credit losses may differ from the Bank's original estimates upon classification of the debt as impaired.

Group provision for credit losses – This is applied for large, homogeneous groups of small debts (whose balance is below NIS 700 thousand, according to Bank policy) (such as: credit card debts, housing loans and consumer debts repaid by installments) as well as for large, non-impaired debts. The provision for credit losses with respect to debts based on group estimate, other than housing loans for which the provision has been calculated based on a formula specified by the Supervisor of Banks based on extent of arrears, is calculated based on rules specified in FAS 5 (ASC 450) "Accounting treatment of contingencies" and in conformity with directives and guidance from the Supervisor of Banks. The group-based provision for credit losses is based, *inter alia*, on historical loss rates in various economic sectors, divided into problematic and non-problematic debt.

On February 20, 2017, the Supervisor of Banks issued a circular concerning provision for credit losses, whereby the "range of years" used as a component in determining the group-based provision for credit losses, should continue to include 2011 on the financial statements for 2016 and 2017.

This directive has been given to the Bank prior to this circular being issued and the Bank has applied it starting with its financial statements for the third quarter of 2016.

In addition to calculating the average range of historic loss rates for various economic sectors, as per the above, for determining the appropriate rate of provision, the Bank also accounts for relevant environmental factors, including trends in credit volume for each sector as well as sector condition, macro-economic data, general quality assessment of credit to each economic sector, changes in volume and in trend of balances in arrears and impaired balances and the effect of changes in credit concentration.

In conformity with directives of the Supervisor of Banks, the Bank has formulated a methodology for measuring the group provision, which takes into account both past loss rates and adjustments with respect to relevant environmental factors.

Furthermore, in conformity with the Supervisor of Banks' directive, the rate of adjustment with respect to relevant environmental factors for group provision for credit losses with respect to individuals is 0.75% of the non-impaired consumer credit balance (excluding credit due to receivables for bank credit cards without interest charge). This is based on a specific directive by the Supervisor of Banks, dated January 19, 2015.

Pursuant to provisions stated in the interim directive, as from January 1, 2011 the Bank is not required to maintain general and supplementary provisions, but continues to calculate the supplementary provision and to verify that in any case, the amount of group provision at the end of each reporting period shall be no less than the sum of general and supplementary provisions which would have been calculated as of the same date, gross of tax. For more information, see section G. below.

Housing loans

A minimum provision with respect to housing loans is calculated based on the formula stipulated by the Supervisor of Banks, by extent of arrears, such that the provision rate is higher the longer the arrears. This directive applies to all housing loans, other than loans not repaid by periodic installments and loans used to finance activity of a business nature.

The Bank also applies Proper Banking Conduct Directive no. 329, as per the Supervisor of Banks' letter dated March 21, 2013 "Update to guidelines with regard to residential real estate".

In conformity with these directives, the Bank has set policies designed to ensure that the Bank would be in compliance with stipulations of this directive and that, as from June 30, 2013, the balance of group provision for credit losses with respect to housing loans shall be at least 0.35% of the outstanding balance of such loans as of the report date.

Off-balance sheet credit

The required provision with regard to off-balance sheet credit instruments is assessed as per rules stated in FAS 5. The provision estimated on group basis for off-balance sheet credit instruments is based on provision rates specified for total credit exposure (as stated above), accounting for expected credit realization rate for the off-balance sheet credit risk. The credit realization rate is calculated by the Bank based on credit conversion factors, as specified in Proper Banking Conduct Directive 203 "Measurement and capital adequacy – Credit risk – Standard approach" with certain adjustments.

E. Revenue recognition

Upon classification of debt as impaired, the Bank classifies the debt as non-accruing debt and discontinues accrual of interest revenues with respect to it, except as stated above for certain restructured debt. Further, upon classification of debt as impaired, the Bank reverses all accrued and uncollected interest revenues recognized as income in profit and loss. The debt continues to be classified as non-accruing debt for as long as it is classified as impaired debt. For further information about revenue recognition on cash basis with respect to debt classified as impaired, see section 4 above.

For debt reviewed and provided for on group basis, the Bank discontinues accrual of interest revenues when conditions for accounting write-off of the debt are fulfilled, usually after 150 days in arrears, unless the debt is well-secured and in collection proceedings. Such debt is subject to assessment of provision for credit losses, which ensures that Bank profit is not skewed upwards.

F. Accounting write-off

The Bank makes accounting write-offs of any debt, or part of it, individually assessed as not collectible and of low value, so that maintaining it as an asset is not justified, or any debt which is subject to long-term collection effort by the Bank (typically defined as terms in excess of two years). For debt whose collection is contingent on collateral, the Bank immediately writes off the debt against the balance of the provision for credit losses amounting to the recorded debt balance in excess of the fair value of collateral. For debt assessed on group basis, write-off rules have been put in place based on extent of arrears (mostly – over 150 consecutive days in arrears) and on other problem parameters. Note that accounting write-offs do not involve any legal concession, and merely reduce the debt balance reported for accounting purposes, while creating a new cost basis for the debt in Bank accounts.

Debt which has been reviewed on group basis and classified as impaired due to restructuring of problematic debt, are subject to accounting write-off no later than the date when the debt is in arrears 60 days or longer, with regard to terms and conditions of such restructuring.

Note 1 – Reporting Principles and Accounting Policies – continued

G. Policies on provision for doubtful debts prior to application of directives on impaired debt, credit risk and provision for credit losses.

Prior to January 1, 2011, the provision for doubtful debts was specifically determined, and a general provision and supplementary provision were also included, as per directives of the Supervisor of Banks.

The supplementary provision for doubtful debts is based on the quality of client indebtedness portfolio, based on risk attributes as defined in directives of the Supervisor of Banks. The supplementary provision for doubtful debts is calculated using percentages specified for each of these risk attributes. The general provision is in amounts adjusted for the end of 2004, an amount which constituted 1% of total indebtedness under responsibility of the Bank and banking investees as of December 31, 1991.

As from January 1, 2011 the Bank is not required to maintain general, supplementary and special provisions doubtful debts, but continues to calculate the supplementary provision and to verify that in any case, the amount of group provision at the end of each reporting period shall be no less than the sum of general and supplementary provisions which would have been calculated as of the same date, gross of tax.

7) Transfer and service of financial assets and discharge of liabilities

The Bank applies measurement and disclosure rules specified in US Accounting Standard FAS 140 (ASC 860-10), "Transfer and service of financial assets and discharge of liabilities", as amended by FAS 166, "Transfer and service of financial assets" (ASC 860-10), for handling the transfer of financial assets and discharge of liabilities.

Under these rules, the accounting treatment of transfer of a financial asset would only be deemed a sale if all of these conditions are fulfilled: (1) the transferred financial asset was separated from the transferring entity, even in case of bankruptcy or other form of Receivership; (2) any recipient may pledge or replace the assets (or the beneficiary interests) received, and there is no condition which limits the recipient from exercising their right to pledge or exchange the financial assets, and grants the transferor a non-trivial benefit; (3) the transferor, or subsidiaries consolidated with its financial statements , or their agents do not retain effective control over the financial assets or beneficiary interests related to these transferred assets.

In transactions involving transfer of financial assets, if it is determined that the transferor maintains effective control over transferred assets, the asset transfer shall be accounted for as secured debt. When all of the following conditions are satisfied, effective control over the asset is maintained:

- The assets repurchased or redeemed are identical or essentially identical to the transferred assets;
- The agreement is to repurchase or redeem them prior to maturity, at a fixed or fixable price.
- The agreement is made simultaneously with the transfer.

Moreover, for the transfer of part of a financial asset to be considered a sale, the transferred part must fulfill the definition of participatory rights. Participatory rights must fulfill the following criteria: the interest should represent an interest proportional to the complete financial asset; all cash flows received from the assets are divided among participatory interest pro-rata to their ownership stake; interests are not subordinated to other interests; there is no recourse to the transferor or to other holders of participatory interests (other than in case of breach of representation or obligation, current contractual obligations to service the financial asset as a whole and management of the transfer contract, and contractual obligations to share in offset of any benefits received by any holder of participatory interests); and the transferor and the holder of participatory interests have no right to pledge or replace the financial asset in whole, unless all holders of participatory interests agree to pledge or replace the financial asset in whole.

If the transaction fulfills the conditions for treating it as a sale, the transferred financial assets are removed from the Bank's balance sheet. If the sale conditions are not fulfilled, the transfer is considered as secured debt. Sale of part of a financial asset, other than a participatory right, is treated as secured debt – that is, the transferred assets remain on the Bank's balance sheet and proceeds from the sale are recognized as a Bank liability.

The Bank applies specific provisions specified in Public Reporting Directives for handling transactions to borrow or loan securities, in which lending is made against the borrower's general credit and collateral quality, where the borrower does not provide as collateral for the loaner any liquid instruments specifically related to the securities loaning transaction, which the loaner may sell or pledge.

Such loaning and borrowing are treated as credit or deposit, measured at fair value of the related security. Revenues on accrual basis with respect to such securities are recognized as interest income from credit and changes to fair value (in excess of changes to accrual basis) are recognized under Non-interest Financing Revenues in case of securities in the held-for-trade portfolio or under Other Comprehensive Income in case of securities available for sale.

The Bank only removes a liability if it has been settled, i.e. if one of the following conditions has been fulfilled: (a) the Bank has paid the lender and is no longer liable for said liability; or (b) the Bank was legally released from the liability by a judicial process or by consent of the lender, being the major party liable for said liability.

8) Buildings, equipment and software

This item includes investments by the Bank in fixed assets (including payments on account), assets leased by the Bank under a financing lease, and cost of software for its own use, recognized as an asset.

Buildings and equipment

Recognition

Fixed asset items are measured at cost net of accumulated depreciation and accumulated impairment loss, if any. Cost includes any cost directly attributable to acquisition of the asset. Cost of self-constructed assets includes the cost of materials and direct labor, as well as any additional cost directly attributable to bringing the asset to the required location and state so as to operate as intended by management.

When significant portions of fixed asset items have a different useful life, they are treated as separate fixed asset items.

Gain or loss from disposition of fixed asset items is determined by comparing the proceeds from asset disposition to its carrying amount and are recognized, net, under "Other revenues" in the statement of profit and loss.

Subsequent costs

Current maintenance costs of fixed asset items are charged to profit and loss when incurred.

Depreciation

Depreciation is methodical allocation of the depreciable amount of an asset over its useful life. Depreciable amount is the asset cost, or another amount which is a substitute for such cost, less the residual value of the asset.

Depreciation is charged to the statement of profit and loss using the straight line method over the estimated useful life of each part of the fixed asset items – since this method best reflects the anticipated consumption pattern of future economic benefits inherent in the asset. Leasehold improvements are depreciated over the lease term or the useful life, whichever is shorter. Owned land is not depreciated.

An asset is depreciated when available for use, i.e. when it has reached the location and state required for it to be put into operation as intended by management.

For more information about estimated useful life of buildings and equipment, as of December 31, 2016, see Note 16 to the financial statements.

Software

Recognition

The Bank applies IAS 38 "Intangible Assets" as well as provisions of SOP 98-I – "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use".

The Bank also applies the Bank of Israel directive concerning capitalization of in-house software development costs, as follows:

- Setting of a materiality threshold for each software development project; The materiality threshold specified by the Bank is NIS 450 thousand.
- Revision of the useful life of capitalized software costs, so as not to exceed 5 years.
- With respect to software development projects for which the total software cost which may be capitalized is higher than the specified materiality threshold, capitalization factors would be specified for work hours – factors which would take into account the potential for deviation in recording work hours and for economic inefficiency.

In conformity with Public Reporting Regulations, the Bank classifies under "Buildings and equipment" the cost of software assets acquired, or costs capitalized to an asset with respect to self-developed software for in-house use.

Software acquired by the Group is measured at cost, net of accumulated amortization and impairment loss. For more information about impairment, see section D. 11 below.

Cost associated with software development or adaptation for in-house use are capitalized only if the development cost may be reliably measured, the software is technically and commercially feasible, future economic benefits are expected and the Bank has the intention and sufficient resources to complete development and to use the software. Cost recognized as an intangible asset with respect to development activities includes direct cost of materials, services and direct payroll cost with respect to employees. Other costs associated with development activities and research costs are charged to the statement of profit and loss when incurred.

In subsequent periods, capitalized development cost is measured a t cost net of accumulated amortization and impairment loss.

Subsequent costs

Cost of upgrades and improvements to software for own use are only capitalized if the expenses incurred are expected to result in additional functionality. Other subsequent costs are expensed when incurred.

Depreciation

Depreciation is methodical allocation of the depreciable amount of an asset over its useful life. Depreciable amount is the asset cost, or another amount which is a substitute for such cost, less the residual value of the asset.

For more information about application of US GAAP with regard to topics 360 and 360-10 of the codification concerning "Fixed assets" as from January , 2018, see section E. 5).

Note 1 – Reporting Principles and Accounting Policies – continued

9) Intangible assets and goodwill

Intangible assets of unspecified useful life are reviewed if there are indicators of impairment at the Asset Group level. An asset group is the smallest group of assets and liabilities which generates a separate cash flow. First is a review of whether the carrying amount of the asset group is higher than the non-discounted cash flow amount expected there from. If so, impairment is to be recognized equal to the difference between the carrying amount and the fair value of the asset group. Impairment is to be proportionately attributed to assets in the asset group, provided that the value of any individual asset does not drop below its fair value.

Assets of unspecified useful life are reviewed for impairment at least once per year. They are reviewed as to whether the carrying amount of the asset exceeds its fair value. If so, impairment is to be recognized, equal to the difference between the carrying amount and the fair value.

Goodwill is not systematically depreciated. For more information about treatment of goodwill, see section D. 2) B. above. Development cost of acquired software or cost capitalized to an asset with respect to software developed in-house for in-house use, are classified under "Buildings and equipment".

10) Leases

Leases, including land leases from the Israel Land Administration ("ILA") or from third parties, where the Bank essentially bears all risk and reward associated with the property, are classified as financing leases. Upon initial recognition, leased assets are measured at their fair value or the present value of minimum future leasing fee, whichever is lower. Future payments for exercise of an option to extend the lease term with ILA are not recognized as part of the referring asset and liability, since they constitute contingent leasing fees, derived from the fair value of the land upon future renewal dates of the lease. Other leases are classified as operating leases, and the leased assets not recognized in the Bank's balance sheet.

Prepaid leasing fees paid to ILA with respect to land leases classified as operating leases are presented on the balance sheet as prepaid expenses, and are recognized in the statement of profit and loss over the lease term. The lease term and amortization amounts account for any option to extend the lease term, if upon contracting the lease it was reasonably certain that the option would be exercised.

In a lease for land and buildings, the land and building components are individually reviewed for the purpose of classifying such leases; the key consideration in classification of the land component is the fact that land typically has an unspecified useful life.

Payments for an operating lease are charged to the statement of profit and loss using the straight line method over the lease term. Lease incentives received are recognized as an integral part of all lease expenses using the straight line method over the lease term.

Minimum leasing fees payable for a financing lease are divided into financing expenses and reduction of the liability balance. Financing expenses are allocated for all periods in the lease term, so as to obtain a fixed periodic interest rate for the outstanding liability balance. Minimum leasing fees with respect to contingent leasing fees are updated when the contingency is resolved.

In case of sale and releasing, the type of lease (financing or operating) should be identified. For operating lease – the capital gain from the sale is deferred and attributed over time, if the sale price exceeds the fair value of the asset. For financing lease – the capital gain from the sale is deferred and attributed over time.

11) Impairment of non-financial assets

Determination of cash-generating units

For review of impairment, assets which may not be individually reviewed are grouped into the smallest asset group which generates cash flows from continued use, which are essentially independent of other assets and groups ("cash-generating unit").

Upon each balance sheet date, a review is made for indications of impairment of various assets within the scope of IAS 36. For some assets, the review for impairment is annual if there are no indications of impairment, namely:

a) Intangible asset not yet ready for use;
b) Assets with unspecified useful life; and
c) Goodwill acquired upon business combination.

Recognition of impairment loss

Impairment loss is recognized when the carrying amount of the asset or of the cash-generating unit exceeds the recoverable amount (which is the higher of the fair value net of selling expenses of the asset (or cash-generating unit) or its value in use) – and is charged to the statement of profit and loss.

For more information about implementation of US GAAP for intangible assets, see section C. 3) above.

Allocation of impairment loss to non-controlling interest

Impairment loss is allocated to equity holders of the Bank and to non-controlling interests on the same basis as allocation of profit or loss.

Reversal of impairment loss

As for assets other than goodwill, for which impairment loss has been recognized in previous periods, on each report date a review is conducted as to any indications that such loss has decreased or has been eliminated. Impairment loss is reversed in case of change to estimates used to determine the recoverable amount – but only if the carrying amount of the asset, after reversal of impairment loss, does not exceed the carrying amount net of depreciation or amortization, which would have been determined if no impairment loss had been recognized.

Impairment of cost of in-house development of computer software

In addition to impairment indicators listed in IAS 36 "Impairment of assets", a review for impairment of cost of in-house development of computer software is also conducted if there are any indicators listed in generally accepted accounting principles for banks in the USA for banks:

SOP 98-1: Accounting for the Costs of Computer Software Developed Or; Obtained for Internal Use (ASC 350-40)

- It is not expected that the software would provide significant potential service;
- A significant change has occurred in the manner or scope of use or expected use of the software;
- A material modification to the software has been made or will be made;
- The cost of development or adaptation of software for in-house use significantly exceeds the anticipated amount;
- It is no longer expected that software development would be completed and that the software would be used.

If one or more such indications exist, a review for impairment should be conducted in conformity with the rules stipulated in IAS 36 "Impairment of Assets".

Investments in associates

Investment in associates is reviewed for impairment in each period, based on the fair value of such investment. If the Group is unable to measure the fair value, impairment is reviewed if an event occurs or circumstances change, which may have material negative impact on the fair value of such investment.

Note 1 – Reporting Principles and Accounting Policies – continued

Impairment is reviewed for the investment as a whole.

Impairment loss is recognized when the carrying amount of the investment, after using equity accounting, exceeds its fair value, provided that such loss is not temporary. In the loss review, the time for which the carrying amount of the investment exceeded its fair value and the financial standing of the associate are taken into account. Non-temporary impairment is first attributed to goodwill, which is part of the investment, until it has decreased to zero. The remaining amount is attributed to non-current assets of the associate *pro-rata* and then to its other assets.

Non-temporary impairment loss previously recognized is not reversed in subsequent periods.

12) **Contingent liabilities**

The financial statements include appropriate provisions to cover possible damage, where, in the estimation of the Bank's management, based on the opinion of its legal counsel, a provision is required.

In accordance with the directives of the Supervisor of Banks, claims have been classified according to the range of probability of realization of the risk exposure, as follows:

A. Probable risk: there is a probability of more than 70% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Probable, an appropriate provision was made in the financial statements.

B. Reasonably Possible risk: there is a probability of between 20% and 70% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Reasonably Possible, an appropriate provision is sometimes made on the financial statements, at the discretion of Bank management and based on the opinion of legal counsel.

C. Remote risk: there is a probability of less than 20% that a loss will be sustained from the claim. For claims whose probability of realization has been classified as Remote, no provision was made in the financial statements.

See Note 26.C.11 for disclosure of material claims (whose amount, excluding interest and expenses, is over 1% of equity attributable to equity holders of the Bank).

Likewise, disclosure is given to motions for recognition as class actions, when the amount claimed in them is material, and to appeals to the High Court of Justice when, in the estimation of the Bank's management, based on the opinion of its legal counsel, it is not possible at this stage to estimate their possible outcome, and therefore, no provision was recorded for them.

In accordance with the directives of the Supervisor of Banks, the Bank is permitted to determine for class actions that it is not possible to estimate the prospects for realization of the exposure to risk in the four financial statements published since the claim was filed, or in case of delay of proceedings by decision of the Court. Beyond this, only in rare cases is the Bank permitted to determine that the prospects for realizing the exposure cannot be determined.

13) **Employee rights**

The Bank applies the Supervisor's directives with regard to adoption of US GAAP concerning employee rights. These principles were codified in the following codification sections (hereinafter: "the directives").

- ASC 710 – Compensation – General.
- ASC 712 – Compensation – Non retirement post employment benefits.
- ASC 715 – Compensation – Retirement benefits.
- ASC 718 – Compensation – Stock Compensation.
- ASC 420 – Exit or Disposal Cost Obligations.

Note 1 – Reporting Principles and Accounting Policies – continued

According to the directives, banking corporations should classify employee benefits according to groups listed in US GAAP, including setting of clear policies and procedures as to how different types of benefits may be distinguished. Employee benefits fall into the following categories:

- Benefits prior to termination
- Benefits post termination and prior to retirement
- Post-retirement benefits

Furthermore, the principle set by the Supervisor of Banks whereby a liability should be included with respect to a material obligation – should be maintained. It is expected that in cases where the Bank expects payment of benefits beyond contractual terms, they would adjust these to situations where a material obligation exists.

According to the Supervisor of Banks' directives, the discount rate for employee benefits is calculated based on yields of government debentures in Israel plus the average spread for corporate debentures rated AA (international rating scale) or higher as of the reporting date. For practical reasons, the spread would be determined by the difference between yields to maturity, by terms to maturity, for corporate debentures rated AA or higher in the USA – and yields to maturity, for the same terms to maturity, for US government debentures, all as of the reporting date.

Below are details for benefit groups at the Bank:

Post-retirement benefits – pension, severance pay and other benefits – defined-benefit programs:

The Bank recognizes amounts with regard to pension programs and other post-retirement programs based on calculations which include actuarial and other assumptions, including: discount rates, mortality rates, increase in remuneration and turnover.

The Bank regularly reviews the need to update actuarial assumptions used in the model.

Changes to assumptions are generally recognized, subject to provisions listed below, first in Cumulative Other Comprehensive Income and are amortized to Profit and Loss in subsequent periods, in conformity with the remaining average terms of service for employees expected to receive benefits.

The liability is accrued over the relevant period, determined in conformity with rules listed in Section 715 of the codification.

The Bank applies the Supervisor of Banks' regulations with regard to internal controls over financial reporting with regard to employee rights, including with regard to review of an "essential commitment" to award benefits to Bank employees with respect to increased severance pay and/or early retirement.

Other long-term benefits to active employees:

- The liability is accrued over the period of eligibility for this benefit.
- In calculating the liability, the Bank accounts for discount rates and for actuarial assumptions.
- All components of the benefit cost for the period, including actuarial gains and losses, are recorded to Profit and Loss.

Absence eligible for compensation – paid leave and sick leave:

The liability with respect to paid leave is measured on a current basis, without accounting for any discount rates or actuarial assumptions.

The Bank does not accrue a liability with respect to sick leave utilized during current service.

For more information about employee benefits, see Note 22 to the financial statements.

As for accounting treatment of actuarial gains / losses recognized under Other Comprehensive Income due to changes to discount rates:

Actuarial loss as of January 1, 2013, arising from the difference between the discount rate used for calculation of provisions to cover employee rights, linked to the Consumer Price Index, as stipulated by the interim directive in the Public Reporting Directives (4%) – and the discount rates as of that date for CPI-linked employee liabilities, determined based on the new rules as noted above (hereinafter: "the loss") is included under Accumulated Other Comprehensive Income.

Any actuarial gains recognized as from January 1, 2013, due to current changes in discount rates during the reported period, would be included under Accumulated Other Comprehensive Income and would decrease the loss balance recorded as noted above – down to zero.

Actuarial losses due to current changes in discount rates during the reported year and actuarial gains due to current changes in discount rates during the reported year after the loss balance has been decreased to zero as noted above, would be amortized using the straight line method over the remaining average terms of service for employees expected to receive benefits over the plan term.

Other actuarial gains and losses(not due to changes in discount rates) as of January 1, 2013 and in subsequent periods are to be included in cumulative other comprehensive income and would be amortized using the straight line method over the average remaining service period of employees expected to receive plan benefits.

In conformity with transition provisions specified in Proper Banking Conduct Directive no. 299, a cumulative other comprehensive loss balance and amounts directly charged to retained earnings as of January 1, 2013 with respect to remeasurement of net liabilities or net assets with respect to defined benefit to employees, would not be immediately taken into account for calculation of the capital requirements, but would rather be subject to transitional provisions, so that the impact would be applied at equal rates of 20%. At 40% as from January 1, 2015 and an additional 20% per year, until full application as from January 1, 2018

Principles of accounting treatment of the streamlining plan:

On December 27, 2016, the Bank’s Board of Directors approved the streamlining plan recommended by Bank management, whereby early retirement would be possible for 300 employees in 2017-2021, at improved conditions.

Bank management is in negotiations with the employee union with regard to the retirement program and as a first step, has started implementation of the plan in the Mizrahi Tefahot Technology Division Ltd., pending agreement with the employee union at the Bank.

The cost of update to the actuarial liability with respect to the streamlining plan, recorded on the financial statements as of December 31, 2016, amounts to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity (under Other Comprehensive Income).

In subsequent periods, the Bank would amortize the plan costs to the statement of profit and loss, under "Actuarial gain and loss" using the straight line method over the average remaining service period for the employees, which is currently at 15 years.

If, in certain periods, total severance pay payments should exceed the cost of service and cost of interest recognized for that year and a settlement would take place (in conformity with US GAAP concerning employee rights), then the ratio of amortization of "actuarial gain and loss" would be adjusted for the settlement pace of the actuarial liability in that period, respectively.

In conformity with the Supervisor of Banks' letter dated January 12, 2016, with regard to operating streamlining of the Israeli banking system, the Supervisor of Banks allowed capital relief with respect to this plan. The Bank applies this capital relief so that supervisory capital used to calculate capital adequacy would be adjusted (increased) and the capital effect of the streamlining (a decrease by 0.14%) would be applied on a straight line basis as from 2017, over a five-year period.

See Notes 22 and 25 to the financial statements for further information.

Note 1 – Reporting Principles and Accounting Policies – continued

14) Share-based payment transactions (employee stock options)

The Bank applies provisions of ASC 718 "Share-based payment transactions" with regard to options awarded to employees. In conformity with these provisions, the Bank recognizes payroll expenses due to the awarded options. Expenses are recognized based on fair value of the options on the award date, concurrently with increase in capital over the term of service for which the options are awarded.

When determining the fair value of options upon the award date, vesting restrictions due to market conditions (such as vesting contingent on share price) are taken into account. Other qualitative restrictions which do not concern market conditions (such as: discretionary component of benefit award) have no impact on determining fair value upon the award date and are reflected in current expensing of the benefit awarded. As allowed by the standard, the Bank treats each awarded lot as a separate award.

As for an award in the gain track, tax authorities in Israel allow an expense to be recognized upon option exercise, so that a tax benefit is expected and deferred taxes should be recognized. According to provisions of the standard, the tax benefit would be recognized based on the cumulative expense carrying amount, multiplied by the tax rate. Upon exercise of the options, when the allowed income tax expense exceeds the expense carried, the difference would be charged to shareholders' equity. Any final tax benefit which is lower than the accrued tax benefit would be offset against accrued tax benefits in the capital reserve down to zero and the balance is charged to the Statement of Profit and Loss upon realization.

15) Derivative instruments and hedging activities

A. The Bank trades in financial derivatives, including currency and interest contracts and credit derivatives. The currency contracts include forwards, futures, swaps and options. These trades are executed in all linkage sectors. The trades are executed with the public and with banks in Israel and overseas, as part of the Bank's day-to-day activities as a market maker, and as part of the overall strategy of managing the expedient level of exposure for the various market risk, including basis and interest risk – risk to which the Bank is exposed in its day-to-day activities.

B. Derivatives are stated at fair value on the Bank balance sheet, under Assets or Liabilities, as the case may be. Changes to fair value of derivatives, other than derivatives used as cash flow hedges, are recognized on the Statement of Profit and Loss.

C. It is possible that the Bank will enter into a contract, which by itself is not a derivative, but contains an embedded derivative. When an embedded derivative has economic characteristics that are not clearly and closely tied to the economic characteristics of the host contract, and a separate instrument with the same conditions as the embedded derivative would qualify as a derivative instrument, then the embedded derivative is detached from the host contract and is treated as a hedge by itself.

   A detached embedded derivative is stated in the balance sheet together with the host contract. Change in fair value of detached embedded derivatives is immediately charged to profit and Loss.

D. In certain cases, in which the embedded derivative must be detached from the host contract, the Bank adopts a policies of measuring the entire contract according to its fair value, and records the changes in its fair value in the statement of profit and loss. This policies was adopted for structured securities in the available-for-sale portfolio.

E. The Bank designates certain derivatives as fair value hedges or as cash flow hedges. The Bank formally documents in writing all of the hedging relationships between the hedging financial derivatives and the hedged items, as well as the objective and strategy of the management of risk through the creating of a hedge transaction. The documentation includes identification of the asset designated as the hedged item and states the manner in which the hedging instrument is expected to hedge the risk related to the hedged item. The Bank estimates the effectiveness of the hedging relationship at the inception of the hedge and continuously, in accordance with its risks management policies. Based on the above, a determination is made as to whether the derivative qualifies as a hedge in accordance with Public Reporting Directives.

F. Changes in the fair value of an item hedged by a fair value hedge using a derivative that meets the above conditions, arising from changes in the specified risk factors, are recorded currently to the statement of profit and loss, concurrent with the changes in the fair value of the hedging derivative.

Changes in the fair value of a derivative which qualifies as a cash flow hedge, which arise from changes in the risk factor being hedged (which impacts the cash flows resulting from the hedged instrument), attributed to an anticipated transaction which is probable and may impact profit and loss, are charged to capital reserve from cash flow hedging, in Other Comprehensive Income, under Shareholders' Equity.

G. The Bank stops hedge accounting henceforth, when:

1) It is determined that a hedge is no longer effective for offsetting the changes in the fair value or cash flow of the hedged item, as the case may be.
2) The derivative expires, is sold, canceled or realized.
3) Management revokes the designation of the derivative as a hedging instrument.

When a fair value hedge is discontinued because it is determined that the hedge no longer qualifies as an effective fair value hedge, the derivative will continue to be recorded in the balance sheet at its fair value, but changes to fair value of the hedged asset or liability will no longer be regularly charged to profit and loss. When a cash flow hedge is discontinued because it is determined that the hedge no longer qualifies as an effective cash flow hedge, changes in the fair value of the derivative since the date of discontinuation of hedging are recorded in the statement of profit and loss. Profit or loss accumulated under Other Comprehensive Income and previously presented under Equity, remains under Equity until the anticipated transaction takes place or until it is beyond any reasonable doubt that the anticipated transaction would not take place. If it is beyond any reasonable doubt that the anticipated transaction would not take place, the accumulated profit or loss with respect to the hedging instrument, recognized under Other Comprehensive Income, would be reclassified to profit and loss.

16) Fair value

א. As from January 1, 2011, the Bank applies FAS 157 (ASC 820-10) defines fair value, and sets forth a consistent work framework for fair value measurement, by defining valuation techniques and a fair value ranking. Moreover, as from January 1, 2012, the Bank applies the Supervisor of Banks' directive on fair value measurement, which includes in the Public Reporting Regulations the rules stipulated by Accounting Standard Update ASU 2011-04 with regard to fair value measurement (ASC 820): Amendments to achieve uniform fair value measurement and disclosure requirements in US GAAP and in IFRS.

The ranking divides instruments measured at fair value into three levels:

Level 1 – fair value measured using prices quoted for identical instruments on an active market accessible by the bank upon the measurement date.

Level 2 – fair value measured using observed data, either direct or indirect, which are not quoted prices as set forth under Level 1. Level 2 data include use of quoted market data on active markets, or on non-active markets, if they exist, or data derived from or based upon such observed market data.

Level 3 – fair value measured by using non-observed data.

FAS 157 expands the disclosure requirements for fair value measurements. Application of the standard allows recognition of "first day" gains, and eliminates the obligation to determine the fair value of derivative instruments not traded on an active market based on the transaction price.

For the purpose of fair value measurement, the basic "in use" assumption is not applied to financial instruments. However, under certain conditions, financial assets and financial liabilities held and managed within a portfolio, are measured at fair value using the price which would have been received or paid upon sale or transfer of the net position in such groups of financial assets or financial liabilities.

Moreover, fair value of financial instruments is measured without accounting for the blockage factor (holding size), both for financial instruments measured based on Level 1 data and for financial instruments measured based on Level 2 or 3, except for cases where a premium or discount would have been accounted for in fair value measurement by market players, in the absence of Level 1 data.

The standard stipulates that the Bank should reflect credit risk and non-performance risk in measuring the fair value of debt, including derivatives, issued there by and measured at fair value. Non-performance risk includes the Bank's credit risk, but is not limited to this risk alone.

The Bank assesses credit risk in derivatives as follows:

– When there is sufficient liquid collateral with respect to the exposure, which specifically secures the derivative, the Bank assumes that credit risk is zero, and does not adjust the fair value with respect to credit quality of the counter-party.
– In other cases, the Bank estimates the fair value based on indications from transactions on an active market of the credit quality of the counter party, if such indications are available at reasonable effort. The Bank derives these indications, inter alia, from prices of debt instruments of the counter-party traded on an active market, and from prices of credit derivatives based on the credit quality of the counter-party. In the absence of such indications, the Bank calculates the adjustments based on internal ratings.

When the counter-party exposure, on consolidated basis, is not material, the Bank calculates the aforementioned adjustment on group basis, using a benchmark for credit quality by groups of similar counter-parties, e.g. based on internal ratings.

Further, the Bank conducts reasonability testing of results obtained from internal assessment with regard to changes in market spreads, and makes the required adjustments, if any.

In order to adapt the Bank's valuation methods to the exit price principle and to provisions stated in the standard, the Bank is required to review the valuation methods applied there by for measuring fair value, taking into consideration the relevant circumstances of the various transactions, including recent transaction prices on the market, indicative prices from valuation services and results of back testing of similar transaction types.

In accordance with Bank of Israel directives, fair value measurement of a derivative instrument, when no quoted prices, liquid collateral or offset agreements exist which adequately secure the derivative's credit quality, and when no market information exists as to the credit quality of the counter-party (such as CDS or negotiable debentures of the counter-party) – shall be classified as a Level 3 fair value measurement.

How fair value is determined:

1) Securities

The fair value of securities held for trade and securities available for sale is determined based on quoted market prices on a major market. When there are multiple markets on which the security is traded, the estimate is based on the quoted market price on the most effective market. In such cases, the fair value of the Bank's investment in securities is the product of the number of units and the aforementioned quoted market price. If a quoted market price is not available, the fair value estimate is based on the best available information, with maximum use of observed data and taking into account the risk inherent in the financial instrument (market risk, credit risk, non-negotiability etc.)

2) Financial derivatives

Financial derivatives with an active market are valued based on market value, determined on the primary market, or in the absence of a primary market – using a quoted market price on the most effective market. Derivative financial derivatives not traded on an active market are valued using models which take into account the risk inherent in the derivative instrument (market risk, credit risk etc.)

3) Financial instruments other than derivatives

Most of the financial instruments in this category (such as: loans to the public and loans to the Government, deposits from the public and deposits with banks, non-negotiable subordinated notes and bonds) no "market price" is quotable, since there is no active market on which they are traded. Therefore, the fair value is estimated using acceptable pricing models, such as present value of future cash flows, discounted at an interest rate that reflects the level of risk inherent in the instrument.

To this end, the future cash flows for impaired and other debt have been calculated net of effects of accounting write-offs and provision for credit losses with respect of said debt.

For more information about principal methods and assumptions used in estimating fair value, see Note 33 to the financial statements.

B. Fair value option

FAS 159 (ASC 825-10) allows banking corporations to elect, upon specified election dates, to measure at fair value financial instruments and certain other items ("qualified items") which, according to Public Reporting Directives, are not required to be measured at fair value. Unrealized gain and loss due to changes in fair value of items for which the fair value option has been selected, are recognized in the statement of profit and loss at each subsequent reporting date. Furthermore, prepaid costs and commissions related to items for which the fair value option has been elected, are recognized in the statement of profit and loss as they are incurred. Election of the fair value option, as stated above, is made for each instrument individually, and may not be canceled.

Further, FAS 159 (ASC 825-10) stipulates presentation and disclosure requirements designed to assist in comparing banking corporations which elect different measurement bases for similar types of assets and liabilities.

Notwithstanding the foregoing, the Supervisor of Banks' directives with regard to application of the standard have clarified that a banking corporation may not elect the fair value option, unless the banking corporation had previously developed knowledge, systems, procedures and high-level controls which would allow it to measure the item with a high degree of reliability. Therefore, the Bank may not elect the fair value option for any asset which may be classified under Level 2 or Level 3 of the fair value ranking, nor for any liability, without prior consent of the Supervisor of Banks.

17) Taxes on income

Taxes on income include current and deferred taxes. Current and deferred taxes are charged to the statement of profit and loss, or charged directly to equity if they arise from items directly recognized under equity.

On February 12, 2017, the Supervisor of Banks issued a circular with regard to transitional provisions for 2016. According to the circular with regard to accounting treatment of taxes on income, banking corporations should refer to enactment of the State budget and Arrangements Act for 2017-2018 as enacted legislation on the date of their approval by a third reading by the Knesset plenum.

Application of this circular has no material impact on the Bank's financial statements.

Note 1 – Reporting Principles and Accounting Policies – continued

A. Current taxes

Current tax is the tax amount expected to be payable (or receivable) on taxable income for the year, calculated using tax rates which apply pursuant to statutes enacted, or essentially enacted, as of the reporting date, including changes to tax payments with regard to previous years.

The provision for taxes on income of the Bank and its subsidiaries that are financial institutions for VAT purposes includes profit tax levied on earnings under the Value Added Tax Act. The payroll tax levied on the salaries of financial institutions is included under “Payroll and associated expenses”.

B. Deferred taxes

Deferred taxes are recognized with respect to temporary difference between the carrying amount of asset and liabilities for the purpose of financial reporting, and their value for tax purposes.

Deferred taxes are measured so as to reflect the tax implications expected to arise from the manner in which the Bank, at the end of the reported period, anticipates recovering or discharging the carrying amount of assets and liabilities.

Deferred taxes are measured using tax rates expected to apply to temporary differences when realized, based on statutes enacted, or essentially enacted, as of the balance sheet date.

Deferred tax assets are recognized with respect to carry-forward loss, tax credits and deductible temporary differences, when taxable revenue is more likely than not in future, which may enable utilization of these deferred tax assets.

Deferred tax assets are reviewed upon each report date and are written-down if the related tax benefits are not expected to be realized.

C. Offset of deferred tax assets and liabilities

The Bank offsets deferred tax assets and liabilities when there is an enforceable legal right of set-off between them, and they are attributed to the same taxable income, taxed by the same tax authority with respect to the same taxable entity, or to consolidated companies, which intend to discharge current tax assets and liabilities on net basis, or with tax assets and liabilities settled concurrently.

D. Additional tax with respect to dividend distributions

The Bank may incur additional tax with respect to earnings of certain Group entities, should these earnings be distributed as dividends by those investees. If the Bank has control as of the distribution date and dividend distributions are not expected in the foreseeable future, no provision for taxes is recorded.

For more information about application of US GAAP with regard to topic 740 of the codification "Taxes on income", applicable as from January 1, 2017, see section E. 2).

E. Uncertain tax positions

The Bank applies the rules for recognition and measurement stipulated in FASB Interpretation No. 48 "Accounting for Uncertainty In Income Taxes". In this context, the Bank only recognizes the effect of tax positions if it is more likely than not that those positions would be accepted by the Tax Authorities or by the Court. Tax positions recognized are measured at the maximum amount whose likelihood of realization exceeds 50%. Changes in recognition or measurement are reflected in the period in which a change in circumstances resulted in a change in judgment.

For more information about application of US GAAP with regard to topic 740 of the codification "Taxes on income", applicable as from January 1, 2017, see section E. 2).

18) Earnings per share

The Bank states earnings per share data, both basic and diluted, for its ordinary share capital. Basic earnings per share is calculated by dividing the earnings attributable to holders of ordinary shares of the Group, by the weighted average number of ordinary shares outstanding during the period, after adjustment for treasury shares.

Diluted earnings per share is calculated by adjusting earnings (such as adjustment for after-tax effect of dividends, financing costs and other changes, if any) related to holders of ordinary shares, and adjusting the weighted average number of ordinary shares outstanding, after adjustment for treasury shares and for the effect of all potentially dilutive ordinary shares, including stock options awarded to employees.

For more information about application of US GAAP with regard to topic 260 of the codification "Earnings per share", applicable as from January 1, 2017, see section E. 5).

19) **Bank operating segments**

The Bank applies the Supervisor of Banks' directive with regard to supervisory operating segments, see section C.1) above.

20) **Transactions with controlling shareholders**

The Bank applies US GAAP for accounting treatment of transactions between the Bank and its controlling shareholder and a company controlled by the Bank. In cases where the aforementioned rules do not refer to the accounting treatment, the Bank applies the rules stated in Standard 23 of the Israel Accounting Standards Board concerning accounting treatment of transactions between an entity and its controlling shareholder.

Assets and liabilities subject to a transaction with a controlling shareholder are measured at fair value as of the transaction date.

E. New accounting standards and new directives by the Supervisor of Banks prior to their implementation

1) Recognition of revenues from contracts with clients

On January 11, 2015, the Supervisor of Banks issued a circular concerning adoption of an update to accounting rules with regard to revenues from contracts with clients. The circular updates the Public Reporting Directives in view of the publication of ASU 2014-09, adopting a new standard on revenue recognition in US accounting rules. The standard stipulates that revenue is to be recognized at the amount expected to be received in consideration of transfer of goods or provision of services to clients.

The new standard does not apply, *inter alia*, to financial instruments and to contractual rights or obligations within the scope of chapter 310 of the codification. Furthermore, the Bank of Israel directives clarify that, in general, provisions of the new standards would not apply to accounting treatment of interest revenues and expenses nor to non-interest financing revenues.

According to transition provisions for 2015, the amendments to Public Reporting Directives should be applied in conformity with the circular on adoption of updated accounting rules concerning "Revenues from contracts with clients", as from January 1, 2018. Upon initial application, it is allowed to choose retroactive application, while restating comparative figures, or to choose prospective application, while charging the cumulative effect to equity upon initial application.

The Bank is reviewing the effect of the such adoption on its financial statements.

2) Reporting by Israeli banking corporations in conformity with US GAAP with regard to income taxes

On October 22, 2015, the Supervisor of Banks issued a circular containing amendments to Public Reporting Directives concerning reporting by banking corporations and credit card companies in Israel, in conformity with US GAAP with regard to income taxes.

According to this circular, banking corporations are required to adopt US GAAP with regard to taxes on income, including the presentation, measurement and disclosure rules specified in provisions of ASC 740 "Income Taxes".

According to the circular, a banking corporation is not required to provide disclosure on financial statements in 2017 with regard to non allowed tax benefits, which are required by section 740-10-50-15-2 and section 740-10-50-15A of the codification.

The provisions listed in the circular would apply as from January 1, 2017.

On October 13, 2016, the Supervisor of Banks issued a circular, whereby the new directives would be applied as from January 1, 2017. Temporary differences with respect to previous periods would continue to be treated in conformity with directives in effect through December 31, 2016.

The circular dated October 13, 2016 clarified the following:

- Interest revenues and expenses with respect to taxes on income would be classified under "Taxes on income".
- Fines payable to tax authorities would be classified under "Taxes on income".
- Laws would be deemed "legislated" only when officially published.
- The requirement to present a Note on information based on historical nominal data for tax purposes has been eliminated.

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

3) Reporting by banking corporations in Israel in conformity with US GAAP on these topics: foreign currency issues, accounting policies, changes in accounting estimates and errors and events subsequent to the balance sheet date

On March 21, 2016, the Supervisor of Banks issued a circular concerning reporting by banking corporations and credit card issuers in Israel, in conformity with US GAAP. The circular revises the Public Reporting Directives and adopts generally accepted accounting standards in the US on these topics:

- US GAAP with regard to topic 830 of the codification "Foreign currency matters".
- US GAAP with regard to accounting policies, changes in accounting estimates and errors, including topic 250 of the codification "Accounting changes and error corrections".
- US GAAP with regard to events after the balance sheet date in conformity with topic 855-10 of the codification "Subsequent events".

The provisions stipulated by the circular would apply as from January 1, 2017. Upon initial application, action should be taken in conformity with transitional provisions included in US GAAP for these matters, *mutatis mutandis*, including retroactive amendment of comparative figures, if required by US GAAP for these matters. Note that when applying provisions of topic 830 of the codification "Foreign currency matters", banks would not include exchange rate differentials with regard to available-for-sale debentures as part of fair value adjustments of such debentures, but would continue to treat these as required by the Public Reporting Directives prior to adoption of this topic.

Furthermore, IAS 29 "Financial Reporting in Hyper inflationary Economies", as adopted in the Public Reporting Regulations, would not be applied as from the effective start date of the circular. Note that there is no change to the date of discontinuation of adjustment for inflation of financial statements of banking corporations, and the financial statements would be compiled based on reported amounts – unless otherwise provided for in the Public Reporting Regulations.

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

Note 1 – Reporting Principles and Accounting Policies – continued

4) **FASB codification update 2014-11 concerning repurchase-to-maturity transactions and repurchase of financings.**

On July 15, 2015, the Supervisor of Banks issued a draft concerning "FASB codification update 2014-11 concerning repurchase-to-maturity transactions and repurchase of financings". According to this draft, in June 2014, FASB issued codification update 2014-11 concerning repurchase-to-maturity transactions and repurchase of financings. This update clarifies, *inter alia*, that repurchase-to-maturity transactions should be treated, for accounting purposes, as secured loan – consistently with the accounting treatment of other repurchase transactions.

The update also clarifies the accounting treatment of repurchase of financings, where one party transfers a financial asset to the other party and concurrently, contracts with the other party an agreement for sale and repurchase of the financial asset, also including certain disclosure requirements. According to the draft, banks are required to apply these updates as from January 1, 2016 in conformity with transitional provisions specified in the USA, *mutatis mutandis*. As of the publication date of the financial statements, a final circular on this matter has yet to be issued.

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

5) **Reporting by banking corporations in Israel in conformity with US GAAP on these topics: Non-current assets held for sale and discontinued operations; fixed assets and impairment of fixed assets, investment property; earnings per share; statement of cash flows; interim reporting; and other topics.**

On October 13, 2016, the Supervisor of Banks issued a circular concerning reporting by banking corporations and credit card issuers in Israel, in conformity with US GAAP. The circular revises the Public Reporting Directives and adopts generally accepted accounting standards in the US on these topics:

- US GAAP with regard to topic 205-20 of the codification "Discontinued operations".
- US GAAP with regard to topic 360 and 360-10 of the codification "Fixed assets".
- US GAAP with regard to topic 260 of the codification "Earnings per share".
- US GAAP with regard to topic 230-10 of the codification "Statement of cash flows".
- US GAAP with regard to topic 270 of the codification "Interim period reporting".

The provisions stipulated by the circular would apply as from January 1, 2018. Upon initial application, action should be taken in conformity with transitional provisions included in US GAAP for these matters, *mutatis mutandis*, including retroactive amendment of comparative figures, if required by US GAAP for these matters.

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

Note 2 – Interest revenues and expenses
For the year ended December 31,
Reported amounts (NIS in millions)

	2016	2015	2014
A. Interest revenues[(1)]			
From loans to the public	5,157	4,691	5,129
From loans to Governments	10	9	9
From deposits with the Bank of Israel and from cash	46	29	108
From deposits with banks	5	6	13
From securities loaned or acquired in resale agreements	–	–	1
From debentures	93	171	87
Total interest revenues	5,311	4,906	5,347
B. Interest expenses			
On deposits from the public	1,045	962	1,393
On deposits from governments	2	2	3
On deposits from banks	12	12	18
On debentures and subordinated notes	472	392	556
On other liabilities	2	4	2
Total interest expenses	1,533	1,372	1,972
Total interest revenues, net	3,778	3,534	3,375
C. Details of net effect of hedging derivative instruments on interest revenues	(24)	44	(46)
D. Details of interest revenues on accrual basis from debentures			
Held to maturity	40	75	33
Available for sale	49	92	45
Held for trading	4	4	9
Total included under interest revenues	93	171	87

(1) Includes the effective element in the hedging ratios.

Note 3 – Non-interest financing revenues
For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
A. Non-interest financing revenues (expenses) with respect to non-trading operations			
1. From activity in derivative instruments			
Non-effective element of hedging ratios[(1)]	8	5	3
Net revenues (expenses) with respect to ALM derivatives[(2)]	(244)	37	1,373
Total from activity in derivative instruments	(236)	42	1,376
2. From investment in debentures			
Gains from sale of debentures held to maturity[(3)]	–	67	–
Gains on sale of debentures available for sale	58	118	110
Loss on sale of debentures available for sale	–	–	–
Total from investment in debentures	58	185	110
3. Exchange rate differences, net	364	136	(1,566)
4. Gains (losses) from investment in shares			
Gains on sale of available-for-sale shares	3	–	5
Provision for impairment of available-for-sale shares	–	–	(2)
Dividends from available-for-sale shares	3	7	8
Total from investment in shares	6	7	11
5. Net gain with respect to loans sold	45	1	–
Total non-interest financing revenues (expenses) with respect to non-trade operations	237	371	(69)

(1) Excludes the effective element in the hedging ratios.

(2) Derivatives which constitute part of the Bank's asset and liability management system, which were not intended as hedges.

(3) Gain from sale of debentures held to maturity at Bank Yahav. See also Note 25 to the financial statements.

Note 3 – Non-interest financing revenues – Continued
For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
B. Non-interest financing revenues (expenses)with respect to trading operations[(1)]			
Net revenues (expenses) with respect to other derivative instruments	44	(8)	238
Realized gains (losses) from adjustment to fair value of debentures held for trade, net	(1)	(9)	37
Unrealized gains (losses) from adjustment to fair value of debentures held for trade, net	15	4	(33)
Total from trading operations[(2)]	58	(13)	242
Details of non-interest financing revenues (expenses) with respect to trading operations, by risk exposure			
Interest exposure	(3)	3	4
Foreign currency exposure	65	(23)	239
Exposure to shares	1	–	–
Exposure to commodities and others	(5)	7	(1)
Total	58	(13)	242

(1) Includes exchange rate differentials resulting from trade operations.
(2) For interest revenues from investment in debentures held for trade, see Note 2.D. to the financial statements.

Note 4 – Commissions
For the year ended December 31,
Reported amounts (NIS in millions)

	2016	2015	2014
Account management[1]	313	303	298
Credit cards	169	158	156
Activities involving securities	221	244	238
Commissions on distribution of financial products[2]	50	55	54
Provident fund operations	23	20	19
Handling credit	29	38	56
Translation differences	188	169	137
Foreign trade activity	43	41	43
Net revenues from credit portfolio service	42	55	62
Life insurance distribution commissions	96	93	95
Home insurance distribution commissions	14	15	21
Other commissions	49	42	35
Total commissions other than from financing business	1,237	1,233	1,214
Commissions from financing transactions	196	193	181
Total commissions	1,433	1,426	1,395

(1) In Israeli and foreign currency
(2) Includes distribution commissions from mutual funds and retirement products.

Note 5 – Other revenues
For the year ended December 31,
Reported amounts (NIS in millions)

	2016	2015	2014
Gain from sale of buildings and equipment	92	36	10
Trustee fees	19	17	15
Revenues from security services	7	6	7
Rent revenues	8	8	5
Other	8	7	7
Total other revenues	134	74	44

Note 6 – Salaries and Related Expenses

For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
Salaries (including bonuses)	1,372	1,263	1,215
Expense arising from share-based payment transactions[1]	8	16	37
Other associated expenses, including study fund and paid leave	57	63	50
Long-term benefits	18	13	10
National Insurance and VAT on salaries	416	399	382
Expenses with respect to retirement (including severance pay and provident funds)			
Defined benefit[2]	62	57	45
Defined contribution	114	112	105
Other post-employment benefits and post-retirement benefits, other than pension payment	7	5	6
Expenses with respect to other employee benefits	17	16	16
Total salaries and related expenses	2,071	1,944	1,866
Of which: Payroll and associated expenses overseas	54	54	51

(1) See Note 23.
(2) See Note 22.

Note 7 – Other Expenses

For the year ended December 31,

Reported amounts (NIS in millions)

	2016	2015	2014
Marketing and advertising	52	57	58
Communications	42	45	40
Computer	92	79	71
Office expenses	35	39	36
Insurance	13	10	10
Professional services	132	195	91
Board members' fees	10	10	9
Training and continuing education	14	10	9
Fees	28	34	32
Cars and travel	34	40	40
Other	83	71	62
Total other expenses	535	590	458

Note 8 – Provision for Taxes on Profit
For the year ended December 31,
Reported amounts (NIS in millions)

A. Composition

	2016	2015	2014
Current taxes -			
For the current year	825	725	649
For prior years	11	9	8
Total current taxes	836	734	657
Changes in deferred taxes -			
For the current year	(4)	28	1
For prior years	1	(1)	(1)
Total deferred taxes	(3)	27	-
Total provision for taxes on income	833	761	657
Includes provision for taxes overseas	33	25	24

B. Movement in deferred taxes:

	2016	2015	2014
Temporary differences created and reversed	(73)	15	-
Change in tax rate	70	12	-
Total movement in deferred taxes	(3)	27	-

C. Reconciliation between the theoretical tax amount that would be applicable had the profit been taxable at the statutory tax rate applicable to banks in Israel, and between the provision for taxes on profit as included in the statement of profit and loss:

	2016	2015	2014
Statutory tax rate applicable to a bank in Israel	35.89%	37.58%	37.71%
Tax amount based on statutory tax rate	768	734	669
Tax (tax saving) from:			
Income of subsidiaries in Israel[(1)]	(21)	(24)	(16)
Income of subsidiaries overseas	3	(1)	(7)
Exempt income	-	-	(2)
Adjustment differences on depreciation, amortization and capital gains	(10)	(1)	-
Other non-deductible expenses	11	34	8
Temporary differences and losses for which deferred taxes have not been recorded	-	(2)	-
Taxes with respect to previous years:			
Additional amounts payable for problematic debt	3	2	4
Others	8	7	1
Change in deferred tax balances due to change in tax rates	70	12	-
Adjustment differences on monetary assets and other differences, net	1	-	-
Total provision for taxes on income	833	761	657

(1) Includes revenues of auxiliary corporations.

Reported amounts (NIS in millions)

D. On September 3, 2015, the Knesset Finance Committee decided to decrease the VAT rate on transactions and imports of goods from 18% to 17%, as from October 1, 2015.

On November 12, 2015, the VAT Ordinance (VAT Rate for Non-Profits and Financial Institutions) (Revised), 2015 was published, updating the profit tax and payroll tax rates applicable to financial institutions, to 17% as from October 1, 2015.

The effect of this change in the VAT rate (effective as from October 1, 2015) is reflected in the 2015 financial statements and amounted to an expense of NIS 12 million. The effect is primarily due to a decrease in deferred taxes.

The effect of the decrease in the payroll tax rate impacts the balance of liabilities with respect to employee rights and, concurrently, also deferred taxes and other comprehensive income, such that the total balance of other comprehensive income increased by NIS 4 million.

On January 4, 2016, the Knesset Plenum approved the Income Tax Ordinance Amendment Act (Amendment no. 216), 2016 which stipulates, *inter alia*, a reduction of the companies' tax rate as from 2016 by 1.5%, to 25% (previous rate: 26.5%). The effect of this decrease in the companies tax rate is reflected in the financial statements for the first quarter of 2016, amounting to a decrease in deferred taxes by NIS 32 million, against recording expenses with respect to provision for profit taxes amounting to NIS 30 million and against Other Comprehensive Income amounting to NIS 2 million.

Moreover, on December 22, the Knesset plenum approved the Economic Streamlining Act (Legislation Amendments to Achieve Budget Goals for 2017 and 2018 Budget Years), 2016, which stipulated a reduction of the corporate tax rate from 25% to 23% in two steps: the first step, to 24%, as from January 2017 and the second step, to 23%, as from January 2018.

The effect of this decrease in the companies tax rate in the fourth quarter of 2016 amounted to a decrease in deferred taxes by NIS 43 million, against recording expenses with respect to provision for profit taxes amounting to NIS 40 million and against Other Comprehensive Income amounting to NIS 3 million.

Following the aforementioned amendments, the statutory tax rates applicable to banking corporations have been amended as follows:

Tax year	Statutory tax rate
2015	37.58%
2016	35.89%
2017	35.04%
2018 and later	34.19%

E. The Bank has final tax assessments, or tax assessments deemed to be final, through the 2010 tax year.

Agreed tax assessments have been issued for 2011-2013, except for some issues under dispute, which have been appealed. The Bank made appropriate provisions for these matters.

The Bank received payroll tax assessments with regard to payroll of local employees at overseas branches of the Bank for 2009-2014. These tax assessments amount to NIS 30 million, including interest and linkage. For the years 2009-2011, the Bank was issued tax assessments by decree. The Bank disputes these tax assessments and therefore has filed an appeal with regard to these years and reservations with regard to 2012-2014. It is more likely than not that the Bank's position would prevail, resulting in cancellation of the order, stating that salary paid to Bank employees at branches overseas should not be subject to payroll tax.

Bank Yahav has finalized tax assessments through the 2012 tax year, as confirmed by the Tax Assessor.

Reported amounts (NIS in millions)

F. Deferred tax assets and provision for deferred taxes

				December 31,
		Balances		Average tax rate in %
	2016	2015	2016	2015
Deferred taxes for:				
Provision for credit losses[1]	479	477	34.3	37.2
Provision for vacation pay, long-service bonuses and employee rights[1]	121	116	33.6	37.2
Excess provision for employee rights on retirement, net[1]	380	287	34.5	37.2
Securities[3][1]	-	-	-	-
Adjustment of depreciable non-monetary assets[2]	(1)	(1)	23.0	26.5
Other – from monetary items[1][2][4]	34	30	34.9	37.2
Other – from non-monetary items, net[1]	(9)	(6)	34.2	37.2
Total deferred taxes	1,004	903	34.3	37.2
Deferred taxes include:				
(1) Deferred tax assets included in "other assets"	1,030	929	34.3	37.2
(2) Deferred taxes payable included in "other liabilities"	(26)	(26)	23.0	26.5
Deferred taxes, net	1,004	903	34.3	37.2

(3) Changes in this item with respect to a loss amounting to NIS 7 million due to adjustment of fair value of securities available for sale (previous year – loss amounting to NIS 10 million) were charged to a separate item in shareholders' equity.

(4) Changes in this item amounting to NIS 3 million due to net loss from cash flow hedges (previous year – loss amounting to NIS 2 million) were charged to a separate item in shareholders' equity.

Note 9 – Earnings per Ordinary Share

	For the year ended December 31,		
	Reported amounts (NIS in millions)		
	2016	2015	2014
Net profit used to calculate earnings per share:			
Basic and diluted earnings per share			
Total net profit attributable to shareholders of the Bank	1,266	1,134	1,092
Weighted average number of shares(1)(2)			
Weighted average number of ordinary shares used to calculate basic earnings	231,948,499	231,342,045	230,281,306
Weighted average number of ordinary shares used to calculate diluted earnings	232,016,679	232,118,646	231,613,393
Earnings per share:			
Total basic earnings attributable to holders of ordinary Bank shares	5.46	4.90	4.74
Total diluted earnings attributable to holders of ordinary Bank shares	5.46	4.89	4.71

(1) Excludes 2,500,000 shares bought back by the Bank. For more information see Note 24.D. to the financial statements.

(2) The weighted average number of ordinary shares used to calculate diluted earnings per share includes the number of options due to share-based payment transactions. See Note 23 to the financial statements for details.

Note 10 – Cumulative other comprehensive income (loss)

Reported amounts (NIS in millions)

A. Changes to cumulative other comprehensive income (loss), after tax effect

	Other comprehensive income (loss), before attribution to non-controlling interest						
	Adjustments for presentation of securities available for sale at fair value	Translation adjustments[1]	Net gain from cash flow hedges	Adjustments with respect to employee benefits	Total	Other comprehensive income attributed to non-controlling interests	Other comprehensive income attributable to shareholders of the Bank
Balance as of January 1, 2014	12	(3)	3	(73)	(61)	(4)	(57)
Net change in the period	(7)	4	15	(29)	(17)	(2)	(15)
Balance as of December 31, 2014	5	1	18	(102)	(78)	(6)	(72)
Net change in the period	(17)	(1)	(4)	(2)	(24)	1	(25)
Balance as of December 31, 2015	(12)	–	14	(104)	(102)	(5)	(97)
Net change in the period	(17)	1	(5)	(199)[2]	(220)	–	(220)
Balance as of December 31, 2016	(29)	1	9	(303)	(322)	(5)	(317)

(1) Foreign currency translation adjustment of associates whose functional currency differs from that of the Bank.

(2) Includes the cost of update to the actuarial liability with respect to the streamlining plan, amounting to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity.

Note 10 – Cumulative other comprehensive income (loss) – continued

Reported amounts (NIS in millions)

B. Changes in items of cumulative other comprehensive income (loss) before and after tax effect

	For the year ended December 31,								
	2016			2015			2014		
	Before tax	Tax effect	After tax	Before tax	Tax effect	After tax	Before tax	Tax effect	After tax
Change in items of other comprehensive income (loss), before attribution to non-controlling interests:									
Adjustments for presentation of securities available for sale at fair value									
Net unrealized gains (losses) from adjustments to fair value	32	(11)	21	158	(60)	98	100	(38)	62
Losses (gains) with respect to available-for-sale securities reclassified to the statement of profit and loss[1]	(58)	20	(38)	(185)	70	(115)	(110)	41	(69)
Net change in the period	(26)	9	(17)	(27)	10	(17)	(10)	3	(7)
Translation adjustments									
Adjustments from translation of financial statements[2]	1	–	1	(1)	–	(1)	6	(2)	4
Net change in the period	1	–	1	(1)	–	(1)	6	(2)	4
Cash flows hedges									
Net gains (losses) with respect to cash flows hedging	(9)	4	(5)	(1)	1	–	30	(10)	20
Net (gains) losses with respect to cash flow hedges reclassified to the statement of profit and loss[3]	–	–	–	(5)	1	(4)	(7)	2	(5)
Net change in the period	(9)	4	(5)	(6)	2	(4)	23	(8)	15
Employee benefits									
Net actuarial gain (loss) for the period[4]	(303)	98	(205)	(7)	3	(4)	(47)	17	(30)
Net losses reclassified to the statement of profit and loss	9	(3)	6	4	(2)	2	1	–	1
Net change in the period	(294)	95	(199)	(3)	1	(2)	(46)	17	(29)
Total net change in the period	(328)	108	(220)	(37)	13	(24)	(27)	10	(17)
Total net change in the period attributable to non-controlling interests	–	–	–	(1)	–	(1)	3	(1)	2
Total net change in the period attributable to shareholders of the Bank	(328)	108	(220)	(38)	13	(25)	(24)	9	(15)

(1) Pre-tax amount included on the statement of profit and loss under "Non-interest financing revenues". For details, see Note 3.A.2. to the financial statements.

(2) Foreign currency translation adjustment of associates whose functional currency differs from that of the Bank.

(3) Pre-tax amount included on the statement of profit and loss under "Interest revenues". For more information see Note 2.C. to the financial statements.

(4) Includes the cost of update to the actuarial liability with respect to the streamlining plan, amounting to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity.

Note 11 – Cash and Deposits with Banks
As of December 31

Reported amounts (NIS in millions)

	2016	2015
Cash and deposits with central banks	40,245	28,597
Deposits with commercial banks	1,480	1,892
Total cash and deposits with banks	41,725	30,489
Includes: Cash, deposits with banks and deposits with central banks for an original period of up to three months	41,495	30,309

Note 12 – Securities

As of December 31, 2016

Reported amounts (NIS in millions)

	Carrying amount	Amortized cost (for shares - cost)	Unrecog-nized gains from adjustments to fair value	Unrecognized losses from adjustments to fair value	Fair value(1)
(1) Debentures held to maturity					
of Government of Israel	3,236	3,236	75	-	3,311
Total debentures held to maturity	3,236	3,236	75	-	3,311

	Carrying amount	Amortized cost (for shares – cost)	Cumulative other comprehensive income		Fair value(1)
			Gains	Losses	
(2) Securities available for sale					
Debentures and bonds -					
Of the Government of Israel(2)	5,002	5,007	29	(34)	5,002
Of foreign governments (2)(5)	1,538	1,578	1	(41)	1,538
Of foreign financial institutions	19	19	-	-	19
Of others overseas	19	19	-	-	19
Total debentures available for sale	6,578	6,623	30	(75)	6,578
Shares(3)	100	101	-	(1)	100
Total securities available for sale	6,678	6,724	(4)30	(4)(76)	6,678

	Carrying amount	Amortized cost (for shares - cost)	Unrecog-nized gains from adjustments to fair value	Unrecognized losses from adjustments to fair value	Fair value(1)
(3) Securities held for trade					
Debentures -					
of Government of Israel	348	347	1	-	348
Total securities held for trade	348	347	1	-	348
Total securities	10,262	10,307	106	(76)	10,337

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities .
(2) Includes: Securities pledged to lenders, amounting to NIS 452 million.
(3) Includes shares for which a fair value is not available, that are stated at cost, net of a provision for decline in value that is not temporary, amounting to NIS 98 million.
(4) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".
(5) Primarily US government debentures.

Remarks:

(1) For more information about operations involving investments in debentures – see Notes 2.D, 3.A.2 and 3.B to the financial statements. For more information about investment in shares - see Note 3.A.4 to the financial statements.

(2) The distinction between Israeli and foreign debentures was made in conformity with the country of residence of the authority which issued the securities.

Note 12 – Securities – Continued

As of December 31, 2015

Reported amounts (NIS in millions)

	Carrying amount	Amortized cost (for shares - cost)	Unrecog-nized gains from adjustments to fair value	Unrecognized losses from adjustments to fair value	Fair value(1)
(1) Debentures held to maturity					
of Government of Israel	3,320	3,320	71	-	3,391
Total debentures held to maturity	3,320	3,320	71	-	3,391

	Carrying amount	Amortized cost (for shares – cost)	Cumulative other comprehensive income		Fair value(1)
			Gains	Losses	
(2) Securities available for sale					
Debentures -					
Of the Government of Israel(2)	6,246	6,254	20	(28)	6,246
Of foreign governments (2)(5)	1,664	1,673	-	(9)	1,664
Of foreign financial institutions	274	275	-	(1)	274
Of others overseas	21	21	-	-	21
Total debentures available for sale	8,205	8,223	20	(38)	8,205
Shares(3)	98	100	-	(2)	98
Total securities available for sale	8,303	8,323	(4) 20	(4)(40)	8,303

	Carrying amount	Amortized cost (for shares - cost)	Unrecog-nized gains from adjustments to fair value	Unrecognized losses from adjustments to fair value	Fair value(1)
(3) Securities held for trade					
Debentures -					
of Government of Israel	222	222	-	-	222
Total securities held for trade	222	222	-	-	222
Total securities	11,845	11,865	91	(40)	11,916

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities .
(2) Includes: Securities pledged to lenders, amounting to NIS 588 million.
(3) Includes shares for which a fair value is not available, that are stated at cost, net of a provision for decline in value that is not temporary, amounting to NIS 96 million.
(4) Included in shareholders' equity in "adjustments on presentation of securities available for sale at fair value".
(5) Primarily US government debentures.

Remarks:

(1) For more information about operations involving investments in debentures – see Notes 2.D, 3.A.2 and 3.B to the financial statements. For more information about investment in shares - see Note 3.A.4 to the financial statements.

(2) The distinction between Israeli and foreign debentures was made in conformity with the country of residence of the authority which issued the securities.

Note 12 – Securities – Continued

Reported amounts (NIS in millions)

(4) Fair value and unrealized losses, by time period and impairment rate, of securities available for sale, which include unrealized loss:

	As of December 31, 2016							
	Less than 12 months				12 months or more			
	Fair value[1]	Unrealized losses 0%-20%	Unrealized losses 20%-40%	Total	Fair value[1]	Unrealized losses 0%-20%	Unrealized losses 20%-40%	Total
Debentures -								
of Government of Israel	3,971	34	-	34	184	1	-	1
Of foreign governments	1,245	40	-	40	-	-	-	-
Shares	-	-	-	-	3	1	-	1
Total securities available for sale	5,216	74	-	74	187	2	-	2

	As of December 31, 2015							
	Less than 12 months				12 months or more			
	Fair value[1]	Unrealized losses 0%-20%	Unrealized losses 20%-40%	Total	Fair value[1]	Unrealized losses 0%-20%	Unrealized losses 20%-40%	Total
Debentures -								
of Government of Israel	1,048	14	-	14	114	12	2	14
Of foreign governments	1,435	9	-	9	-	-	-	-
Of banks and financial institutions overseas	78	1	-	1	-	-	-	-
Shares	-	-	-	-	2	2	-	2
Total securities available for sale	2,561	24	–	24	116	14	2	16

(1) Fair value data are generally based on stock exchange prices, which do not necessarily reflect the price to be obtained on the sale of a large volume of securities.
(2) The Bank has no securities in a position with unrecognized loss.

(5) Asset-backed and mortgage-backed securities

As December 31, 2016 and 2015, there was no balance of asset-backed or mortgage-backed securities.

Note 13 - Credit risk, loans to the public and provision for credit losses

Reported amounts (NIS in millions)

A. Debts[(1)], loans to the public and balance of provision for credit losses

						December 31, 2016
	Commercial	Housing	Individual – other	Total to the public	Banks and governments	Total
Recorded debt balance of debt s[(1)]						
reviewed on individual basis	29,972	27	725	30,724	2,839	33,563
reviewed on group basis	9,634	114,959	17,462	142,055	–	142,055
Of which: By extent of arrears	1,243	114,373	–	115,616	–	115,616
Total debts	39,606	[(2)]114,986	18,187	172,779	2,839	175,618
Of which:						
Impaired debts under restructuring	102	–	46	148	–	148
Other impaired debts	482	27	24	533	–	533
Total impaired debts	584	27	70	681	–	681
Debts in arrears 90 days or longer	79	853	26	958	–	958
Other problematic debts	762	–	89	851	–	851
Total problematic debts	1,425	880	185	2,490	–	2,490
Provision for credit losses with respect to debts [(1)]						
reviewed on individual basis	518	2	7	527	2	529
reviewed on group basis	108	613	190	911	–	911
Of which: Provision by extent of arrears[(3)]	5	613	–	618	–	618
Total provision for credit losses	626	615	197	1,438	2	1,440
Of which: With respect to impaired debts	132	2	12	146	–	146

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Includes general-purpose loans secured by a lien on a residential apartment, amounting to NIS 5,731 million.

(3) Includes balance of provision in excess of that required by the extent of arrears method, assessed on group basis, amounting to NIS 401 million.

Note 13 - Credit risk, loans to the public and provision for credit losses - continued

Reported amounts (NIS in millions)

A. Debts[1], loans to the public and balance of provision for credit losses - continued

December 31, 2015						
	Commercial	Housing	Individual – other	Total to the public	Banks and governments	Total
Recorded debt balance of debts[1]						
reviewed on individual basis	29,656	24	758	30,438	3,412	33,850
reviewed on group basis	(4)8,799	105,922	(4)15,445	130,166	-	130,166
Of which: By extent of arrears	1,046	105,419	-	106,465	-	106,465
Total debts	38,455	(2)105,946	16,203	160,604	3,412	164,016
Of which:						
Impaired debts under restructuring	175	-	54	229	-	229
Other impaired debts	537	24	27	588	-	588
Total impaired debts	712	24	81	817	-	817
Debts in arrears 90 days or longer	38	957	17	1,012	-	1,012
Other problematic debts	296	-	92	388	-	388
Total problematic debts	1,046	981	190	2,217	-	2,217
Provision for credit losses with respect to debts [1]						
reviewed on individual basis	516	1	22	539	3	542
reviewed on group basis	(4)87	613	(4)161	861	-	861
Of which: Provision by extent of arrears[3]	4	613	-	617	-	617
Total provision for credit losses	603	614	183	1,400	3	1,403
Of which: With respect to impaired debts	118	1	10	129	-	129

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Includes general-purpose loans secured by a lien on a residential apartment, amounting to NIS 5,421 million.

(3) Includes balance of provision in excess of that required by the extent of arrears method, assessed on group basis, amounting to NIS 368 million.

(4) Reclassified.

Note 13 - Credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Change in balance of provision for credit losses

						December 31, 2016
	Commercial	Housing	Individual - other	Total to the public	Banks and governments	Total
Balance of provision for credit losses at start of period	700	614	192	1,506	3	1,509
Expenses with respect to credit losses	96	13	92	201	(1)	200
Net accounting write-off[(1)]	(191)	(12)	(133)	(336)	-	(336)
Recovery of debts written off in previous years[(1)]	119	-	57	176	-	176
Net accounting write-offs	(72)	(12)	(76)	(160)	-	(160)
Balance of provision for credit losses at end of period	724	615	208	1,547	2	1,549
Of which: With respect to off balance sheet credit instruments	98	-	11	109	-	109

						December 31, 2015
Balance of provision for credit losses at start of period	[(2)] 635	624	[(2)] 186	1,445	5	1,450
Expenses with respect to credit losses	149	9	55	213	(2)	211
Net accounting write-off[(1)]	(211)	(20)	(114)	(345)	-	(345)
Recovery of debts written off in previous years[(1)]	127	1	65	193	-	193
Net accounting write-offs	(84)	(19)	(49)	(152)	-	(152)
Balance of provision for credit losses at end of period	700	614	192	1,506	3	1,509
Of which: With respect to off balance sheet credit instruments	97	-	9	106	-	106

						December 31, 2014
Balance of provision for credit losses at start of period	[(2)] 633	640	[(2)]145	1,418	10	1,428
Expenses with respect to credit losses	83	6	93	182	(9)	173
Net accounting write-off[(1)]	(220)	(22)	(123)	(365)	-	(365)
Recovery of debts written off in previous years[(1)]	139	-	71	210	4	214
Net accounting write-offs	(81)	(22)	(52)	(155)	4	(151)
Balance of provision for credit losses at end of period	635	624	186	1,445	5	1,450
Of which: With respect to off balance sheet credit instruments	92	-	10	102	-	102

(1) Net accounting write-offs presented in the Note primarily consists of write-offs of a technical nature, due to passage of time of clients being in arrears, in conformity with US standards applicable to the Bank in this regard. Thus, for example, the balance of provision for large impaired debt s will typically be subject to accounting write-off after two years. Debt measured on group basis will be subject to write-off after 150 days in arrears. This means that the Bank's collection effort may sometimes take longer than the timing for write-off according to accounting rules. Consequently, relatively high balances of "accounting write-offs" and relatively high balances of "Recovery of debts written off in previous years" are presented.

(2) Reclassified.

Note 14 – Loans to Governments

As of December 31

Reported amounts (NIS in millions)

	2016	2015
Loans to Government of Israel	–	–
Loans to foreign governments	330	316
Total loans to governments	330	316

Note 15 – Investments in Investees and Details

As of December 31

Reported amounts (NIS in millions)

A. Item composition:

	2016	2015
	Associates	Associates
Investment in shares stated on equity basis	(1)	1
Subordinated notes and capital notes	35	35
Total investments	34	36
Of which:		
Losses accrued since acquisition date	(15)	(14)
Post-acquisition items accrued in shareholders' equity:		
Adjustments from translation of financial statements	(1)	(1)

B. Bank's share in profits (losses) of associates:

	2016	2015	2014
Bank's share in net profits of associates(1)(2)	–	–	5

(1) There are no losses or reversal of losses from impairment of investees.
(2) The tax effect on earnings of associates is less than NIS 1 million.

Note 15 – Investments in Associates and Details – continued

Reported amounts (NIS in millions)

	Company information	Share in capital conferring rights to profits		Share in voting rights	
				As of December 31	
		2016	2015	2016	2015
C. Details of principal investees[2]:					
1) Subsidiaries					
Bank Yahav for Government Employees Ltd.[3]	The Bank	50%	50%	50%	50%
Tefahot Insurance Agency (1989) Ltd.	Insurance agency	100%	100%	100%	100%
Mizrahi International Holding Company Ltd (B.V. Holland)[4]	International holding company	100%	100%	100%	100%
Etgar Investment Portfolio Management Company of the Mizrahi Tefahot Group Ltd.	Portfolio management	100%	100%	100%	100%
Mizrahi Tefahot Issue Company Ltd.	Issuance company	100%	100%	100%	100%
Mizrahi Tefahot Trust Company Ltd.	Trust company	100%	100%	100%	100%
2) Associates					
Psagot Jerusalem Ltd. ("Psagot")	Land for construction	[8]20%	[8]*20%*	20%	20%
Rosario Capital Ltd. ("Rosario")	Underwriting company	19.99%	19.99%	19.99%	19.99%
Mustang Mezzanine Fund Limited Partnership	Extending credit	20%	20%	–	–
Planus Technology Fund	Extending credit	20%	20%	–	–
3) Main subsidiary of a subsidiary of United Mizrahi Overseas International Holding Ltd. (BV Holland)					
United Mizrahi Bank (Switzerland) Ltd.[6]	Commercial bank	100%	100%	100%	100%

(1) Includes capital notes.
(2) The above list does not include wholly owned and controlled subsidiaries constituting property companies that provide services to the Bank, or companies that provide services to the Bank, and whose assets and liabilities and operating results are included in the Bank's financial statements.
(3) Balance of goodwill with respect to acquisition of Bank Yahav is included on the consolidated balance sheet under Intangible Assets and Goodwill and on the Bank's balance sheet under Investments in Investees.
(4) The company is incorporated in Holland; for a subsidiary of the Company, see section C.3.
(5) Includes loss due to revaluation of the shekel, relative to foreign currency exchange rates, amounting to NIS 10 million in 2016 (in 2015: gain amounting to NIS 1 million).
(6) United Mizrahi Bank (Switzerland) Ltd. is a commercial bank registered in Switzerland. The investment is presented on the Bank's financial statements as an affiliate whose functional currency is identical to the Bank's.
(7) Includes loss due to revaluation of the NIS vs. the CHF, amounting to NIS 9 million (2015 – no effect on profit).
(8) Share of contribution in case of loss is 27%.
(9) Includes goodwill balance included on the consolidated balance sheet under "Intangible assets and goodwill".
(10) Including adjustments from translation of financial statements and adjustments with respect to presentation of certain securities of investees at fair value and changes to Other Comprehensive Income with respect to employee benefits.

	Investment in shares at equity value[9]		Goodwill balance [3]		Other capital investments[1]		Contribution to net profit (loss) attributable to equity holders of the banking corporation		Dividend recorded		Other items accrued under shareholders equity[10]	
					As of December 31		For the year ended December 31,		For the year ended December 31,		For the year ended December 31,	
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
	679	637	69	69	573	550	42	60	–	–	–	–
	888	816	–	–	–	–	72	68	–	–	–	–
	323	329	–	–	–	–	[5](6)	[5]3	–	–	–	–
	27	27	–	–	–	–	–	1	–	–	–	–
	46	43	–	–	–	–	3	1	–	–	–	–
	55	44	–	–	–	–	11	11	(1)	–	–	–
	(16)	(16)	–	–	35	35	–	–	–	–	–	–
	1	2	–	–	–	–	–	–	–	–	–	–
	12	13	–	–	–	–	–	1	–	–	–	(2)
	2	2	–	–	–	–	–	(1)	–	–	–	–
	222	227		–		–	(5)[7]	3[7]		–		–

Note 15 - Investments in Associates and Details - continued

Reported amounts (NIS in millions)

D. Balance of goodwill with respect to investees:(1)(2)

	December 31, 2016		
	Cost	Accumulated amortization	Amortized balance
Consolidated	140	53	87

(1) The goodwill balance includes goodwill with respect to acquisition of Tefahot Mortgage Bank Ltd., whose amortized balance as of December 31, 2016 amounted to NIS 14 million (identical to amortized balance as of December 31, 2015 and as of December 31, 2014), and with respect to acquisition of Adanim Mortgage Bank Ltd., whose amortized balance as of December 31, 2016 amounted to NIS 4 million (identical to amortized balance as of December 31, 2015 and as of December 31, 2014).

(2) Balance of goodwill with respect to subsidiaries is included on the consolidated balance sheet under Intangible Assets and Goodwill.

Note 16 - Buildings and Equipment

Reported amounts (NIS in millions)

	Buildings and land (including installations and leasehold improvements)	Equipment, furniture, and vehicles	Cost of software	Total
A. Composition				
Cost of assets				
December 31, 2014	1,561	1,064	1,429	4,054
Additions	28	48	179	255
Disposals	(56)	–	–	(56)
Cost of assets as of December 31, 2015	1,533	1,112	1,608	4,253
Additions	29	54	175	258
Disposals	(87)	(1)	–	(88)
Cost of assets as of December 31, 2016	1,475	1,165	1,783	4,423
Depreciation and impairment loss				
Accumulated as of December 31, 2014	617	789	1,078	2,484
Depreciation	38	65	118	221
Impairment	–	–	2	2
Disposals	(37)	–	–	(37)
Accumulated as of December 31, 2015	618	854	1,198	2,670
Depreciation	39	67	116	222
Impairment	–	–	1	1
Disposals	(54)	(1)	–	(55)
Accumulated depreciation as of December 31, 2016	603	920	1,315	2,838
Carrying amount:				
As of December 31, 2016(1)	872	245	468	1,585
As of December 31, 2015(1)	915	258	410	1,583
As of December 31, 2014(1)	944	275	351	1,570

Weighted average depreciation rate as of December 31, 2016	3.8%	13.4%	22.4%	
Weighted average depreciation rate as of December 31, 2015	3.7%	13.3%	22.0%	

(1) Includes amortized capitalized cost of independently developed computer software as of December 31, 2016 amounting to NIS 320 million (December 31, 2015: NIS 273 million; December 31, 2014: NIS 233 million).

Note 16 – Buildings and Equipment – continued

Reported amounts (NIS in millions)

B. Additional information

Depreciation rates are as follows:

Buildings	2%-4%
Leasehold improvements	10%
Office equipment and furniture	6%-25%
Vehicles	15%-20%
Computers, software usage rights and costs	20%-33%

C. Assets not used by the Group (depreciable balance):

		Consolidated
		December 31,
	2016	2015
Not designated for sale	31	43
Includes – leased to others	27	43
Designated for sale(1)	11	8

(1) In addition, assets used by the Group and designated for sale of December 31, 2016 amounted to NIS 1 million (as of December 31, 2015: NIS 31 million).

D. Leasehold rights in buildings (depreciable balance)

	End dates		Consolidated
	Lease term		December 31,
	(In years)	2016	2015
Capitalized lease	3-56	68	69
Non-capitalized lease	0-7	27	28

E. This item includes installations, leasehold rights and payments on account. Part of the buildings and leasing rights, amounting to NIS 295 million (as of December 31, 2015: NIS 322 million), have yet to be recorded at the Land Registry Office in the name of the Bank or its subsidiaries, primarily due to delays in land consolidation or where rights are in the process of being recorded.

F. As of December 31, 2016, the Bank Group has an obligation to acquire and refurbish buildings, amounting to NIS 6 million (December 31, 2015 – NIS 3 million).

Note 17 – Other Assets

As of December 31

Reported amounts (NIS in millions)

	December 31,	
	2016	2015
Deferred taxes receivable, net[1]	1,030	929
Excess of advance tax payments over current provisions	50	112
Revenues receivable	112	111
Other receivables and debit balances	306	848
Total other assets	1,498	2,000

(1) See Note 8 to the financial statements.

Note 18 – Deposits from the Public

As of December 31

Reported amounts (NIS in millions)

A. Deposit types by location and depositor type

	2016	2015
In Israel		
On-call		
Non interest-bearing	40,470	33,973
Interest-bearing	18,935	18,142
Total on-call	59,405	52,115
Term deposits	113,598	106,224
Total deposits in Israel[(1)]	173,003	158,339
Outside of Israel		
On-call		
Non interest-bearing	694	556
Interest-bearing	7	7
Total on-call	701	563
Term deposits	4,548	3,478
Total deposits overseas	5,249	4,041
Total deposits from the public	178,252	162,380

(1) Of which:

Deposits from individuals	82,501	75,467
Deposits from institutional investors	35,964	36,127
Deposits from corporations and others	54,538	46,745

B. Deposits from the public by size

	2016	[(1)]2015
Maximum deposit		
Up to 1	59,606	55,229
Over 1 to 10	38,805	35,229
Over 10 to 100	25,042	22,301
Over 100 to 500	24,120	25,616
Above 500	30,679	24,005
Total	178,252	162,380

(1) Reclassified. Reclassification was due to adjustment of deposit composition by size, to also take into consideration the independent legal entity of depositors. Previously, some deposits have been classified as a single depositor group with no such distinction.

Note 19 – Deposits from Banks

Reported amounts (NIS in millions)

	Consolidated	
	December 31,	
	2016	2015
In Israel		
Commercial banks:		
On-call deposits	92	117
Term deposits	1,267	786
Acceptances	176	253
Outside of Israel		
Commercial banks:		
On-call deposits	2	9
Term deposits	–	1
Total deposits from banks	1,537	1,166

Note 20 – Debentures and Subordinated Notes

As of December 31

Reported amounts (NIS in millions)

Debentures and subordinated notes not convertible into shares:

	Average maturity in years (1)	Internal rate of return(2)	Consolidated 2016	2015
In Israeli currency – non-linked				
Debentures	5.01	2.11%	5,465	4,883
Subordinated notes(3)	6.41	3.15%	192	100
In Israeli currency – CPI-linked				
Debentures	3.48	0.82%	15,803	13,173
Subordinated notes(3)	4.77	4.46%	5,574	5,563
Total debentures and subordinated notes	4.50	2.00%	27,034	23,719

(1) Average maturity is the average of the repayment periods, weighted by the flows discounted according to the internal rate of return.

(2) Internal rate of return is the interest rate used to discount the projected flow of payments to the carrying value in the financial statements.

(3) Upon dissolution, the subordinated notes issued by the Bank and included under this item are repayable after all other liabilities.

A. On October 30, 2006, the Bank's Board of Directors approved the issuance of Bank subordinated notes (Series A) which will be deemed complex capital instruments ("Upper Tier II capital"), as the term is defined in Proper Business Conduct Directive 311 and in accordance with the approval received from the Supervisor of Banks on November 12, 2006), amounting up to NIS 500 million. The subordinated notes are obligatory notes that, if certain events specified in advance in their terms should occur, will be converted in a forced conversion, according to a formula prescribed in advance, into shares of the Bank. On November 15, 2006, Ma'alot Israel Securities Rating Company Ltd. issued a rating of AA- for the subordinated notes issued. The rating of the subordinated notes in its offering is based on the rating of the Bank's debentures, including subordinated notes, with the changes required by the terms of the subordinated notes.

On September 15, 2009, the Bank and the Trustee for the Bank's subordinated capital notes (Series A) signed an addendum, revising the Deed of Trust dated November 16, 2006, which is effective as of the signing date there of ("the revision"). According to the revision, the capital note section stipulating that interest payment to holders of capital notes would be suspended, inter alia, in case "within a period of six consecutive quarters, the financial statements for the most recent of which was published prior to the date set for payment of such interest, the Bank has not reported a cumulative net profit" (i.e. if the simple summation of quarterly net profit or loss amounts stated on the Bank financial statements, with respect to six consecutive quarters, should be negative).
On January 4, 2017, Maalot announced that the subordinated capital notes, which qualify as Tier II equity in conformity with transitional provisions of Basel III, are rated ilA+.
The balance of subordinated capital notes (Series A) as of December 31, 2016 amounted to NIS 1,958 million, NIS 1,702 million par value, issued for consideration of NIS 1,644 million.

B. Mizrahi Tefahot Issue Company ("the Company"), a company wholly-owned and controlled by the Bank, issued to the public CPI-linked pursuant to prospectus, debentures and subordinated notes with a par value of NIS 15,709 million and non-linked debentures with a par value of NIS 5,357 million, as of December 31, 2016, and deposited the proceeds in the Bank earmarked for its day-to-day activities.
The Company issued in 2016 additional debentures (Series 40 and 42) of NIS 566 and NIS 125 million par value, respectively for consideration of NIS 590 and NIS 119 million. The Company also issued new debentures (Series 43 and 44), amounting to NIS 2,071 and NIS 3,014 million, respectively for consideration amounting to NIS 2,071 and NIS 3,014 million; in total, the Company issued NIS 5,776 million par value for consideration amounting to NIS 5,794 million.

Note 20 – Debentures and Subordinated Notes – continued

C. In December 2015 and in January 2016, the Bank issued contingent subordinated notes (Contingent Convertibles – CoCo) with loss-absorption provisions through principal write-off, amounting to NIS 600 million. These notes qualify for recognition as Tier II equity pursuant to Basel III provisions.

The notes include loss-absorption provisions if the Bank's Tier I equity should drop below 5% or in case of another event leading to dissolution of the Bank, in conformity with the Supervisor of Banks' decision.

In such case, the notes would be partially or completely written off.

Should the Tier I equity ratio exceed the minimum required ratio, the Bank may announce a principal write-off, in whole or in part.

Standard & Poor's Ma'alot rated the contingent subordinated notes ilAA-.

In July 2016, Bank Yahav issued contingent subordinated notes (Contingent Convertibles – CoCo) with loss-absorption provisions through principal write-off, amounting to NIS 218 million.

These notes qualify for recognition as Tier II equity pursuant to Basel III provisions.

D. **Issue of prospectus – Mizrahi Tefahot Issue Company Ltd.**

On July 4, 2016, Mizrahi Tefahot Issue Company Ltd. (hereinafter: "Mizrahi Tefahot Issue") issued a shelf prospectus (dated July 5, 2016) whereby the company may issue to the public securities of different types subject to statutory provisions – non-convertible debentures, non-convertible subordinated notes and commercial paper – through shelf offering reports in which it would complete all specifics of each offering, including details, terms and conditions of the securities and composition of the offered units, subject to statutory provisions and to bylaws and directives of the Tel Aviv Stock Exchange Ltd., as they may be at that time.

The prospectus is valid for two years from the issue date and may be extended for a further 12 months by the company.

E. **Publication of prospectus – the Bank**

On September 25, 2016, the Bank issued a shelf prospectus (dated September 26, 2016) whereby the Bank may issue to the public securities of different types subject to statutory provisions – including Bank ordinary shares in the holder's name of NIS 0.1 par value each, as well as other securities of the Bank (including debentures, subordinated notes (including contingent subordinated notes (CoCo), options exercisable for shares and options exercisable for debentures) – through a shelf offering report in which it would complete all specifics of each offering, including details, terms and conditions of the securities and composition of the offered units, subject to statutory provisions and to bylaws and directives of the Tel Aviv Stock Exchange Ltd., as they may be at that time.

Note 21 – Other Liabilities

Reported amounts (NIS in millions)

	December 31,	
	2016	2015
Provision for deferred taxes, net[(1)]	26	26
Excess of provision over funding severance pay, retirement and pension[(2)]	1,043	763
Unearned revenues	110	164
Accrued expenses	443	293
Provision for unutilized vacations and long- service bonus	154	156
Guarantees payable	93	84
Provision for doubtful debts for off-balance sheet and other items	109	106
Payables for credit card operations	3,714	3,530
Market value of securities sold short	205	122
Other payables and credit balances	795	542
Total other liabilities	6,692	5,786

(1) See Note 8 to the financial statements.

(2) See Note 22 to the financial statements.

Note 22 – Employee Rights

A. Description of benefits

1. On June 17, 2013, the General Meeting of shareholders approved the contracting by the Bank of terms of office and employment of the Chairman of the Bank's Board of Directors.

   Below is a summary of terms of office and employment of the Chairman of the Board of Directors, Mr. Moshe Vidman, in conformity with the approved employment agreement (hereinafter: "the previous employment agreement").

   Mr. Moshe Vidman serves as Chairman of the Bank's Board of Directors, in a full-time position equivalent, as from December 1, 2012. The employment agreement is for a 3-year term from the actual start date in office, and was terminated on November 30, 2015. Notwithstanding the foregoing, each party may inform the other party of termination of employment on any date, even before the end of the specified term, by three months' prior notice.

   For his work, the Chairman is entitled to monthly salary at NIS 180 thousand, fully linked to the Consumer Price Index, based on the CPI known on December 1, 2012. The Chairman was also eligible to receive an annual bonus of up to nine monthly salaries and an additional deferred bonus of up to nine monthly salaries, deferred until the end of his term in office. The bonus payments will be calculated based on return on equity, annual return of Bank shares, the Bank's operating efficiency ratio and the Board of Directors' evaluation of the Chairman's performance in discharging his special duties in the assigned areas.

   The Bank provides to the Chairman of the Board of Directors a budget equal to 15.83% of his salary for contributions towards provident fund, retirement and severance pay. The Bank also contributes, on behalf of the Chairman of the Board of Directors, to a study fund at 7.5% of his salary. These amounts are contributed to provident / pension / study funds as selected by the Chairman of the Board of Directors.

   Pursuant to the previous employment agreement, upon termination of the Chairman's employment, the Bank will pay him an amount equal to 150% of his last monthly salary multiplied by his number of years in service. The Bank will also pay an acclimation bonus equal to 6 monthly salaries plus social benefits.

   In addition to the foregoing, should the Chairman be terminated prior to completion of the specified term, he will be paid additional amounts as specified in the employment agreement – subject to conditions stated in the employment contract.

   Upon termination of employment of the Chairman, the Bank will provide him with a letter releasing all contributions made to provident, pension and severance pay funds – in lieu of the full severance pay to which the Chairman of the Board of Directors is entitled. The Bank will also release the study fund to the Chairman.

   On September 9, 2015, the General Meeting of Bank shareholders approved, after approval by the Bank's Remuneration Committee and Board of Directors, to pay the Chairman of the Board of Directors the amount of NIS 246 thousand (1.35 monthly salaries), which is the full amount with respect to the discretionary portion of the bonus payable to the Chairman of the Board of Directors for 2014, such that the total annual bonus paid to the Chairman of the Board of Directors for 2014 amounted to NIS 764 thousand.

   On April 4, 2016, the General Meeting of Bank shareholders approved, after approval by the Bank's Remuneration Committee and Board of Directors, to pay the Chairman of the Board of Directors the amount of NIS 246 thousand (1.35 monthly salaries), which is the full amount with respect to the discretionary portion of the bonus payable to the Chairman of the Board of Directors for 2015, such that the total annual bonus paid to the Chairman of the Board of Directors for 2015 amounted to NIS 764 thousand.

Note 22 – Employee Rights – Continued

Moreover, pursuant to the previous employment agreement, the Chairman of the Board of Directors was entitled to a deferred bonus with respect to 2013-2015, amounting to NIS 711 thousand (equivalent to 3.9 months' salary).

On March 8, 2016, the General Meeting of Bank shareholders approved, after approval by the Bank's Remuneration Committee and Board of Directors, the terms of office and employment of Mr. Vidman as Chairman of the Bank Board of Directors pursuant to the approved employment agreement (hereinafter: "the additional employment agreement"). The employment term according to the additional employment agreement is from December 1, 2015 through December 31, 2017 and will be automatically renewed, every year, for one additional year – all subject to provisions of the employment agreement. For his work, the Chairman was entitled to a monthly salary of NIS 220 thousand, fully linked to the Consumer Price Index. The Bank provides to the Chairman of the Board of Directors a budget equal to 13.33% for contributions towards provident fund, retirement fund and severance pay payable by the Bank (5% for provident fund and 8.33% for severance pay). The Chairman of the Board of Directors is also eligible to employer contributions to a study fund at 7.5% of the salary. These amounts are contributed to provident / pension / study funds as selected by the Chairman of the Board of Directors.

Upon termination of employment pursuant to the Additional Employment Agreement, the Bank will pay to the Chairman of the Board of Directors an acclimation bonus in exchange for non-competition, equal to three monthly salaries (hereinafter: "Acclimation Bonus").

The additional employment agreement also specifies that the acclimation bonus payable to the Chairman of the Board of Directors, as noted above, is the sole acclimation bonus for which the Chairman of the Board of Directors would be eligible upon termination of their employment pursuant to the additional employment agreement and the Chairman of the Board of Directors will not be eligible for an acclimation bonus with respect to their employment period pursuant to the previous employment agreement.

The Bank will pay to the Chairman of the Board of Directors the retirement bonus to which he is eligible pursuant to the previous employment agreement, with respect to employment from December 1, 2012 through November 30, 2015, equal to 150% of the Chairman's final salary pursuant to the previous employment agreement, multiplied by the number of years of service (three years) pursuant to the previous employment agreement.

It is hereby clarified that the Chairman of the Board of Directors is not eligible to a retirement bonus pursuant to the additional employment agreement and that payment of the retirement bonus to the Chairman of the Board of Directors upon termination of his employment would be in conformity with his eligibility for a retirement bonus pursuant to the previous employment agreement as noted above.

Should the Chairman of the Board of Directors be eligible for severance pay, pursuant to the Severance Pay Law, 1963 (hereinafter: "the Severance Pay Law") and should the amount accrued in the provident fund with respect to Bank contributions towards severance pay (8.33%) and all accrued returns as of the termination date and as reported by the provident fund, be lower than the Severance Pay Amount, as defined in the Severance Pay Law, gross (hereinafter: "Statutory severance pay"), then the aforementioned retirement grant (pursuant to the previous employment agreement), in whole or as required, will be on account of the statutory severance pay; should the amount accrued in the provident fund plus the retirement grant amount together be lower than the statutory severance pay – then the Bank will make up the difference up to the statutory severance pay.

On September 21, 2016, the Bank's Board of Directors, following a resolution by the Remuneration Committee, resolved that consequently to implementation of the Remuneration of Officers in Financial Corporations Act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 ("the Executive Remuneration Act"), the Chairman of the Board of Directors and the Bank President & CEO would not be eligible for remuneration for which the expected cost would exceed the maximum specified in section 2(a) of the Act – NIS 2.5 million.

Note 22 – Employee Rights – Continued

This applies for an interim period, from October 12, 2016 (the effective start date of the Remuneration Act, with regard to such contracts) or from a later date to be specified for this matter in conformity with the Supreme Court ruling (if any), whichever is later, through the date of approval of terms of office and employment for the Bank President and for the Chairman of the Board of Directors by the qualified organs of the Bank which terms are in compliance with provisions of the Remuneration Act. For the period ended October 11, 2016, the terms of office and employment of the Chairman of the Bank Board of Directors and of the Bank President & CEO would remain in effect as prior to the effective start date of the Remuneration Act.

For more information about the Remuneration of officers in financial corporations act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 – see chapter "Corporate governance, audit, other information about the Bank business and its management" (Legislation and Supervision of Bank Group Operations) of these annual financial statements.

Due to enactment of the Executive Remuneration Act, the Bank was required to amend the terms of office and employment of the Chairman of the Board of Directors. On February 14, 2017, the General Meeting of Bank shareholders approved, in line with the resolution by the Board of Directors and after approval by the Remuneration Committee, the terms of office and employment of Mr. Vidman as Chairman of the Bank's Board of Directors in line with a new officer remuneration policy, also approved by the General Meeting on said date, which was made to conform to provisions of the Executive Remuneration Act and with due attention to amendments required by Proper Banking Conduct Directive 301A with regard to remuneration ("the new remuneration policy").

For more information about terms of office and employment of the Chairman of the Board of Directors, see Addendum B to report dated January 9, 2017 (reference: 2017-01-003454), included herein by way of reference.

The employment term according to the approved employment agreement ("the amended employment agreement") is from December 1, 2016 through December 31, 2017 and will be automatically renewed, every year, for one additional year - all subject to provisions of the amended employment agreement ("the additional employment term").

Notwithstanding the foregoing, either party may announce discontinuation of employment at any time during the additional employment period, for any reason and with no need to justify their position to the other party, subject to providing six months' advance notice to the other party.

During the advance notice period, the Chairman of the Board of Directors will be required to fully work as usual, but the Bank may waive such notice period, in whole or in part, and may terminate employment of the Chairman of the Board of Directors; in such case, the Bank will pay to the Chairman of the Board of Directors for the portion of the advance notice period for which the Bank waived the Chairman's work - in an amount equal to the salary for the waived period plus an amount equal to Bank contributions to provident fund, retirement fund, severance pay and study fund as stated above.

The Chairman of the Board of Directors would be entitled to monthly salary of NIS 189,660. This salary is fully linked to changes in the Consumer Price Index. The Bank provides to the Chairman of the Board of Directors a budget equal to 14.83% for contributions towards provident fund, retirement fund and severance pay payable by the Bank (6.5% for provident fund and 8.33% for severance pay). The Chairman of the Board of Directors is also eligible to employer contributions to a study fund at 7.5% of the salary. These amounts are contributed to provident / pension / study funds as selected by the Chairman of the Board of Directors.

Note 22 – Employee Rights – Continued

Should the Chairman of the Board of Directors request, from time to time, the Bank would update the Chairman's monthly salary, subject to required adjustments and changes to payment of associated expenses, so that any increase or decrease in the salary would be against concurrent decrease or increase in associated expenses and vice versa, provided that the total cost of employment of the Chairman would remain unchanged, including the tax cost to the Bank, all subject to statutory provisions and subject to the maximum remuneration allowed by the Executive Remuneration Act and the statutory rate of contributions to severance pay and provident funds.

Upon approval of the terms of office and employment of the Chairman of the Board of Directors by the Remuneration Committee and by the Board of Directors, the total maximum remuneration which the Bank may pay to the Chairman of the Board of Directors (subject to obtaining statutory approvals), pursuant to Section 2(b) to the Executive Remuneration Act, amounted to NIS 2,746 thousand per annum (for this matter, any remuneration for which expenses are not expected pursuant to GAAP and contribution towards severance pay and provident funds by law would not be taken into account).

Should the maximum remuneration pursuant to the Executive Remuneration Act, including pursuant to Section 2(b) of the Act, allow this, the Bank would pay the Chairman of the Board of Directors an additional fixed remuneration component equal to up to 2 months' salary (based on the salary for December of that year). With respect to this additional fixed remuneration component, the Bank would make all statutory payments and contributions as well as contribution towards severance pay and provident funds by law.

Since the expense with respect to cost of salary to be incurred by the Bank, directly or indirectly, in the tax year with respect to the Chairman of the Board of Directors would exceed the "Maximum payment", as defined in Section 4 of the Executive Remuneration Act, part of the remuneration payable to the Chairman of the Board of Directors would not be tax deductible for the Bank pursuant to provisions of the aforementioned Section 4.

Upon termination of employment pursuant to the amended employment agreement, the Bank will pay to the Chairman of the Board of Directors an acclimation bonus in exchange for non-competition, equal to three monthly salaries ("Acclimation Bonus").

The amended employment agreement clarifies that the Acclimation Bonus payable to the Chairman of the Board of Directors, as noted above, is the only acclimation bonus to which the Chairman of the Board of Directors would be entitled upon termination of their employment term pursuant to the amended employment agreement.

Furthermore, upon termination of employment pursuant to the amended employment agreement, the Bank would pay the Chairman of the Board of Directors the retirement bonus to which the Chairman is eligible pursuant to the Previous Employment Agreement. for the employment term from December 1, 2012 to November 30, 2015, equal to 150% of the Chairman's final salary, according to the Previous Employment Agreement for 2012-2015, multiplied by the number of years in office (three years), in conformity with the Previous Employment Agreement for said period ("retirement bonus").

Note that the cost of the retirement bonus and acclimation bonus payable to the Chairman of the Board of Directors, as noted above, has been fully provided for on the Bank's financial statements prior to the end of the transition period for the Executive Remuneration Act.

Should the Chairman of the Board of Directors be eligible for severance pay, pursuant to the Severance Pay Law, 1963 ("the Severance Pay Law") and should the amount accrued in the provident fund with respect to Bank contributions towards severance pay (8.33%) and all accrued returns as of the termination date and as reported by the provident fund, be lower than the Severance Pay Amount, as defined in the Severance Pay Law, gross (hereinafter: "Statutory severance pay"), then the aforementioned retirement grant (pursuant to the previous employment agreement), in whole or as required, will be on account of the statutory severance pay; should the amount accrued in the provident fund plus the retirement grant amount together be lower than the statutory severance pay – then the Bank will make up the difference up to the statutory severance pay.

Note 22 – Employee Rights – Continued

For the period starting at the end of the transition period for the Executive Remuneration Act through 2016 ("Pro rata share for 2016"), the parties decided that the Chairman's previous employment terms and conditions would continue to apply, as approved by the General Meeting of shareholders on March 8, 2016, provided that the total remuneration to the Chairman (excluding contribution to severance pay and provident fund by law) for the pro rata share for 2016, would not exceed the (pro rata) maximum stipulated in Section 2(b) of the Executive Remuneration Act. Should total remuneration exceed the aforementioned pro rata maximum, the excess amount would be deducted from the total fixed remuneration of the Chairman of the Board of Directors for the pro rata share for 2016.

2. On June 17, 2013, the Bank's Board of Directors approved the appointment of Mr. Eldad Fresher as Bank President. Mr. Fresher started in his office as full-time Bank President on August 16, 2013.

   On May 4, 2014, the Bank's Board of Directors approved, after approval by the Remuneration Committee, the Bank President's terms of office and employment. On June 10, 2014, these terms of office and employment were approved by the General Meeting of Bank shareholders.

   Employment terms of the President & CEO were determined in conformity with the Bank's officer remuneration policy, as adapted to Proper Banking Conduct Directive 301A with regard to remuneration policy of a banking corporation. This policy was approved by the Remuneration Committee, the Bank's Board of Directors and the General Meeting of Bank shareholders.

   Below is a summary of the terms of office and employment of the Bank President & CEO – as listed in Appendix B to a report issued by the Bank on May 4, 2014, reference 2014-01-056838 (hereinafter: "Appendix B to the immediate report"):

   The employment contract is for an unlimited term and either party may terminate it for any reason by three months' advance notice to the other party.

   For his work, the Bank President is entitled to monthly salary at NIS 185 thousand, fully linked to the Consumer Price Index, based on the CPI known on August 16, 2013, and to benefits.

   The Bank provides to the Bank President a budget equal to 15.83% of his salary for contributions towards provident fund, retirement and severance pay. The Bank also contributes, on behalf of the Bank President & CEO, to a study fund at 7.5% of his salary.

   Upon termination of the Bank President & CEO's employment, at any time and for any reason, the Bank will pay him a retirement bonus equal to 150% of his last monthly salary multiplied by his number of years in service. The Bank will also issue a letter releasing all contributions made pursuant to the individual employment contract signed by the Bank and by the Bank President & CEO, with regard to the latter's work for the Bank prior to their appointment as President & CEO.

   The Bank will also release to the President his study fund and will also pay, in exchange for non-competition, an acclimation bonus equal to 6 monthly salaries plus social benefits. Furthermore, upon termination of the Bank President's employment, he will be paid other amounts as described in the employment contract, subject to conditions specified in the employment contract.

   The Bank President committed that for six months after termination of his position and employment with the Bank, for any reason, he will not directly or indirectly act or engage in or on behalf of any other banking corporation and would not serve as officer of or on behalf of any entity which competes with Bank business.

   Variable remuneration based on targets and performance

   According to the employment contract, the Bank President will be eligible for a monetary bonus and equity-based remuneration, in conformity with the Bank's remuneration policy as it may be from time to time, with a mix and subject to conditions as approved.

Note 22 – Employee Rights – Continued

Monetary bonus – According to the employment contract, the Bank President will be eligible for a monetary bonus, capped at NIS 1,517 thousand plus CPI linkage differentials, based on the CPI known on August 16, 2013 – for each calendar year between 2014-2016. This is subject to meeting threshold conditions during the bonus year, based on rates of return on equity, overall capital adequacy ratio and core capital adequacy ratio at the Bank for the bonus years. The monetary bonus is performance-dependent and constitutes part of the Bank President's variable remuneration. For details of threshold conditions for eligibility for the monetary bonus, conditions for eligibility for the monetary bonus, the Board of Directors' authority to reduce the monetary bonus and provisions with regard to reimbursement of the monetary bonus – see Appendix B to the Immediate Report.

Equity-based remuneration – As part of the Bank President's variable remuneration for 2014-2016, the Bank President is eligible for equity-based remuneration which includes a plan for award of options by private offering the Bank President.

For more information about the option plan, see Note 23.A. to the financial statements.

On September 21, 2016, the Bank's Board of Directors, following a resolution by the Remuneration Committee, resolved that consequently to implementation of the Remuneration of Officers in Financial Corporations Act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 ("the Executive Remuneration Act"), the Chairman of the Board of Directors and the Bank President & CEO would not be eligible for remuneration for which the expected cost would exceed the maximum specified in section 2(a) of the Act – NIS 2.5 million. This applies for an interim period, from October 12, 2016 (the effective start date of the Remuneration Act, with regard to such contracts) or from a later date to be specified for this matter in conformity with the Supreme Court ruling (if any), whichever is later, through the date of approval of terms of office and employment for the Bank President and for the Chairman of the Board of Directors by the qualified organs of the Bank which terms are in compliance with provisions of the Remuneration Act. For the period ended October 11, 2016, the terms of office and employment of the Chairman of the Bank Board of Directors and of the Bank President & CEO would remain in effect as prior to the effective start date of the Remuneration Act.

For more information about the Remuneration of officers in financial corporations act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 – see chapter "Corporate governance, audit, other information about the Bank business and its management" (Legislation and Supervision of Bank Group Operations) of these annual financial statements.

On February 14, 2017, the General Meeting of Bank shareholders approved, in line with the resolution by the Board of Directors and after approval by the Remuneration Committee, the terms of office and employment of Mr. Fresher as Bank President & CEO, in line with a new officer remuneration policy, also approved by the General Meeting on said date, which was made to conform to provisions of the Executive Remuneration Act and with due attention to amendments required by Proper Banking Conduct Directive 301A with regard to remuneration ("the new remuneration policy").

For more information about terms of office and employment of the Bank President & CEO, see Addendum C to report dated January 9, 2017 (reference: 2017-01-003454), included herein by way of reference.

The Bank President & CEO would be entitled to monthly salary of NIS 190,660. This salary is fully linked to changes in the Consumer Price Index. The Bank provides to the Bank President & CEO a budget of 15.83% for contributions to provident, pension and severance pay funds (5% for provident funds and 8.33% for severance pay); the Bank would also obtain, on behalf of the Bank President & CEO, disability insurance by payment at 2.5% or such rate as to provide to the Bank President & CEO a disability pension equal to 75% of their salary, whichever is lower). The Bank President & CEO is also eligible to employer contributions to a study fund at 7.5% of the salary. These amounts are contributed to provident / pension / study funds as selected by the Bank President & CEO.

Note 22 – Employee Rights – Continued

Should the Bank President & CEO request, from time to time, the Bank would update the Bank President & CEO's monthly salary, subject to required adjustments and changes to payment of associated expenses, so that any increase or decrease in the salary would be against concurrent decrease or increase in associated expenses and vice versa, provided that the total cost of employment of the Bank President & CEO would remain unchanged, including the tax cost to the Bank, all subject to statutory provisions and subject to the maximum remuneration allowed by the Executive Remuneration Act and the statutory rate of contributions to severance pay and provident funds.

Upon approval of the terms of office and employment of the Bank President & CEO by the Remuneration Committee and by the Board of Directors, the total maximum remuneration which the Bank may pay to the Bank President & CEO (subject to obtaining statutory approvals), pursuant to Section 2(b) to the Executive Remuneration Act, amounted to NIS 2,746 thousand per annum (for this matter, any remuneration for which expenses are not expected pursuant to GAAP and contribution towards severance pay and provident funds by law would not be taken into account).

Should the maximum remuneration pursuant to the Executive Remuneration Act, including pursuant to Section 2(b) of the Act, allow this, the Bank would pay the Bank President & CEO an additional fixed remuneration component equal to up to 1 month' salary (based on the salary for December of that year). With respect to this additional fixed remuneration component, the Bank would make all statutory payments and contributions as well as contribution towards severance pay and provident funds by law.

Since the expense with respect to cost of salary to be incurred by the Bank, directly or indirectly, in the tax year with respect to the Bank President & CEO would exceed the "Maximum payment", as defined in Section 4 of the Executive Remuneration Act, part of the remuneration payable to the Bank President & CEO would not be tax deductible for the Bank pursuant to provisions of the aforementioned Section 4.

Upon termination of employment pursuant to the additional employment agreement, the Bank will pay to the Bank President & CEO an acclimation bonus in exchange for non-competition, equal to six monthly salaries ("Acclimation Bonus").

Furthermore, upon termination of employment pursuant to the amended employment agreement, the Bank would pay the Bank President & CEO a retirement bonus equal to 150% of the last monthly salary of the Bank President & CEO prior to end of the transition period pursuant to the Executive Remuneration Act (October 12, 2016) multiplied by the number of years of service with the Bank through the end of the transition period, all subject to provisions of Section 4.9.4 of Addendum B to the immediate report issued by the Bank on May 4, 2014 (reference 2014-01-056838) ("the retirement bonus").

Note that the cost of the retirement bonus and acclimation bonus payable to the Bank President & CEO, as noted above, has been fully provided for on the Bank's financial statements prior to the end of the transition period for the Executive Remuneration Act. The retirement bonus and one half of the acclimation bonus would be deemed variable retirement remuneration, payable in 4 lots, three of which would be deferred and payable in the three years subsequent to the employment termination date. All provided that the financial statements published soon prior to payment of any such deferred lot would not include deviation in excess of 10% of the minimum ratios for total capital adequacy and Tier I capital adequacy.

The Remuneration Committee and the Board of Directors may, at their discretion, award the Bank President & CEO a monetary bonus for each of 2017, 2018 and 2019, amounting up to three months' salary. Notwithstanding the foregoing, should the Remuneration Committee and the Board of Directors resolve that the performance-based bonus awarded for a given year to officers (other than the Bank President & CEO or Board members) would also include equity-based remuneration, they may resolve, at their own discretion, that the performance-based remuneration to be awarded to the Bank President & CEO for the bonus year would also include equity-based remuneration.

Note 22 – Employee Rights – Continued

Eligibility of the Bank President & CEO for any performance-based remuneration, should it be awarded, would be contingent on the Bank's total capital adequacy ratio and Tier I capital adequacy ratio, in conformity with the Bank's annual financial statements for the bonus year, would not be lower than the minimum ratios stipulated by Bank of Israel directives.

The variable remuneration to be awarded to the Bank President & CEO would be subject to restitution provisions as per Section 6.10 of Addendum A to the immediate Report issued by the Bank on January 9, 2017 (reference: 2017-01-003454).

For the period starting at the end of the transition period for the Executive Remuneration Act through 2016 ("Pro rata share for 2016"), the parties decided that the Bank President & CEO's previous employment terms and conditions would continue to apply, as approved by the General Meeting of shareholders on June 10, 2014, including the monetary bonus and equity-based remuneration awarded to the Bank President & CEO pursuant to the previous remuneration policy, provided that the total remuneration to the Bank President & CEO (excluding contribution to severance pay and provident fund by law) for the pro rata share for 2016, would not exceed the (pro rata) maximum stipulated in Section 2(b) of the Executive Remuneration Act. Should the total remuneration exceed this pro rata maximum, the excess amount would be deducted from the monetary bonus to which the Bank President & CEO would be entitled (if any) for the pro rata share of 2016 and any remaining balance would be deducted from the Bank President & CEO's fixed remuneration for the pro rata share of 2016.

Either party may announce discontinuation of employment at any time during the additional employment period, for any reason and with no need to justify their position to the other party, subject to providing six months' advance notice to the other party.

During the notice period, the Bank President & CEO will be required to fully work as usual, but the Bank may waive such notice period, in whole or in part, and may terminate employment of the Bank President & CEO; in such case, the Bank will pay to the Bank President & CEO for the portion of the notice period in which the Bank waived the Bank President & CEO's work – in an amount equal to the salary for the waived period plus an amount equal to Bank contributions to provident fund, retirement fund, severance pay and study fund as stated above.

3. Officer remuneration policy

On November 19, 2013, the Supervisor of Banks issued Proper Banking Conduct Directive 301A concerning remuneration policies at banking corporations. As this directive became effective and further to discussions between the Bank and the Supervisor of Banks, the Bank has acted to revise the remuneration policy for officers, approved by the General Meeting of Bank shareholders on August 27, 2013 (hereinafter: "the original remuneration policy").

As noted, on June 10, 2014 the General Meeting of Bank shareholders approved the amended officer remuneration policy, in conformity with the resolution by the Bank’s Board of Directors, as recommended by the Remuneration Committee.

The revised remuneration policy incorporates provisions of the Companies Law and directives by the Supervisor of Banks concerning remuneration, with general principles which the Bank’s Board of Directors, after recommendations by the Remuneration Committee, saw fit to adopt with regard to officer remuneration at the Bank with due attention, *inter alia*, to the Bank's strategic plan and to current employment terms of officers at the Bank.

The remuneration of officers, other than Board members, will include two major components: A monthly salary (as well as related benefits) and variable, performance-based remuneration which will include a monetary bonus and long-term share-based remuneration. The remuneration package may also include remuneration related to retirement.

The mid-term remuneration (annual bonus) and the long-term remuneration are designed to align the interests of officers with those of the Bank and to strengthen the link between overall Bank performance and the officer's contribution to achievement of such performance to the officer's remuneration, in line with the Bank's risk profile.

As stipulated by Bank of Israel directives with regard to remuneration, the maximum variable remuneration shall not exceed 100% of the fixed remuneration. The Bank’s Board of Directors also stipulated that the maximum variable remuneration for officers who are gatekeepers would not exceed 77% of fixed remuneration and that such officers would be eligible for a retention bonus equal to two months' salary, which constitutes fixed remuneration pursuant to the remuneration policy.

The new remuneration policy incorporates the general principles which the Bank’s Board of Directors, after recommendations by the Remuneration Committee, saw fit to adopt with regard to officer remuneration at the Bank with due attention, *inter alia*, to the Bank's strategic plan and to current employment terms of officers at the Bank.

The remuneration of officers, other than Board members, will include two major components: monthly salary (and associated components) and performance-based variable remuneration (based on the Bank's performance targets, on individual performance benchmarks and including discretionary remuneration), to include a monetary bonus and which may include long-term equity-based remuneration not to exceed one half of the performance-based variable remuneration. The remuneration package may also include remuneration related to retirement.

As for the Bank President & CEO, most of the remuneration package would constitute of fixed remuneration and would also include discretionary variable remuneration, up to half of which may be in the form of equity-based remuneration, so that the total amount of discretionary variable remuneration would not exceed three months' salary.

The mid-term remuneration (annual bonus) and the long-term remuneration are designed to align the interests of officers with those of the Bank and to strengthen the link between overall Bank performance and the officer's contribution to achievement of such performance to the officer's remuneration, in line with the Bank's risk profile.

In conformity with the new remuneration policy, the maximum variable remuneration shall not exceed 85% of the fixed remuneration. The Bank’s Board of Directors also stipulated that the maximum variable remuneration for officers who are gatekeepers would not exceed 55% of fixed remuneration and that such officers would be eligible for a retention bonus equal to two months' salary, which constitutes fixed remuneration pursuant to the remuneration policy.

In conformity with the new remuneration policy, the maximum remuneration as defined in the Executive Remuneration Act (i.e. excluding payments for severance pay and provident funds by law) for the Chairman of the Board of Directors and the Bank President & CEO would be less than 35 times the lowest salary of any full-time Bank employee, including contractors. The maximum remuneration of other officers (other than Board members) would be NIS 2.5 million.

The policy stipulates that the variable remuneration may be subject to restitution, in whole or in part, under circumstances listed in the remuneration policy.

For more information about the revised remuneration policy, its principles and scope, see Addendum A to the immediate report dated January 9, 2017 (reference: 2017-01-003454), included herein by way of reference.

Given the uncertainty with regard to interpretation of the law with respect to past employee rights and in order to allow Bank officers additional time to review the legal status, the Bank Board of Directors resolved on June 20, 2016 after approval by the Remuneration Committee and recommendation by the Audit Committee with regard to the Chief Internal Auditor, to waive part of the notice period to which the Bank is entitled from the President and other officers reporting there to, including the Chief Internal Auditor, with regard to termination of their employment by the Bank, so that the notice period would be of 45 days instead of 3 months (and for one officer - instead of 6 months) according to their employment contracts - provided that such notice be given to the Bank by end of 2016. It was further stipulated that as from January 1, 2017, the notice period would once again be of 3 or 6 months, as the case may be.

4. Senior officers are eligible upon their retirement to an acclimation grant equal up to six months’ salary, for which a provision was recorded in the financial statements. Officers are also entitled to a retirement bonus at 150% per year through December 31, 2017 for officers, or through October 11, 2016 for the Bank President & CEO, all subject to provisions of the revised remuneration policy.

Note 22 – Employee Rights – Continued

5. On September 16, 2009, a special collective bargaining agreement was signed with the employee union – clerks sector, whereby the special collective bargaining agreement signed on April 27, 2006 was extended by a further 5 years, from January 1, 2011 through December 31, 2015. This agreement was approved by the Bank Board of Directors on October 19, 2009.

   Highlights of this agreement are as follows:
   - Extension of the "employment constitution" through December 31, 2015.
   - Maintaining absolute calm labor relations during the agreement period. The obligation to maintain calm labor relations shall not apply in case of a labor dispute involving all bank sector employees in Israel.
   - Specification of dispute resolution mechanisms: negotiation, facilitation, arbitration.
   - The Bank committed not to terminate for economic reasons any permanent employees during the term of the agreement. This commitment does not apply to individual termination for cause, incompatibility or regulatory changes.
   - Enactment of a voluntary retirement program by up to 200 employees during the term of the agreement, starting in 2011. Management has the right to veto any specific voluntary retirement application without being required to provide any justification.
   - Management has the option of terminating up to 50 permanent employees during the term of the agreement period, for incompatibility reasons, starting in 2011.

   In late 2015, an economic arbitration process was launched between the Bank and the employee union, to discuss the demands made by the employee union for 2005-2015.

   In 2016, the arbitrators tried to move the discussion of employee union demands to a reconciliation process. This attempt was un-successful and in late 2016, the issue was referred back to arbitration.

   Moreover, concurrently with the economic arbitration, there are negotiations under way to renew the payroll agreement between Bank management and the employee union for 2016-2020.

   Due to disagreement with the employee union with regard to the value per hour for calculating extra time, since the parties failed to reach agreement in the reconciliation process, in 2016 the parties launched an arbitration proceeding on this matter. In December 2016, the arbitration verdict was given and the Bank is acting to implement it.

   The Bank made appropriate provisions for these matters.

6. Some Bank employees who take early retirement, sometimes receive, upon retirement, higher amounts than their entitlement pursuant to the law and to agreements. Sometimes the Bank pays these employees a pension until they reach the full retirement age. According to the Supervisor of Banks' directive, an actuarial reserve with respect to these payments is included on the financial statements.

7. On December 27, 2016, the Bank’s Board of Directors approved the streamlining plan recommended by Bank management, whereby early retirement would be possible for 300 employees in 2017-2021, at improved conditions.

   Note that the retiring employees, who would be allowed to take such early retirement, include Bank employees and 50 employees of a wholly-owned and wholly-controlled subsidiary of the Bank, the Mizrahi-Tefahot Technology Division Ltd. The number of retiring employees from each group may change, but the total number will not exceed 300.

   Bank management is in negotiations with the employee union with regard to the retirement program and as a first step, has started implementation of the plan in the Mizrahi Tefahot Technology Division Ltd., pending agreement with the employee union at the Bank.

Note 22 – Employee Rights – Continued

In conformity with the streamlining plan, the retiring employees would be entitled to an early pension through the official retirement age or to increased severance pay at 150% (in addition to receiving ownership of provident fund accounts in their name), based on the criteria listed in the plan. It is possible that retirement terms and conditions could offer additional, non-material benefits to such employees.

The cost of update to the actuarial liability with respect to the streamlining plan, recorded on the financial statements as of December 31, 2016, amounts to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity (under Other Comprehensive Income).

8. A small group of employees who retired in the past is entitled to a fixed monthly pension from the Bank. Employees who retired from the Bank prior to June 30, 1997 are entitled to pension payments from the Bank for certain salary components. Bank retirees are also eligible to receive non-pension benefits. The Bank's liability for these payments is covered by provisions, based on an actuarial calculation.

9. Personal employment contracts have been signed with a group of senior employees, entitling them to a special bonus upon termination, under the circumstances prescribed in the agreements that could, in a few years' time, reach seventeen months' salary for certain employees with high seniority. These employees are entitled upon retirement to moneys and other rights accrued on their behalf in various funds as well as to advance termination notice three to six months in advance. The Bank has no intention to terminate any of these senior Bank employees.

   The Bank's liability for these payments is covered by provisions, based on an actuarial calculation.

10. A senior Bank employee is eligible, upon leaving the Bank, to early retirement pension at 70% of the amount specified in a special agreement dated 2010, linked to the Consumer Price Index. for which a provision was recorded in the financial statements.

11. Reserves with respect to long-service bonuses and voluntary retirement programs were made based on an actuarial calculation, with the discount rate based on the yield of Government debentures in Israel plus the average yield spread for corporate debentures rated AA (international rating scale) or higher upon the report date. For practical reasons, the spread would be determined by the difference between yields to maturity, by terms to maturity, for corporate debentures rated AA or higher in the USA – and yields to maturity, for the same terms to maturity, for US government debentures, all as of the reporting date.

    The calculation takes into account future real increase in pay of between 1.7%-3.5%.

    The provision with respect to voluntary retirement was calculated in conformity with the retirees' eligibility to have their pension linked to the Consumer Price Index.

12. Long-service bonuses

    Bank employees are entitled to special lump-sum bonuses upon attaining thirteen and eighteen years of service. A provision for these liabilities was recorded in the financial statements according to an actuarial calculation based on past experience and the likelihood that the employee will still be employed by the Bank on the vesting date.

13. Reserve with respect to tuition pay

    Bank employees under the collective bargaining agreement are entitled to tuition reimbursement for biblical studies and for higher education, based on reimbursement percentage customary at the Bank. A provision for these liabilities was recorded in the financial statements according to an actuarial calculation based on past experience and the likelihood that the employee is still employed by the Bank.

Note 22 – Employee Rights – Continued

14. Bonuses for all Bank employees

    On June 19, 2014, the Bank's Board of Directors, based on recommendations by the Remuneration Committee, approved a remuneration policy for all Bank employees other than officers. The remuneration policy is based on Proper Banking Conduct Directive 301A with regard to remuneration policy at banking corporations (hereinafter: "the remuneration policy").

    The remuneration policy discusses remuneration terms of key employees at the Bank and those of other managers at the Bank and of other Bank employees for 2014-2016.

    The terms of office or employment of Bank employees include fixed and variable remuneration, as customary at the Bank, as well as retirement terms and any other benefit, payment or commitment to make a payment, provided with respect to the aforementioned office or employment.

15. Bank Yahav has a defined benefit plan, funded and unfunded, with respect to all employees thereof. The plan provides a defined benefit based on years of service and most recent salary.

    Bank Yahav's obligation to pay severance or retirement pay is primarily covered by current deposits based on the salary for pension purposes to official provident and pension funds in the name of the employees. Bank Yahav customarily makes up the difference, for employees eligible to receive severance pay, between the employee's most recent salary multiplied by their number of years in service and the amount accrued in their name in the aforementioned provident funds. Bank Yahav may not withdraw the funded amounts other than for severance payment.

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

B. Liability amounts with respect to benefits by type:

		December 31,
	2016	2015
		NIS in millions
Post-retirement benefits[1]		
Liability amount	149	141
Excess liability over plan assets	149	141
Benefits post termination and prior to retirement[2]		
Liability amount	[3]1,006	726
Fair value of plan assets	112	104
Excess liability over plan assets	894	622
Benefits prior to termination[4]		
Liability amount	76	64
Excess liability over plan assets	76	64
Total		
Excess liability included under Other Liabilities	1,119	827
Of which: With respect to overseas employee benefits	11	10

(1) Holiday gifts and other post-retirement employee benefits

(2) Pension, severance pay and other benefits on defined-benefit plan, including balance of liability with respect to employees who have retired.

(3) Includes effect of the streamlining plan, for more information see section 7 below.

(4) Primarily jubilee bonus and tuition for current employees.

Note 22 - Employee Rights - Continued

C. Defined benefit plans (pension, severance pay and other benefits)(1)

1. Obligations and funding status

1.1. Change in obligations with respect to expected benefit

		December 31,
	2016	2015
		NIS in millions
Obligation with respect to expected benefit at start of period	867	871
Cost of service	26	26
Cost of interest	31	31
Actuarial loss(2)	303	7
Benefits paid	(72)	(68)
Obligation with respect to expected benefit at end of period	1,155	867
Obligation with respect to cumulative benefit at end of period(3)	1,066	816

1.2. Change in fair value of plan assets and plan funding status

		December 31,
	2016	2015
		NIS in millions
Fair value of plan assets at start of period	104	99
Actual return on plan assets	3	1
Deposits to plan by the banking corporation	6	6
Benefits paid	(1)	(2)
Fair value of plan assets at end of period	112	104
Funding status – net asset recognized at end of period	112	104

(1) Post-employment pre-retirement benefits and post-retirement benefits, including balance of liability with respect to employees who have retired.

(2) On December 27, 2016, the Bank Board of Directors approved the streamlining plan. For more information, see section 7 below.

(3) Excludes any assumptions with regard to future remuneration.

Note 22 - Employee Rights - Continued

C. Defined benefit plans (pension, severance pay and other benefits)[1]

1. Obligations and funding status – continued

1.3. Amounts recognized on the consolidated balance sheet

		December 31,
	2016	2015
		NIS in millions
Amounts recognized under Other Liabilities	1,043	763
Net liability recognized on the balance sheet at end of period	1,043	763

1.4. Amounts recognized under Other Comprehensive Income (Loss), before tax effect

		December 31,
	2016	2015
		NIS in millions
Net actuarial loss	(452)	(150)
Net liability with respect to transition	–	(8)
Total - recognized under Other Comprehensive Income	(452)	(158)

1.5. Plans for which the obligation with respect to cumulative and expected benefit exceeds plan assets

		December 31,
	2016	2015
		NIS in millions
Obligation with respect to expected benefit	1,155	867
Obligation with respect to cumulative benefit	1,066	816
Fair value of plan assets	112	104

Note 22 – Employee Rights – Continued

C. Defined benefit plans (pension, severance pay and other benefits)[1]

2. Expenses during the reported period

2.1. Net benefit cost components recognized on Profit and Loss

	For the year ended December 31,		
	2016	2015	2014
			NIS in millions
Cost of service	26	26	20
Cost of interest	31	31	28
Expected return on plan assets	(4)	(4)	(4)
Deduction of non-allowed amounts:			
Net actuarial loss	9	4	1
Total benefit cost, net	62	57	45

2.2. Changes to obligation recognized under Other Comprehensive Income (Loss), before tax effect

	For the year ended December 31,		
	2016	2015	2014
			NIS in millions
Net actuarial loss for the period	303	7	47
Amortization of actuarial loss[2]	(9)	(4)	(1)
Total – recognized under Other Comprehensive Income	294	3	46
Total benefit cost, net	62	57	45
Total recognized under benefit cost, net for the period and under Other Comprehensive Income	356	60	91

2.3. Estimated amounts included under Cumulative Other Comprehensive Income expected to be deducted from Cumulative Other Comprehensive Income to the Statement of Profit and Loss as expense in 2017, before tax effect

	NIS in millions
Net actuarial loss	16
Total expected to be deducted from Cumulative Other Comprehensive Income	16

(1) Post-employment pre-retirement benefits and post-retirement benefits, including balance of liability with respect to employees who have retired.

(2) Actuarial loss due to current changes in discount rates during the reported year and actuarial gains due to current changes in discount rates during the reported year after the loss balance as of the transition date has been decreased to zero, would be amortized using the straight line method over the remaining average terms of service for employees expected to receive benefits over the plan term or, alternatively, over the average remaining term for receipt of benefits by employees. See also Note 1.D.13 to the financial statements.

Note 22 – Employee Rights – Continued

D. Assumptions

1. Assumptions based on weighted average, used to determine the obligation with respect to benefit and to measure the benefit cost, net

1.1. Key assumptions used to determine the obligation with respect to benefit:

	December 31,	
	2016	2015
		In %
Discount rate	1.70	2.00
Discount rate – CPI	2.00	2.00
Departure rate	3.40	4.20
Remuneration increase rate	1.72	1.75

1.2. Key assumptions used to measure benefit cost for the period (in %):

			December 31,
	2016	2015	2014
			In %
Discount rate	4.18	4.17	4.17
Expected long-term return on plan assets	4.07	4.08	4.68
Remuneration increase rate	1.72	1.75	1.75

1.3. Effect of change of 1 percentage point on obligation with respect to expected benefit, before tax effect:

	Increase by 1 percentage point		Decrease by 1 percentage point	
	December 31,		December 31,	
	2016	2015	2016	2015
Discount rate	(94)	(61)	113	74
Departure rate	54	82	(76)	(100)
Remuneration increase rate	65	44	(55)	(36)

Note 22 – Employee Rights – Continued

E. Plan assets

1.1. Fair value composition of plan assets

Property type	December 31,	
	2016	2015
Shares	42	21
Government assistance to legacy pension funds	11	11
Other	8	10
Debentures: Government	15	20
Designated Government	12	23
Corporate	24	19
Total	112	104

1.2 Fair value of plan assets by asset type and allocation target for 2017 (in %)

	Allocation target	Percentage of plan assets	
Property type	For	As of December 31	
	2017	2016	2015
Shares	36	38	21
Government assistance to legacy pension funds	11	10	10
Other	8	7	9
Debentures: Government	14	14	20
Designated Government	10	10	22
Corporate	21	21	18
Total	100	100	100

1.3 Deposits to defined-benefit pension plans

	Allocation target	Actual deposits	
Property type	For	For the year ended December 31,	
	(1)2017	2016	2015
Deposits	6.0	6.2	6.0

(1) Estimated deposits to be paid into defined-benefit pension plans in 2017.

F. Cash flows – Benefits which the corporation expects to pay in future:

Year	NIS in millions
2017	93
2018	94
2019	94
2020	94
2021	94
2022-2026	315
2027 and later	606
Total	1,390

Note 23 – Share-based Payment Transactions

A. Stock option plan for the President

As part of the option plan and in conformity with its terms and conditions, the Bank will allot to a trustee, on behalf of the Bank President & CEO, options in three annual lots as follows: 186,915 options for 2014, 177,720 options for 2015 and 172,503 options for 2016. Each option may be exercised for one Bank ordinary share of NIS 0.1 par value, subject to adjustments for bonus share distribution, rights issuance, share split or reverse-split, dividend distributions etc.

Assuming full exercise of all options, and assuming allotment of the maximum possible number of exercise shares, all options allotted under the stock option plan to the Bank President pursuant to the option plan (based on the report "Equity status and securities registries of the corporation and changes there to", issued by the Bank on April 10, 2014) would be equal to 0.23% of the Bank's issued share capital and voting rights (after allotment of the full number of exercise shares), and assuming full dilution – 0.18% of the Bank's issued share capital and voting rights.

The President & CEO's eligibility for options allotted with respect to any bonus year is contingent on the following threshold conditions being fulfilled for the bonus year:

1. Return on equity for the bonus year shall be at least 9%.
2. Overall capital adequacy ratio and core capital adequacy ratio for the Bank, for the bonus year, shall be no less than the minimum ratios specified in Bank of Israel regulations.

The Bank President's eligibility for options included in any annual lot would be calculated soon after publication of the Bank's financial statements for the bonus year for which the annual lot has been allotted, based on fulfillment of the specified eligibility conditions.

Each of the annual lots for 2014-2016 would vest in three equal parts as from April 1 of 2016-2020.

The exercise price for each option to be allotted to the Bank President pursuant to the plan is NIS 46.19 plus CPI linkage differentials, from the known CPI upon approval by the Board of Directors to the known CPI upon the exercise date. The exercise price was determined based on the average closing price per Bank ordinary share on the stock exchange over the thirty trading days preceding the date of approval by the Board of Directors. Accordingly, note that on the exercise date, the Bank President would not be required to pay the exercise price – which would only serve to determine the monetary benefit amount and the number of exercise shares actually allotted to the Bank President.

For calculation of fair value as of approval of the option award by the General Meeting of Bank shareholders, as noted above, the following terms of the option plan were taken into account as well as annualized standard deviation between 26.7%-32.1%, reflecting the standard deviation for periods of 3.41-7.42 years. Risk-free interest ranges between (0.82%)-0.55% for the various lots.

Based on these assumptions, the average fair value of each option awarded to the Bank President pursuant to the option plan, as of the approval date of option award by the General Meeting of Bank shareholders, is as follows: Options included in the first lot – NIS 7.90; options included in the second lot – NIS 8.37; options included in the third lot – NIS 8.67.

Accordingly, the theoretical benefit value of the options in this plan (the fair value), calculated in accordance with accounting standards, amounts to NIS 4.5 million (NIS 5.3 million including Payroll Tax). This value will be recognized over the eligibility period in non-linear fashion.

The options would be allotted under the "wages" track, pursuant to the Section 102 of the Income Tax Ordinance. Therefore, any benefit arising to the Bank President from exercise of these options shall be taxed at the marginal tax rate applicable to the Bank President upon exercise of the options. The Bank would be required to pay the payroll tax with respect to the benefit arising to the President from exercise of the options under the stock option plan. Furthermore, upon payment of the tax with respect to this benefit by the Bank President & CEO, the Bank may make a deduction for tax purposes with respect to the aforementioned options based on the effective tax rate applicable upon the exercise date.

In conformity with financial results for 2015, in 2016 some 58,141 options (2015: 72,843 options) with an exercise price of NIS 46.19 (similar to 2015) were forfeited. As of December 31, 2016, the President & CEO has a total of 406,154 options (2015: 464,295 options) at an exercise price of NIS 46.19 (same as in 2015).

B. Stock option plan for VPs

On March 29, 2009, the Bank Board of Directors, after obtaining approval of the Bank Audit Committee, decided to approve a plan for allotment of options by private placement which does not constitute a material private placement (hereinafter: "the plan") to nine officers of the Bank who are VP members of Bank management (of which one offeree who had served as VP, took unpaid leave from the Bank and currently serves as the CEO of Bank Yahav for Government Employees Ltd.) (hereinafter: "the offerees"). The Board of Directors further decided, after obtaining approval of the Audit Committee, that allotment of the options is contingent on the Supervisor of Banks allowing the Bank to buy back at least 1,400,000 shares of NIS 0.1 par value in the Bank's issued share capital. For details of 2,500,000 Bank shares bought back by the Bank in accordance with approval of the Supervisor of Banks, see Note 24.D below.

In conjunction with the stock option plan, the Bank allotted on June 23, 2009 to the trustee, on behalf of the offerees, 5,850,000 options which would not be listed for trading on the stock exchange. The options may each be exercised for one Bank ordinary share of NIS 0.1 par value for no consideration, subject to terms and conditions of the plan. Allotment of the maximum number of exercise shares is only theoretical. Upon the exercise date of the options, offerees would not be allotted the full number of exercised shares arising from the options which the offerees may exercise, pursuant to plan terms, but rather only the number of shares reflecting the monetary benefit inherent in the aforementioned options.

The exercise price for each option allotted to offerees pursuant to the plan is NIS 21.18, plus CPI linkage differentials, adjusted for any dividends or bonus shares to be distributed by the Bank. The exercise price was determined based on the closing price of Bank shares on the stock exchange on November 9, 2008 – which was also the basis for the exercise price of options allotted to the Bank President as stated above. Note that the exercise price is higher than the closing price of Bank shares on the stock exchange on March 26, 2009 – the most recent trading day prior to the date on which the Board of Directors approved the stock option plan.

The options allotted to the trustee for each offeree, in accordance with the plan, were allotted in 5 equal lots. Each lot shall vest upon vesting dates on each anniversary of the allotment date, from the first anniversary (for the first lot) to the fifth anniversary (for the fifth lot).

The number of options which the offerees may exercise shall be reviewed upon each reporting date, based on information available at that time. The results of this review may reduce the expense charged in the Bank's financial statements with respect to options over plan years, but may not change the fair value of each option included in each lot.

On November 9, 2009, the Bank Board of Directors, after obtaining approval by the Bank Audit Committee, resolved to approve allotment of a further 1,104,999 options, under identical terms and conditions with the exception of the exercise price, to two VPs appointed subsequent to the approval date of the stock option plan for VPs.

On April 30, 2012, the Bank’s Board of Directors resolved, after approval by the Bank Audit Committee, to approve a plan for award of 238,333 options to an officer who was hired by the Bank in March 2012. The option plan is based on the principles of the stock option plan for VPs at the Bank, as described above.

Options will awarded in 2 lots vesting on three dates ("vesting dates") starting on the first anniversary (lot 1) and second anniversary (lot 2) of the award date, subject to net profit rate of return on average equity for each year preceding each vesting date, as stated above.

Note 23 – Share-based Payment Transactions – continued

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted:

	Lot 1	Lot 2	Lot 3	Lot 4	Lot 5	Total
Allotment approved on March 29, 2009						
Number of options (in thousands)	910	910	910	650	650	4,030[(1)]
Annualized standard deviation	32.75%	32.04%	30.95%	30.11%	30.27%	
Exercise price (in NIS)	21.18	21.18	21.18	21.18	21.18	
Risk-free interest rate	0.65%	0.77%	0.92%	1.09%	1.28%	
Term to exercise (in years)	4.10	4.60	5.10	5.60	6.10	
Fair value per single option	4.78	5.02	5.19	5.39	5.77	
Total fair value per lot (NIS in thousands)	4,346	4,569	4,724	3,504	3,751	20,894
Allotment approved on November 9, 2009						
Number of options (in thousands)	65	260	260	260	260	1,105
Annualized standard deviation	35.00%	34.00%	33.00%	33.00%	32.00%	
Exercise price (in NIS)	29.85	29.85	29.85	29.85	29.85	
Risk-free interest rate	0.46%	0.65%	0.83%	1.02%	1.20%	
Term to exercise (in years)	3.60	4.10	4.60	5.10	5.60	
Fair value per single option	8.00	8.39	8.73	9.16	9.44	
Total fair value per lot (NIS in thousands)	520	2,181	2,270	2,381	2,455	9,807
Allotment approved on April 30, 2012						
Number of options (in thousands)	–	–	–	108	130	238
Annualized standard deviation	–	–	–	30.23%	32.27%	
Exercise price (in NIS)	–	–	–	33.79	33.79	
Risk-free interest rate	–	–	–	0.20%	0.30%	
Term to exercise (in years)	–	–	–	2.70	3.20	
Fair value per single option	–	–	–	6.63	7.75	
Total fair value per lot (NIS in thousands)	–	–	–	718	1,008	1,726

(1) After expiration of 1,820 thousand options with respect to four VPs who resigned from the Bank.

Note 23 – Share-based Payment Transactions – continued

Details of the number of stock options and their exercise price are as follows:

	2016		2015		2014	
	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)
Outstanding at year start	60,000	21.57	545,000	26.48	1,346,666	26.83
Exercised during the year(1)	60,000	21.27	485,000	26.74	801,666	26.96
Outstanding at year end	–	–	60,000	21.57	545,000	26.48

(1) The weighted average share price upon exercise of options into shares during 2016 was NIS 44.75 (2015 - NIS 47.94; 2014 - NIS 44.51).

C. Stock option plan for employees

1. On May 19, 2008, the Bank's Board of Directors resolved, after obtaining approval of the Bank" Audit Committee and the recommendations of the Bank Board's Compensation and Management Committees with regard to principles of the stock option plan, to approve a stock option plan ("the plan" or "the option plan") for Bank officers, branch-, department- and affiliate managers as well as for other employees of the Bank and its subsidiaries – as stated in the option plan and in the outline published on June 8, 2008 ("the outline"). No stock options will be awarded, pursuant to the plan, to members of the Bank Board of Directors, including the Chairman of the Board, nor to the Bank President.

   The option plan is for a term of 5 years and 90 days, starting on the date of option allotment in accordance with the plan. In conjunction with approval of the plan, the Board of Directors resolved that the number of options to be used as a pool for allotment of options pursuant to the plan, would include 32,500,000 options, registered in the owner's name, not listed for trading on the Tel Aviv Stock Exchange, which would be granted at no cost to offerees, and which may be exercised for up to 32,500,000 Bank ordinary shares, NIS 0.1 par value each, subject to adjustments as specified in the plan, and subject to achieving the eligibility conditions stated there

   The options allotted to the trustee for each offeree, in accordance with the plan, will be allotted in 5 equal lots. The vesting period for each such lot will be at the end of each of the 1st, 2nd, 3rd, 4th and 5th anniversaries of the allotment date of options pursuant to the plan, respectively. The number of exercised shares, as stated, is the maximum number of shares arising from exercise of all options which may be allotted pursuant to the plan. However, the number of options which the offerees may actually exercise, pursuant to terms of the plan, will be based on the net operating profit return on the Bank's average shareholders' equity, up to an annual rate of return equal to 18% (under the original plan), based on the exercise eligibility formula, as set forth in the option plan.

   The personal eligibility rate for each offeree included in the group of branch-, department- and affiliate managers (as defined in the plan) to exercise the options granted to them in accordance with the plan will be determined, in addition to the aforementioned, also by the quality rating assigned to them, as set forth in the option plan.

   Furthermore, allotment of the full number of exercised shares is merely theoretical, since in actual fact the offerees would not be allotted the full number of exercised shares arising from the options which the offerees may exercise, pursuant to plan terms, but rather only the number of shares reflecting the monetary benefit inherent in the aforementioned options, as stated in the option plan.

   On July 8, 2008, 28,625,300 options were allotted, in accordance with the plan, at no cost to 313 offerees who are Bank officers, branch-, department- and affiliate managers, as well as other employees of the Bank and its subsidiaries, as stated in the option plan.

The options pursuant to the plan were allotted in accordance with terms of the work income track, via a trustee, pursuant to provisions of Section 102 of the Income Tax Ordinance (New Version), 1961 including all regulations, rules, circulars and guidelines issued based there upon.

On November 24, 2008, the Board of Directors resolved, after receiving approval of the Bank Audit Committee dated November 23, 2008, to extend the exercise periods of all options allotted in accordance with the plan and the framework, and which would be allotted thereby in the future, by 24 months.

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted on July 8, 2008, as of the grant date and as of the date of modification of terms:

	Lot 1	Lot 2	Lot 3	Lot 4	Lot 5
As of July 8, 2008 – the grant date					
Annualized standard deviation	26.05%	26.23%	25.44%	24.71%	24.98%
Exercise price (in NIS)	25.15	25.15	25.15	25.15	25.15
Interest	2.03%	2.20%	2.34%	2.47%	2.58%
Term to exercise (in years)	3.10	3.60	4.10	4.60	5.10
Fair value per single option	5.25	5.79	6.13	6.45	6.95
As of November 24, 2008 – for the original exercise period (exercise price unchanged)					
Annualized standard deviation	29.84%	29.22%	28.76%	28.35%	27.43%
Share price	15.70	15.70	15.70	15.70	15.70
Exercise price	25.70	25.70	25.70	25.70	25.70
Interest	4.08%	4.11%	4.13%	4.15%	4.16%
Term to exercise (in years)	2.75	3.25	3.75	4.25	4.75
Fair value per single option	1.17	1.43	1.69	1.94	2.12
As of November 24, 2008 – for the updated exercise period (exercise price unchanged)					
Annualized standard deviation	28.76%	28.35%	27.43%	26.77%	27.18%
Share price	15.70	15.70	15.70	15.70	15.70
Exercise price	25.70	25.70	25.70	25.70	25.70
Interest	4.13%	4.15%	4.16%	4.18%	4.19%
Term to exercise (in years)	3.75	4.25	4.75	5.25	5.75
Fair value per single option	1.69	1.94	2.12	2.32	2.66
Value of change per single option	0.52	0.51	0.43	0.38	0.54
Cumulative value per single option	5.77	6.30	6.56	6.83	7.49

On June 29, 2009, the Bank Board of Directors approved allotment of a further 2,263,700 options, under identical terms and conditions except for the exercise price, to two officers and 37 additional employees.

On November 9, 2009, the Bank Board of Directors, after receiving approval of the Bank Audit Committee, resolved to approve allotment of a further 1,085,432 options, under identical terms and conditions with the exception of the exercise price, to four officers of the Bank.

On October 26, 2010, the Bank's Board of Directors, after receiving approval of the Bank's Audit Committee, resolved to approve a plan for allotment of a further 1,652,500 options, under identical terms and conditions with the exception of the exercise price, to 41 employees, including one officer of the Bank. Options would be allotted in 3 equal lots vesting on three dates ("vesting dates") starting on the first anniversary (lot 1), second anniversary (lot 2) and third anniversary (lot 3) of the allotment date, subject to net profit rate of return on average equity for each year preceding each vesting date, as stated above.

On October 3, 2011, the Bank's Board of Directors, after receiving approval of the Bank's Audit Committee, resolved to approve a plan for allotment of a further 701,300 options, under identical terms and conditions with the exception of the exercise price, to 31 employees, including one officer of the Bank. Options would be allotted in 2 equal lots vesting on three dates ("vesting dates") starting on the first anniversary (lot 1) and second anniversary (lot 2) of the allotment date, subject to net profit rate of return on average equity for each year preceding each vesting date, as stated above.

The options were allotted to employees on November 17, 2011.

Note 23 – Share-based Payment Transactions – continued

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots awarded on June 28, 2009, on November 9, 2009, on October 26' 2010 and on October 3, 2011:

	Lot 1	Lot 2	Lot 3	Lot 4	Total
Allotment approved on June 29, 2009					
Number of options (in thousands)	566	566	566	566	2,264
Annualized standard deviation	34.27%	33.29%	32.65%	31.55%	
Exercise price (in NIS)	23.60	23.60	23.60	23.60	
Risk-free interest rate	0.91%	1.20%	1.50%	1.71%	
Term to exercise (in years)	3.70	4.20	4.70	5.20	
Fair value per single option	6.40	8.75	7.15	7.45	
Total fair value per lot, NIS in thousands	3,622	3,820	4,046	4,194	15,682
Allotment approved on November 9, 2009					
Number of options (in thousands)	248	279	279	279	1,085
Annualized standard deviation	34.88%	33.92%	33.15%	32.45%	
Exercise price (in NIS)	29.85	29.85	29.85	29.85	
Risk-free interest rate	0.49%	0.68%	0.87%	1.05%	
Term to exercise (in years)	3.70	4.20	4.70	5.20	
Fair value per single option	8.05	8.43	8.82	9.21	
Total fair value per lot, NIS in thousands	2,000	2,352	2,461	2,569	9,382
Allotment approved on October 26, 2010					
Number of options (in thousands)	–	551	551	551	1,653
Annualized standard deviation	–	36.73%	35.07%	33.88%	
Exercise price (in NIS)	–	35.40	35.40	35.40	
Risk-free interest rate	–	0.22%	0.38%	0.53%	
Term to exercise (in years)	–	3.20	3.70	4.20	
Fair value per single option	–	9.23	9.55	9.92	
Total fair value per lot (NIS in thousands)	–	5,084	5,260	5,464	15,808
Allotment approved on October 3, 2011					
Number of options (in thousands)	–	–	351	351	702
Annualized standard deviation	–	–	31.93%	36.90%	
Exercise price (in NIS)	–	–	31.62	31.62	
Risk-free interest rate	–	–	1.07%	1.13%	
Term to exercise (in years)	–	–	2.71	3.21	
Fair value per single option	–	–	6.93	8.63	
Total fair value per lot (NIS in thousands)	–	–	1,700	2,783	4,483

Note 23 – Share-based Payment Transactions – continued

Details of the number of stock options and their exercise price are as follows:

	2016		2015		2014	
	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)
Outstanding at year start	222,441	34.72	1,549,740	29.93	2,163,977	30.11
Awarded during the year	–	–	–	–	–	–
Expired during the year	–	–	91,167	33.61	–	–
Forfeited during the year	–	–	–	–	–	–
Exercised during the year[1]	222,441	34.58	1,236,132	28.38	614,237	30.42
Outstanding at year end	–	–	222,441	34.72	1,549,740	29.93

(1) The weighted average share price upon exercise of options into shares during 2016 was NIS 43.84 (2015 - NIS 46.32; 2014 - NIS 45.47).

(2) On April 29, 2013, the Bank's Board of Directors, after receiving approval of the Bank's Audit Committee, resolved to approve a plan for allotment of a further 5,921,340 options to 330 offerees who are employees of the Bank and its subsidiaries but who are not officers of the Bank. The option plan is based on the principles of the stock option plan for employees at the Bank.

The stock option plan is based on the format and principles of the employee stock option plans approved by the Bank in 2008 through 2011, whereby the Bank allocated options on July 8, 2008, on September 24, 2009, on December 5, 2010 and on November 17, 2011. Terms of the aforementioned options were listed in detail in outlines made public by the Bank, as amended. The stock option plan pursuant to this outline is intended for Bank employees other than officers and to employees of Bank subsidiaries. For more information see Note 23.C.1. below.

The number of options which offerees may actually exercise, pursuant to plan terms and conditions, is derived from the average rate of net operating profit return on equity for the Bank, based on the formula for exercise eligibility – all as described and similar to plans approved in 2008 through 2011.

The options were awarded in one lot, exercisable as from the first anniversary through 90 days after the second anniversary of the award date. Subject to the average rate of net operating profit return on equity for the Bank, as described above.

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted:

Number of options	5,901,340
Annualized standard deviation	31.36%
Exercise price (in NIS)	36.60
Risk-free interest rate	(0.18%)
Term to exercise (in years)	1.71
Fair value per single option	5.894
Total fair value per grant (NIS in thousands)	34,899

Note 23 – Share-based Payment Transactions – continued

Details of the number of stock options and their exercise price are as follows:

	2016		2015		2014	
	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)
Outstanding at year start	–	–	2,353,390	36.67	5,860,240	36.71
Awarded during the year[(1)]	–	–	–	–	–	–
Forfeited during the year	–	–	–	–	2,828,487	36.68
Exercised during the year[(2)]	–	–	2,353,390	36.44	678,363	36.71
Outstanding at year end	–	–	–	–	2,353,390	36.67

(1) The weighted average fair value of stock options granted in 2013, as of the measurement date, was NIS 5.54.

(2) The weighted average share price upon exercise of options into shares during 2015 was NIS 45.75 (2014 – NIS 44.49).

3. On June 10, 2014, the General Meeting of Bank shareholders approved, after approval by the Board of Directors and recommendation by the Remuneration Committee, the revised officer remuneration policy at the Bank (for details see section C. above).

On June 19, 2014, the Bank's Board of Directors approved, after approval by the Remuneration Committee on June 16, 2014, the offering of options to Bank officers, pursuant to section 15B(1)(a) of the Securities Act. Further, the Bank's Board of Directors approved, after approval by the Remuneration Committee, an option offering to key Bank employees and to other managers of the Bank and its subsidiaries, pursuant to section 15B(1)(a) of the Securities Act, all as delisted a report issued by the Bank on June 19, 2014, reference 2014-01-091176 (hereinafter: "the outline report").

As resolved by the Board of Directors on June 19, 2014, the following option plans were approved:

- Option plan A – up to 2,083,197 options A to be awarded to up to eight Bank officers who are not gatekeepers, exercisable for up to 2,083,197 Bank ordinary shares of NIS 0.1 par value each.
- Option plan B – up to 873,066 options B to be awarded to up to five Bank officers who are gatekeepers, exercisable for up to 873,066 Bank ordinary shares of NIS 0.1 par value each.
- Option plan C – up to 2,708,060 options C to be awarded to up to forty-three key Bank employees and up to ten managers at Bank subsidiaries, which have been approved for inclusion in this group, exercisable for up to 2,708,060 Bank ordinary shares of NIS 0.1 par value each.
- Option plan D – up to 1,183,110 options D to be awarded to up to twenty-eight managers employed by the Bank subject to individual employment contracts and up to eight managers at Bank subsidiaries, which have been approved for inclusion in this group, exercisable for up to 1,183,110 Bank ordinary shares of NIS 0.1 par value each.
- Option plan E – up to 5,046,390 options E to be awarded to up to two hundred fifty-three managers employed by the Bank subject to collective bargaining agreements, exercisable for up to 5,046,390 Bank ordinary shares of NIS 0.1 par value each.

The number of exercise shares, as stated above, is the maximum number of shares arising from exercise of all options which may be issued pursuant to all plans. However, the number of options which offerees may actually exercise, pursuant to terms and conditions of each plan, would be derived from the eligibility terms set for each plan, as follows. Furthermore, allotment of the maximum number of exercise shares is but theoretical, since in actual fact the Bank would not allot to the offerees the full number of exercise shares arising from the options which the offerees may exercise pursuant to terms and conditions of each plan – but only the number of shares reflecting the monetary benefit inherent in those options, based, *inter alia*, on the closing price cap of NIS 80 plus linkage differentials from the known CPI upon approval by the Board of Directors to the known CPI upon the exercise date.

Also note that the number of exercise shares for each plan is subject to adjustments for bonus share distribution, rights issuance, share split or reverse-split, dividend distributions etc.

The options to be issued in the name of the trustee for each officer, pursuant to option plans A or B, would be divided into three annual lots, one for each bonus year. The total number of options in each annual lot of options A, awarded to all officers who are not gatekeepers, is: 728,451 options for 2014; 689,523 options for 2015; and 665,223 options for 2016.

The total number of options in each annual lot of options B, awarded to all officers who are gatekeepers, is: 314,100 options for 2014; 284,136 options for 2015; and 274,830 options for 2016.

The options to be issued in the name of the trustee for each officer, pursuant to option plans C, D or E, would be divided into three equal annual lots, one for each bonus year. Each of the annual lots would vest in three equal portions as from April 1 of 2016-2020, as state din the outline report.

Each of the annual lots for options D and E would vest as follows:

- The adjusted annual lot for 2014 may be exercised from the first anniversary of the option issuance date through 4.5 years thereafter.
- The adjusted annual lot for 2015 may be exercised from the second anniversary of the option issuance date through 4.5 years thereafter.
- The adjusted annual lot for 2016 may be exercised from the third anniversary of the option issuance date through 4.5 years thereafter.

Threshold conditions and eligibility conditions for options

An offeree's eligibility for options pursuant to each of the aforementioned option plans, for any bonus year, is contingent on fulfillment of all of the following threshold conditions in the bonus year:

- Return on equity for the bonus year shall be at least 9%.
- Overall capital adequacy ratio and core capital adequacy ratio for the Bank, for the bonus year, shall be no less than the minimum ratios specified in Bank of Israel regulations.

In addition, eligibility conditions for options would be based on the following criteria:

– Options A and options B to be issued to offerees who are officers of the Bank, as noted above, constitute part of these officers' variable remuneration. Officer eligibility to options A or to options B included in any annual lot would be determined based on four criteria which are measurable "company-wide criteria" (hereinafter: "the quantitative benchmarks") and on two qualitative criteria based on supervisor assessment of achievement of individual targets (hereinafter: "the individual targets") of the officer specified in the employee offering outline and on assessment of the officer's performance by the supervisor at the latter's discretion (hereinafter: "supervisor's discretion"). The individual targets and supervisor's discretion, hereinafter: "the qualitative benchmarks").

  The total weight assigned to quantitative benchmarks would be 80% of the annual lot of options A or options B. The total weight assigned to the qualitative benchmarks would be 20%: the weight assigned to the individual target benchmark would be 10% and the weight assigned to the supervisor's discretion benchmark would be 10%.

Note 23 – Share-based Payment Transactions – continued

Eligibility of offerees who are not officers of the Bank to options C and options D, with respect to any bonus year, would be determined based on the quantitative benchmarks and would not be based on any qualitative benchmark. Eligibility of offerees who are not officers of the Bank to options C and options E, with respect to any bonus year, would be determined based on the quantitative benchmarks and on the quality rating assigned to such offerees, as stated in section 2.12.9 of the outline report.

The quantitative benchmarks specified in the option plan are: return on equity, return on Bank shares relative to benchmark, operating efficiency ratio and average ratio of deposits to loans.

The exercise price for each option to be issued pursuant to any of the plans is NIS 46.21 plus CPI linkage differentials, from the known CPI upon approval of option issuance to offerees by the Board of Directors to the known CPI upon the option exercise date by the offeree. The exercise price was determined based on the average closing price per Bank ordinary share on the stock exchange over the thirty trading days preceding the date of approval by the Board of Directors. Accordingly, note that on the exercise date, the offeree would not be required to pay the exercise price – which would only serve to determine the monetary benefit amount and the number of exercise shares actually issued to the offeree.

For calculation of fair value as of approval of the option award by the Board of Directors, as noted above, the terms of the option plans and the data and assumptions as listed in the outline report were taken into account.

Based on the aforementioned assumptions, as stated in the outline report, the average fair value of each option awarded pursuant to each of the option plans, as of the approval date of option issuance by the Board of Directors, is as follows:

- Options A: options included in the first lot – NIS 7.69; options included in the second lot – NIS 8.13; options included in the third lot – NIS 8.43.
- Options B: options included in the first lot – NIS 7.73; options included in the second lot – NIS 8.16; options included in the third lot – NIS 8.44.
- Options C: options included in the first lot – NIS 7.64; options included in the second lot – NIS 8.06; options included in the third lot – NIS 8.35.
- Options D and E: options included in the first lot – NIS 8.42; options included in the second lot – NIS 8.17; options included in the third lot – NIS 7.64.

The theoretical benefit value of the options in these plans, calculated in accordance with accounting standards, amounts to NIS 96 million (NIS 113 million including Payroll Tax). When spreading the theoretical benefit value in the Bank's accounts, the estimated expected churn rate for plan offerees would be taken into account.

The options would be allotted under the "wages" track, pursuant to the Section 102 of the Income Tax Ordinance. Therefore, any benefit arising to the offerees from exercise of these options shall be taxed at the marginal tax rate applicable to the offerees upon exercise of the options. The Bank would be required to pay the wages tax with respect to the benefit arising to the offerees from exercise of the options under the stock option plan. Furthermore, upon payment of the tax with respect to this benefit by the offerees, the Bank may make a deduction for tax purposes with respect to the aforementioned options based on the effective tax rate applicable upon the exercise date.

All other details of the plans and the outline of offering to employees (including the threshold conditions for eligibility for options, vesting and exercise periods of options and the Board of Directors' authority to reduce the number of options and provisions with regard to reimbursement of the monetary benefit are described in an Immediate Report dated June 19, 2014, reference 2014-01-091176. This mention constitutes inclusion by way of reference of all information provided in the aforementioned Immediate Report.

On August 3, 2015, the Bank's Board of Directors, after receiving the recommendation of the Bank Remuneration Committee, resolved to approve the outline of an offering to employees, whereby the Bank would allot 229,990 options to 19 offerees who are managers at the Bank.

The option plan is based on the principles of the stock option plan approved by the Bank in 2014, according to which the Bank allotted options to managers on June 19, 2014. See below.

The options were allotted as follows:

- Up to 11,494 options D to be awarded to up to one Bank officer who is employed by an individual employment contract, exercisable for up to 11,494 Bank ordinary shares of NIS 0.1 par value each. In conformity with Option Plan D dated June 19, 2014.
- Up to 218,496 options E to be awarded to up to eighteen managers employed by the Bank subject to collective bargaining agreements, exercisable for up to 218,496 Bank ordinary shares of NIS 0.1 par value each. In conformity with Option Plan E dated June 19, 2014.

The number of exercise shares, as stated above, is the maximum number of shares arising from exercise of all options which may be issued pursuant to all plans. However, the number of options which offerees may actually exercise, pursuant to terms and conditions of each plan, would be derived from the eligibility terms set for each plan, as follows. Furthermore, allotment of the maximum number of exercise shares is but theoretical, since in actual fact the Bank would not allot to the offerees the full number of exercise shares arising from the options which the offerees may exercise pursuant to terms and conditions of each plan – but only the number of shares reflecting the monetary benefit inherent in those options, based, *inter alia*, on the closing price cap of NIS 80 plus linkage differentials from the known CPI upon approval by the Board of Directors to the known CPI upon the exercise date.

Also note that the number of exercise shares for each plan is subject to adjustments for bonus share distribution, rights issuance, share split or reverse-split, dividend distributions etc.

The options issued in the name of the trustee for each officer, pursuant to option plans D or E, were divided into two equal annual lots, one for each bonus year. Each of the annual lots would vest on April 1 of each year between 2016-2020, as specified in the outline report.

Each of the annual lots for options D and E would vest as follows:
- The adjusted annual lot for 2015 may be exercised from the first anniversary of the option issuance date through 3.5 years thereafter.
- The adjusted annual lot for 2016 may be exercised from the second anniversary of the option issuance date through 3.5 years thereafter.

An offeree's eligibility for options pursuant to each of the aforementioned option plans, for any bonus year, is contingent on fulfillment of all of the following threshold conditions in the bonus year:
- Return on equity for the bonus year shall be at least 9%.
- Overall capital adequacy ratio and core capital adequacy ratio for the Bank, for the bonus year, shall be no less than the minimum ratios specified in Bank of Israel regulations.

In addition, eligibility conditions for options would be based on the following criteria:
- Eligibility of offerees who are not officers of the Bank to options D, with respect to any bonus year, would be determined based on the quantitative benchmarks and would not be based on any qualitative benchmark. Eligibility of offerees who are not officers of the Bank to options C and options E, with respect to any bonus year, would be determined based on the quantitative benchmarks and on the quality rating assigned to such offerees, as stated in section 2.12.7 of the outline report.

  The quantitative benchmarks specified in the option plan are: return on equity, return on Bank shares relative to benchmark, operating efficiency ratio and average ratio of deposits to loans.

Note 23 – Share-based Payment Transactions – continued

The exercise price for each option to be issued pursuant to any of the plans is NIS 47.76 plus CPI linkage differentials, from the known CPI upon approval of option issuance to offerees by the Board of Directors to the known CPI upon the option exercise date by the offeree. The exercise price was determined based on the average closing price per Bank ordinary share on the stock exchange over the thirty trading days preceding the date of approval by the Board of Directors. Accordingly, note that on the exercise date, the offeree would not be required to pay the exercise price – which would only serve to determine the monetary benefit amount and the number of exercise shares actually issued to the offeree.
For calculation of fair value as of approval of the option award by the Board of Directors, as noted above, the terms of the option plans and the data and assumptions as listed in the outline report were taken into account.

Based on the aforementioned assumptions, as stated in the outline report, the average fair value of each option awarded pursuant to each of the option plans, as of the approval date of option issuance by the Board of Directors, is as follows:

Options D and E: options included in the first lot – NIS 7.08; options included in the second lot – NIS 6.91.
The theoretical benefit value of the options in these plans, calculated in accordance with accounting standards, amounts to NIS 1.6 million (NIS 1.9 million including Wages Tax). When spreading the theoretical benefit value in the Bank's accounts, the estimated expected churn rate for plan offerees would be taken into account.

The options would be allotted under the "wages" track, pursuant to the Section 102 of the Income Tax Ordinance. Therefore, any benefit arising to the offerees from exercise of these options shall be taxed at the marginal tax rate applicable to the offerees upon exercise of the options. The Bank would be required to pay the wages tax with respect to the benefit arising to the offerees from exercise of the options under the stock option plan. Furthermore, upon payment of the tax with respect to this benefit by the offerees, the Bank may make a deduction for tax purposes with respect to the aforementioned options based on the effective tax rate applicable upon the exercise date.

All other details of the plans and the outline of offering to employees (including the threshold conditions for eligibility for options, vesting and exercise periods of options and the Board of Directors' authority to reduce the number of options and provisions with regard to reimbursement of the monetary benefit are described in an Immediate Report dated August 3, 2015, reference 2015-01-088305. This mention constitutes inclusion by way of reference of all information provided in the aforementioned Immediate Report.

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots awarded on June 19, 2014:

	Lot 1	Lot 2	Lot 3	Total
Option plan A				
Number of options (in thousands)	728	690	665	2,083
Annualized standard deviation	20.07%-28.99%	22.00%-34.72%	25.94%-35.64%	
Exercise price (in NIS)	46.21	46.21	46.21	
Risk-free interest rate	0.08%-(0.45%)	0.64%-(0.87%)	1.08%-(0.70%)	
Term to expiration (in years)	2.75-4.75	3.75-5.75	4.75-6.75	
Fair value per single option	7.70	8.12	8.43	
Total fair value per lot, NIS in thousands	5,605	5,605	5,605	16,815
Option plan B				
Number of options (in thousands)	314	284	275	873
Annualized standard deviation	20.07%-28.99%	22.00%-34.72%	25.94%-35.64%	
Exercise price (in NIS)	46.21	46.21	46.21	
Risk-free interest rate	0.08%-(0.45%)	0.64%-(0.87%)	1.08%-(0.70%)	
Term to expiration (in years)	2.75-4.75	3.75-5.75	4.75-6.75	
Fair value per single option	7.73	8.17	8.43	
Total fair value per lot, NIS in thousands	2,428	2,319	2,319	7,066
Option plan C				
Number of options (in thousands)	917	896	896	
Annualized standard deviation	20.07%-28.99%	22.00%-34.72%	25.94%-35.64%	2,709
Exercise price (in NIS)	46.21	46.21	46.21	
Risk-free interest rate	0.08%-(0.45%)	0.64%-(0.87%)	1.08%-(0.70%)	
Term to expiration (in years)	2.75-4.75	3.75-5.75	4.75-6.75	
Fair value per single option	7.64	8.06	8.35	
Total fair value per lot (NIS in thousands)	7,006	7,222	7,482	21,710
Option plan D				
Number of options (in thousands)	394	394	394	1,182
Annualized standard deviation	20.07%-27.06%	22.00%-28.31%	25.94%-26.81%	
Exercise price (in NIS)	46.21	46.21	46.21	
Risk-free interest rate	(0.12%)-(0.16%)	0.26%-(0.87%)	0.61%-(0.70%)	
Term to expiration (in years)	4.5	4.5	4.5	
Fair value per single option	8.42	8.17	7.64	
Total fair value per lot (NIS in thousands)	3317	3219	3010	9,546
Option plan E				
Number of options (in thousands)	1,682	1,682	1,682	5,046
Annualized standard deviation	20.07%-27.06%	22.00%-28.31%	25.94%-26.81%	
Exercise price (in NIS)	46.21	46.21	46.21	
Risk-free interest rate	(0.12%)-(0.16%)	0.26%-(0.87%)	0.61%-(0.70%)	
Term to expiration (in years)	4.5	4.5	4.5	
Fair value per single option	8.42	8.17	7.64	
Total fair value per lot (NIS in thousands)	14,162	13,742	12,850	40,754

Below are the assumptions used in calculating the fair value of a single option, as well as the resulting fair value per single option, for each of the lots granted on August 3, 2015:

	Lot 1	Lot 2	Lot 3	Total
Option plan D				
Number of options (in thousands)	–	6	6	12
Annualized standard deviation	–	17.48%-21.01%	17.48%-22.92%	
Exercise price (in NIS)	–	47.76	47.76	
Risk-free interest rate	–	(0.58%)-(0.86%)	(0.45%)-(0.86%)	
Term to expiration (in years)	–	3.5	3.5	
Fair value per single option	–	7.08	6.91	
Total fair value per lot (NIS in thousands)	–	40	40	80
Option plan E				
Number of options (in thousands)	–	109	109	218
Annualized standard deviation	–	17.48%-21.01%	17.48%-22.92%	
Exercise price (in NIS)	–	47.76	47.76	
Risk-free interest rate	–	(0.58%)-(0.86%)	(0.45%)-(0.86%)	
Term to expiration (in years)	–	3.5	3.5	
Fair value per single option	–	7.08	6.91	
Total fair value per lot (NIS in thousands)	–	774	755	1,529

Details of the number of stock options and their exercise price for all plans are as follows:

		2016		2015
	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)
Outstanding at year start	10,420,496	46.24	11,893,823	46.21
Granted during the year(1)	–	–	229,990	47.76
Forfeited during the year	1,599,747	46.26	1,699,397	46.21
Exercised during the year(2)	748,827	46.27	3,920	46.21
Outstanding at year end	8,071,922	46.24	10,420,496	46.24

(1) The weighted average fair value of stock options granted in 2015, as of the measurement date, was NIS 6.99. (in 2014 – NIS 8.06).
(2) The weighted average share price upon exercise of options into shares during 2016 was NIS 53.09 (2015 – NIS 47.0).

Below is information about stock options outstanding at year end by exercise price range:

Exercise price range	December 31, 2016	December 31, 2015
(in NIS)	40-50	40-50
Number of stock options	8,071,922	10,420,496
Weighted average exercise price (in NIS)	46.24	46.24
Weighted average remaining contractual term (in years)	2.57	3.51
Of which vested:		
Number of stock options	2,136,379	1,157,176
Weighted average exercise price (in NIS)	46.25	46.21

Note 24 – Share capital and shareholders' equity[1]

A. Details on share capital of the Bank (in NIS):

	Registered		Issued and paid-in[3]	
	December 31,		December 31,	
	2016	2015	2016	2015
Ordinary shares, NIS 0.1 par value[2]	40,000,000	40,000,000	23,456,851	23,438,032

(1) For allotment of stock options – see Note 23 to the financial statements.
(2) The shares are listed for trading on the Tel Aviv Stock Exchange.
(3) Includes 2,500,000 dormant shares, acquired and held by the Bank. For details, see section D. below.

B. Dividend distribution policies:

2015-2016

On December 23, 2014, the Bank Board of Directors resolved to approve the dividend distribution policy for 2015-2016.

The dividends policy calls for dividends to be distributed with respect to quarterly earnings in 2015 and 2016 (as from the first quarter of 2015), at a rate of up to 15% of net profit attributable to shareholders.

This dividends policies are subject to the Bank's maintaining proper safety margins so that Tier I capital ratio would not be lower than the ratio required by the Supervisor of Banks' directives, as adopted by the Board of Directors.

On this date, it was resolved that in 2017 the dividends policy would continue to be annual distribution of 40% of net operating profit and 80% from extraordinary items.

2017-2021

On November 21, 2016, the Bank's Board of Directors approved a new five-year strategic plan for 2017-2021 and resolved to approve a revised dividends policy as from 2017.

The Bank's revised dividends policy is to distribute dividends with respect to quarterly earnings, at 30% of net profit attributable to equity holders of the Bank.

The Bank has received approval from the Supervisor of Banks for the aforementioned outline of its revised dividends policies.

The Bank's Board of Directors would monitor execution of the new strategic plan in order to consider optional increase of the aforementioned dividends rate by a further step as from 2018. This would be subject to approval by the Supervisor of Banks.

The revised dividends policy is subject to the Bank achieving a ratio of Tier I capital to risk elements as required by the Supervisor of Banks and maintaining appropriate safety margins.

Below is a summary of previous Board resolutions with regard to dividend distribution policies:

- On April 3, 2006, the Board decided on annual dividend distribution at 40% of net operating profit and 80% of net profit from extraordinary items.
- On July 23, 2012, the Board decided that during the five-year plan for 2013-2017, the Bank would retain its dividend distribution policies.
- On August 14, 2013, a guideline was stipulated whereby, through December 31, 2014, the Bank would distribute dividends equal to up to 30% of annual operating net profit and 80% of annual profit from extraordinary items.

Note 24 – Share capital and shareholders' equity – continued

C. Information on dividend distribution limitations is provided below:

- According to the directives of the Supervisor of Banks with respect to a dividend distribution by banking corporations, a bank may not distribute cash dividends, as long as its non-monetary assets exceed its adjusted shareholders' equity. As of December 31, 2014, the Bank's reported capital exceeds its non-monetary assets by NIS 7,371 million.
- The permit issued to the purchasers of the controlling interest by the Governor of the Bank of Israel stipulates that dividends will not be distributed out of profits accruing until September 30, 1994, the amount of which (after capitalization to a capital reserve in 1998) is NIS 100 million.

Furthermore, the Bank may not distribute dividends without prior consent of the Supervisor of Banks for such distribution, when:

1. The Bank's retained earnings, net of negative differences included under Other Comprehensive Income, are not positive.
2. One or more of the most recent three years ended in comprehensive loss.
3. Cumulative results for the three quarters ending at the end of the interim period for which the most recent financial statements have been published – show a comprehensive loss.

D. On May 27, 2009, the Bank received the Supervisor's approval, allowing the Bank to buy back on a non-recurring basis 2,500,000 shares of NIS 0.1 par value of the Bank's issued share capital, subject to statute and to conditions set forth in the Supervisor's approval. On July 20, 2009 the Bank Board of Directors approved a share buy-back plan by the Bank, to acquire up to 2,500,000 shares of NIS 0.1 par value each, subject to terms and conditions set forth in the Supervisor's approval. On September 24, 2009, the Bank completed the buy-back, purchasing in total 2,500,000 shares at a cost of NIS 76 million.

The shares held by the Bank are designated to be provided as consideration for exercise of stock options under the stock option plan for VPs – for details see Note 23 to the financial statements. In accordance with the condition stated in the Supervisor's approval, the Bank would sell all excess shares (if any) immediately after the end of the exercise period of all options allotted pursuant to the stock option plan, i.e. immediately after the seventh anniversary of the date of allotment of options in accordance with the stock option plan.

In accordance with a pre-ruling obtained from the Tax Authority, the Bank would not incur any tax liability upon purchase of shares as stated above. The Bank's Board of Directors has concluded that buy-back of Bank shares in accordance with the aforementioned buy-back program meets the distribution criteria stipulated in the Companies Law and is compliant with terms and conditions specified in Proper Banking Conduct Directive No. 331. The Board of Directors has reexamined Bank compliance with distribution tests specified by the Companies Law, as well as compliance with conditions stated in Directive 331, immediately prior to these acquisitions.

On January 30, 2013, the Bank of Israel allowed the Bank to use the excess shares for its 2013 stock option plan for managers who are not part of Bank management nor Bank officers. The Bank must sell the remaining excess shares (if any) immediately after the end of the exercise period of options pursuant to the stock option plan for managers who are not part of Bank management nor Bank officers, or pursuant to the original plan – whichever is later.

Note 24 – Share capital and shareholders' equity – continued

On June 2, 2014, the Bank applied to the Supervisor of Banks for approval of a buy-back of 5 million Bank shares.

On July 17, 2014, the Bank submitted the detailed buy-back plan by date, as requested by the Supervisor of Banks.

The buy-back plan which was presented is in five stages, from the fourth quarter of 2015 to the fourth quarter of 2017, with restrictions for each buy-back lot and in total not to exceed 5 million shares. According to the plan, the Bank would sell any surplus shares after the end date for exercising all options under the stock option plan.

On July 27, 2014, the Supervisor of Banks approved the buy-back plan subject to conditions set between the Bank and the Supervisor of Banks.

On August 13, 2014, the Bank's Board of Directors approved the aforementioned share buy-back outline. The buy-back plan, including the manner of execution shall be brought for approval by the Board of Directors, should it be put into action.

Buy-back of Bank shares is tantamount to a dividend distribution.

Note 25 – Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks

Reported amounts (NIS in millions)

A. Capital adequacy pursuant to directives of the Supervisor of Banks

Calculated in accordance with Proper Conduct of Banking Business Directive No. 201-211 "Measurement and Capital Adequacy"

	December 31, 2016 (audited)	December 31, 2015 (audited)
1. Consolidated data		
A. Capital for purpose of calculating minimum capital ratio		
Tier I capital	13,318	12,299
Tier I capital	13,318	12,299
Tier II capital	4,888	4,916
Total capital	18,206	17,215
B. Weighted risk asset balances		
Credit risk	122,605	120,793
Market risks	1,184	950
Operating risk	8,113	7,743
Total weighted risk asset balances	(1)131,902	129,486
C. Ratio of capital to risk elements		
Bank data:		
Ratio of Tier I capital to risk elements	10.10	9.50
Ratio of Tier I capital to risk elements	10.10	9.50
Ratio of total capital to risk elements	13.80	13.29
Minimum Tier I capital ratio required by Supervisor of Banks(2)	9.76	9.30
Total minimum capital ratio required by the Supervisor of Banks(2)	13.26	12.80
2. Significant subsidiaries		
Bank Yahav for Government Employees Ltd. and subsidiaries thereof		
Ratio of Tier I capital to risk elements	9.41	9.97
Ratio of Tier I capital to risk elements	9.41	9.97
Ratio of total capital to risk elements	13.27	13.23
Minimum Tier I capital ratio required by Supervisor of Banks	9.00	9.00
Total minimum capital ratio required by the Supervisor of Banks(3)	12.50	13.00

(1) Of the total weighted risk asset balances, NIS 245 million was deducted due to adjustments with respect to the streamlining plan.

(2) Capital ratios required by the Supervisor of Banks as from January 1, 2015. As from January 1, 2015, an additional capital requirement was added to these ratios at 1% of the housing loan balance as of the reporting date. This requirement is gradually implemented through January 1, 2017. Accordingly, the minimum Tier I capital ratio and the minimum total capital ratio required by the Supervisor of Banks, as of January 1, 2017, on a consolidated basis, in conformity with data as of the current reporting date, are 9.87% and 13.37%, respectively.

(3) In May 2016, the Bank of Israel reduced its overall capital ratio requirement for Bank Yahav from 13.00% to 12.50%.

Note 25 – Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks – Continued

Reported amounts (NIS in millions)

A. Capital adequacy pursuant to directives of the Supervisor of Banks – continued

Calculated in accordance with Proper Conduct of Banking Business Directive No. 201-211 "Measurement and Capital Adequacy" – continued

	As of December 31	As of December 31
	2016	2015
3. Capital components for calculation of capital ratio (on consolidated basis)		
A. Tier I capital		
Shareholders' equity	13,324	12,415
Differences between shareholder equity and Tier I capital	(91)	(18)
Total Tier I equity before regulatory adjustments and deductions	13,233	12,397
Regulatory adjustments and deductions:		
Goodwill	(87)	(87)
Regulatory adjustments and other deductions – Tier I capital	(16)	(11)
Total supervisory adjustments and deductions, before adjustments with respect to the streamlining plan – Tier I capital	(103)	(98)
Total adjustments with respect to the streamlining plan – Tier I capital	188	–
Total Tier I capital after regulatory adjustments and deductions	13,318	12,299
B. Tier II capital		
Tier II capital: Instruments, before deductions	3,491	3,544
Tier II capital: Provisions, before deductions	1,397	1,372
Total Tier II capital, before deductions	4,888	4,916
Deductions:		
Total deductions – Tier II capital	–	–
Total Tier II capital	4,888	4,916

4. Effect of transitional provisions on Tier I capital ratio (for details see section J. below):

	As of December 31	As of December 31
	2016	2015
Ratio of capital to risk elements		
Ratio of Tier I capital to risk elements, before effect of transition provision of Directive 299 and before effect of adjustments with respect to the streamlining plan(1)	9.83%	9.32%
Effect of transition provisions, before effect of adjustments with respect to the streamlining plan	0.13%	0.18%
Effect of adjustments with respect to the streamlining plan	0.14%	–
Ratio of Tier I equity to risk elements before application of transitional provisions	10.10%	9.50%

(1) Including adoption of US GAAP with regard to employee rights.

Note 25 - Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks - Continued

Reported amounts (NIS in millions)

B. Liquidity coverage ratio pursuant to directives of the Supervisor of Banks

Calculated in accordance with Proper Conduct of Banking Business Directive No. 221 "Liquidity coverage ratio"

	As of December 31 2016 In %	As of December 31 2015 In %
1. Consolidated data		
Liquidity coverage ratio	117	91
Minimum liquidity coverage ratio required by the Supervisor of Banks(1)	80	60
2. Bank data		
Liquidity coverage ratio	117	90
Minimum liquidity coverage ratio required by the Supervisor of Banks(1)	80	60
3. Significant subsidiaries		
Bank Yahav for Government Employees Ltd. and subsidiaries thereof		
Liquidity coverage ratio	286	382
Minimum liquidity coverage ratio required by the Supervisor of Banks(2)	100	100

(1) The minimum liquidity coverage ratio required by the Supervisor of Banks would gradually increase to 100% as of January 1, 2017.
(2) According to Proper Conduct of Banking Business Directive 221, it is expected that any banking corporation achieving a liquidity coverage ratio of 100% upon the start date of applying the directive would maintain the ratio at or over 100% during the transition period.

C. Leverage ratio pursuant to directives of the Supervisor of Banks

Calculated in conformity with Proper Conduct of Banking Business Directive 218 "Leverage ratio"

	As of December 31 2016	As of December 31 2015
1. Consolidated data		
Tier I capital	13,318	12,299
Total exposure	252,489	231,291
Leverage ratio(1)	5.27	5.32
Minimum leverage ratio required by the Supervisor of Banks	5.00	5.00
2. Significant subsidiaries		
Bank Yahav for Government Employees Ltd. and subsidiaries thereof		
Leverage ratio(2)	5.00	(4)4.89
Minimum leverage ratio required by the Supervisor of Banks(3)	4.70	4.85

(1) Leverage Ratio – ratio of Tier I capital, according to Basel rules, to total exposure. This ratio is calculated in conformity with Proper Banking Conduct Directive 218
(2) Banking corporations are required to achieve the minimum leverage ratio required by the Supervisor of Banks as from January 1, 2018. Banking corporations which comply with the requirement upon publication of the directive may not drop below the threshold stated in the regulation.
(3) In March 2016, the Supervisor of Banks specified that the minimum leverage ratio required of Bank Yahav is 4.70%.
(4) In order to reinforce Bank Yahav's compliance with the leverage ratio outline, Bank Yahav has realized its debenture portfolio held to maturity.

Note 25 - Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks - Continued

D. On June 30, 2010, the Supervisor of Banks issued a letter to banking corporations, on capital policies for interim periods, in which they are required to adopt a target for Tier I capital ratio by December 31, 2010, to be no less than 7.5%. Concurrently, the banks are required to submit to the Supervisor a work plan for achieving this target. The letter further stipulates that in absence of prior approval by the Supervisor of Banks, the bank shall not distribute dividends if the target has not been achieved, or if such dividend distribution would cause the bank not to achieve the target. This directive is intended to clarify the expectations of the Supervisor of Banks from banking corporations in the interim period, pending adaptation of the Supervisor's directives to emerging changes in recommendations of the Basel Committee.

E. On October 25, 2010, the Bank's Board of Directors decided that the target core capital ratio would be no less than 7.5%. Further, the Board of Directors resolved to direct Bank management to act so as to maintain appropriate safety margins, in order to ensure that the core capital ratio shall be no less than the foregoing. The Bank's Board of Directors further resolved that the overall capital adequacy ratio shall be no less than 12.5%.

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

G. On July 23, 2012, the Bank's Board of Directors instructed Bank management to bring forward implementation of the Supervisor of Banks' directive dated March 28, 2012 – so as to implement it, if possible, as from January 1, 2014. Moreover, the Board of Directors has resolved to instruct Bank management to maintain, in as much as possible, appropriate safety margins to this end.

H. On March 21, 2013, the Supervisor of Banks issued directives with regard to residential real estate. In conformity with the directives, capital allocation for loans originated as from January 1, 2013 is calculated using the following weighting:

For loans with LTV up to 45%	- 35% risk weighting
For loans with LTV from 45% to 60%	- 50% risk weighting
For loans with LTV over 60%	- 75% risk weighting
For leveraged loans with LTV ratio over 60% with A variable interest component of 25% or higher	- 75% risk weighting
This compares with the former weighting:	
For loans with LTV up to 75%	- 35% risk weighting
For loans with LTV over 75%	- 75% risk weighting
For leveraged loans with LTV ratio over 60% with A variable interest component of 25% or higher	- 100% risk weighting

In addition, the credit conversion factor for guarantees to secure investments of apartment buyers was reduced from 20% to 10% if the apartment has been delivered to the resident.

Note 25 - Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks - Continued

I. On April 30, 2013, the Supervisor of Banks issued a letter confirming that notes to be issued by the Bank would count as lower Tier II capital with regard to maintaining a minimum capital ratio.

Changes to conditions for recognition as lower Tier II capital, following implementation of Basel III directives, would retroactively apply to these notes.

J. On May 30, 2013, the Supervisor of Banks issued an amendment to Proper Banking Conduct Directives 201-211 concerning adoption of Basel III instructions with regard to supervisory capital and with regard to risk assets (hereinafter: "the directives").

The amendments to the regulations are primarily focused on improving capital quality and size and improving the coverage for Credit Valuation Adjustment (CVA) risk.

The directives are effective as from January 1, 2014, subject to transitional provisions.

Below are the key amendments included in these directives:

– **Capital structure**

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

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

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

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

– **Non-controlling interest**

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

– **Group provision for credit losses**

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

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

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

- Deferred taxes due to temporary differences would be accounted for as follows:
  Up to 10% of Tier I equity – weighted at 250% risk weighting.
  Over 10% of Tier I equity – would be deducted from capital.
- Investments in equity components of financial institutions – banks, insurance companies and any company doing business in the capital market segment – would be accounted for as a deduction from capital or by risk weighting, subject to specified tests.
- The accumulated gain with respect to cash flow hedging of items not listed at fair value on the balance sheet – would be deducted from capital. This means that positive amounts would be deducted from capital and negative amounts would be added to capital.
- Accounting adjustments with respect to liabilities of derivative instruments arising from a change in the Bank's credit risk (Debit Valuation Adjustment – DVA) would be deducted from capital.

Note 25 - Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks - Continued

- **Capital allocation with respect to CVA loss (Credit Value Adjustments) – loss due to revaluation at market value with respect to counter-party credit risk.**

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

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

  - Supervisory adjustments and deductions from capital and non-controlling interest not qualified for inclusion under supervisory capital – an annual 20% deduction as from January 1, 2014.
  - Capital instruments not qualified as supervisory capital – recognition of 80% of the balance of such instruments as from the effective start date and a 10% deduction annually through January 1, 2022.

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

  The Bank is prepared to implement these directives and is reviewing their impact on the Bank's strategic plan.

K. Following the publication of these directives, the Bank has revisited its compliance with the schedules for achieving the target core capital ratio of no less than 9%.

Following this review and based on assumptions, as of the review date, with regard to expected profit in 2013-2014 and to growth rate of risk assets, the Bank presented to the Supervisor of Banks an outline of expected evolution of its core capital ratio, including dividend distribution, while maintaining appropriate safety margins.

After checking with the Supervisor of Banks, the Bank’s Board of Directors resolved, on August 14, 2013, to adopt a core capital ratio target as of December 31, 2014 of 9% or higher. Furthermore, the Board of Directors then resolved to distribute dividends amounting to NIS 75 million and to adopt a guideline whereby, through December 31, 2014, the Bank would distribute dividends equal to up to 30% of annual operating net profit and 80% of annual profit from extraordinary items.

These resolutions supersede the Board of Directors' resolutions with regard to bringing forward the implementation of the Supervisor of Banks' directives, dated March 28, 2012, with the intention of implementing these, in as much as possible, as from January 1, 2014, and with regard to the dividend distribution policies – as described in section 1 of the Immediate Report issued by the Bank, dated July 23, 2012 (reference 2012-01-191649). This mention constitutes inclusion by way of reference of all information provided in section 1 of the aforementioned report.

L. On August 29, 2013, the Supervisor of Banks issued directives with regard to "Restrictions on provision of housing loans". According to the directives, as from September 1, 2013 a bank may not approve nor originate housing loans where the ratio of monthly repayment to borrower income exceeds 50%.

Furthermore, loans with a ratio of monthly repayment to borrower income in excess of 40% will have a 100% risk weighting in calculation of capital allocation.

Note 25 - Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks - Continued

M. On September 28, 2014, the Supervisor of Banks issued a circular updating Proper Banking Conduct Directive no. 329, as well as a Q&A file on this issue. The circular consists of two amendments to the directive:

- Increase to the capital target – the target Tier I capital to risk elements ratio is to include an addition equal to 1% of the housing loan portfolio balance. The equity targets would be increased by fixed quarterly steps from January 1, 2015 to January 1, 2017 (over eight quarters).
- Risk weighting of leveraged loans bearing variable interest – the risk weighting of leveraged loans bearing variable interest would be reduced from 100% to 75%.

Following implementation of this directive, the target ratio of Tier I capital to risk elements increased by 0.1%, according to data as of the reporting date, in each of the seven quarters as from the implementation date of this directive, for a total increase of 0.87% when implementation is complete. This target may change based on actual data for the housing loan portfolio and for total risk assets.

N. On December 23, 2014, the Bank's Board of Directors resolved to approve the revised dividend distribution policy for 2015 and 2016. The revised dividends policy calls for dividends to be distributed with respect to quarterly earnings in 2015 and 2016 (as from the first quarter of 2015), at a rate of up to 15% of net profit attributable to shareholders.

The revised dividends policies are subject to the Bank's maintaining proper safety margins, as specified for this matter, so that the Bank's Tier I capital ratio would not be lower than the target required by the Supervisor of Banks' directives, as adopted by the Board of Directors.

O. As from January 1, 2015, the Bank has adopted US GAAP with regard to employee rights.

In conformity with transition provisions specified in Proper Conduct of Banking Business Directive no. 299, a cumulative other comprehensive loss balance and amounts directly charged to retained earnings as of January 1, 2013 with respect to remeasurement of net liabilities or net assets with respect to defined benefit to employees, would not be immediately taken into account for calculation of the capital requirements, but would rather be subject to transitional provisions, so that the impact would be applied at equal rates of 20% as from January 1, 2014, 40% as from January 1, 2015 and through to full application as from January 1, 2018.

P. On April 28, 2015, the Supervisor of Banks issued a new Proper Banking Conduct Directive 218 concerning "Leverage ratio". This directive 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 according to Basel rules 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 shall maintain a leverage ratio of 5% or higher on consolidated basis, as from January 1, 2018. Banking corporations which comply with the requirement upon publication of the directive may not drop below the threshold stated in the regulation. Any banking corporation which does not meet the requirements of this directive is required to increase its leverage ratio at fixed quarterly steps by January 1, 2018.

Note 25 - Capital adequacy, liquidity and leverage pursuant to directives of the Supervisor of Banks - Continued

Q. On October 22, 2015, the Supervisor of Banks issued a circular concerning capital requirements with respect to exposure to central counter-parties (CCP). The circular includes an amendment to Proper Conduct of Banking Business Directive 203 with regard to capital measurement and adequacy, in conformity with directives of the Basel Committee on this matter.

The directive stipulates rules for treatment of exposure to clearinghouses, arising from trading of OTC derivatives, from transactions in negotiable derivatives and from transactions for financing securities.

Below are highlights of the amended directive:

- A central counter-party has been defined as a clearinghouse operating as a financial broker between counter-parties to contracts traded on a financial market.
- The trading exposure of a bank which is a member of the clearinghouse to a qualified central counter-party (QCCP) would be weighted at a risk weighting of 2% (compared to zero exposure currently). The trading exposure of a bank which is a member of the clearinghouse, that makes transfers to the clearinghouse's risk fund would be weighted in conformity with a formula specified in the directive.
- The trading exposure of a bank which is a member of the clearinghouse to clients active on a stock exchange in Israel would be calculated based on the calculation method for bi-lateral transactions (compared to current calculation according to rules of the stock exchange in Israel).
- The trading exposure of a bank acting through a member of the clearinghouse would carry a risk weighting of 2% or 4%, subject to compliance with business, operational and legal conditions specified in the directive.
- The trading exposure of a bank to a Non-Qualified Central Counter-Party would carry a risk weighting as applicable to that counter-party.

On June 9, 2016, the Supervisor of Banks issued a letter, whereby the provisions of the circular would apply as from January 1, 2017.

Note that the provision allows the Tel Aviv Stock Exchange to be treated as a Qualified Central Counter-Party through June 30, 2017.

On December 28, 2016, the Supervisor of Banks' issued a letter whereby, notwithstanding the foregoing, calculation of exposure with respect to clients with activities on the MAOF stock exchange would continue to be based on the scenario method.

The Bank believes that the expected impact of application of provisions in this circular for relevant balances as of the report date, is not material.

R. In December 2015 and in January 2016, the Bank issued contingent subordinated notes (Contingent Convertibles – CoCo) with loss-absorption provisions through principal write-off, amounting to NIS 600 million.

These notes qualify for recognition as Tier II equity pursuant to Basel III provisions.

The notes include loss-absorption provisions if the Bank's Tier I equity should drop below 5% or in case of another event leading to non-sustainability of the Bank, in conformity with the Supervisor of Banks' decision.

In such case, the notes would be partially or completely written off.

Should the Tier I equity ratio exceed the minimum required ratio, the Bank may announce a principal write-off, in whole or in part.

Standard & Poor's Ma'alot rated the contingent subordinated notes ilAA-.

In July 2016, Bank Yahav issued contingent subordinated notes (Contingent Convertibles – Coco) with loss-absorption provisions through principal write-off, amounting to NIS 218 million.

These notes qualify for recognition as Tier II equity pursuant to Basel III provisions.

S. On November 21, 2016, the Bank's Board of Directors approved a new five-year strategic plan for 2017-2021 and resolved to approve a revised dividends policy as from 2017.

The Bank's revised dividends policy is to distribute dividends with respect to quarterly earnings, at 30% of net profit attributable to equity holders of the Bank.

The Bank has received approval from the Supervisor of Banks for the aforementioned outline of its revised dividends policies.

The Bank's Board of Directors would monitor execution of the new strategic plan in order to consider optional increase of the aforementioned dividends rate by a further step as from 2018. This would be subject to approval by the Supervisor of Banks.

The revised dividends policy is subject to the Bank achieving a ratio of Tier I capital to risk elements as required by the Supervisor of Banks and maintaining appropriate safety margins.

T. On December 27, 2016, the Bank's Board of Directors approved the streamlining plan recommended by Bank management, whereby early retirement would be possible for 300 employees in 2017-2021, at improved conditions.

Bank management is in negotiations with the employee union with regard to the retirement program and as a first step, has started implementation of the plan in the Technology Division Ltd., pending agreement with the employee union at the Bank.

The cost of update to the actuarial liability with respect to the streamlining plan, recorded on the financial statements as of December 31, 2016, amounts to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity (under Other Comprehensive Income).

In conformity with the Supervisor of Banks' letter dated January 12, 2016, with regard to operating streamlining of the Israeli banking system, the Supervisor of Banks allowed capital relief with respect to this plan. The Bank applies this capital relief so that supervisory capital used to calculate capital adequacy would be adjusted (increased) and the capital effect of the streamlining (a decrease by 0.14%) would be applied on a straight line basis as from 2017, over a five-year period.

For more information about the streamlining plan, see Note 22 to the financial statements.

U. On December 28, 2016, the Bank acquired an insurance policy for credit exposure due to guarantees provided by the Bank pursuant to the Sale Act (Apartments) (Securing Investments of Home Buyers), 1974 and obligations to issue such guarantees.

The insurance policy covers 80% of the guarantees amounting to NIS 15.5 billion and is effective as from December 31, 2016.

Obtaining this insurance resulted in a reduction of NIS 3.3 billion in the Bank's risk assets and in an increase of 0.25% in the Bank's Tier I capital ratio.

Note 26 – Contingent Liabilities and Special Commitments

Reported amounts (NIS in millions)

A. Off-balance sheet liability for activities based on extent of collection at year end[1]

1. Balance of loans from deposits based on extent of collection[2]

	As of December 31	
	2016	2015
Israeli currency – linked to the CPI	4,148	4,965
Israeli currency – non-linked	3,538	3,242
Foreign currency	169	114
Total	7,855	8,321

2. Cash flows with respect to collection commissions on activities based on extent of collection[2]

	As of December 31							
	2016							2015
	Up to 1 year	Over 1 year to 3 years	Over 3 years to 5 years	Over 5 years to 10 years	Over 10 years to 20 years	Over 20 years	Total	Total
In the CPI-linked sector[3]								
Cash flows of futures contracts	37	70	54	66	19	2	248	308
Expected future cash flows net of management's estimate of early repayments	38	69	53	61	15	1	237	297
Discounted expected future flows net of management's estimate of early repayments[4]	37	66	49	53	11	–	216	270
In the non-linked NIS-denominated sector								
Cash flows of futures contracts	3	1	–	–	–	–	4	4
Expected future cash flows net of management's estimate of early repayments	1	1	–	–	–	–	2	3
Discounted expected future flows net of management's estimate of early repayments[4]	–	–	–	–	–	–	–	1

3. Information on loans extended by mortgage banks during the year

	2016	2015
Loans out of deposits according to extent of collection	98	65
Standing loans and grants	88	124

(1) Loans and deposits from deposits the repayment of which to the depositor is contingent upon collection of the loans (or deposits), with margin or with collection commission (instead of margin).
(2) Standing loans and Government deposits given with respect there to totaling NIS 1,606 million (2015: NIS 1,892 million) are not included in this table.
(3) Includes foreign currency sector.
(4) Discounted at the rate of 2.10% (2015: 1.76%).

Note 26 – Contingent Liabilities and Special Commitments – continued

As of December 31

Reported amounts (NIS in millions)

B. Other liabilities and special commitments

	2016	2015
Obligations with respect to:		
Long-term leases[(1)(2)]	2,401	730
Computerization and software service contracts	233	203
Acquisition and renovation of buildings	6	3

(1) The Bank and subsidiaries have long-term leases on buildings, equipment and software for which the rental payments are as follows (subject to linkage conditions):

	2016	2015
First year	162	62
Second year	155	60
Third year	153	52
Fourth year	145	50
Fifth year	143	47
Sixth year and thereafter	1,643	459
Total	2,401	730

(2) Includes IT and operating services provided to Bank Yahav by an international Tata Group company as from January 1, 2017. The company specializes, *inter alia*, in providing IT services to financial institutions and banking corporations world-wide. In this regard, Bank Yahav uses a core banking system which includes banking services in various channels, based on the bank's lines of business. Bank Yahav also receives operating services from the company with respect to IT systems it provides, as well as additional outsourced services.

Bank Yahav's contract with the company is a long-term one and Bank Yahav may optionally extend it for additional terms of up to 30 years.

C. Contingent liabilities and other special commitments

1) In accordance with a resolution of the Board of Directors of the Tel Aviv Stock Exchange (“TASE”), a risk fund was established, which totaled NIS 532 million as of December 31, 2016. The Bank's share of the fund as of December 31, 2016 is estimated at NIS 45 million (as of December 31, 2015 – NIS 57 million). The size of the risk fund is updated semi-annually based on the average daily total clearing volume – but no less than NIS 150 million. Each member’s share in the risk fund will be determined by a ratio between the member’s clearing volume and the total clearing volume of all members (except for the Bank of Israel) during that period, but no less than NIS 500 thousand.

   In accordance with a decision by the stock exchange clearinghouse Board of Directors, starting on December 15, 2008 each member of the clearing house deposits in cash at least 25% of their share in the risk fund.

   On October 31, 2016, the Board of Directors of the Stock Exchange resolved to approve opening of an account with the Bank of Israel for deposit of collateral provided by members of the stock exchange clearing house (as set forth above), which have been deposited with other commercial banks through the account opening date.

   See Note 27.A regarding liens that the Bank has undertaken to furnish for this liability. to the financial statements.

2) The Bank has undertaken toward the MAOF Clearinghouse Ltd., a subsidiary of the TASE (“MAOF Clearinghouse”), to pay any monetary charge deriving from transactions in derivatives traded on the TASE, executed through it by its customers, and from such transactions executed by several members of the TASE that are not members of the MAOF Clearinghouse, for their customers.

   The amount of the liability for these customers, as of the balance sheet date, amounts to NIS 168 million (as of December 31, 2015 – NIS 230 million).

   Likewise, the Bank has undertaken to refund its share in the risk fund of the MAOF Clearinghouse, which totaled NIS 874 million as of December 31, 2016. The Bank's share of the fund as of December 31, 2016 is estimated at NIS 53 million (as of December 31, 2015 – NIS 125 million).

   In accordance with a decision by the MAOF clearinghouse Board of Directors, starting on December 15, 2008 each member of the clearing house deposits in cash at least 25% of their share in the risk fund.

   On October 31, 2016, the Board of Directors of the MAOF clearing house resolved to approve opening of an account with the Bank of Israel for deposit of collateral provided by members of the MAOF clearing house (as set forth above), which have been deposited with other commercial banks through the account opening date.

   For information regarding charges that the Bank undertook to furnish with respect to these liabilities, see Note 27.B. to the financial statements.

3) The Bank has made undertakings to the Tel Aviv Stock Exchange (“TASE") for operations of a company which is a member of the stock exchange but not a member of the clearinghouse. The undertaking is to honor any monetary charge arising from transactions executed by that company.

4) In 1992, a General Meeting of the Bank’s shareholders ratified a resolution to indemnify officers of the Bank with the following wording:
   – The Bank will indemnify in full each of the officers for financial liabilities and legal expenses incurred for actions, acts, and omissions performed within the framework stipulated in the Companies Ordinance and the Bank’s by-laws, and subject to the above provisions.
   – These officers will be indemnified whether the claim is brought against them during their employment period at the Bank, or whether subsequently and refers to an act performed in their capacity as officers.

Note 26 – Contingent Liabilities and Special Commitments – continued

There are differing legal opinions regarding a company's authority to approve such broad indemnification, and whether invoking it in a specific case requires additional approval, in a manner stipulated by law. Should the Bank be required to pay any amounts on the basis of the above decision, it will seek advice from its legal counsel regarding its obligation, taking into consideration the specific and special circumstances of each incident, if applicable.

5) In December 2001, a General Meeting of the Bank's shareholders ratified the granting an advance exemption from liability (as described below) as well as advance commitment by the Bank to indemnify Board members and other officers (hereinafter jointly: "the officers"). Pursuant to the resolution by the General Meeting of shareholders, the Bank exempts in advance any liability by officers of the Bank towards the Bank with respect to any damage incurred by the Bank due to breach of the officer's duty of care towards the Bank in the officer's conduct, arising from his position as officer of the Bank. Committed to indemnify officers of the Bank for any liability or expense incurred by the officer in conjunction with his action in the course of their office, all as stated in the letter of commitment to indemnify, including with regard to actions by officers who are not Board members in conjunction with their action as Board member on behalf of the Bank, or at the Bank's request, of another company whose shares are owned by the Bank (hereinafter: "the original letter of indemnification").

According to the original letter of indemnification, the amount if indemnification paid by the Bank to all officers on aggregate shall not exceed 25% of the Bank's shareholder equity on the Bank's 2000 financial statements, adjusted for the CPI as from December 2000 (hereinafter: ("total indemnification amount). This indemnification applies to action related, directly or indirectly, to one or more of the event types listed in the Addendum to the letter of commitment to indemnify.

On October 28, 2004, the General Meeting of Bank shareholders resolved to add to the list of events for which the Bank granted a commitment to indemnify to its officers, pursuant to the original letter of indemnification, a merger event, as defined in the Companies Law, including any decision, action or reporting with regard to a merger. It was resolved that in all that relates to indemnification resulting from a merger event, the maximum amount of the indemnification will be the lesser of: 25% of the Bank's shareholders' equity according to its financial statements as of December 31, 2000, plus linkage differentials beginning from the CPI for December 2000, or 25% of the Bank's shareholders' equity according to the last financial statements published in proximity to the actual payment date with respect to the indemnification.

On May 14, 2006, the General Meeting of Bank shareholders resolved to adapt the wording of the letter of indemnification to the provisions of the Companies Law (Amendment 3), 2005 and resolved to grant advance commitment to indemnify, of identical wording, to Bank employees serving as Board member on a company in which the Bank owns some shares, and to those serving, from time to time at the Bank's request, as Board member on a company controlled by the Bank.

On November 9, 2011, the General Meeting of Bank shareholders resolved to add a commitment by the Bank to indemnify Bank employees who are not officers of the Bank, who serve from time to time, upon request by the Bank, as officers of companies controlled by the Bank (such a resolution was also passed by the Bank's Board of Directors on February 16, 2009 – resolving to provide a letter of indemnification identical to the one granted to Bank officers), and to those who are not employees or officers of the Bank, who serve from time to time as officers of a company, other than a banking corporation, wholly-owned by the Bank (jointly: "the parties eligible for indemnification").

The General Assembly of Bank shareholders further decided to add a commitment by the Bank to indemnify the parties eligible for indemnification for any monetary liability arising from payment to any party injured by the breach and with respect to expenses related to any administrative proceeding, including reasonable litigation expenses – all as specified in the ISA Enforcement Proceeding Streamlining Act (Legislative Amendments), 2011.

Note 26 – Contingent Liabilities and Special Commitments – continued

The General Assembly of Bank shareholders also resolved that the maximum indemnification amount payable by the Bank, on aggregate to all those eligible for indemnification pursuant to the letter of commitment to indemnify, shall not exceed 25% of the Bank's shareholders equity, based on its most recent financial statements published soon prior to the actual payment date of the indemnification amount ("maximum indemnification amount"). Should the total indemnification amount exceed the maximum indemnification amount specified above, the maximum amount payable by the Bank on aggregate to all those eligible for indemnification shall not exceed the total indemnification amount, but the differences between these two amounts would only be used for indemnification with respect to action taken before November 9, 2011.

On September 20, 2012, the General Assembly of Bank shareholders further decided to add a commitment by the Bank to indemnify the parties eligible for indemnification for any monetary liability arising from payment to any party injured by the breach and with respect to expenses related to any administrative proceeding, including reasonable litigation expenses – all as specified in the ISA Enforcement Proceeding Streamlining Act (Legislative Amendments), 1981 and in the Financial Services Supervision Act (Provident Funds), 2005 and with respect to expenses related to any administrative proceeding, including reasonable litigation expenses – all as specified in the Restrictive Trade Practices Act, 1988.

The General Assembly of Bank shareholders further decided to add a commitment by the Bank to indemnify the parties eligible for indemnification for any monetary liability arising from payment to any party injured by the breach or similar, pursuant to any other statute, including reasonable litigation expenses, including attorneys' fees, with regard to any administrative proceeding pursuant to any other statute, provided that such indemnification is not prohibited by law.

On December 23, 2015, the General Assembly of Bank shareholders resolved to reduce the liability exemption for officers, so that it would not apply to any breach of duty of care after the approval date by the General Assembly of Bank shareholders, when making a decision or approving a transaction in which the controlling shareholder of the Bank or any officer of the Bank (including another officer, other than the officer who received the waiver) has a personal interest.

The General Assembly of Bank shareholders also resolved to add clarifications, details and elaboration to the events listed in the addendum to the letter of commitment to indemnify, according to events which the Board of Directors considers to be likely in view of actual Bank operations. The General Assembly of Bank shareholders further resolved to amend the letter of commitment to indemnify with regard to obtaining indemnification from an insurer or from a third party, so that the indemnification cap equal to the difference between the liabilities imposed on the officer or on the employee and/or legal expenses incurred by or charged to them, would also apply if the officer or employee would be reimbursed by any third party or by any third party's insurer who provided indemnification to the officer or employee for the same matter. It was further resolved that if the liability or legal expenses would not be actually covered in a timely manner by the insurer or by the third party, the Bank would indemnify the officer or employee for such liability and/or legal expenses – provided that the officer or employee would assign to the Bank their rights vis-a-vis the insurer or third party, so that the Bank would replace them vis-a-vis the insurer or third party.

Note 26 – Contingent Liabilities and Special Commitments – continued

6) In May 1998, General Assemblies of the shareholders of the Bank and of Bank Tefahot ratified an undertaking to indemnify officers, which had previously been approved by their Audit Committees and Boards of Directors as follows:

   The Bank and Bank Tefahot will irrevocably indemnify any of their officers for any action taken in their capacity as officers, in connection with the causes of action listed below, and for any financial obligation to be imposed by a court judgment, including a compromise, or arbitrator's decision that is subsequently approved by a court, and also for any reasonable legal expenses for which they may be indemnified in accordance with provisions of the Companies Ordinance.

   The indemnification will be made for all the officers on a cumulative basis, up to a sum not to exceed – for each bank separately – NIS 750 million (linked to the CPI of March 1998), for any financial liability that the officer incurs as a result of an action that he took that is directly or indirectly connected to the prospectus published in 1998, or to the draft prospectus that was filed in that year, in connection with the offer of sale of the Bank's securities by the State, including in connection with the reports submitted by the banks subsequent to the date of the prospectus regarding any matter that occurred before the date of the prospectus.

   Furthermore, the total cumulative amount of indemnification to be paid for all officers for any action or matter related to the insurance of borrowers by mortgage banks mentioned in the above prospectus included in the letter of indemnification – by each bank separately – will not exceed NIS 750 million (linked to the CPI of March 1998).

   The letters of undertaking for indemnification stipulated further that, notwithstanding the aforesaid, the total cumulative amount of indemnification to be paid for all the officers with regard to all the causes of action included in the letter of indemnification – by each bank separately – will be limited to NIS 1,000 million (linked to the CPI of March 1998).

   Under terms and conditions of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

7) In November 2001, approval was given by General Assemblies of the shareholders of Bank Tefahot and of a wholly-owned and controlled subsidiary of Bank Tefahot ("Tefahot Issuance"), in connection with the prospectus for issuance of debentures and subordinated notes of Bank Tefahot from November 2001, that Tefahot Issuance irrevocably undertakes to indemnify all of its officers, for any action taken in connection with matters detailed in the letter of indemnity, by virtue of his being an officer ("indemnification").

   The indemnification will be given for any financial debt, if imposed by a judgment, including a judgment issued in a compromise or arbitration that was approved by a court, and with respect to any reasonable legal expenses (including fees to attorneys and other experts), which may be indemnified in accordance with the provisions of the Companies Law, all up to a limit of NIS 1 billion, linked to the CPI.

   Bank Tefahot undertook vis-à-vis Tefahot Issuance that, should it be unable to fulfill its obligations to the indemnity recipients, or any one of them, Bank Tefahot would pay to Tefahot Issuance any amount that Tefahot Issuance will be found liable to indemnify, beyond the amounts paid by Tefahot Issuance.

   Under terms and conditions of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

8) In October 2002, the Board of directors of Bank Tefahot, following the approval of the Audit Committee, approved the bestowing of an advance undertaking for indemnification of directors and other officers of Bank Tefahot (together – "the officers"). Accordingly, Bank Tefahot undertakes, subject to the conditions detailed in the letter of undertaking and to the provisions of the Companies Law, to indemnify the officers for any liabilities or expenses imposed on the officer due to his capacity as an officer in Bank Tefahot, provided that these activities are related, directly or indirectly, to one or more of the events listed in the addendum to the letter of undertaking the indemnification.

The cumulative amount of the indemnification to be paid by Bank Tefahot to all the officers will not exceed 25% of the shareholders' equity of Bank Tefahot according to its annual financial statements for 2001, adjusted for the CPI, beginning from December 2001, or 25% of the shareholders' equity of Bank Tefahot according to the latest financial statements published as of the actual payment date of the indemnification, whichever is lower.

In November 2002, a General Meeting of the shareholders of Bank Tefahot ratified this resolution.

Under terms and conditions of the merger of Bank Tefahot into the Bank, the Bank assumed this commitment.

9) On June 30, 1998, an extraordinary general meeting of Bank Adanim, following approval by its Board of Directors and approval of its Audit Committee, ratified an undertaking to indemnify ("indemnification letter") for officers in Bank Adanim. The indemnification letter will apply to officers, as defined in Section 96(24) of the Companies Ordinance, who, on the approval date of the indemnification by the General Meeting ("date of record"), are serving in Bank Adanim or whose tenure ended in a period not earlier than 4 years from the date of record.

Pursuant to the indemnification letter, Bank Adanim will indemnify any officers in Bank Adanim for any financial liabilities imposed on them by a ruling, including legal expenses, for an act or omission done directly or indirectly in the matters itemized in the letter of indemnification, namely the offer of sale to the public of securities of Mizrahi Tefahot by the State, pursuant to a prospectus published in May 1998.

Pursuant to the indemnification letter, the amount of the indemnification to be paid by Bank Adanim (in addition to the amounts to be received according to the officers' insurance policies as detailed below) to all officers, on a cumulative basis will not exceed NIS 70 million, with the amount linked to the last CPI published before the date of record until the CPI published before the date of payment.

Bank Adanim will take action, to the extent possible, so that during the 10-year period beginning on the date of record, an officers' insurance policies will be purchased by or for Bank Adanim, which will cover the matters covered by the indemnification, the amount of which, including restitution/reinstatement will not be lower than the aforementioned amounts.

On December 16, 2002, a General Meeting of Bank Adanim, following approval by the Audit Committee and ratification by its Board of Directors, ratified the letter of indemnification undertaking ("indemnification letter") for officers in Bank Adanim. The indemnification letter will apply to officers, as defined in Section 1 of the Companies Law, 1999, who, on the approval date of the indemnification letter by the general meeting ("date of record") serve in Bank Adanim. Pursuant to the indemnification letter, Bank Adanim will indemnify all of the officers in Bank Adanim for all the financial liabilities to be imposed on them by a ruling, including legal expenses, relating to an act or omission done directly or indirectly in matters listed in the indemnification letter, up to the indemnification amounts.

The indemnification amounts to be paid by Bank Adanim for each officer, on a cumulative basis, for one or more of the types of events provided in the addendum to the letter of undertaking, shall not exceed 25% of the shareholders' equity of Bank Adanim according to its financial statements for the year 2001, adjusted from time to time, according to the rate of increase in the CPI compared with the CPI for December 2001 that was published in January 2002 ("total indemnification amount). In the event the officer will receive indemnification from the insurer of the officers' insurance policies for the matter covered by the indemnification, the indemnification will be provided by Bank Adanim in the amount of the difference between the amount of financial liabilities imposed on the officer and/or legal expenses incurred by or charged to the officer, and between the amount received from the insurer on this matter, provided that the amount of indemnification for which Bank Adanim will be charged will not exceed the total indemnification amount.

Beginning December 2002, Bank Adanim was one of the insured parties in the officers' insurance policies purchased by the Bank for itself and its subsidiaries and related companies, which is in effect until April 5, 2007.

Under terms and conditions of the merger of Bank Adanim into the Bank, the Bank assumed this commitment.

Note 26 – Contingent Liabilities and Special Commitments – continued

10) Various claims are pending against the Bank and its subsidiaries, namely, claims of customers, as well as motions for recognition of various class actions. In the estimation of the management of the Bank, based on the estimation of the managements of its subsidiaries and on the opinion of their legal counsel as to the possible outcome of the pending claims and motions for approval of claims as class actions, the financial statements include appropriate provisions, where necessary, to cover possible damages.

    Below are details of significant claims, including motions for approval of class action status and claims in which the amount claimed (excluding interest and fees) exceeds 1% of Bank equity attributable to equity holders of the Bank:

    A) In May 2011, the Bank received a claim and motion for approval of class action status. The claim concerns two alleged claims made against the Bank – firstly, late reporting to the Court Order Execution Service of payments made to reduce debt which is subject to proceedings at the Court Order Execution Service. Secondly, failure to indicate on the reporting forms the number of the principal to be reduced by the reported credit, and the number of the interest calculation rule applied to the reported payment amount. The lawsuit and motion allege that, by late reporting to the Court Order Execution Service and by failure to provide the aforementioned indications on the reporting forms, the Bank misleads clients, causes clients not to be credited with interest in line with the date of their payment and in accordance with the correct interest rate, creates a situation in which the debt on Court Order Execution Service files is higher than the real debt, and over-charges in payments. The lawsuit and motion further allege that the Enforcement and Collection Authority and the Court Order Execution Service admit that under crediting occurs in case of late reporting and failure to provide the required indications on the reporting form.

       The plaintiff claims he is unable to estimate the damage incurred by the entire class of plaintiffs, but believes (on a basis which is not clear to the Bank) that it amounts to hundreds of millions of NIS.

       On January 9, 2012, the Bank filed its response to the motion, describing in detail the factual and legal defense claims made by the Bank. On May 20, 2012, the plaintiff filed their response to the Bank's response to the motion. In view of new claims made by the plaintiff in their response to the Bank's response, the Bank filed a further, more detailed response on August 15, 2012.

       On October 17, 2012 and on October 29, 2012, the Court held preliminary hearings in this case.

       The parties have agreed and launched a reconciliation process aimed to try and resolve their differences. The reconciliation process was concurrent with regard to other motions filed against other banks for the same cause, as well as with regard to other motions for class action status filed against the Bank and against other banks for causes related to debt management in Court Order Execution Service files. The parties negotiated directly from August 2014 and in January 2016, due to a specific disagreement, the negotiations between the parties were terminated. They were resumed soon there after, in an attempt to reached an agreed arrangement. On August 29, 2016, a Court hearing took place and the Court resolved that the parties to this lawsuit and to the lawsuit described in section E. below, should file a settlement agreement and motion for approval thereof, no later than October 30, 2016. The resolution dated November 7, 2016 allowed the parties an extension to file a settlement agreement and motion for approval thereof, no later than November 30, 2016. On January 16, 2017, a hearing took place with regard to the settlement agreement, after which it was agreed that the parties would file, within 45 days, a settlement agreement and motion for approval thereof; a hearing is scheduled for March 28, 2017.

    B) In August 2011, a claim and motion for class action status was filed with the Central District Court amounting to "hundreds of millions of NIS". No specific amount was specified in the statement of claim. The plaintiff seeks a verdict, pursuant to the Class Action Lawsuit Act, whereby the claim would be made on behalf of all Bank clients whose account was charged legal fees not approved by any legal jurisdiction, or whose account was charged unlawful interest with respect to approved legal fees.

In February 2012, the Bank filed its response to the motion and in August 2012, the plaintiff filed their response to the Bank's response to the motion.

In November 2012, the parties launched a reconciliation process designed to try and settle their disagreements. The reconciliation process was concurrent with regard to other motions filed against other banks for the same cause, as well as with regard to other motions for class action status filed against the Bank and against other banks for causes related to debt management in Court Order Execution Service files. The parties negotiated directly from August 2014 and in January 2016, due to a specific disagreement, the negotiations between the parties were terminated. They were resumed soon there after, in an attempt to reached an agreed arrangement.

Following direct negotiations between the parties, the parties reached an agreed settlement brought for approval by the Court on November 14, 2016. On January 16, 2017, a hearing took place at which the parties agreed for the Bank to respond to questions raised at the hearing with regard to the settlement agreement and motion for approval filed by the parties. On February 8, 2017, the Bank filed its comments with the Court.

C) In September 2011, a claim and motion for class action status was filed with the Central District Court against the Bank, Bank Leumi Le Israel Ltd. and Bank HaPoalim Ltd., for alleged unlawful charging of compounded interest, in contravention of statutes and agreements, on housing loans – including targeted loans, eligibility loans and additional loans, excluding standing loans. The total claim amount against the banks was NIS 927 million. The Bank's share of this claim amounts to NIS 364 million.

In May 2012, the Bank filed its response to this claim, claiming *inter alia* that it was unfounded, that the Bank acted in accordance with statutory provisions and did not charge any compounded interest in the manner in which banks in general and the Bank, in particular, acted.

The position of the Supervisor of Banks, which supports the banks' position, was also filed in this case.

In July 2013, an evidentiary hearing took place and the experts on behalf of the parties were questioned. The plaintiffs filed their summation. In September 2014, the Bank filed its summation and in December 2014, the plaintiffs filed their summary responses.

On August 16, 2015 a verdict was issued, rejecting the motion for class action status.

On December 7, 2015, the parties appealed the verdict to the Supreme Court. The parties were ordered to file their summations. A hearing is scheduled for October 25, 2017.

D) In October 2012, a claim with motion for class action status was filed with the Tel Aviv District Court, against the five large banks – including the Bank – alleging failure to match the client debt amount on Bank accounts and the debt amount indicated in Court Order Execution Service files. The plaintiffs indicate that the claim amount cannot be estimated at this stage.

In March 2014, the Bank filed its response to the motion and in April 2014, the plaintiff filed their response to the Bank's response. In its resolution dated September 14, 2014, the Court forwarded the issues raised by the motion to the Supervisor of Banks and the Attorney General for their opinions. On February 1, 2015, the Attorney General filed its position (on behalf of the Enforcement and Collection Authority and on behalf of the Bank of Israel) and on March 26, 2015 the banks filed their response to the position of the Attorney General. The plaintiffs' response to the aforementioned response by the banks was filed on April 1, 2015.

A preliminary hearing took place on April 19, 2015 and as resolved by the Court, a further hearing took place on June 21, 2015, attended by representatives of the Enforcement and Collection Authority, in which the Court ordered, inter alia, that the Enforcement and Collection Authority should file its revised position – which was filed on October 8, 2015. On December 20, 2015, the banks filed their response to the revised position by the Attorney General and also filed a motion to allow them to file a third-party notice against the Enforcement and Collection Authority. The Enforcement and Collection Authority filed its response to the motion and the Bank filed its response on July 10, 2016.

At a hearing held on July 13, 2016, the Court proposed an outline for a settlement of disagreements in this case; the proposed settlement was discussed and consequently, the banks filed a notice of consent to the Court proposal and principles thereof with regard to how the disagreements in this case should be resolved, as proposed to the parties at the July 13 hearing.
As resolved by the Court on October 5, the position of the Attorney General with regard to the proposed outline and the notice filed by the banks in this regard, was filed on October 31, 2016. As ruled by the Court, the Bank filed its response to the position of the Attorney General on November 10, 2016.

On November 15, 2016, a verdict was issued – approving the plaintiff's withdrawal of the lawsuit and dismissal thereof.

E) In December 2012, an action and a motion for recognition as a class action were filed with the Tel Aviv District Court, with regard to setting rates of arrears interest charged by the Bank in Court Order Execution Service cases filed against debtors. According to the plaintiff, the Bank charges interest significantly higher than the maximum interest rate on checking accounts. The plaintiff is unable to estimate the amount claimed.
The parties agreed to add this motion to the reconciliation process on-going with regard to other motions which also concern collection processes conducted by the Bank against clients in debt, as stated in sections A. and B. above and on January 4, 2016, a resolution was issued to refer the above claim for hearing by the same party as the above claims.
As noted above, the parties negotiated directly from August 2014 and in January 2016, due to a specific disagreement, the negotiations between the parties were terminated and were recently resumed. Upon resumption of negotiations between the parties, on July 31, 2016 the Bank filed an agreed motion seeking an extension to file its response by September 30, 2016. On August 29, 2016, a Court hearing took place and the Court resolved that the parties to this lawsuit and to the lawsuit described in section A. above, should file a settlement agreement and motion for approval thereof. Concurrently, the Court approved a further extension for the Bank to file its response to this motion, by November 30, 2016.
On January 16, 2017, a hearing took place with regard to the settlement agreement, at which it was agreed that the parties would file, within 45 days, a settlement agreement and motion for approval thereof. A hearing was scheduled for March 28, 2017.

F) 1. In August 2013, a claim and motion for class action status in the amount of NIS 10.5 billion were filed with the Tel Aviv District Court against the 5 major banks, including the Bank, and against bank Presidents, including the Bank President & CEO, in person – with respect to unlawful charging of commissions by the banks with regard to foreign currency conversion and transfer, which the plaintiffs allege was made without proper disclosure. The plaintiffs also claim that a restrictive trade practice exists among the banks.

In September 2013, the defendants filed a motion with the Court, seeking dismissal of the personal claim against bank Presidents, and the individual claim against them was dismissed.

A revised motion for class action status filed on February 3, 2014 set the claim amount at NIS 11.15 billion for all banks on aggregate.

2. In March 2014, a claim and motion for class action status in the amount of NIS 2.07 billion were filed with the Tel Aviv District Court against the Bank and against Bank Otzar HaChayal, Mercantile Discount Bank, Bank Igud Le Israel and Bank Yahav, alleging unlawful commissions charged by the banks with regard to conversion and transfer of foreign currency (this claim is identical to the aforementioned one).

A motion has been filed to combine heating of this motion with the first aforementioned motion and the Court has agreed to said motion and has combined both claims.

On December 23, 2014. the Bank filed its response to each of the motions for class action status. The plaintiffs filed their response to the combined response to the two aforementioned motions, in which they attributed part of the claim amount to each of the plaintiffs; the Bank's alleged share for both these claims amounted to NIS 1.145 billion in principal.

On March 8, 2015, a pre-trial hearing of this case took place, after which the Court set deadlines for completion of the statements of claim by all parties.

On April 23, 2015, the plaintiffs filed, in conformity with the Court decision, a summary motion for approval of class action status, based on the current motions. The Bank filed its response to the summary motion on October 18, 2015.

On October 25, 2015, another pre-trial hearing took place. In this hearing, the Court combined the hearing of motions filed against the credit card companies and the Postal Bank with those filed against the banks. Evidentiary hearings took place in March 2016. The plaintiffs filed their summations in April 2016. Given the banks' motion to dismiss the plaintiffs' summation, an extension was granted for the banks to file their summations within 60 days after the decision on the motion to dismiss. On August 10, 2016, the Court accepted the motion by the banks and ordered the summation by the plaintiffs to be dismissed; on September 4, 2016, the plaintiffs filed new summations; and on January 17, 2017, the Bank filed its summation.

G) In March 2014, a claim and motion for class action status were filed with the Central District Court against the Bank, alleging unlawful charging of warning letter commission and excessive interest charged for exceeding the authorized limit on accounts, allegedly in breach of Proper Banking Conduct Directive 325 concerning "management of credit facility in checking account". The plaintiff claims that this directive is breached, *inter alia*, by the Bank allowing charges to clients which the Bank could and should have rejected, since the Bank may not allow clients to exceed their credit facility – thereby causing them to exceed their credit facility.

The plaintiff claims to be unable to estimate the damage caused to potential class members, but believes this amounts to hundreds of millions of NIS.

The Bank filed its response to the motion in October 2014. On March 10, 2015, the plaintiff filed their response to the Bank's response to the motion. A common pre-trial hearing for the three motions filed against the Bank, Bank Leumi and Discount Bank – against which claims were filed citing similar causes – took place on March 26, 2015. On November 2, the Bank filed its motion to reject parts of the plaintiff's response to the Bank's response. The plaintiff has yet to file its response. On April 18, 2016, another preliminary hearing took place; according to the Court decision, the plaintiffs were granted an extension to file their response to the motion by the Bank to dismiss part of the plaintiff's response to the Bank's response. On October 27, 2016, another pre-trial hearing took place to discuss motions by the banks to dismiss sections in the plaintiffs' response to the banks' response to the motion; another pre-trial hearing took place on April 18, 2016. On October 27, 2016, a pre-trial hearing took place to discuss motions by the banks to dismiss sections in the plaintiffs' response to the banks' response to the motion; an evidentiary hearing is scheduled for April 2017.

H) In August 2014, a counter-claim was filed with the Supreme Court in New York by a plaintiff who is subject to debt collection proceedings concerning his guarantee to secure credit obtained by a company it controlled The plaintiff claims it has sustained damage in excess of USD 57 million due to a breach of verbal commitment made by the Bank to the plaintiff not to enforce his personal guarantee. The plaintiff claims that deeds and omissions by the Bank have resulted in failure to meet his various obligations and in destruction of his business. In March 2015, the Bank filed a motion to dismiss. The plaintiff filed its response in May 2015. On July 10, 2015, the Bank filed its response to the plaintiff's claim and to the motion to dismiss.

On July 31, 2015, a hearing of the motion to dismiss took place. On December 14, the Court rejected the plaintiff's claim with regard to alleged Bank omissions – but left in place the cause of claim with regard to verbal termination of their guarantee.

The Bank filed its response to the plaintiff's claim on February 11, 2016 and document discovery is now under way.

On August 18, 2016, the Bank filed an appeal of the Court resolution to partially dismiss the motion to dismiss filed by the Bank, with regard to the plaintiff's claim that the Bank has verbally approved the termination of their guarantee; on November 11, 2016, the plaintiff filed their response to the appeal.

I) In March 2015, a counter-claim was filed against the Bank with the Central District Court, along with a motion for class action status, with respect to alleged over-charging of commissions in an "individual" account and in a "small business" account, allegedly in breach of Banking Rules (Customer Service) (Commissions), 2008. The plaintiff alleges that the breach was due, inter alia, to the Bank charging holders of "individual" or "small business" account commissions for certain services at higher tariffs than those set for large corporations, in contravention of the aforementioned Banking Rules.

The plaintiff claimed they were unable to estimate the damage incurred by potential class members.

The Bank filed its response to the motion on June 30, 2015. The plaintiff also filed their response to the Bank's response.

According to a Court resolution dated September 10, 2015, the Bank of Israel filed its position on December 15, 2015. On December 16, 2015, another pre-trial hearing took place – at which the parties were urged to negotiate a potential settlement agreement. Another pre-trial hearing took place on March 29, 2016. An evidentiary hearing took place on July 12, 2016. On November 8, 2016, the plaintiff filed their summation and on January 22, 2017, the Bank filed their summation.

J) In March 2015, a claim and motion for class action status was filed with the District Court in Tel Aviv against the Bank, its President, Board members and controlling shareholders, with regard to damage allegedly caused to the plaintiff and to class members due to the alleged breach of mandatory disclosure of material information to investors.

The plaintiff alleges that the defendants have allegedly acted in contravention of the Securities Act, 1968 and relevant regulations, by failing to disclose on the Bank's financial statements that a provision has been made with respect to an investigation against the Bank in the USA, the nature and amounts of such provisions and the fact that the Supervisor of Banks has required the Bank to make provisions on the Bank's financial statements with regard to exposure to investigation by authorities in the USA.

The plaintiff claims that – due to the requirement by the Supervisor of Banks – the Bank made provisions amounting to tens of millions of NIS on its financial statements for the second and third quarters of 2014, classified under "Other expenses".

The plaintiff claims that, based on information in the aforementioned financial statements, tens of thousands of investors have bought Bank shares without having the aforementioned material information. The plaintiff also claims that the price at which class members purchased those Bank shares was higher than the price they would have paid for the shares, had the proper disclosure been made.

No specific amount was specified in the statement of claim. However, the plaintiff referred to the mechanism for calculation of damage whereby, on the date when the alleged deception was made public, the Bank share under-performed the Bank Share Index by 2.19% (excluding Bank HaPoalim and Bank Mizrahi Tefahot).

The plaintiff wishes to specify, in conformity with the Class Action Lawsuit Act, that the lawsuit would be filed on behalf of "anyone who bought shares of Bank Mizrahi-Tefahot Ltd. from the publication date of the financial statements for the second quarter of 2014 (August 13, 2014) and held the shares on February 26, 2015".

The response by the Bank and other defendants was filed on November 19, 2015; discovery proceedings have been completed. On August 3, 2016, the Court approved the consent by the parties to dismiss the controlling shareholders of the Bank from the motion. The plaintiff's filed their response to the response by the Bank and other defendants to the motion on September 11, 2016; on October 9, 2016, the defendants filed a motion to dismiss the plaintiffs' response claiming, *inter alia*, a broader scope. The plaintiff also filed a motion to call the Supervisor of Banks in the relevant period to testify on the motion. The Bank filed its response to the motion on November 2, 2016.

On January 3, 2017, a resolution was given by the Court, whereby the Bank and other defendants may file their response to the plaintiff's response to the defendants' response to the motion. The Court also rules that on the date to be set for hearing of the actual motion, the then Supervisor of Banks would be invited.

See also section 12 with regard to inquiry by the US Department of Justice concerning Bank Group business with its US clients.

K.) In October 2015, a claim was filed with the Central Region District Court, along with a motion for class action status, in the amount of NIS 141.4 million, for charging a fee for "Non-recurring foreign currency transfer to / from overseas". The plaintiff claims that the Bank charges this fee for a non-recurring foreign currency transfer to / from overseas, denominated in USD, in NIS – in contravention of the price list, using the Bank's "Buy/Sell" rate with alleged deception with regard to the cost of the service and the fee amount and in breach of mandatory disclosure. The Bank filed its response on February 17; a pre-trial hearing is scheduled for May 19, 2016.

On May 19, 2016 a verdict was issued, confirming the plaintiff's withdrawal of the motion for class action status.

L) In December 2015, a motion for class action status was filed against Bank Yahav, alleging that Bank Yahav charged individual clients (and small businesses) commissions whose amount and rate exceed the allowed maximum, specified in the price list for non-small businesses. This claim does not specify an estimated claim amount.

M.) In February 2016, a claim and application for class action status was filed with the Tel Aviv District Court against the Bank and against Bank HaPoalim Ltd., Bank Leumi Le-Israel Ltd., Bank Discount Le-Israel Ltd. and First International Bank of Israel Ltd. (hereinafter: "the defendants"). The plaintiff set the claim amount for all defendant Banks, jointly and severally, at NIS 219 million. The motion concerns alleged discrimination in providing service to student groups by age, allegedly in violation of the Prohibition of Discrimination in Products, Services and in Access to Entertainment Venues and to Public Venues Act, 2000 (hereinafter: "the Non-Discrimination Act") and the Banking Act (Customer Service), 1981 (hereinafter: "the Banking Act").

According to the plaintiffs, this is a general policy of all defendants, which seeks to exclude the "non-young" population from student benefit plans and/or from being able to open an account with the terms and conditions of a student account, by setting an age cap for receiving student benefits.

The plaintiff asks, in conformity with the Class Actions Law, for the claim to be filed on behalf of all students discriminated against due to their age, by comparison to younger students, who were precluded from receiving student benefits from the defendants in the past seven years (for causes pursuant to the Banking Act (Customer Service), 1981 or as from July 15, 2014 (pursuant to the amendment to the Non-Discrimination Act). The Bank filed its response to the motion on September 13, 2016 and the plaintiff has filed their response to this response. On October 27, 2016, the plaintiff filed its response to the Bank's response to the motion. A hearing was held on January 25, 2017 and dates for evidentiary hearings were scheduled for September 2017.

N) In January 2016, a claim and motion for class action status was filed with the Jerusalem District Court, amounting in total to NIS 697.5 million, against the Bank, First International Bank of Israel Ltd., Bank Otzar HaChayal Ltd., Bank Yahav for Government Employees Ltd. and Bank Igud LeIsrael Ltd. (hereinafter: "the defendants"). This claim alleges discrimination of the Arab population with regard to access to banking services, in that the defendants do not maintain branches close to Arab population and do not make their banking services accessible to this population – in alleged violation of the Prohibition of Discrimination in Products, Services and in Access to Entertainment Venues and to Public Venues Act, 2000.

The plaintiff seeks a verdict stating, in conformity with the Class Action Lawsuit Act, that the claim is to be filed on behalf of all Israeli residents who are Muslim, Christian or Druze, who suffer from discrimination in access to banking services by the defendants, due to absence of bank branches of the defendants in their town.

The plaintiffs set their claim against all defendants at NIS 697.5 million, noting that each defendant's share of the damage caused to class members is based on their market share – as is their share in compensation to class members. The Bank filed its response to the motion on August 4, 2016 and the plaintiffs filed their response there to on November 13, 2016.

A pre-trial hearing took place on December 19, 2016, at which the Court recommended that the parties reach a settlement in this case. As proposed by the Court, the parties have started negotiations, which have yet to be completed.

For all claims against the Bank Group in individual amounts over NIS 2 million, excluding claims listed in section 10 below, there is additional, non-remote exposure for which no provision was made, amounting to NIS 76 million.

11) Motions for class action status are pending against the Bank and subsidiaries thereof, where the amount claimed is material, as well as appeals to the High Court of Justice, as itemized below, which, in the opinion of the Bank's management, based on the opinion of the managements of its subsidiaries, and on the opinion of their legal counsel, the prospects for which cannot be estimated on the date of the financial statements, hence no provision was made for these.

A) In March 2015, a motion for approval of derivative claim was filed with the District Court in Tel Aviv ("the motion") on behalf of the Bank and its subsidiary, UMB (Switzerland) Ltd. ("Mizrahi Switzerland") against past and incumbent officers of the Bank and of Mizrahi Switzerland, at a minimum amount of NIS 95 million, for damage allegedly sustained by Mizrahi Group due to the defendants' deeds and omissions with regard to providing assistance to US clients in avoiding taxes in the USA. The plaintiff claims that defendants should reimburse the Bank for the damage they have caused to Mizrahi Group in general and to the Bank in particular.

On March 24, 2015, a Bank shareholder filed a motion in conjunction with the aforementioned proceeding, seeking to join as a party to said proceeding and to delay the hearing or, alternatively, to dismiss it out of hand, given the motion for document discovery filed by that shareholder in December 2014 with the Tel Aviv District Court against the Bank and its officers pursuant to provisions of Section 198a of the Companies Law 1999 ("the motion for discovery"). In conjunction with the motion for discovery, the plaintiff asked the Court to instruct the Bank and the other defendants to provide to the plaintiff various documents with regard to on-going proceedings in the USA, so as to allow the plaintiff to review potential filing of a motion for derivative defense (on behalf of the Bank in the USA) or filing of a motion for approval of derivative claim (against executives and employees of the Bank). The plaintiff claims in the motion for discovery that the process of the motion for discovery is a pending process which has priority over the motion for approval – which is why hearing of the motion for approval should be delayed and even dismissed out of hand.

On May 10, 2015, the Court approved, in conjunction with the motion for approval, a hearing arrangement agreed by the parties in this case, with regard to dates for filing statements of claim whereby, *inter alia*, at this stage the deadlines for filing the defendants' responses to the motion for approval would be suspended and soon after a decision is given, *inter alia*, with regard to the aforementioned motion to join and subject to it, the schedule for filing these responses would be set considering, *inter alia*, the progress made in proceedings with the Department of Justice in the USA.

It should be noted, with regard to the motion for discovery, that on May 3, 2015, a preliminary hearing of this motion took place wherein the Court approved the agreement reached by the parties, that the hearing of the actual motion for discovery would currently be suspended, pending completion of document discovery for filing with authorities in the USA. In December 2015, the Court resolved that the motion for approval would be dismissed, but the dismissal would be delayed that should the motion for discovery be allowed and should the plaintiff of the motion for discovery file a motion for approval 90 days after receiving the documents in a timely manner as instructed by the Court in its resolution, the motion for approval would be dismissed. Should the discovery motion be dismissed, or should a motion for approval not be filed by 90 days after receiving the documents – the motion for approval would be considered a preliminary motion to any other motion, if filed.

On April 18, 2016, the Court resolved to postpone the hearing of the motion pending conclusion of the inquiry and reporting of its outcome.

See also section 12 with regard to inquiry by the US Department of Justice concerning Bank Group business with its US clients.

B) In May 2016, a lawsuit was filed against the Bank with the Tel Aviv Yafo District Court, along with a motion for class action status, amounting to NIS 220 million. The lawsuit alleges unlawful over-charging of commissions to clients eligible to be classified as a small business, in breach of the Bank's duties in its relations with clients.

The plaintiff claims that the Bank has not disclosed to clients who manage a small business that they are eligible for the lower commission schedule of a "small business", in order to foil the commission reform and to charge small businesses commissions other than according to the small business tariff, allegedly resulting in unlawful gain at the expense of these clients.

The Bank filed its response to the motion on November 1, 2016 and the plaintiff filed their response to the Bank's response on November 30, 2016.

A pre-trial hearing of the motion is scheduled for April 23, 2017.

C) In May 2016, a claim and application for class action status was filed with the Central District Court against the Bank and against Bank HaPoalim Ltd., Bank Discount Le-Israel Ltd. and Bank Leumi Le-Israel Ltd. ("the defendants"). The motion alleges over-charging of commissions to clients eligible for reduced commissions (senior citizens, new immigrants, students etc.) for transactions conducted through a teller, where a cash commission was charged as well as over-charging of a commission up to the monthly minimum – without taking into account the teller transaction commission paid in cash, which is allegedly unlawful.

The plaintiffs claim that when the teller transaction commission is charged in cash at the counter, the defendants do not apply the rates applicable to clients in these population groups – and charge them the commission based on the standard price list. They also claim that the defendants do not take into account commissions charged in cash at the counter for calculation of the monthly minimum and therefore the defendants over-charge the minimum commission. The plaintiffs claim they are unable to estimate the exact amount unlawfully charged, allegedly, to all class members – but estimate this to be "a large amount, in the millions of NIS or even higher". The Bank filed its response to the motion on November 22, 2016 and the plaintiffs filed their response to the Bank's response to the motion on December 22, 2016.

On January 5, 2017, a pre-trial hearing took place; in conformity with the Court's resolution, on January 16, 2017 the parties consented to the suggestion made by the Court, whereby the case would be decided based on the existing statements of claims. A resolution dated January 18, 2017 ratified the parties' consent and the parties would be invited to elaborate their claims at another hearing. A new date has yet to be scheduled.

D) In August 2016, a motion for class action status filed with the Tel Aviv-Yafo District Court, against the Bank and 9 other banks, alleging unlawful over-charging of fees to clients not classified as individuals or small businesses, in breach of the Bank's duties in its relations with clients.

The plaintiffs claim that the defendant banks charge any clients not classified as individuals or small businesses, fees not listed in the binding statutory price list, in conformity with the Banking Act (Customer Service), 1981 or in amounts higher than specified there in, allegedly in violation of the Act. The plaintiff claim that upon filing the motion, they are unable to demonstrate the exact size of the class or of the damage. However, they set the total damage incurred by the class at an estimated NIS 1 billion or higher, against all defendant banks together.

The Bank has yet to file a response to this motion.

E) In December 2016, a motion for class action status was filed with the Central District Court against the Bank, Bank HaPoalim, Bank Leumi and Discount Bank, alleging charging of foreign currency-related fees not in conformity with provisions of the complete price list, as stated in Banking Regulations (Customer Service) (Fees), 2008 and in violation of Section 9 of the Banking Act (Customer Service), 1981. According to the plaintiff, the defendant banks charge minimum fees with respect to various foreign currency-related transactions, graduated according to transaction amount, allegedly in contravention of provisions of the complete price list, whereby the defendant banks must list the fee they charge for a range of transactions as "Percentage (minimum, maximum)". The plaintiff further claims that the defendant banks are in breach of the Anti-Trust Act by maintaining a restrictive arrangement.

The plaintiff notes that they do not have the final data, which are available to the defendants. However, they estimate the damage incurred to be at least NIS 500 million.

The Bank has yet to file a response to this motion.

F) In August 2016, a motion for class action status was filed against Bank Yahav and other banks, alleging charging of commissions to clients which are not, allegedly, in the complete price list as issued by the Bank of Israel. The plaintiff estimates the claim amount at NIS 1 billion for all of the banks.

G) In February 2017, a motion for class action status was filed against Bank Yahav with the Central District Court. The plaintiff claims that Bank Yahav's transition to a new core system caused its clients to incur damage due to impact to service levels in various service channels which, allegedly, left the clients unable to conduct transactions in their accounts.

The plaintiff estimates damages to each class member at NIS 1,000 or higher and has set the claim amount at NIS 370 million (based on 370,000 Bank Yahav clients).

Note 26 – Contingent Liabilities and Special Commitments – continued

12) In 2011, authorities in the USA and in Switzerland have been negotiating the tax treaty between these countries. As requested by Swiss authorities, several Swiss banks, including Mizrahi Bank Switzerland, have provided, as from September 2011, to Swiss authorities quantitative data as requested about their business with US clients, to be provided to US authorities.

In a letter dated August 2013, Mizrahi Bank Switzerland was informed by the US Department of Justice that an investigation of its business has been launched. The letter did not indicate the suspicions which led to the launch of this investigation. This notice means that Mizrahi Bank Switzerland is not in Category 2, which qualifies for a Non-Prosecution Agreement pursuant to the US DOJ program for Swiss banks ("the Swiss program"). The financial implications of the Swiss program for Category 2 banks are determined based on the amount of assets held by US citizens and residents and the dates of such holdings. Although the Swiss program does not apply to Mizrahi Bank Switzerland due to the aforementioned letter, the bank has expressed its willingness to cooperate with and to assist the US Department of Justice in conformity with the Swiss program and has provided the requested quantitative data, as noted.

In addition to the foregoing, in August 2013 the Bank was informed that the US DOJ continued to review loans extended to clients by the Los Angeles branch against collateral provided in the form of monetary deposits in Israel. Thereafter, the Bank has provided to the US DOJ quantitative data about such back-to-back transactions.

On April 14, 2014, the Bank branch in Los Angeles received a subpoena, demanding it to produce documents related to a Bank employee and to a Bank employee who retired five years ago, as well as to banking services provided at the Los Angeles branch, provided that such documents are available at the Bank branch in Los Angeles. The branch has provided the required documents.

On April 30, 2014, an indictment was filed with the Court in Los Angeles against the former Bank employee in Los Angeles who has retired; the indictment alleges , *inter alia*, that the employee aided US clients of the Bank to avoid tax payment. The Bank is not named on the indictment, no violation is attributed to the Bank, referred to exclusively as "Bank A of Tel Aviv". On September 19, 2014, the Bank was required by US DOJ to provide documents and quantitative information with regard to this indictment. On October 31, 2014, the retired Bank employee was acquitted by a jury of all charges.

In June 2014, the Bank was first informed of expansion of the US DOJ investigation, which would apply to all inter-state activities of the Bank Group with its US clients, including the aforementioned back-to-back transactions.

In a letter dated July 25, 2014, the US DOJ required the Bank to provide data and information with regard to a wide range of issues concerning inter-state transactions with US clients of the Bank Group, including quantitative data with regard to accounts of US clients for the period from January 1, 2002 to the letter date ("the effective period"); internal and external communications by electronic messages; operations and marketing, compliance, employee training, remuneration, policy documents and procedures; internal audit and external audit reports with regard to Bank Group operations with its US clients and a long list of other documents and data as listed in the aforementioned letter.

In order to collect the information and date thus required by the US DOJ, the Bank engaged, in August 2014, the services of external experts for data research and validation and the services of legal counsel in the USA, who joined the Bank Group's team of legal counsel (in Israel and in the USA) and in the first quarter of 2015, this team was expanded with additional legal counsel.

In a letter dated November 25, 2014 to the US Department of Justice, the advisors handling this issue on behalf of the Bank together with the external experts, provided a preliminary detailed description of the mapping process of available computer-based information at the Bank Group (in Israel, Switzerland, London and Los Angeles) with regard to accounts of US clients and of electronic messages, following visits to various Bank Group sites and on discussions with Bank Group officers, in order to assess the scope and complexity of the information and data required by the US DOJ.

In the aforementioned letter, the external experts estimated the schedules required for review of computer-based information with regard to the Bank Group's US clients, for analysis of this information based on specified criteria and for validation of their findings. According to the preliminary estimate provided by the external experts, the required quantitative data should have been ready for delivery to the US DOJ by April 30, 2015, subject to conditions, assumptions and reservations listed by these experts.

In December 2014, agreements signed with an Israeli bank subject to an investigation were made public – including a Deferred Prosecution Agreement with the US DOJ. The aforementioned report also noted that a banking subsidiary of said bank in Switzerland was made subject to the Swiss program. The Bank maintains that the conduct of other banks, the structure of their inter-state operations and individual agreements by those banks should not be used in comparison to the Bank Group, including with regard to a potential arrangement between the Bank Group and the US DOJ.

Nevertheless, the Supervisor of Banks, after reviewing the circumstances and for reasons of accounting conservatism, directed the Bank to accrue a provision with respect to issues related to the aforementioned events and later on instructed the Bank to disclose the same on its 2014 annual report. Consequently, while the Bank Group fully retains its rights and claims, the Bank's 2014 financial statements include a provision amounting to NIS 95 million, estimated based on a calculation founded on a theoretical assumption, as directed by the Supervisor of Banks, whereby Mizrahi Bank Switzerland would be included in the Swiss program, although the bank was informed that this program does not apply there to and based on the Bank's understanding of the implications of the Swiss program.

In conformity with ISA requirement, a Note to the 2014 annual financial statements includes additional detailed explanations as well as details of provisions made in 2014, although the Bank maintains that these provision amounts are not material.

In 2015, the Bank continued to intensively create a computer-based information repository to include the quantitative information about US clients, as required by the US DOJ. Accordingly, the external experts have revised the schedule for delivery of the quantitative data to the US DOJ, as noted above, to March 15, 2016.

Other than the content of the letter dated July 25, 2014, the US DOJ, in another letter dated November 4, 2015, gave instructions designed to clarify, focus the required documents and data in conjunction with the Bank Group's co-operation with regard to the investigation concerning its business with its US clients.

Validation of the quantitative data in the repository with regard to business with US clients throughout the Bank Group was completed in the first quarter of 2016.

On February 8, 2016, the Bank provided to the US DOJ the requested quantitative information with regard to closed accounts of US clients at Bank branches in Israel and on March 14, 2016, the Bank delivered to the US DOJ the quantitative data with regard to balances of its US clients in Israel. On May 27, 2016, the Bank also delivered to the US DOJ additional quantitative information requested by the US DOJ in December 2015.

The process of collecting electronic messages with regard to activity of US clients at the Bank Group has been completed and their review by the Bank experts and advisors has yet to be completed. In co-ordination with the US DOJ, some of these electronic messages have been provided to the US DOJ.

Note 26 – Contingent Liabilities and Special Commitments – continued

According to the letters, the Court order and additional discussions, the Bank should provide additional information and documents. The great majority of these have already been provided, including in meetings with representatives of the US DOJ, who also indicated actions which the Bank should take in order for the investigation to be concluded. This is part of the constant contact of the Bank and of Mizrahi Bank Switzerland with the US DOJ, in order to reach a comprehensive outline for the entire Bank Group with regard to this investigation.However, at this stage there are no negotiations taking place with the US DOJ with regard to the inquiry or to its implications in terms of any arrangement and in terms of any monetary implications for the Bank Group, if any, of such an arrangement when formulated.

The Bank regularly reports these events to the Supervisor of Banks and Mizrahi Bank Switzerland reports these to the Swiss supervisory authorities.

According to the opinion of the Bank's legal counsel, based on data in the computer-based repository which has been validated and considering arrangements made by the US DOJ with other banks with regard to investigations concerning undisclosed accounts of US taxpayers, certain data in the repository may be relevant to Bank Group exposure, should the Bank's position about these data not prevail.

Based on the aforementioned opinion, the provision with respect to this inquiry amounts to USD 44.3 million (NIS 170 million). This amount was calculated for data which may be relevant, according to opinion of the Bank's legal counsel and for components which, according to the opinion of the Bank's legal counsel, should be accounted for, as the case may be. The estimated tax amount which the US clients associated with said data ("the relevant clients") should have paid to the IRS in the USA, revenues accrued by the Bank due to banking activity of the relevant clients and the percentage of monetary assets of the relevant clients. As for data related to Mizrahi Switzerland business with US clients, the provision was calculated based on a theoretical assumption whereby Mizrahi Switzerland Bank is included under Category 2 of the Swiss Program.

Note that the Bank's legal counsel have expressed their opinion that at this stage, it is not possible to estimate the potential loss which the Bank Group may incur with respect to this inquiry, the relevant exposure amount nor the exposure range for the Bank Group. This is due, *inter alia*, to the fact that based on the professional experience of US legal counsel, such conclusions cannot be made prior to analysis of all of all data and information to be provided and because, as noted above, discussions with the US DOJ with regard to formulating an appropriate outline for the Bank Group have yet to start.

Because, as noted above, discussions with the US DOJ with regard to formulating an appropriate outline for the Bank Group have yet to start, it may transpire in future that the realized loss significantly exceeds the provision made to date.

13) On November 18, 2008, the Bank entered into an agreement with Israel Credit Cards Ltd. (hereinafter: "CAL") and with Diners Club Israel Ltd., a company controlled by CAL (hereinafter: "Diners") – (hereinafter jointly: "CAL Group") with regard to jointly providing Visa, MasterCard and Diners Club charge cards, including cards under the Bank brand (hereinafter: "the cards"), to be distributed by the Bank to its clients. The agreement sets forth the parties' rights as well as operating arrangements and service provision by CAL Group for the cards, as well as all other terms and conditions related there to.

In conjunction with the agreement, the Bank received an option to acquire from CAL, by way of allotment, up to 121,978 ordinary CAL shares, which if allotted upon the date of signing the agreement would have constituted up to 10% of CAL's ordinary share capital, fully diluted.

The agreement expired on November 18, 2013 and the Bank did not exercise any options during this period.

On March 2, 2014, the Bank and CAL Group signed an agreement revising the joint issuance agreement. The revised agreement is effective for a 5-year term from its signing date.

This agreement updated the operating and marketing arrangements for the cards, as well as remuneration of the parties.

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

14) A trust company that is a subsidiary of the Bank executes trust transactions that include primarily trusteeships for trust funds, for debenture holders, for owners of restricted shares and for the maintenance of bank accounts.

15) In a labor agreement signed between the Bank and its employee representatives on December 30, 1993, the Bank made available long-term loans to its employees, to finance the retroactive purchase of pension rights from certain pension funds with which the Bank had undertakings in this connection, which bear specified interest and are CPI-linked. It was agreed that if, on the maturity date of each of the aforementioned loans, it becomes clear that the linkage differentials and the interest accrued exceed the yield accumulated in an agreed provident fund, they would be reduced accordingly. The tax effects, if any, related to this reduction will devolve on the Bank. When such a difference is created, an appropriate provision is made.

    At the balance sheet date, the balances of these loans amount to NIS 11 million.

16) The Bank has undertaken vis-à-vis the trustee for debentures and subordinated notes issued by Mizrahi Tefahot Issue Company Ltd., to fulfill the payment terms, as stated in the debentures and subordinated notes.

17) The Bank has committed to borrowers in certain savings plans who would borrow from the Bank, to the following fixed terms[(1)]:

	December 31,	
	2016	2015
0.25% less than the interest prevailing at the time the loan was issued	632	766

(1) The commitment may be utilized only if certain conditions stipulated in the savings plans are met. Granting of credit is subject at all times to the Bank's exclusive discretion, in accordance with procedures specified by the Bank, with due consideration to client attributes and subject to review of the actual client application for credit to be granted by the Bank.

18) As from July 1, 2004, a two-year agreement went into effect between Bank Tefahot, at that time, and the Government, whereby the collection commission rate determined by the tender held by the Ministry of Finance, with the participation of the mortgage banks will apply to loans to eligible borrowers issued on or after said date. This agreement has been continuously extended each year, most recently through June 30, 2015.

    In May 2008, another agreement between the Ministry of Finance and the banks became effective (the agreement is expected to be renewed annually, unless any of the parties gives notice of their wish to terminate the agreement), whereby loans to eligible borrowers with low point rating are provided out of Bank funds and at Bank risk. The interest on these loans is determined based on interest for special assistance loans out of Ministry of Finance funds.

    Loan terms have been specified to be 25, 20, 15 or up to 10 years, at the customer's choice, but no longer than the term of assistance out of Ministry of Finance funds. The remainder of the conditions would be in line with generally acceptable conditions for assistance out of Ministry of Finance funds, including a waiver of early repayment commission.

    For loans granted to certain eligible borrowers, the Ministry of Finance pays the banks which grant loans out of Bank funds the difference between the actual interest rate charged and the average interest rate published by the Bank of Israel, plus spread. Concurrently with loan origination, as stated above, the banks may continue to grant loans out of Ministry of Finance funds to low-rated eligible borrowers, under terms of the previous agreement (dated 2004) and subject to total loans for the Group of low-rated eligible borrowers not exceeding 8% of total Bank loans to this group (out of Bank funds and out of budgeted funds).

Note 26 – Contingent Liabilities and Special Commitments – continued

The agreement for provision of assistance to eligible borrowers out of Bank funds, signed in 2008, has been extended through April 30, 2015.

Group revenues from all loans to eligible borrowers under State responsibility in 2016 amounted to NIS 41 million, compared to NIS 54 million in 2015.

On January 1, 2015, the Bank joined the fast track process to refinance directed loans, as initiated by the Bank of Israel and the Ministry of Construction and Housing. According to a circular issued by the Bank of Israel (Bank-Client Division), this campaign, started on January 1, 2015, was designed to allow eligible borrowers who took out a loan out of Government funds to improve the terms of their loans in the NIS, CPI-linked track. The change in terms was made in a fast-track process at a low cost and the loans were provided out of Bank funds in the CPI-linked track bearing fixed interest for the remainder of the loan term. According to this circular, loans provided by the Bank as part of this campaign are exempt from group-based provision at 0.35%, as specified in Proper Banking Conduct Directive 329. The risk weighting of these loans is a reduced risk weighting with regard to capital adequacy. The circular also included further concessions to encourage borrowers to join this campaign. The campaign ended on December 31, 2015.

19) The Bank contracts loan syndication transactions with multiple institutional investors. Some of these transactions are organized, managed and operated by the Bank.

Note 27 – Liens

A. Stock exchange members are required to deposit a system of collateral to secure the fulfillment of all the obligations of their customers and the obligations of the other stock exchange members that are not members of the clearinghouse and their customers, to the stock exchange clearinghouse, with respect to transactions executed through the stock exchange clearinghouse, and to secure their share in the risks fund for this activity as discussed below in Note 26.C.1).

In the framework of system of collateral, the Bank deposits liquid collateral, as provided below:

1) In the account opened by the stock exchange clearinghouse in its name ("collateral account in clearinghouse") government debentures of the Bank were deposited as collateral in favor of the stock exchange clearinghouse, at the full value of the customers' obligations plus the Bank’s share in the risk fund. As of December 31, 2016: NIS 38 million were deposited. (As of December 31, 2015: NIS 53 million).
2) Additionally, in the account opened by the stock exchange clearinghouse in its name for the Bank in another bank, cash is deposited that the Bank furnishes as collateral, as well as the cash to be paid as income on securities that were deposited in the account, the clearinghouse's collateral or cash originating in any other financial right deriving from those securities, including cash proceeds from their sale. As of December 31, 2016, deposits to this account amounted to NIS 19 million (as of December 31, 2015: NIS 15 million).
3) As resolved by the Board of Directors of the Stock Exchange clearing house, the stock exchange clearing house would open an account in its own name with the Bank of Israel for deposit of collateral provided by members of the stock exchange clearing house, which have been deposited with other commercial banks through the account opening date (as set forth in section 2 above). As of December 31, 2016, no funds were deposited in this account.
4) The accounts discussed in Par. 1 and 2 above have been pledged under a first-level fixed lien in favor of the stock exchange clearinghouse. The aforementioned account in section 3 above was pledged by a first-ranked lien and by assignment by way of pledge of unlimited amount in favor of the stock exchange clearing house.

B. Stock exchange members are required to deposit a system of collateral that secures the fulfillment of their obligations relating to MAOF transactions that are executed by them or their customers or by stock exchange members that are not members of the MAOF Clearinghouse, and to secure their share in the risks fund covering this activity, as provided below in Note 26.C.2).

Accordingly, the Bank was required to deposit only liquid collateral, for the full exposure of activity in derivatives and for its share in the risks fund, as provided below:

1) In the account opened in the TASE Clearinghouse in the name of the MAOF Clearinghouse ("main MAOF collateral account"), government debentures of the Bank were deposited as security in favor of the MAOF Clearinghouse, at the full value of the requirements for customers' collateral plus the Bank’s share in the risks fund. The value of debentures deposited as of December 31, 2016 is NIS 331 million (as of December 31, 2015: NIS 440 million).
2) Additionally, in the account opened by the MAOF clearinghouse in its own name on behalf of the Bank with another bank, cash is deposited that the Bank furnishes as collateral, as well as the cash to be paid as income on securities that will be deposited in a major clearinghouse collateral account or cash originating in any other financial right deriving from said securities, including cash proceeds from their sale. As of December 31, 2016, deposits to this account amounted to NIS 20 million (as of December 31, 2015: NIS 48 million).

Note 26 – Contingent Liabilities and Special Commitments – continued

3) As resolved by the Board of Directors of the MAOF clearing house, the MAOF clearing house would open an account in its own name with the Bank of Israel for deposit of collateral provided by members of the MAOF clearing house, which have been deposited with other commercial banks through the account opening date (as set forth in section 2 above). As of December 31, 2016, no funds were deposited in this account.
4) The aforementioned accounts in sections 1-2 are pledged under a floating and fixed lien to benefit the MAOF clearinghouse. The aforementioned account in section 3 above was pledged by a first-ranked lien and by assignment by way of pledge of unlimited amount in favor of the MAOF clearing house.

C. The Bank of Israel operates the Real Time Gross Settlement system (RTGS) – a system which allows customers to transfer in real time NIS-denominated amounts between bank accounts in the same bank or between banks.

The Bank of Israel provides daily and intra-day credit for participants in the RTGS system against specific liens on Bank debentures in the Bank of Israel account with the stock exchange clearinghouse. As of December 31, 2016 and as of December 31, 2015, no debentures were deposited in this account.

D. The Bank conducts securities operations through the EuroClear clearinghouse, which is a settlement system for securities traded on international markets. For these operations, the Bank pledged securities valued, as of December 31, 2016, at USD 10 million (similar to December 31, 2015).

E. In accordance with the requirement of the regulatory agencies in the U.S., the Bank's branch there pledged securities worth USD 20 million as of the balance sheet date (as of December 31, 2015– USD 14 million), used to secure deposits of the public or to comply with other government regulations, or to fulfill other government directives. Most of the amount pledged, which as of December 31, 2016 amounted to USD 18 million (as of December 31, 2015 – USD 11 million), relates to a demand by U.S. regulatory agencies to secure 7.5% of the branch's liabilities, as defined by the authorities there.

F. To secure credit facilities provided to the Bank by the Bank of Israel, the Bank has pledged an account containing foreign securities. As of December 31, 2016 and December 31, 2015, the Bank pledged no foreign securities.

G.

	December 31,	
	2016	2015
Sources of securities which have been received and which the Bank may sell or pledge, at fair value excluding set-offs:		
Securities received in transactions for borrowing securities against cash	9	71

Note 28 – Derivative instruments and hedging activities

Reported amounts (NIS in millions)

a) Description of derivative instruments and the risks inherent in such activity

1) Overview

The Bank's activities in derivative instruments, such as futures contracts and forward trades, options and financial swaps, are executed both as broker for its customers and as part of the management of its assets and liabilities and in order to minimize as much as possible the Bank's exposure to market risks.

The Bank designates certain derivatives as fair value hedges or as cash flow hedges. For more information, see Note 1.D.15. to the financial statements.

2) Types and description of activity in derivative instruments

The activities in derivative instruments include currency contracts, interest rate contracts and other contracts, and contracts for customers in the MAOF market, on different indices and assets, as outlined below:

- Forward transactions and futures contracts:
  A contract between two parties to buy or sell a specified quantity of commodities, currencies, interest or other financial instruments ("underlying asset"), to be executed on a future date and at a price specified in advance.
- Swaps:
  Contracts to exchange a specified quantity of underlying assets on the transaction date, with a reciprocal obligation to re-exchange the items that had been exchanged on a future date.
- Options:
  Contracts that confer, in return for the payment of a premium, the right to purchase (call) or sell (put) the underlying assets at a pre-determined fixed price, quantity and time.
- Spot trades (transactions for immediate delivery):
  Exchanges of two currencies, based on an exchange rate agreed in advance, to be executed within two business days.
- Credit derivatives:
  Contracts that confer, in return for the payment of a one-time or periodic premium, the right to receive payment in the event of a change in credit rating, the inability to honor obligations or any other credit event, relating to the State or the company, as stipulated in the contract.

3) Risks inherent in derivative instrument activities:

The Bank's activities in derivative instruments expose it to credit risks and to market risks that include interest risks, basis risks and liquidity risks, as detailed below:

A. Credit exposure in derivative instruments, which is defined by the Supervisor of Banks as "present credit exposure", quantifies the maximum possible loss that the Bank will sustain if the other party does not fulfill the terms of the transaction, after deducting enforceable set-off agreements, and without taking collateral into account. To manage the credit extent of the exposure inherent in derivative instruments over the life of the transaction, the exposure is estimated at the price of the commitment in the reverse transaction for the remaining life of the transaction.

Collateral requirements are determined according to the type of customer, and sometimes, at a fixed percentage of the credit facility determined for a given customer. In other cases, exposure is determined according to scenarios based on the Black and Scholes Model. The collateral required by the Bank usually includes liquid collateral such as securities, deposits, etc., and is valued as collateral in accordance with the various collateral coefficients used by the Bank.

In the credit derivatives written by the Bank, the credit exposure is expressed in the amount that the Bank will be obliged to pay if the event stipulated in the contract occurs.

B. Market risk – the risk of fluctuation in value of derivatives due to unforeseen changes in interest rates, inflation rate, exchange rates and other financial benchmarks. The Bank manages the market risks involved in financial derivatives by including these instruments within the management of exposure to market risks of the entire range of the Bank's operations.

C. Liquidity risk – the risk of inability to quickly close the exposure by cash payment or by creating reverse exposure. The derivative instruments and their effect on liquidity needs are an integral part of the management of the Bank's liquidity risk in accordance with Proper Banking Conduct Directive 342.

D. Operating risk – the risk of erroneous operation of transactions, beginning from the date they are entered into until they are settled, due to human error or to machine error. The Bank minimizes operating risk in its derivatives operations by using computer-based processes and a complementary set of controls.

For more information see the Detailed Risk Management Report on the Bank website.

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

b) Activity on consolidated basis

	As of December 31, 2016					
	Interest contracts					
	NIS – CPI	Other	Currency contracts	Contracts for shares	Commodities and other contracts	Total
1. Stated amounts of derivative instruments						
A. Hedging derivatives[1]						
Forward contracts	2,196	–	–	–	–	2,196
Other option contracts:						
Options written	–	19	–	–	–	19
Swaps	–	1,218	–	–	–	1,218
Total	2,196	1,237	–	–	–	3,433
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	–	1,218	–	–	–	1,218
B. ALM derivatives[1][2]						
Forward contracts	6,756	200	103,041	–	53	110,050
Option contracts traded on stock exchange:						
Options written	–	–	4	–	–	4
Options purchased	–	–	21	–	–	21
Other option contracts:						
Options written	–	–	11,058	–	–	11,058
Options purchased	–	–	10,251	–	–	10,251
Swaps	1,810	31,906	8,256	–	–	41,972
Total	8,566	32,106	132,631	–	53	173,356
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	1,647	17,889				19,536
C. Other derivatives[1]						
Forward contracts	–	–	1,148	–	–	1,148
Option contracts traded on stock exchange:						
Options written	–	–	6,590	14,194	2	20,786
Options purchased	–	–	6,590	14,194	2	20,786
Other option contracts:						
Options written	–	–	–	41	–	41
Options purchased	–	200	–	27	–	227
Swaps	–	4	14	9,200	–	9,218
Total	–	204	14,342	37,656	4	52,206
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	–	4	–	–	–	4

(1) Except for credit derivatives and spot contracts for foreign currency swaps.

(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

b) Activity on consolidated basis – continued

	As of December 31, 2016					
	Interest contracts					
	NIS – CPI	Other	Currency contracts	Contracts for shares	Commodities and other contracts	Total
D. Credit derivatives and spot contracts for foreign currency swaps						
Credit derivatives in which the Bank is beneficiary	–	–	–	–	882	882
Foreign currency spot swap contracts	–	–	4,024	–	–	4,024
Total	–	–	4,024	–	882	4,906
Total stated amounts of derivative instruments	10,762	33,547	150,997	37,656	939	233,901
2. Fair value, gross, of derivative instruments						
A. Hedging derivatives(1)						
Positive fair value, gross	34	8	–	–	–	42
Negative fair value, gross	3	89	–	–	–	92
B. ALM derivatives(1)(2)						
Positive fair value, gross	349	1,016	1,486	–	3	2,854
Negative fair value, gross	198	1,298	1,310	–	3	2,809
C. Other derivatives(1)						
Positive fair value, gross	–	–	86	606	–	692
Negative fair value, gross	–	2	83	579	–	664
D. Credit derivatives						
Credit derivatives in which the Bank is beneficiary						
Positive fair value, gross	–	–	–	–	4	4
Negative fair value, gross	–	–	–	–	1	1
Total						
Positive fair value, gross(3)	383	1,024	1,572	606	7	3,592
Fair value amounts offset on the balance sheet	–	–	–	–	–	–
Carrying amount of assets with respect to derivative instruments	383	1,024	1,572	606	7	3,592
Of which: Carrying amount of assets with respect to derivative instruments not subject to a master netting agreement or to similar agreements	123	154	769	294	6	1,346
Total						
Negative fair value, gross	201	1,389	1,393	579	4	3,566
Fair value amounts offset on the balance sheet	–	–	–	–	–	–
Carrying amount of liabilities with respect to derivative instruments	201	1,389	1,393	579	4	3,566
Of which: Carrying amount of liabilities with respect to derivative instruments not subject to a master netting agreement or to similar agreements	13	231	894	564	3	1,705

(1) Except for credit derivatives.
(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.
(3) Includes: Positive gross fair value of assets with respect to embedded derivatives amounting to NIS 8 million.

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

b) Activity on consolidated basis

						As of December 31, 2015
	Interest contracts					
	NIS – CPI	Other	Currency contracts	Contracts for shares	Commodities and other contracts	Total
1. Stated amounts of derivative instruments						
A. Hedging derivatives(1)						
Forward contracts	1,990	–	–	–	–	1,990
Other option contracts:						
Options written	–	59	–	–	–	59
Swaps	–	1,347	–	–	–	1,347
Total	1,990	1,406	–	–	–	3,396
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	–	1,347	–	–	–	1,347
B. ALM derivatives(1)(2)						
Forward contracts	6,447	200	87,248	–	21	93,916
Option contracts traded on stock exchange:						
Options written	–	–	1,934	564	–	2,498
Options purchased	–	–	1,390	592	–	1,982
Other option contracts:						
Options written	–	–	8,848	–	–	8,848
Options purchased	–	–	8,519	–	–	8,519
Swaps	1,814	35,685	8,095	–	–	45,594
Total	8,261	35,885	116,034	1,156	21	161,357
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	1,543	20,369	–	–	–	21,912
C. Other derivatives(1)						
Forward contracts	–	–	1,244	–	–	1,244
Option contracts traded on stock exchange:						
Options written	–	–	5,485	22,343	–	27,828
Options purchased	–	–	5,485	22,343	–	27,828
Other option contracts:						
Options written	–	24	–	51	–	75
Options purchased	–	27	–	45	–	72
Swaps	–	4	133	9,759	–	9,896
Total	–	55	12,347	54,541	–	66,943
Includes interest rate swaps on which the Bank agreed to pay a fixed interest rate	–	4	–	–	–	4

(1) Except for credit derivatives and spot contracts for foreign currency swaps.
(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

b) Activity on consolidated basis – continued

	As of December 31, 2015					
	Interest contracts					
	NIS – CPI	Other	Currency contracts	Contracts for shares	Commodities and other contracts	Total
D. Credit derivatives and spot contracts for foreign currency swaps						
Credit derivatives in which the Bank is beneficiary	–	–	–	–	709	709
Foreign currency spot swap contracts	–	–	4,742	–	–	4,742
Total	–	–	4,742	–	709	5,451
Total stated amounts of derivative instruments	10,251	37,346	133,123	55,697	730	237,147
2. Fair value, gross, of derivative instruments						
A. Hedging derivatives(1)						
Positive fair value, gross	47	1	–	–	–	48
Negative fair value, gross	–	135	–	–	–	135
B. ALM derivatives(1)(2)						
Positive fair value, gross	375	1,210	1,300	98	1	2,984
Negative fair value, gross	220	1,526	1,148	–	1	2,895
C. Other derivatives(1)						
Positive fair value, gross	–	–	86	412	–	498
Negative fair value, gross	–	–	86	518	–	604
Total						
Positive fair value, gross(3)	422	1,211	1,386	510	1	3,530
Fair value amounts offset on the balance sheet	–	–	–	–	–	–
Carrying amount of assets with respect to derivative instruments	422	1,211	1,386	510	1	3,530
Of which: Carrying amount of assets with respect to derivative instruments not subject to a master netting agreement or to similar agreements	96	113	582	492	1	1,284
Total						
Negative fair value, gross	220	1,661	1,234	518	1	3,634
Fair value amounts offset on the balance sheet	–	–	–	–	–	–
Carrying amount of liabilities with respect to derivative instruments	220	1,661	1,234	518	1	3,634
Of which: Carrying amount of liabilities with respect to derivative instruments not subject to a master netting agreement or to similar agreements	5	96	604	362	–	1,067

(1) Except for credit derivatives.

(2) Derivatives that constitute part of the Bank's asset and liability management system, which were not intended as hedges.

(3) Includes: Positive gross fair value of assets with respect to embedded derivatives amounting to NIS 3 million.

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

c) Credit risk on financial derivatives according to counter-party to the contract – Consolidated – continued

	As of December 31, 2016					
	Stock exchanges	Banks	Dealers/ Brokers	Governments and central banks	Others	Total
Carrying amount of assets with respect to derivative instruments [(1)]	**215**	**2,264**	**14**	**–**	**1,099**	**3,592**
Gross amounts not offset on the balance sheet:						
Mitigation of credit risk with respect to financial instruments	–	(1,634)	–	–	(44)	(1,678)
Mitigation of credit risk with respect to cash collateral received	–	(500)	–	–	(38)	(538)
Net amount of assets with respect to derivative instruments	215	130	14	–	1,017	1,376
Off-balance sheet credit risk on derivative instruments[(2)]	145	1,353	152	–	965	2,615
Mitigation of off-balance sheet credit risk	–	(547)	–	–	(134)	(681)
Net off-balance sheet credit risk with respect to derivative instruments	145	806	152	–	831	1,934
Total credit risk on derivative instruments	360	936	166	–	1,848	3,310
Carrying amount of liabilities with respect to derivative instruments	**215**	**2,115**	**14**	**29**	**1,193**	**3,566**
Gross amounts not offset on the balance sheet:						
Financial instruments	–	(1,634)	–	–	(44)	(1,678)
Pledged cash collateral	–	(295)	–	(23)	–	(318)
Net amount of liabilities with respect to derivative instruments	215	186	14	6	1,149	1,570

(1) Includes positive fair value, gross, of embedded derivative instruments amounting to NIS 8 million.

(2) The difference, if positive, between the total amount with respect to derivative instruments (including with respect to derivative instruments with negative fair value) included under borrower indebtedness, as calculated for restrictions on indebtedness of a borrower, before mitigation of credit risk, and the carrying amount of assets with respect to derivative instruments of the borrower.

In 2016, the Bank recognized revenues with respect to decrease in credit losses with respect to derivatives, amounting to NIS 14 million (in 2015, the Bank recognized revenues with respect to decrease in credit losses amounting to NIS 11 million; in 2014 the Bank recognized credit losses amounting to NIS 10 million).

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

c) Credit risk on financial derivatives according to counter-party to the contract – Consolidated

	As of December 31, 2015					
	Stock exchanges(3)	Banks	Dealers/ Brokers	Governments and central banks	Others(3)	Total
Carrying amount of assets with respect to derivative instruments (1)	**151**	**1,955**	**28**	**–**	**1,396**	**3,530**
Gross amounts not offset on the balance sheet:						
Mitigation of credit risk with respect to financial instruments	–	(1,778)	–	–	(41)	(1,819)
Mitigation of credit risk with respect to cash collateral received	–	(82)	–	–	(2)	(84)
Net amount of assets with respect to derivative instruments	151	95	28	–	1,353	1,627
Off-balance sheet credit risk on derivative instruments(2)	–	1,275	116	–	1,201	2,592
Mitigation of off-balance sheet credit risk	–	(678)	–	–	(29)	(707)
Net off-balance sheet credit risk with respect to derivative instruments	–	597	116	–	1,172	1,885
Total credit risk on derivative instruments	151	692	144	–	2,525	3,512
Carrying amount of liabilities with respect to derivative instruments	**42**	**2,600**	**–**	**33**	**959**	**3,634**
Gross amounts not offset on the balance sheet:						
Financial instruments	–	(1,778)	–	–	(41)	(1,819)
Pledged cash collateral	–	(653)	–	–	–	(653)
Net amount of liabilities with respect to derivative instruments	42	169	–	33	918	1,162

(1) Includes positive fair value, gross, of embedded derivative instruments amounting to NIS 3 million.

(2) The difference, if positive, between the total amount with respect to derivative instruments (including with respect to derivative instruments with negative fair value) included under borrower indebtedness, as calculated for restrictions on indebtedness of a borrower, before mitigation of credit risk, and the carrying amount of assets with respect to derivative instruments of the borrower.

(3) Reclassified.

Note 28 – Derivative instruments and hedging activities – continued

Reported amounts (NIS in millions)

d) Maturity dates – stated amounts: year-end balances – Consolidated

					As of December 31, 2016
	Up to three months	3 months to 1 year	1-5 years	Over 5 years	Total
Interest contracts:					
NIS – CPI	2,052	1,386	6,458	866	10,762
Other	2,808	5,055	17,150	8,534	33,547
Currency contracts	92,907	46,200	9,704	2,186	150,997
Contracts for shares	28,755	8,757	144	–	37,656
Commodities and other contracts	45	229	243	422	939
Total	126,567	61,627	33,699	12,008	233,901

					As of December 31, 2015
	Up to three months	3 months to 1 year	1-5 years	Over 5 years	Total
Interest contracts:					
NIS – CPI	730	2,016	6,943	562	10,251
Other	3,221	6,593	17,143	10,389	37,346
Currency contracts	87,832	35,464	7,601	2,226	133,123
Contracts for shares	47,693	7,806	198	–	55,697
Commodities and other contracts	9	12	490	219	730
Total	139,485	51,891	32,375	13,396	237,147

Note 29 – Operating Segments

A. Information regarding supervisory operating segments

On November 3, 2014, the Supervisor of Banks issued an update to the Public Reporting Directives concerning supervisory operating segments. According to the directive, the Bank is required to provide, on its financial statements, disclosure with regard to supervisory operating segments in conformity with a uniform, comparable layout specified by the Supervisor of Banks; attribution to supervisory operating segments is typically determined by the turnover volume for clients.

Financial information in the Report by the Board of Directors and Management is included in conformity with definitions of supervisory operating segments.

In addition, the financial statements include, in this Note, disclosure with regard to "Operating segments in conformity with management approach".

An operating segment in conformity with management approach is a Bank component with operations which may derive revenues and incur expenses which meet the following criteria:

- Its operating results are regularly reviewed for the purpose of decision making about resource allocation and for performance evaluation.
- Separate financial information is available with regard to it.

In fact, there is a strong correlation between supervisory operating segments and "operating segments in conformity with management approach" but nevertheless, there are some differences in client attribution to segments and in decision making. Therefore, at this stage, the financial statements also include reporting of operating results in conformity with "management approach", as noted above.

Supervisory operating segments

Supervisory operating segments include operating segments for individuals and operating segments for other than individuals (including business operating segments, institutional investors and financial management of the Bank).

Individuals are defined as persons with no indebtedness to the Bank or whose indebtedness is classified as indebtedness of "individuals – housing loans and others", in conformity with definitions of credit risk classification by economic sector.

Definitions of supervisory operating segments are as follows:

Households – individuals, other than private banking clients, as noted below.

Private banking – individuals who manage a financial asset portfolio in excess of NIS 3 million.

Small and micro businesses – businesses with turnover amounting up to NIS 50 million.

Medium businesses – businesses with turnover higher than NIS 50 million and lower than NIS 250 million.

Large businesses – businesses with turnover higher than NIS 250 million

Institutional investors – Businesses which own pension funds, study funds, mutual funds, ETFs, insurance companies, stock exchange members, portfolio managers.

Financial management – includes trading operations, asset and liability management and non-banking investments.

Trade operations – Investment in securities held for trade, market making operations for securities, operations involving derivatives not designated as hedges and which are not part of asset and liability management for the Bank, borrowing of securities for trading, short selling of securities, underwriting services for securities.

Note 29 – Operating Segments - Continued

Asset and liability management – including investment in debentures available for sale and in debentures held to maturity, hedging using derivatives, ALM hedging, deposits with banks and deposits from banks in Israel and overseas, currency hedging of investments overseas, deposits with and from Governments.

Real investments – Investment in shares available for sale and in associates of businesses.

Other financial management operations – management, operation, trust and custody services for banks, sale and management of loan portfolios.

The aforementioned operating segments are divided into operations in Israel and operations overseas; operations overseas are presented separately and are divided into operations of individuals and business operations only.

Exceptions for classification of business clients by turnover

According to the Bank of Israel Q&A File, the Bank classified business clients to operating segments other than by turnover, in the following cases:

- When the Bank has no information about the revenues of a business client and client indebtedness is smaller than NIS 300 thousand, the client is classified to the appropriate supervisory operating segment based on the client's total financial assets with the Bank.
  Such classification would be in accordance with the aforementioned categories for revenues, with total financial assets multiplied by 10 for the purpose of such classification.

- When the Bank is of the opinion that the volume of revenues of a business client are not indicative of their total operations and the client's total assets on the balance sheet exceed NIS 100 million, the Bank classifies such client to the Large Businesses segment. Such classification is used, for example, in the real estate sector. When total assets on the balance sheet amount to less than NIS 100 million and the revenues are not indicative, as noted above, the client is typically classified as follows:

  Small and micro businesses – total assets on client balance sheet amount up to NIS 50 million.

  Medium businesses – businesses where total assets on the client balance sheet amount to between NIS 50 million and NIS 215 million.

  Large business es– businesses where total assets on the client balance sheet exceeds NIS 215 million.

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

– **Banking and finance** – an array of banking services offered to private and corporate clients, including management of checking accounts, provision of a current loan account, different kinds of credit and guarantees, receiving deposits, foreign trade activities (imports, exports, documentary credit, etc.), trading in derivative instruments, including trading in currencies and interest rates, etc.

– **Capital market** – security transactions for clients on stock exchanges in Israel and overseas, provident fund operating services and mutual fund distribution (management of provident funds and mutual funds until sold) which are among investment tracks available to Bank clients.

– **Credit cards** – A set of financial products and banking services given in conjunction with credit cards issued to Bank clients by credit card companies in Israel.

– **Mortgages** – Housing loans secured by charges on a residence, out of the Bank's funds and within the framework of government aid programs.

– **Construction and real estate** – banking operations vis-à-vis companies in the real estate sector, as well as unique banking services for the real estate sector, including the financing of real estate products by the closed financing method.

Note 29 – Operating Segments - Continued

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

- Credit interest revenues and deposit interest expenses are directly attributed to the client. For credit, expense set at cost of capital raised (transfer cost) is attributed to clients, against an inter-segment credit to the Financial Management segment. Each segment is also charged any excess premium inherent in the cost of raising qualified equity instruments for capital adequacy. This is based on the capital attributed for segment operations. For deposits, revenue set at cost of capital raised is attributed to clients, against an inter-segment debit to the Financial Management segment. Transfer prices for loans and deposits are similar. Each of the segments is credited for capital attributed to operations there of, against a debit to the Financial Management segment. Capital consumption is measured by the average risk-free assets managed by the segment.
- When calculating risk assets attributed to each segment, any off-balance sheet credit exposures are "converted" to credit equivalent using coefficients specified in directives on measurement of capital adequacy.
- For derivative instrument operations, profits are attributed to the client at the spread incorporated in the price of the derivative instrument quoted to the client. Gains arising from changes to fair value of derivatives is attributed to Financial Management.
- Gains and losses from Bank investment in securities and from strategic positions are attributed to Financial Management.
- Expenses with respect to credit losses are directly attributed to clients on behalf of whom they were made.
- Commissions and other revenues are specifically attributed to clients.
- Payroll expenses, building maintenance and other expenses specifically attributed to Bank branches are attributed to branch clients using loading factors which reflect the client operations and the number of transactions in their account. Later on, an additional (inter-segment) settlement takes place, which attributes some of the direct expenses of the branch to clients in non-retail operating segments.

  Intersegment settlement reflects the fact that branches also serve non-retail clients. This settlement is presented under inter-segment expenses / revenues in the Note.
- Payroll expenses of headquarters staff, maintenance and other expenses not specifically related to branches, are loaded on clients based on appropriate load bases which take into account the ratio of the expense for the segment.
- Certain headquarters expenses may sometimes be attributed to a specific operating segment and may sometimes be attributed based on the current estimate of resources allocated to each operating segment.
- When headquarters expenses may not be attributed, they are assigned by weighted business and IT transactions, as noted above In this regard, IT expenses directly associated with specific operating segments are attributed to these segments and other IT expenses are assigned to operating segments based on headcount.
- Provision for tax on operating profit is attributed to clients, is9 pro-rated in accordance with the effective tax rate and accounting for tax impact referring to specific segments and not to all Bank operations.
- Return on equity is calculated as the ratio of net profit to attributed equity. Equity is attributed based on the average risk assets of the customers.
- Balance sheet and assets-under-management balances are specifically attributed to clients.
- Fixed assets are attributed based on appropriate ratios.

Note 29 – Supervisory operating segments – continued

For the year ended December 31, 2016

Reported amounts (NIS in millions)

B. Information on operating segments

	Households other	Households – housing loans	Private banking	Small and micro businesses	Medium businesses	Large businesses	Institutional investors	Financial Management Segment	Total – operations in Israel	Private individuals	Business operations	Total – operations overseas	Total
Interest revenues from externals	806	2,676	1	817	200	499	53	64	5,116	20	175	195	5,311
Interest expenses from externals	378	–	101	45	25	133	308	507	1,497	3	33	36	1,533
Interest revenues, net from externals	428	2,676	(100)	772	175	366	(255)	(443)	3,619	17	142	159	3,778
Interest revenues, net – inter-segment	656	(1,576)	147	9	12	78	362	317	5	1	(6)	(5)	–
Total interest revenues, net	1,084	1,100	47	781	187	444	107	(126)	3,624	18	136	154	3,778
Total non-interest financing revenues	–	–	–	–	–	–	–	291	291	–	4	4	295
Total commissions and other revenues	523	154	10	313	68	147	82	239(3)	1,536	25	6	31	1,567
Total non-interest revenues	523	154	10	313	68	147	82	530	1,827	25	10	35	1,862
Total revenues	1,607	1,254	57	1,094	255	591	189	404	5,451	43	146	189	5,640
Expenses with respect to credit losses	91	13	1	109	11	(24)	(1)	(1)	199	–	1	1	200
Operating and other expenses to externals	1,492	465	40	611	57	92	114	354	3,225	25	49	74	3,299
Operating and other expenses – inter-segment	(77)	–	5	(44)	39	50	25	2	–	–	–	–	–
Total operating and other expenses	1,415	465	45	567	96	142	139	356	3,225	25	49	74	3,299
Pre-tax profit	101	776	11	418	148	473	51	49	2,027	18	96	114	2,141
Provision for taxes on profit	39	302	4	163	58	184	20	19	789	7	37	44	833
After-tax profit	62	474	7	255	90	289	31	30	1,238	11	59	70	1,308
Share of banking corporation in earnings of associates	–	–	–	–	–	–	–	–	–	–	–	–	–
Net profit before attribution to non-controlling interests	62	474	7	255	90	289	31	30	1,238	11	59	70	1,308
Net profit attributed to non-controlling interests	(42)	–	–	–	–	–	–	–	(42)	–	–	–	(42)
Net profit attributable to shareholders of the banking corporation	20	474	7	255	90	289	31	30	1,196	11	59	70	1,266

(1) Risk assets – as calculated for capital adequacy (Proper Conduct of Banking Business Directive 201).
(2) Assets under management – includes clients' provident funds, study funds, mutual funds and securities.
(3) Includes capital gains under Other Revenues amounting to NIS 92 million before tax, from realization of assets in conjunction with asset reorganization and streamlining of the Bank's branch network, compared to NIS 36 million in the corresponding period last year.

Note 29 – Supervisory operating segments – continued

For the year ended December 31, 2016

Reported amounts (NIS in millions)

B. Information on operating segments

	Households other	Households – housing loans	Private banking	Small and micro businesses	Medium businesses	Large businesses	Institutional investors	Financial Management Segment	Total – operations in Israel	Private individuals	Business operations	Total – operations overseas	Total
Average balance of assets	32,665	110,612	113	14,772	4,862	13,527	2,872	27,231	206,654	1,141	9,040	10,181	216,835
Of which: Investments in associates	–	–	–	–	–	–	–	35	35	–	–	–	35
Average balance of loans to the public	17,961	110,612	73	14,772	4,862	13,071	2,858	–	164,209	564	2,631	3,195	167,404
Balance of loans to the public at end of reported period	19,140	114,691	82	15,387	4,869	12,731	2,629	–	169,529	503	2,747	3,250	172,779
Balance of impaired debts	70	27	–	312	66	206	–	–	680	–	1	1	681
Balance of debt in arrears 90 days or longer	26	853	–	52	21	6	–	–	958	–	–	–	958
Average balance of liabilities	71,294	–	10,637	14,955	6,549	28,061	35,340	28,226	195,062	972	7,852	8,824	203,886
Of which: Average balance of deposits from the public	69,137	–	10,637	14,955	6,549	28,061	35,337	–	164,676	924	3,846	4,770	169,446
Balance of deposits from the public at end of reported period	71,334	–	11,167	15,738	7,378	31,422	35,964	–	173,003	973	4,276	5,249	178,252
Average balance of risk assets (1)	15,935	60,850	27	13,345	6,306	22,731	2,964	5,414	127,572	388	3,206	3,594	131,166
Balance of risk assets at end of reported period(1)	16,892	63,247	24	13,963	5,920	20,346	2,842	5,277	128,510	344	3,047	3,391	131,902
Average balance of assets under management(2)	39,164	6,104	2,074	13,224	3,687	22,572	141,469	248	228,542	–	–	–	228,542
Composition of interest revenues, net:													
Margin from credit granting operations	760	1,073	1	709	161	378	46	–	3,128	11	81	92	3,220
Margin from activities of receiving deposits	322	–	46	54	23	55	61	–	561	5	6	11	572
Other	2	27	–	18	3	11	–	(126)	(65)	2	49	51	(14)
Total interest revenues, net	1,084	1,100	47	781	187	444	107	(126)	3,624	18	136	154	3,778

(1) Risk assets – as calculated for capital adequacy (Proper Conduct of Banking Business Directive 201).
(2) Assets under management – includes clients' provident funds, study funds, mutual funds and securities.
(3) Includes capital gains under Other Revenues amounting to NIS 92 million before tax, from realization of assets in conjunction with asset reorganization and streamlining of the Bank's branch network, compared to NIS 36 million in the corresponding period last year.

Note 29 – Supervisory operating segments – continued

For the year ended December 31, 2015

Reported amounts (NIS in millions)

B. Information on operating segments

	Households – other	Households – housing loans	Private banking	Small and micro businesses	Medium businesses	Large businesses	Institutional investors	Financial Management Segment	**Total – operations in Israel**	Private individuals	Business operations	**Total – operations overseas**	**Total**
Interest revenues from externals	748	2,267	1	759	189	551	63	194	4,772	14	120	134	4,906
Interest expenses from externals	292	–	70	31	13	114	588	238	1,346	1	25	26	1,372
Interest revenues, net from externals	456	2,267	(69)	728	176	437	(525)	(44)	3,426	13	95	108	3,534
Interest revenues, net – inter-segment	506	(1,275)	104	(2)	(7)	(3)	637	37	(3)	–	3	3	–
Total interest revenues, net	962	992	35	726	169	434	112	(7)	3,423	13	98	111	3,534
Total non-interest financing revenues	–	–	–	–	–	–	–	353	353	–	5	5	358
Total commissions and other revenues	527	170	12	301	64	150	77	167	1,468	27	5	32	1,500
Total non-interest revenues	527	170	12	301	64	150	77	520	1,821	27	10	37	1,858
Total revenues	1,489	1,162	47	1,027	233	584	189	513	5,244	40	108	148	5,392
Expenses with respect to credit losses	55	9	–	88	13	45	(7)	(2)	201	–	10	10	211
Operating and other expenses to externals	1,445	442	33	610	46	76	88	406	3,146	29	51	80	3,226
Operating and other expenses – inter-segment	(107)	(1)	6	(57)	44	66	43	6	–	–	–	–	–
Total operating and other expenses	1,338	441	39	553	90	142	131	412	3,146	29	51	80	3,226
Pre-tax profit	96	712	8	386	130	397	65	103	1,897	11	47	58	1,955
Provision for taxes on profit	36	268	3	145	49	149	24	65	739	4	18	22	761
After-tax profit	60	444	5	241	81	248	41	38	1,158	7	29	36	1,194
Share of banking corporation in earnings of associates	–	–	–	–	–	–	–	–	–	–	–	–	–
Net profit before attribution to non-controlling interests	60	444	5	241	81	248	41	38	1,158	7	29	36	1,194
Net profit attributed to non-controlling interests	(39)	–	–	–	–	–	–	(21)	(60)	–	–	–	(60)
Net profit attributable to shareholders of the banking corporation	21	444	5	241	81	248	41	17	1,098	7	29	36	1,134

(1) Risk assets – as calculated for capital adequacy (Proper Conduct of Banking Business Directive 201).
(2) Assets under management – includes clients' provident funds, study funds, mutual funds and securities.

Note 29 - Supervisory operating segments - continued

For the year ended December 31, 2015

Reported amounts (NIS in millions)

B. Information on operating segments

	Households – other	Households – housing loans	Private banking	Small and micro businesses	Medium businesses	Large businesses	Institutional investors	Financial Management Segment	**Total – operations in Israel**	Private individuals	Business operations	**Total – operations overseas**	**Total**
Average balance of assets	27,000	102,194	74	14,360	4,849	14,324	2,176	24,858	189,835	1,182	8,114	9,296	199,131
Of which: Investments in associates	–	–	–	–	–	–	–	43	43	–	–	–	43
Average balance of loans to the public	16,034	102,194	74	14,360	4,849	14,189	2,176	–	153,876	505	2,160	2,665	156,541
Balance of loans to the public at end of reported period	16,994	105,719	68	14,452	4,857	13,359	2,063	–	157,512	536	2,556	3,092	160,604
Balance of impaired debts	81	24	–	235	41	402	27	–	810	2	5	7	817
Balance of debt in arrears 90 days or longer	17	956	–	38	–	–	1	–	1,012	–	–	–	1,012
Average balance of liabilities	63,179	79	9,828	13,661	5,985	21,489	37,447	29,517	181,185	830	6,556	7,386	188,571
Of which: Average balance of deposits from the public	63,108	–	9,828	13,661	5,927	21,286	37,447	–	151,257	793	2,181	2,974	154,231
Balance of deposits from the public at end of reported period	65,225	–	10,242	13,959	6,098	26,688	36,127	–	158,339	896	3,145	4,041	162,380
Average balance of risk assets (1)	14,964	55,922	34	12,098	6,077	26,726	3,437	5,224	124,482	377	2,641	3,018	127,500
Balance of risk assets at end of reported period(1)	15,094	58,761	31	12,166	6,084	25,267	3,184	5,377	125,964	405	3,117	3,522	129,486
Average balance of assets under management(2)	40,245	6,546	1,889	15,085	3,305	19,473	146,343	153	233,039	–	–	–	233,039
Composition of interest revenues, net:													
Margin from credit granting operations	699	946	1	677	158	404	47	–	2,932	9	69	78	3,010
Margin from activities of receiving deposits	258	–	34	36	8	24	60	–	420	4	3	7	427
Other	5	46	–	13	3	6	5	(7)	71	–	26	26	97
Total interest revenues, net	962	992	35	726	169	434	112	(7)	3,423	13	98	111	3,534

(1) Risk assets – as calculated for capital adequacy (Proper Conduct of Banking Business Directive 201).
(2) Assets under management – includes clients' provident funds, study funds, mutual funds and securities.

Note 29 – Supervisory operating segments – Continued
Individuals – households and private banking – operations in Israel

For the year ended December 31, 2016

Reported amounts (NIS in millions)

	Household Segment				Private Banking Segment			
	Housing loans	Credit cards	Other	Total – House-holds	Credit cards	Other	Total – private banking	Total
Interest revenues from externals	2,676	23	783	3,482	–	1	1	3,483
Interest expenses from externals	–	–	378	378	–	101	101	479
Interest revenues, net from externals	2,676	23	405	3,104	–	(100)	(100)	3,004
Interest revenues, net – inter-segment	(1,576)	(5)	661	(920)	–	147	147	(773)
Total interest revenues, net	1,100	18	1,066	2,184	–	47	47	2,231
Total non-interest financing revenues	–	–	–	–	–	–	–	–
Total commissions and other revenues	154	143	380	677	1	9	10	687
Total non-interest revenues	154	143	380	677	1	9	10	687
Total revenues	1,254	161	1,446	2,861	1	56	57	2,918
Expenses with respect to credit losses	13	1	90	104	–	1	1	105
Operating and other expenses to externals	465	28	1,464	1,957	1	39	40	1,997
Operating and other expenses – inter-segment	–	(8)	(69)	(77)	–	5	5	(72)
Total operating and other expenses	465	20	1,395	1,880	1	44	45	1,925
Pre-tax profit	776	140	(39)	877	–	11	11	888
Provision for taxes on profit	302	54	(15)	341	–	4	4	345
After-tax profit	474	86	(24)	536	–	7	7	543
Share of banking corporation in earnings of associates	–	–	–	–	–	–	–	–
Net profit before attribution to non-controlling interests	474	86	(24)	536	–	7	7	543
Net profit attributed to non-controlling interests	–	–	(42)	(42)	–	–	–	(42)
Net profit attributable to shareholders of the banking corporation	474	86	(66)	494	–	7	7	501
Average balance of assets	110,612	3,537	29,128	143,277	10	103	113	143,390
Of which: Investments in associates	–	–	–	–	–	–	–	–
Average balance of loans to the public	110,612	3,537	14,424	128,573	10	63	73	128,646
Balance of loans to the public at end of reported period	114,691	3,731	15,409	133,831	10	72	82	133,913
Balance of impaired debts	27	–	70	97	–	–	–	97
Balance of debt in arrears 90 days or longer	853	–	26	879	–	–	–	879
Average balance of liabilities	–	3,537	67,757	71,294	10	10,627	10,637	81,931
Of which: Average balance of deposits from the public	–	–	69,137	69,137	–	10,637	10,637	79,774
Balance of deposits from the public at end of reported period	–	–	71,334	71,334	–	11,167	11,167	82,501
Average balance of risk assets	60,850	–	15,935	76,785	–	27	27	76,812
Balance of risk assets at end of reported period	63,247	–	16,892	80,139	–	24	24	80,163
Average balance of assets under management	6,104	–	39,164	45,268	–	2,074	2,074	47,342
Composition of interest revenues, net:								
Margin from credit granting operations	1,073	18	742	1,833	–	1	1	1,834
Margin from activities of receiving deposits	–	–	322	322	–	46	46	368
Other	27	–	2	29	–	–	–	29
Total interest revenues, net	1,100	18	1,066	2,184	–	47	47	2,231

Note 29 – Supervisory operating segments – Continued
Individuals – households and private banking – operations in Israel

For the year ended December 31, 2015

Reported amounts (NIS in millions)

	Household Segment				Private Banking Segment			
	Housing loans	Credit cards	Other	Total – House-holds	Credit cards	Other	Total – private banking	Total
Interest revenues from externals	2,267	22	726	3,015	–	1	1	3,016
Interest expenses from externals	–	–	292	292	–	70	70	362
Interest revenues, net from externals	2,267	22	434	2,723	–	(69)	(69)	2,654
Interest revenues, net – inter-segment	(1,275)	(4)	510	(769)	–	104	104	(665)
Total interest revenues, net	992	18	944	1,954	–	35	35	1,989
Total non-interest financing revenues	–	–	–	–	–	–	–	–
Total commissions and other revenues	170	134	393	697	1	11	12	709
Total non-interest revenues	170	134	393	697	1	11	12	709
Total revenues	1,162	152	1,337	2,651	1	46	47	2,698
Expenses with respect to credit losses	9	–	55	64	–	–	–	64
Operating and other expenses to externals	442	20	1,425	1,887	–	33	33	1,920
Operating and other expenses – inter-segment	(1)	(2)	(105)	(108)	–	6	6	(102)
Total operating and other expenses	441	18	1,320	1,779	–	39	39	1,818
Pre-tax profit	712	134	(38)	808	1	7	8	816
Provision for taxes on profit	268	50	(14)	304	–	3	3	307
After-tax profit	444	84	(24)	504	1	4	5	509
Share of banking corporation in earnings of associates	–	–	–	–	–	–	–	–
Net profit before attribution to non-controlling interests	444	84	(24)	504	1	4	5	509
Net profit attributed to non-controlling interests	–	–	(39)	(39)	–	–	–	(39)
Net profit attributable to shareholders of the banking corporation	444	84	(63)	465	1	4	5	470
Average balance of assets	102,194	2,827	24,173	129,194	9	65	74	129,268
Of which: Investments in associates	–	–	–	–	–	–	–	–
Average balance of loans to the public	102,194	2,827	13,207	118,228	9	65	74	118,302
Balance of loans to the public at end of reported period	105,719	3,211	13,783	122,713	8	60	68	122,781
Balance of impaired debts	24	–	81	105	–	–	–	105
Balance of debt in arrears 90 days or longer	956	–	17	973	–	–	–	973
Average balance of liabilities	79	2,827	60,352	63,258	–	9,828	9,828	73,086
Of which: Average balance of deposits from the public	–	–	63,108	63,108	–	9,828	9,828	72,936
Balance of deposits from the public at end of reported period	–	–	65,225	65,225	–	10,242	10,242	75,467
Average balance of risk assets	55,922	–	14,964	70,886	–	34	34	70,920
Balance of risk assets at end of reported period	58,761	–	15,094	73,855	–	31	31	73,886
Average balance of assets under management	6,546	–	40,245	46,791	–	1,889	1,889	48,680
Composition of interest revenues, net:								
Margin from credit granting operations	946	18	681	1,645	–	1	1	1,646
Margin from activities of receiving deposits	–	–	258	258	–	34	34	292
Other	46	–	5	51	–	–	–	51
Total interest revenues, net	992	18	944	1,954	–	35	35	1,989

Note 29 - Supervisory operating segments – continued
Small and micro, medium and large business – operations in Israel

For the year ended December 31, 2016

Reported amounts (NIS in millions)

	Small and micro business segment			Medium business segment			Large business segment		
	Construction and real estate	Other	Total	Construction and real estate	Other	Total	Construction and real estate	Other	Total
Interest revenues from externals	153	664	817	60	140	200	225	274	499
Interest expenses from externals	6	39	45	2	23	25	7	126	133
Interest revenues, net from externals	147	625	772	58	117	175	218	148	366
Interest revenues, net-inter-segment	(4)	13	9	(7)	19	12	(30)	108	78
Total interest revenues, net	143	638	781	51	136	187	188	256	444
Total non-interest financing revenues	–	–	–	–	–	–	–	–	–
Total commissions and other revenues	47	266	313	28	40	68	125	22	147
Total non-interest revenues	47	266	313	28	40	68	125	22	147
Total revenues	190	904	1,094	79	176	255	313	278	591
Expenses with respect to credit losses	6	103	109	(1)	12	11	(17)	(7)	(24)
Operating and other expenses to externals	45	566	611	8	49	57	30	62	92
Operating and other expenses – inter-segment	(3)	(41)	(44)	4	35	39	10	40	50
Total operating and other expenses	42	525	567	12	84	96	40	102	142
Pre-tax profit	142	276	418	68	80	148	290	183	473
Provision for taxes on profit	56	107	163	27	31	58	113	71	184
After-tax profit	86	169	255	41	49	90	177	112	289
Share of banking corporation in earnings of associates	–	–	–	–	–	–	–	–	–
Net profit before attribution to non-controlling interests	86	169	255	41	49	90	177	112	289
Net profit attributed to non-controlling interests	–	–	–	–	–	–	–	–	–
Net profit attributable to shareholders of the banking corporation	86	169	255	41	49	90	177	112	289
Average balance of assets	2,905	11,867	14,772	1,399	3,463	4,862	5,768	7,759	13,527
Of which: Investments in associates	–	–	–	–	–	–	–	–	–
Average balance of loans to the public	2,905	11,867	14,772	1,399	3,463	4,862	5,768	7,303	13,071
Balance of loans to the public at end of reported period	3,121	12,266	15,387	1,388	3,481	4,869	6,035	6,696	12,731
Balance of impaired debts	76	236	312	20	46	66	89	116	206
Balance of debt in arrears 90 days or longer	8	44	52	–	21	21	–	6	6
Average balance of liabilities	2,298	12,657	14,955	1,206	5,343	6,549	4,388	23,673	28,061
Of which: Average balance of deposits from the public	2,298	12,657	14,955	1,206	5,343	6,549	4,388	23,673	28,061
Balance of deposits from the public at end of reported period	2,385	13,353	15,738	1,244	6,134	7,378	4,900	26,522	31,422
Average balance of risk assets	4,175	9,170	13,345	2,479	3,827	6,306	14,888	7,843	22,731
Balance of risk assets at end of reported period	4,222	9,741	13,963	2,208	3,712	5,919	13,203	7,143	20,346
Average balance of assets under management	876	12,348	13,224	556	3,131	3,687	2,594	19,978	22,572
Composition of interest revenues, net:									
Margin from credit granting operations	129	580	709	47	114	161	179	199	378
Margin from activities of receiving deposits	8	46	54	3	20	23	6	49	55
Other	6	12	18	1	2	3	3	8	11
Total interest revenues, net	143	638	781	51	136	187	188	256	444

Note 29 – Supervisory operating segments – continued
Small and micro, medium and large business – operations in Israel
For the year ended December 31, 2015

Reported amounts (NIS in millions)

	Small and micro business segment			Medium business segment			Large business segment		
	Construction and real estate	Other	Total	Construction and real estate	Other	Total	Construction and real estate	Other	Total
Interest revenues from externals	144	615	759	46	143	189	240	311	551
Interest expenses from externals	4	27	31	1	12	13	4	110	114
Interest revenues, net from externals	140	588	728	45	131	176	236	201	437
Interest revenues, net- inter-segment	(7)	5	(2)	(4)	(2)	(7)	(27)	24	(3)
Total interest revenues, net	133	593	726	41	129	169	209	225	434
Total non-interest financing revenues	–	–	–	–	–	–	–	–	–
Total commissions and other revenues	40	261	301	25	39	64	120	30	150
Total non-interest revenues	40	261	301	25	39	64	120	30	150
Total revenues	173	854	1,027	66	168	233	329	255	584
Expenses with respect to credit losses	20	68	88	(3)	16	13	19	26	45
Operating and other expenses to externals	42	568	610	6	40	46	23	53	76
Operating and other expenses – inter-segment	(4)	(53)	(57)	4	40	44	13	53	66
Total operating and other expenses	38	515	553	10	80	90	36	106	142
Pre-tax profit	115	271	386	59	72	130	274	123	397
Provision for taxes on profit	43	102	145	22	27	49	103	46	149
After-tax profit	72	169	241	37	45	81	171	77	248
Share of banking corporation in earnings of associates	–	–	–	–	–	–	–	–	–
Net profit before attribution to non-controlling interests	72	169	241	37	45	81	171	77	248
Net profit attributed to non-controlling interests	–	–	–	–	–	–	–	–	–
Net profit attributable to shareholders of the banking corporation	72	169	241	37	45	81	171	77	248
Average balance of assets	2,710	11,650	14,360	1,207	3,642	4,849	5,941	8,383	14,324
Of which: Investments in associates	–	–	–	–	–	–	–	–	–
Average balance of loans to the public	2,764	11,596	14,360	1,217	3,632	4,849	6,022	8,167	14,189
Balance of loans to the public at end of reported period	2,930	11,522	14,452	1,208	3,649	4,857	5,606	7,753	13,359
Balance of impaired debts	55	180	235	14	27	41	131	271	402
Balance of debt in arrears 90 days or longer	3	35	38	–	–	–	–	–	–
Average balance of liabilities	2,230	11,431	13,661	1,109	4,876	5,985	2,927	18,562	21,489
Of which: Average balance of deposits from the public	2,230	11,431	13,661	1,143	4,784	5,927	2,974	18,312	21,286
Balance of deposits from the public at end of reported period	2,172	11,787	13,959	1,122	4,976	6,098	4,557	22,131	26,688
Average balance of risk assets	3,790	8,308	12,098	2,312	3,765	6,077	16,072	10,654	26,726
Balance of risk assets at end of reported period	3,788	8,378	12,166	2,313	3,771	6,084	15,911	9,356	25,267
Average balance of assets under management	1,443	13,642	15,085	544	2,761	3,305	2,933	16,540	19,473
Composition of interest revenues, net:									
Margin from credit granting operations	122	555	677	37	121	158	189	215	404
Margin from activities of receiving deposits	7	29	36	2	6	8	5	19	24
Other	4	7	13	1	2	3	15	(9)	6
Total interest revenues, net	133	591	726	40	129	169	209	225	434

Note 29 – Operating Segments - Continued

B. Operating segments in conformity with management approach.

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

For more information about measurement of Bank operations in conformity with the supervisory segments approach, as specified by the Supervisor of Banks, see chapter "Supervisory operating segments" below and Note 1.B.1 to the financial statements.

Below are the Bank's operating segments in conformity with management approach:

Household segment – under responsibility of the Retail Division. This segment includes small household clients and mortgage operations. The division provides appropriate banking services and financial products to segment clients, including in the field of mortgages.

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

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

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

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

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

The major products and guidelines for attribution of balances, revenues and expenses to clients in the system to operating segments in conformity with management approach, are similar to products and guidelines according to the supervisory operating segment approach.

Note 29 – Operating Segments - Continued

Operating segments in conformity with management approach.

For the year ended December 31, 2016

Reported amounts (NIS in millions)

	Households – other	Households – mortgages	Private banking	Small businesses	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net:								
From outside operating segments	709	2,461	(5)	544	158	580	(669)	3,778
Inter-segment	582	(1,518)	78	61	6	186	605	–
Total interest revenues, net	1,291	943	73	605	164	766	(64)	3,778
Non-interest financing revenues	3	–	1	2	5	21	263	295
Commissions and other revenues	543	149	60	259	49	257	250	1,567
Total revenues	1,837	1,092	134	866	218	1,044	449	5,640
Expenses with respect to credit losses	81	11	(2)	120	5	(14)	(1)	200
Operating and other expenses	1,422	384	95	516	118	321	443	3,299
Pre-tax profit	334	697	41	230	95	737	7	2,141
Provision for taxes on profit	130	271	16	89	37	287	3	833
After-tax profit	204	426	25	141	58	450	4	1,308
Share in net profits of associates, after tax	–	–	–	–	–	–	–	–
Net profit:	–	–	–	–	–	–	–	–
Before attribution to non-controlling interests	204	426	25	141	58	450	4	1,308
Attributable to non-controlling interests	(42)	–	–	–	–	–	–	(42)
Net profit attributable to shareholders of the Bank	162	426	25	141	58	450	4	1,266
Return on equity (percentage of net profit attributed to shareholders of the banking corporation out of average equity)(1)	10.4%	7.2%	30.2%	17.1%	11.6%	12.9%	0.0%	10.2%
Average balance of loans to the public, net	21,918	106,108	1,002	10,345	4,550	22,379	–	166,302
Average balance of deposits from the public	75,583	–	8,429	15,138	5,665	54,370	10,284	169,469
Average balance of assets	22,793	106,421	1,765	10,446	4,613	27,569	43,229	216,836
Average balance of risk assets (2)	18,642	58,656	820	8,181	4,964	34,446	5,457	131,166

(1) Calculated in conformity with capital attributed to this segment based on risk elements attributed there to in conformity with provisions of Basel III.

(2) Risk weighted assets – as calculated for capital adequacy (Proper Banking Conduct Directive No. 201).

Note 29 – Operating Segments – continued

Operating segments in conformity with management approach.

For the year ended December 31, 2015

Reported amounts (NIS in millions)

	Households – other	Households – mortgages	Private banking	Small businesses	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net:								
From outside operating segments	728	2,066	9	531	166	617	(583)	3,534
Inter-segment	428	(1,229)	55	24	1	135	586	–
Total interest revenues, net	1,156	837	64	555	167	752	3	3,534
Non-interest financing revenues	2	–	1	2	–	32	321	358
Commissions and other revenues	544	164	66	244	50	241	191	1,500
Total revenues	1,702	1,001	131	801	217	1,025	515	5,392
Expenses with respect to credit losses	42	10	3	104	16	38	(2)	211
Operating and other expenses	1,362	350	90	508	113	305	498	3,226
Pre-tax profit	298	641	38	189	88	682	19	1,955
Provision for taxes on profit	112	241	14	71	33	257	33	761
After-tax profit	186	400	24	118	55	425	(14)	1,194
Share in net profits of associates, after tax	–	–	–	–	–	–	–	–
Net profit:	–	–	–	–	–	–	–	–
Before attribution to non-controlling interests	186	400	24	118	55	425	(14)	1,194
Attributable to non-controlling interests	(39)	–	–	–	–	–	(21)	(60)
Net profit attributable to shareholders of the Bank	147	400	24	118	55	425	(35)	1,134
Return on equity (percentage of net profit attributed to shareholders of the banking corporation out of average equity)(1)	7.8%	8.2%	33.3%	19.6%	12.1%	11.4%	0.0%	10.0%
Average balance of loans to the public, net	20,764	96,373	1,018	9,340	4,376	21,972	–	153,843
Average balance of deposits from the public	68,519	–	8,356	12,819	5,126	46,344	13,067	154,231
Average balance of assets	20,784	96,752	1,871	9,568	4,531	26,522	39,103	199,131
Average balance of risk assets (2)	17,252	54,120	916	6,700	4,783	38,057	5,352	127,180

(1) Calculated in conformity with capital attributed to this segment based on risk elements attributed there to in conformity with provisions of Basel III.

(2) Risk weighted assets – as calculated for capital adequacy (Proper Banking Conduct Directive No. 201).

Note 29 – Operating Segments - Continued

Operating segments in conformity with management approach.

For the year ended December 31, 2014

Reported amounts (NIS in millions)

	Households – other	Households – mortgages	Private banking	Small businesses	Commercial banking	Business banking	Financial management	Total consolidated
Interest revenues, net:								
From outside operating segments	525	2,444	1	495	173	509	(772)	3,375
Inter-segment	612	(1,709)	62	22	(12)	235	790	–
Total interest revenues, net	1,137	735	63	517	161	744	18	3,375
Non-interest financing revenues	6	–	1	–	1	18	147	173
Commissions and other revenues	534	185	62	233	45	241	139	1,439
Total revenues	1,677	920	126	750	207	1,003	304	4,987
Expenses with respect to credit losses	88	6	3	98	(10)	(3)	(9)	173
Operating and other expenses	1,429	285	84	474	114	309	344	3,039
Pre-tax profit	160	629	39	178	103	697	(31)	1,775
Provision for taxes on profit	59	233	14	66	38	258	(11)	657
After-tax profit	101	396	25	112	65	439	(20)	1,118
Share in net profits of associates, after tax	–	–	–	–	–	–	5	5
Net profit:								
Before attribution to non-controlling interests	101	396	25	112	65	439	(15)	1,123
Attributable to non-controlling interests	(31)	–	–	–	–	–	–	(31)
Net profit attributable to shareholders of the Bank	70	396	25	112	65	439	(15)	1,092
Return on equity (percentage of net profit attributed to shareholders of the banking corporation out of average equity)(1)	5.8%	8.5%	33.1%	21.7%	15.4%	12.8%	0.0%	10.6%
Average balance of loans to the public, net	19,322	88,032	955	8,266	4,365	23,470	–	144,410
Average balance of deposits from the public	62,518	–	7,973	10,233	4,046	45,861	16,241	146,872
Average balance of assets	19,330	88,037	2,143	8,287	4,396	25,666	39,959	187,818
Average balance of risk assets (2)	16,178	49,192	840	5,734	4,700	38,162	5,245	120,051

(1) Calculated in conformity with capital attributed to this segment based on risk elements attributed there to in conformity with provisions of Basel III.

(2) Risk weighted assets – as calculated for capital adequacy (Proper Banking Conduct Directive No. 201).

Note 29 – Operating Segments - Continued

C. Effect of attribution of expenses related to the US DOJ inquiry on operating segments

Had the expenses related to the US DOJ inquiry been attributed to the private banking segment and to overseas operations (rather than to the financial management segment, as attributed by the Bank), according to the supervisory approach, the results of the private banking segment for 2016 would have amounted to a loss of NIS 52 million and for 2015, a loss amounting to NIS 106 million.

Results of the financial management segment under the supervisory approach for 2016 would have amounted to profit of NIS 89 million and for 2015, profit amounting to NIS 144 million.

Results of overseas operations under the supervisory approach for 2016 would have been unchanged and for 2015, profit amounting to NIS 20 million.

Results of the private banking segment under the management approach for 2016 would have amounted to loss of NIS 34 million and for 2015, loss amounting to NIS 103 million.

Results of the financial management segment under the management approach for 2016 would have amounted to profit of NIS 63 million and for 2015, profit amounting to NIS 92 million.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses

Reported amounts (NIS in millions)

A. Off balance sheet debt[1] and credit instruments

1. Change in balance of provision for credit losses

						December 31, 2016
						Provision for credit losses
	Loans to the public					
	Commercial	Housing	Individual – other	Total	Banks and governments	Total
Balance of provision for credit losses at start of period	700	614	192	1,506	3	1,509
Expenses with respect to credit losses	96	13	92	201	(1)	200
Net accounting write-off[2]	(191)	(12)	(133)	(336)	–	(336)
Recovery of debts written off in previous years[2]	119	–	57	176	–	176
Net accounting write-offs	(72)	(12)	(76)	(160)	–	(160)
Balance of provision for credit losses at end of period	724	615	208	1,547	2	1,549
Of which: With respect to off balance sheet credit instruments	98	–	11	109	–	109
						December 31, 2015
Balance of provision for credit losses at start of period	[3]635	624	[3]186	1,445	5	1,450
Expenses with respect to credit losses	149	9	55	213	(2)	211
Net accounting write-off[2]	(211)	(20)	(114)	(345)	–	(345)
Recovery of debts written off in previous years[2]	127	1	65	193	–	193
Net accounting write-offs	(84)	(19)	(49)	(152)	–	(152)
Balance of provision for credit losses at end of period	700	614	192	1,506	3	1,509
Of which: With respect to off balance sheet credit instruments	97	–	9	106	–	106
						December 31, 2014
Balance of provision for credit losses at start of period	[3]633	640	[3]145	1,418	10	1,428
Expenses with respect to credit losses	83	6	93	182	(9)	173
Net accounting write-off[2]	(220)	(22)	(123)	(365)	–	(365)
Recovery of debts written off in previous years[2]	139	–	71	210	4	214
Net accounting write-offs	(81)	(22)	(52)	(155)	4	(151)
Balance of provision for credit losses at end of period	635	624	186	1,445	5	1,450
Of which: With respect to off balance sheet credit instruments	92	–	10	102	–	102

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Net accounting write-offs presented in the Note primarily consists of write-offs of a technical nature, due to passage of time of clients being in arrears, in conformity with US standards applicable to the Bank in this regard. Thus, for example, the balance of provision for large impaired debt s will typically be subject to accounting write-off after two years. Debt measured on group basis will be subject to write-off after 150 days in arrears. This means that the Bank's collection effort may sometimes take longer than the timing for write-off according to accounting rules. Consequently, relatively high balances of "accounting write-offs" and relatively high balances of "Recovery of debts written off in previous years" are presented.

(3) Reclassified.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

A. Off balance sheet debt[1] and credit instruments

2. Additional information about calculation of the provision for credit losses with respect to debts, and debts for which the provision has been calculated

						December 31, 2016
						Provision for credit losses
	Loans to the public					
	Commer-cial	Housing	Indivi-dual – other	Total	Banks and govern-ments	Total
Recorded debt balance of debt s[1]						
reviewed on individual basis	29,972	27	725	30,724	2,839	33,563
reviewed on group basis	9,634	114,959	17,462	142,055	–	142,055
Of which: Loans for which a provision for credit losses is assessed by extent of arrears	1,243	114,373	–	115,616	–	115,616
Total debts	39,606	(2)114,986	18,187	172,779	2,839	175,618
Provision for credit losses with respect to debts [1]						
reviewed on individual basis	518	2	7	527	2	529
reviewed on group basis	108	613	190	911	–	911
Of which: for which a provision for credit losses is assessed by extent of arrears[3]	5	613	–	618	–	618
Total provision for credit losses	626	615	197	1,438	2	1,440

						December 31, 2015
Recorded debt balance of debt s[1]						
reviewed on individual basis	29,656	24	758	30,438	3,412	33,850
reviewed on group basis	(4)8,799	105,922	(4)15,445	130,166	–	130,166
Of which: Loans for which a provision for credit losses is assessed by extent of arrears	1,046	105,419	–	106,465	–	106,465
Total debts	38,455	(2)105,946	16,203	160,604	3,412	164,016
Provision for credit losses with respect to debts [1]						
reviewed on individual basis	516	1	22	539	3	542
reviewed on group basis	(4)87	613	(4)161	861	–	861
Of which: for which a provision for credit losses is assessed by extent of arrears[3]	4	613	–	617	–	617
Total provision for credit losses	603	614	183	1,400	3	1,403

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Includes general-purpose loans secured by a lien on a residential apartment, amounting to NIS 5,731 million (as of December 31, 2015 – NIS 5,421 million).

(3) Includes balance of provision in excess of that required by extent of arrears, assessed on group basis, amounting to NIS 401 million (as of December 31, 2015: NIS 368 million).

(4) Reclassified.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts[1]

1.A. Credit quality and arrears

	As of December 31, 2016					
		Problematic[2]			Non impaired debts – additional information	
	Non problematic	Non impaired	Impaired[3]	Total	In arrears 90 days or longer[4]	In arrears 30 to 89 days[5]
Borrower activity in Israel						
Public – commercial						
Construction and real estate – construction[8]	10,006	38	106	10,150	10	18
Construction and real estate – real estate operations	2,016	2	78	2,096	–	4
Financial services	3,156	311	17	3,484	1	6
Commercial – other	19,727	490	379	20,596	68	74
Total commercial	34,905	841	580	36,326	79	102
Private individuals – housing loans	113,811	[7]853	27	114,691	[7]853	[6]407
Private individuals – other	17,728	115	70	17,913	26	64
Total public – activity in Israel	166,444	1,809	677	168,930	958	573
Banks in Israel	275	–	–	275	–	–
Government of Israel	–	–	–	–	–	–
Total activity in Israel	166,719	1,809	672	169,205	958	573
Borrower activity overseas						
Construction and real estate	1,653	–	1	1,654	–	–
Commercial – other	1,623	–	3	1,626	–	–
Total commercial	3,276	–	4	3,280	–	–
Private individuals	569	–	–	569	–	–
Total public – activity overseas	3,845	–	4	3,849	–	–
Overseas banks	2,234	–	–	2,234	–	–
Overseas governments	330	–	–	330	–	–
Total activity overseas	6,409	–	4	6,413	–	–
Total public	170,289	1,809	681	172,779	958	573
Total banks	2,509	–	–	2,509	–	–
Total governments	330	–	–	330	–	–
Total	173,128	1,809	681	175,618	958	573

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.
(2) Credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer.
(3) Generally, impaired debts do not accrue interest revenues. For information about certain impaired debt restructured using problematic debt restructuring, see Note 30.B.2.c. to the financial statements.
(4) Classified as problematic non-impaired debts. Accruing interest revenues.
(5) Accruing interest revenues. Debts in arrears 30 to 89 days amounting to NIS 31 million were classified as problematic non-impaired debts.
(6) In conformity with Public Reporting Directives, excludes the balance of housing loans in arrears up to 2 months.
(7) Includes balance of housing loans amounting to NIS 125 million provided for by extent of arrears of borrower, for which an agreement has been signed for repayment of arrears by the borrower, where a change was made to the repayment schedule for the outstanding loan balance not yet due.
(8) Includes debts amounting to NIS 1,544 million, extended to certain purchase groups which are in the process of construction.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts[1]

1.A. Credit quality and arrears – continued

					As of December 31, 2015	
		Problematic[2]			Non impaired debts – additional information	
	Non problematic	Non impaired	Impaired[3]	Total	In arrears 90 days or longer[4]	In arrears 30 to 89 days[5]
Borrower activity in Israel						
Public – commercial						
Construction and real estate – construction[8]	8,719	64	83	8,866	10	14
Construction and real estate – real estate operations	2,023	2	124	2,149	1	2
Financial services	3,380	3	15	3,398	1	4
Commercial – other	[9]19,975	265	476	20,716	26	136
Total commercial	34,097	334	698	35,129	38	156
Private individuals – housing loans	104,655	[7]956	24	105,635	[7]956	[6]347
Private individuals – other	[9]15,687	109	81	15,877	17	81
Total public – activity in Israel	154,439	1,399	803	156,641	1,011	584
Banks in Israel	758	–	–	758	–	–
Government of Israel	–	–	–	–	–	–
Total activity in Israel	155,197	1,399	803	157,399	1,011	584
Borrower activity overseas						
Public – commercial						
Construction and real estate	1,942	–	5	1,947	–	–
Commercial – other	1,370	–	9	1,379	–	–
Total commercial	3,312	–	14	3,326	–	–
Private individuals	636	1	–	637	1	–
Total public – activity overseas	3,948	1	14	3,963	1	–
Overseas banks	2,338	–	–	2,338	–	–
Overseas governments	316	–	–	316	–	–
Total activity overseas	6,602	1	14	6,617	1	–
Total public	158,387	1,400	817	160,604	1,012	584
Total banks	3,096	–	–	3,096	–	–
Total governments	316	–	–	316	–	–
Total	161,799	1,400	817	164,016	1,012	584

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.
(2) Credit risk which is impaired, inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer.
(3) Generally, impaired debts do not accrue interest revenues. For information about certain impaired debts restructured using problematic debt restructuring, see Note 30.B.2.c. to the financial statements.
(4) Classified as problematic non-impaired debts. Accruing interest revenues.
(5) Accruing interest revenues. Debts in arrears 30 to 89 days amounting to NIS 20 million were classified as problematic non-impaired debts.
(6) In conformity with Public Reporting Directives, excludes the balance of housing loans in arrears up to 2 months.
(7) Includes balance of housing loans amounting to NIS 161 million provided for by extent of arrears of borrower, for which an agreement has been signed for repayment of arrears by the borrower, where a change was made to the repayment schedule for the outstanding loan balance not yet due.
(8) Includes debts amounting to NIS 1,285 million, extended to certain purchase groups which are in the process of construction.
(9) Reclassified.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

1. B. Credit quality

The state of debts arrears is monitored daily and automatically, providing one of the key indications of credit quality. The state of arrears, and consequently classification of the debt, are based, *inter alia*, on the actual number of days in arrears for each debt.

Non-performing debts

Debt measured on individual basis is classified as non-performing (not accruing interest revenues) after 90 days in arrears. Debt previously restructured as problematic debt and which is again in arrears with regard to the new terms thereof – is also classified as non-performing. Debt measured on group basis is classified as non-performing (inferior) after 150 days in arrears. At that time, accounting write-off of the debt is also carried out.

Inferior debts

Debt in the individual track is classified as inferior debt accruing revenues after 60 days in arrears. Debt in the group track is classified as inferior after 90 days in arrears.

Housing loans

The state of arrears for housing loans is monitored by the extent of arrears for the loan, except for loans with no monthly or quarterly payment.

Credit risk attributes, including specific risk for housing loans, are included on the Report of the Board of Directors and Management under "Risks Overview".

Below is the recorded debt balance by credit quality and by credit segment of the Bank:

						December 31, 2016
						Credit segment
Debt quality	Commercial	Housing	Individuals	Governments	Banks	Total
Debts in good standing	38,181	114,106	18,002	330	2,509	173,128
Problematic non-impaired debts(1)	841	853	115	–	–	1,809
Impaired debts	584	27	70	–	–	681
Total	39,606	114,986	18,187	330	2,509	175,618
						December 31, 2015
Debts in good standing	(2)37,409	104,965	(2)16,013	316	3,096	161,799
Problematic non-impaired debts(1)	334	957	109	–	–	1,400
Impaired debts	712	24	81	–	–	817
Total	38,455	105,946	16,203	316	3,096	164,016

(1) Balance sheet credit risk which is inferior or under special supervision, including with respect to housing loans for which a provision was made by extent of arrears, and housing loans for which no provision was made by extent of arrears and which are in arrears of 90 days or longer.

(2) Reclassified.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts[1]

2. Additional information about impaired debts

A. Impaired debts and individual provision

					December 31, 2016
	Balance of impaired debts for which an individual provision has been made[2][3]	Balance of individual provision	Balance of impaired debts for which no individual provision has been made[2]	Total balance of impaired debts[2]	Contractual principal balance of impaired debts
Borrower activity in Israel					
Public – commercial					
Construction and real estate – construction	61	14	45	106	185
Construction and real estate – real estate operations	55	1	23	78	242
Financial services	9	5	8	17	28
Commercial – other	299	112	80	379	485
Total commercial	424	132	156	580	940
Private individuals – housing loans	16	2	11	27	27
Private individuals – other	23	12	47	70	75
Total public – activity in Israel	463	146	214	677	1,042
Banks in Israel	–	–	–	–	–
Government of Israel	–	–	–	–	–
Total activity in Israel	463	146	214	677	1,042
Borrower activity overseas					
Public – commercial					
Construction and real estate	1	–	–	1	1
Commercial – other	3	–	–	3	3
Total commercial	4	–	–	4	4
Private individuals	–	–	–	–	–
Total public – activity overseas	4	–	–	4	4
Overseas banks	–	–	–	–	–
Overseas governments	–	–	–	–	–
Total activity overseas	4	–	–	4	4
Total public	467	146	214	681	1,046
Total banks	–	–	–	–	–
Total governments	–	–	–	–	–
Total	467	146	214	681	1,046
Of which:					
Measured at present value of cash flows	407	144	195	602	
Debts under problematic debts restructuring	90	7	58	148	

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Recorded debt balance.

(3) Debt balance net of accounting write-off, if made.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts[1]

2. Additional information about impaired debts

A. Impaired debts and individual provision – continued

	December 31, 2015				
	Balance of impaired debts for which an individual provision has been made[(2)(3)]	Balance of individual provision	Balance of impaired debts for which no individual provision has been made[(2)]	Total balance of impaired debts[(2)]	Contractual principal balance of impaired debts
Borrower activity in Israel					
Public – commercial					
Construction and real estate – construction	59	13	24	83	191
Construction and real estate – real estate operations	108	12	16	124	275
Financial services	9	7	6	15	25
Commercial – other	393	86	83	476	573
Total commercial	569	118	129	698	1,064
Private individuals – housing loans	7	1	17	24	24
Private individuals – other	24	10	57	81	89
Total public – activity in Israel	600	129	203	803	1,177
Banks in Israel	–	–	–	–	–
Government of Israel	–	–	–	–	–
Total activity in Israel	600	129	203	803	1,177
Borrower activity overseas					
Public – commercial					
Construction and real estate	5	–	–	5	6
Commercial – other	9	–	–	9	9
Total commercial	14	–	–	14	15
Private individuals	–	–	–	–	3
Total public – activity overseas	14	–	–	14	18
Overseas banks	–	–	–	–	–
Overseas governments	–	–	–	–	–
Total activity overseas	14	–	–	14	18
Total public	614	129	203	817	1,195
Total banks	–	–	–	–	–
Total governments	–	–	–	–	–
Total	614	129	203	817	1,195
Of which:					
Measured at present value of cash flows	508	118	127	635	
Debts under problematic debts restructuring	155	17	74	229	

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Recorded debt balance.

(3) Debt balance net of accounting write-off, if made.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts[1]

2. Additional information about impaired debts

B. Average balance and interest revenues[4]

	December 31, 2016			December 31, 2015			December 31, 2014		
	Average balance of impaired debts[2]	Interest revenues recorded[3]	Of which: Recorded on cash basis	Average balance of impaired debts[2]	Interest revenues recorded[3]	Of which: Recorded on cash basis	Average balance of impaired debts[2]	Interest revenues recorded[3]	Of which: Recorded on cash basis
Borrower activity in Israel									
Public – commercial									
Construction and real estate – construction	95	3	3	95	4	4	149	20	20
Construction and real estate – real estate operations	106	–	–	184	–	–	337	5	5
Financial services	17	1	1	68	4	4	110	1	1
Commercial – other	453	8	8	360	13	13	330	16	15
Total commercial	671	12	12	707	21	21	926	42	41
Private individuals – housing loans	27	–	–	8	–	–	2	–	–
Private individuals – other	75	2	2	80	3	2	78	4	3
Total public – activity in Israel	773	14	14	795	24	23	1,006	46	44
Banks in Israel	–	–	–	–	–	–	–	–	–
Government of Israel	–	–	–	–	–	–	–	–	–
Total activity in Israel	773	14	14	795	24	23	1,006	46	44
Borrower activity overseas									
Public – commercial									
Construction and real estate	4	–	–	5	–	–	16	–	–
Commercial – other	6	–	–	5	–	–	3	–	–
Total commercial	10	–	–	10	–	–	19	–	–
Private individuals	–	–	–	–	–	–	1	–	–
Total public – activity overseas	10	–	–	10	–	–	20	–	–
Overseas banks	–	–	–	–	–	–	–	–	–
Overseas governments	–	–	–	–	–	–	–	–	–
Total activity overseas	10	–	–	10	–	–	20	–	–
Total public	783	14	14	805	24	23	1,026	46	44
Total banks	–	–	–	–	–	–	–	–	–
Total governments	–	–	–	–	–	–	–	–	–
Total[4]	783	14	14	805	24	23	1,026	46	44

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.
(2) Average recorded debt balance of impaired debts during reported period.
(3) Interest revenues recorded in the reported period with respect to average balance of debts in arrears, in the period in which the debts were classified as impaired.
(4) Had the impaired debts accrued interest at the original terms, the Bank would have recognized interest revenues amounting to NIS 53 million (As of December 31, 2015: NIS 71 million; as of December 31, 2014: NIS 91 million).

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts [1]

2. Additional information about impaired debts

C. Problematic debts under restructuring

					December 31, 2016
					Recorded debt balance
	Not accruing interest revenues	Accruing interest revenues[2] in arrears 90 days or longer	Accruing interest revenues[2], in arrears 30-89 days	Accruing interest revenues [2] not in arrears	Total[3]
Borrower activity in Israel					
Public – commercial					
Construction and real estate – construction	13	–	–	–	13
Construction and real estate – real estate operations	50	–	–	1	51
Financial services	3	–	–	–	3
Commercial – other	32	–	–	2	34
Total commercial	98	–	–	3	101
Private individuals – housing loans	–	–	–	–	–
Private individuals – other	22	–	–	24	46
Total public – activity in Israel	120	–	–	27	147
Banks in Israel	–	–	–	–	–
Government of Israel	–	–	–	–	–
Total activity in Israel	120	–	–	27	147
Borrower activity overseas					
Public – commercial					
Construction and real estate	–	–	–	1	1
Commercial – other	–	–	–	–	–
Total commercial	–	–	–	1	1
Private individuals	–	–	–	–	–
Total public – activity overseas	–	–	–	1	1
Overseas banks	–	–	–	–	–
Overseas governments	–	–	–	–	–
Total activity overseas	–	–	–	1	1
Total public	120	–	–	28	148
Total banks	–	–	–	–	–
Total governments	–	–	–	–	–
Total	120	–	–	28	148

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Accruing interest revenues.

(3) Included under impaired debts.

Reported amounts (NIS in millions)

B. Debts[(1)]

2. Additional information about impaired debts

C. Problematic debts under restructuring – continued

					December 31, 2015
					Recorded debt balance
	Not accruing interest revenues	Accruing interest revenues[(2)] in arrears 90 days or longer	Accruing interest revenues[(2)], in arrears 30-89 days	Accruing interest revenues[(2)] not in arrears	Total[(3)]
Borrower activity in Israel					
Public – commercial					
Construction and real estate – construction	21	–	–	–	21
Construction and real estate – real estate operations	102	–	–	–	102
Financial services	3	–	–	–	3
Commercial – other	35	–	–	12	47
Total commercial	161	–	–	12	173
Private individuals – housing loans	–	–	–	–	–
Private individuals – other	24	–	1	29	54
Total public – activity in Israel	185	–	1	41	227
Banks in Israel	–	–	–	–	–
Government of Israel	–	–	–	–	–
Total activity in Israel	185	–	1	41	227
Borrower activity overseas					
Public – commercial					
Construction and real estate	1	–	–	1	2
Commercial – other	–	–	–	–	–
Total commercial	1	–	–	1	2
Private individuals	–	–	–	–	–
Total public – activity overseas	1	–	–	1	2
Overseas banks	–	–	–	–	–
Overseas governments	–	–	–	–	–
Total activity overseas	1	–	–	1	2
Total public	186	–	1	42	229
Total banks	–	–	–	–	–
Total governments	–	–	–	–	–
Total	186	–	1	42	229

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Accruing interest revenues.

(3) Included under impaired debts.

As of December 31, 2016, the Bank had no commitments to provide additional credit to debtors subject to problematic debt restructuring, for which credit terms have been revised.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts [1]

2. Additional information about impaired debts

C. Problematic debts under restructuring – continued

	December 31, 2016			December 31, 2015			December 31, 2016 Restructurings made [2]		
	Number of contracts	Recorded debt balance before restruc-turing	Recorded debt balance after restruc-turing	Number of contracts	Recorded debt balance before restruc-turing	Recorded debt balance after restruc-turing	Number of contracts	Recorded debt balance before restruc-turing	Recorded debt balance after restruc-turing
Borrower activity in Israel									
Public – commercial									
Construction and real estate – construction	22	4	3	22	4	2	12	2	1
Construction and real estate – real estate operations	5	1	1	–	–	–	4	–	–
Financial services	7	1	–	8	–	–	5	–	–
Commercial – other	127	17	16	149	17	13	109	58	56
Total commercial	161	23	20	179	21	15	130	60	57
Private individuals – housing loans	–	–	–	–	–	–	–	–	–
Private individuals – other	730	29	28	792	28	26	882	39	33
Total public – activity in Israel	891	52	48	971	49	41	1,012	99	90
Banks in Israel	–	–	–	–	–	–	–	–	–
Government of Israel	–	–	–	–	–	–	–	–	–
Total activity in Israel	891	52	48	971	49	41	1,012	99	90
Borrower activity overseas									
Public – commercial									
Construction and real estate	–	–	–	–	–	–	–	–	–
Commercial – other	–	–	–	–	–	–	–	–	–
Total commercial	–	–	–	–	–	–	–	–	–
Private individuals	–	–	–	–	–	–	–	–	–
Total public – activity overseas	–	–	–	–	–	–	–	–	–
Overseas banks	–	–	–	–	–	–	–	–	–
Overseas governments	–	–	–	–	–	–	–	–	–
Total activity overseas	–	–	–	–	–	–	–	–	–
Total public	891	52	48	971	49	41	1,012	99	90
Total banks	–	–	–	–	–	–	–	–	–
Total governments	–	–	–	–	–	–	–	–	–
Total	891	52	48	971	49	41	1,012	99	90

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Included under impaired debts.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts [1]

2. Additional information about impaired debts

C. Problematic debts under restructuring - continued

	Restructurings made which are in default[2]					
	December 31, 2016		December 31, 2015		December 31, 2014	
		Recorded debt balance				
	Number of contracts	Recorded debt balance	Number of contracts	Recorded debt balance	Number of contracts	Recorded debt balance
Borrower activity in Israel						
Public – commercial						
Construction and real estate – construction	5	–	2	–	3	–
Construction and real estate – real estate operations	–	–	–	–	–	–
Financial services	–	–	–	–	1	–
Commercial – other	36	3	43	2	32	3
Total commercial	41	3	45	2	36	3
Private individuals – housing loans	–	–	–	–	–	–
Private individuals – other	96	2	126	3	117	5
Total public – activity in Israel	137	5	171	5	153	8
Banks in Israel	–	–	–	–	–	–
Government of Israel	–	–	–	–	–	–
Total activity in Israel	137	5	171	5	153	8
Borrower activity overseas						
Public – commercial						
Construction and real estate	–	–	–	–	–	–
Commercial – other	–	–	–	–	–	–
Total commercial	–	–	–	–	–	–
Private individuals	–	–	–	–	–	–
Total public – activity overseas	–	–	–	–	–	–
Overseas banks	–	–	–	–	–	–
Overseas governments	–	–	–	–	–	–
Total activity overseas	–	–	–	–	–	–
Total public	137	5	171	5	153	8
Total banks	–	–	–	–	–	–
Total governments	–	–	–	–	–	–
Total	137	5	171	5	153	8

(1) Loans to the public, loans to governments, deposits with banks and other debts, except for debentures and securities borrowed or acquired in conjunction with resale agreements, except for deposits with Bank of Israel.

(2) Debts which became, in the reported period, debts in arrears of 30 days or longer, which were restructured under problematic debt restructuring in the 12 months prior to the date on which they became debts in arrears

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

B. Debts

3. Additional information about housing loans

Below is the composition of balances by loan-to-value ratio (LTV)(1), repayment type and interest type:

					December 31, 2016
				Housing loan balance	Off-balance sheet credit risk
		Total	Of which: Bullet / balloon	Of which: Variable interest	Total
Senior lien: LTV ratio	Up to 60%	72,138	2,499	46,751	3,621
	Over 60%	42,672	470	28,299	1,446
Junior lien or no lien		176	2	133	1,083
Total		114,986	2,971	75,183	6,150

					December 31, 2015
Senior lien: LTV ratio	Up to 60%	65,486	2,136	43,710	3,887
	Over 60%	40,347	457	27,978	2,064
Junior lien or no lien		113	2	88	1,649
Total		105,946	2,595	71,776	7,600

(1) Ratio of approved facility upon extending the facility to the property value, as approved by the Bank upon extending the facility

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

C. Balances of loans to the public and off-balance sheet credit risk according to extent of borrower credit risk:

				December 31, 2016
Loan ceiling and credit risk (NIS in thousands)		Numbet of	Credit[(2)]	Off balance sheet[(3)]
	Up to 10	210,521	274	288
Above 10	Up to 20	84,139	538	684
Above 20	Up to 40	121,913	1,657	1,872
Above 40	Up to 80	128,142	4,214	3,153
Above 80	Up to 150	95,825	8,004	2,633
Above 150	Up to 300	82,049	15,532	2,126
Above 300	Up to 600	77,306	31,831	2,701
Above 600	Up to 1,200	66,719	51,186	4,960
Above 1,200	Up to 2,000	14,836	19,581	2,235
Above 2,000	Up to 4,000	4,106	9,354	1,413
Above 4,000	Up to 8,000	1,124	4,780	1,216
Above 8,000	Up to 20,000	623	5,535	1,921
Above 20,000	Up to 40,000	239	3,900	2,414
Above 40,000	Up to 200,000	268	10,065	10,846
Above 200,000	Up to 400,000	46	4,206	5,684
Above 400,000	Up to 772,000	19	2,122	8,638
Total		887,875	172,779	52,784

(1) Number of borrowers is based on total loans and off-balance sheet credit risk.

(2) Off-balance sheet credit and credit risk is stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limitation. Data is in conformity with the definition of indebtedness in Proper Banking Conduct Directive 313.

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

C. Balances of loans to the public and off-balance sheet credit risk according to extent of borrower credit risk – continued

				December 31, 2015
Loan ceiling and credit risk (NIS in thousands)		Number of Borrowers(1)	Credit(2)	Off balance sheet(3)
	Up to 10	191,122	247	297
Above 10	Up to 20	76,835	498	649
Above 20	Up to 40	114,518	1,552	1,833
Above 40	Up to 80	132,678	4,151	3,540
Above 80	Up to 150	97,221	7,732	3,055
Above 150	Up to 300	79,926	14,933	2,225
Above 300	Up to 600	74,897	30,586	2,830
Above 600	Up to 1,200	61,750	45,719	5,768
Above 1,200	Up to 2,000	13,414	17,275	2,533
Above 2,000	Up to 4,000	3,637	8,186	1,484
Above 4,000	Up to 8,000	1,076	4,544	1,238
Above 8,000	Up to 20,000	594	5,063	2,237
Above 20,000	Up to 40,000	217	3,639	2,274
Above 40,000	Up to 200,000	254	11,027	10,136
Above 200,000	Up to 400,000	37	3,990	6,384
Above 400,000	Up to 677,000	16	1,462	8,789
Total		848,192	160,604	55,272

(1) Number of borrowers is based on total loans and off-balance sheet credit risk.

(2) Off-balance sheet credit and credit risk is stated before impact of provision for credit losses, and before impact of deductible collateral with respect to indebtedness of borrower and of borrower group.

(3) Credit risk of off-balance-sheet financial instruments as calculated for the purpose of determining per-borrower indebtedness limitation. Data is in conformity with the definition of indebtedness in Proper Banking Conduct Directive 313.

D. Purchase and sale of debts

				2016				2015
	Commercial	Housing	Other	Total	Commercial	Housing	Other	Total
Loans acquired	–	–	265	265	–	–	312	312
Loans sold	1,168	1,431	–	2,599	410	607	–	1,017

Note 30 – Additional information about credit risk, loans to the public and provision for credit losses – continued

Reported amounts (NIS in millions)

E. Off-balance sheet financial instruments

Contractual balances or their denominated amounts at the end of the year

				As of December 31
	2016	2015	2016	2015
	Balance(1)	Balance(1)	Provision for credit losses	Provision for credit losses
Transactions in which the balance represents a credit risk:				
– Unutilized debitory account and other credit facilities in accounts available on demand	16,688	16,588	26	25
- Guarantees to home buyers	12,461	11,597	7	7
– Irrevocable commitments for loans approved but not yet granted	10,651	12,901	13	13
- Unutilized revolving credit card facilities	7,559	7,848	7	5
- Commitments to issue guarantees	5,797	5,629	4	4
– Guarantees and other liabilities	4,869	4,546	22	23
- Loan guarantees	2,606	2,245	29	26
- Documentary credit	384	472	1	3

(1) Contract balances or their stated amounts at the end of the period, before effect of provision for credit losses.

(2) Includes the Bank's liabilities for its share in the risks fund of the MAOF Clearinghouse of NIS 38 million. (on December 31, 2015: NIS 53 million) see Note 26.C. 2. and Note 27.A.1. to the financial statements.

Note 31 – Assets and Liabilities by Linkage Basis

As of December 31, 2016

Reported amounts (NIS in millions)

	Israeli currency		In foreign currency[1]				
	Non-linked	CPI-linked	US dollars	Euro	Other currencies	Non-monetary items[2]	Total
Assets							
Cash and deposits with banks	39,128	121	1,865	331	280	–	41,725
Securities	5,981	146	3,516	499	20	100	10,262
Securities loaned or acquired in conjunction with resale agreements	9	–	–	–	–	–	9
Loans to the public, net[3]	111,144	49,369	7,394	1,862	1,572	–	171,341
Loans to Governments	–	–	139	191	–	–	330
Investments in associates	35	–	–	–	–	(1)	34
Buildings and equipment	–	–	–	–	–	1,585	1,585
Intangible assets and goodwill	–	–	–	–	–	87	87
Assets with respect to derivative instruments	2,031	333	1,051	146	23	–	3,584
Other assets	989	383	68	1	13	44	1,498
Total assets	159,317	50,352	14,033	3,030	1,908	1,815	230,455
Liabilities							
Deposits from the public	122,611	17,039	28,804	7,180	2,618	–	178,252
Deposits from banks	160	265	899	195	18	–	1,537
Deposits from the Government	20	3	27	–	–	–	50
Debentures and subordinated notes	5,656	21,378	–	–	–	–	27,034
Liabilities with respect to derivative instruments	2,113	168	1,105	160	20	–	3,566
Other liabilities	5,207	1,030	255	9	36	155	6,692
Total liabilities	135,767	39,883	31,090	7,544	2,692	155	217,131
Difference	23,550	10,469	(17,057)	(4,514)	(784)	1,660	13,324
Impact of hedging derivative instruments:							
Derivative instruments (other than options)	2,159	(2,159)	–	–	–	–	–
Non-hedging derivative instruments:							
Derivative instruments (other than options)	(19,238)	(3,431)	17,656	4,405	608	–	–
Net in-the-money options (in terms of underlying asset)	152	–	(388)	208	28	–	–
Net out-of-the-money options (in terms of underlying asset)	115	–	(47)	(87)	19	–	–
Total	6,738	4,879	164	12	(129)	1,660	13,324
Net in-the-money options (capitalized par value)	(1,212)	–	608	518	86	–	–
Net out-of-the-money options (capitalized par value)	1,323	–	(638)	(615)	(70)	–	–

(1) Includes linked to foreign currency.

(2) Includes derivatives whose base relates to a non-monetary item.

(3) Where the provision for credit losses may not be attributed to any specific linkage basis, such provision was deducted *pro-rata* from the different linkage bases.

Note 31 – Assets and Liabilities by Linkage Basis – Continued

As of December 31, 2015

Reported amounts (NIS in millions)

	Israeli currency		In foreign currency[1]				
	Non-linked	CPI-linked	US dollars	Euro	Other currencies	Non-monetary items[2]	Total
Assets							
Cash and deposits with banks	27,705	121	2,053	290	320	–	30,489
Securities	7,002	66	3,755	914	10	98	11,845
Securities loaned or acquired in conjunction with resale agreements	–	71	–	–	–	–	71
Loans to the public, net[3]	95,814	51,836	7,660	2,142	1,752	–	159,204
Loans to Governments	–	–	160	156	–	–	316
Investments in associates	35	–	–	–	–	1	36
Buildings and equipment	–	–	–	–	–	1,583	1,583
Intangible assets and goodwill	–	–	–	–	–	87	87
Assets with respect to derivative instruments	2,291	356	757	84	39	–	3,527
Other assets	1,576	283	59	1	22	59	2,000
Total assets	134,423	52,733	14,444	3,587	2,143	1,828	209,158
Liabilities							
Deposits from the public	109,091	16,764	27,751	6,030	2,744	–	162,380
Deposits from banks	259	287	539	70	11	–	1,166
Deposits from the Government	20	9	29	–	–	–	58
Debentures and subordinated notes	4,982	18,737	–	–	–	–	23,719
Liabilities with respect to derivative instruments	2,311	181	873	243	26	–	3,634
Other liabilities	4,478	822	245	17	46	178	5,786
Total liabilities	121,141	36,800	29,437	6,360	2,827	178	196,743
Difference	13,282	15,933	(14,993)	(2,773)	(684)	1,650	12,415
Impact of hedging derivative instruments:							
Derivative instruments (other than options)	1,939	(1,939)	–	–	–	–	–
Non-hedging derivative instruments:							
Derivative instruments (other than options)	(13,382)	(3,972)	14,132	2,816	406	–	
Net in-the-money options (in terms of underlying asset)	(845)	–	649	84	108	4	–
Net out-of-the-money options (in terms of underlying asset)	(270)	–	246	(11)	38	(3)	–
Total	724	10,022	34	116	(132)	1,651	12,415
Net in-the-money options (capitalized par value)	(760)	–	1,010	(110)	(140)	–	–
Net out-of-the-money options (capitalized par value)	595	–	(500)	(262)	167	–	–

(1) Includes linked to foreign currency.

(2) Includes derivatives whose base relates to a non-monetary item.

(3) Where the provision for credit losses may not be attributed to any specific linkage basis, such provision was deducted *pro-rata* from the different linkage bases.

Note 32 – Assets and liabilities by currency and by term to maturity[(1)]

As of December 31, 2016

Reported amounts (NIS in millions)

	Expected contractual future cash flows					
	On-call to 1 month	1-3 months	3 months to 1 year	1-2 years	2-3 years	3-4 years
Israeli currency (including linked to foreign currency)						
Assets	[(3)]53,247	7,531	21,647	18,765	15,046	13,975
Liabilities	86,983	13,816	31,378	6,448	8,228	8,891
Difference	(33,736)	(6,285)	(9,731)	12,317	6,818	5,084
Futures transactions	(16,454)	(10,883)	5,275	193	138	(487)
Options	129	230	(192)	(3)	(4)	(4)
Difference after effect of derivative instruments	(50,061)	(16,938)	(4,648)	12,507	6,952	4,593
Foreign currency						
Assets	3,651	1,175	3,143	1,468	1,818	1,053
Liabilities	21,333	9,926	8,540	299	291	369
Difference	(17,682)	(8,751)	(5,397)	1,169	1,527	684
Of which: Difference in USD	(11,846)	(7,472)	(4,563)	551	669	546
Of which: Difference with respect to foreign operations	(493)	(1,269)	(446)	545	804	297
Futures transactions	16,454	10,883	(5,275)	(193)	(138)	487
Options	(129)	(230)	192	3	4	4
Difference after effect of derivative instruments	(1,357)	1,902	(10,480)	979	1,393	1,175
Total						
Assets	56,898	8,706	24,790	20,233	16,864	15,028
Liabilities	108,316	23,742	39,918	6,747	8,519	9,260
Difference	(51,418)	(15,036)	(15,128)	13,486	8,345	5,768
Of which: Loans to the public	14,386	7,852	22,387	18,498	14,326	13,249
Of which: Deposits from the public	102,725	22,729	33,454	5,382	3,376	2,792

(1) Presented in this note are expected contractual future cash flows with respect to assets and liabilities, according to linkage basis, according to the remaining contractual period to maturity of each flow .The data is stated net of provisions for doubtful debts.

(2) Includes assets totaling NIS 425 million which are past due.

(3) Includes NIS 5,773 million of loans at debitory account terms and NIS 327 million exceeding limits in debitory account facilities.

(4) Contractual rate of return is the interest rate which discounts the expected contractual future cash flows, as presented in this Note, for the monetary item to its balance sheet balance.

4-5 years	5-10 years	10-20 years	Over 20 years	Total cash flows	Balance sheet balance Without maturity	Balance sheet balance Total	Contractual rate of return(4)
9,317	41,454	45,132	15,545	241,659	1,503(2)	213,110	3.27%
5,927	8,215	9,075	3,081	182,042	167	175,974	1.76%
3,390	33,239	36,057	12,464	59,617	1,336	37,136	
(172)	(471)	–	–	(22,861)	–	(22,861)	
31	50	–	–	237	–	237	
3,249	32,818	36,057	12,464	36,993	1,336	14,512	
702	1,229	1,350	461	16,050	32(2)	15,530	2.26%
246	69	71	26	41,170	6	41,002	0.89%
456	1,160	1,279	435	(25,120)	26	(25,472)	
364	892	1,003	334	(19,522)	–	(21,025)	
289	429	196	149	501	–	510	
172	471	–	–	22,861	–	22,861	
(31)	(50)	–	–	(237)	–	(237)	
597	1,581	1,279	435	(2,496)	26	(2,848)	
10,019	42,683	46,482	16,006	257,709	1,535	228,640	3.19%
6,173	8,284	9,146	3,107	223,212	173	216,976	1.73%
3,846	34,399	37,336	12,899	34,497	1,362	11,664	
8,833	40,675	45,760	15,253	201,219	–	171,341	3.50%
1,861	3,859	4,341	1,447	181,966	–	178,252	1.66%

Note 32 – Assets and liabilities by currency and by term to maturity[1] – continued

As of December 31, 2015

Reported amounts (NIS in millions)

	Expected contractual future cash flows					
	On-call to 1 month	1-3 months	3 months to 1 year	1-2 years	2-3 years	3-4 years
Assets	[2]43,463	7,355	23,794	19,146	14,451	16,181
Liabilities	97,121	29,441	29,193	11,158	3,683	10,228
Difference	(53,658)	(22,086)	(5,399)	7,988	10,768	5,953

(1) Presented in this note are expected contractual future cash flows with respect to assets and liabilities, according to linkage basis, according to the remaining contractual period to maturity of each flow. The data is stated net of provisions for doubtful debts.
(2) Includes NIS 6,953 million of loans at debitory account terms and NIS 315 million exceeding limits in debitory account facilities.
(3) Includes assets totaling NIS 399 million which are past due.
(4) Contractual rate of return is the interest rate which discounts the expected contractual future cash flows, as presented in this Note, for the monetary item to its balance sheet balance.

4-5 years	5-10 years	10-20 years	Over 20 years	Total cash flows	Book balance: Without maturity	Book balance: Total	Contractual rate of return[4]
10,368	40,481	44,571	14,744	234,554	[3]2,054	207,345	3.06%
1,918	13,261	4,937	262	201,202	98	196,566	2.07%
8,450	27,220	39,634	14,482	33,352	1,956	10,779	

Note 33 – Balances and Estimates of Fair Value of Financial Instruments

1) Fair value of financial instruments

For most of the Bank's financial instruments, a "market price" cannot be quoted, because there is no active market in which they are traded. Therefore, the fair value is estimated using acceptable pricing models, such as present value of future cash flows, discounted at an interest rate that reflects the level of risk inherent in the instrument.

The estimate of fair value using future cash flows and determination of a discount rate is subjective. Therefore, for most financial instruments, the estimation of fair value is not necessarily an indication of the realization value of the financial instrument on the balance sheet date. The fair value valuation uses interest rates prevailing at the balance sheet date, and does not take into account fluctuations in interest rates. The assumption of different interest rates will result in fair values that could be substantially different. Essentially, this relates to financial instruments that bear fixed interest or are interest-free, or to CPI-linked financial instruments with shorter maturities than those in which similar transactions are actually effected. In addition, in determining the fair value, the commissions to be received or paid as a result of the business activity are not taken into account, nor does it include the tax effect. Moreover, the difference between the carrying value and the fair value balances may not be realized, because, in most cases, the Bank will hold the financial instrument to maturity. Consequently, it should be emphasized that the data included in this note do not indicate the value of the Bank as a going concern. In addition, because of the broad range of valuation techniques and the possible estimates to be applied during the valuation of the fair value, one must be cautious when comparing the fair values between different banks.

2) The principal methods and assumptions for estimating fair value of financial instruments:

A. Fair value was calculated taking into account the possibility of early repayment based on empirical analysis.

The early repayment assumptions in mortgages are based on empirical testing and on a borrower behavior model with regard to early repayment rate out of all mortgages, on annual basis. These assumptions are verified from time to time against actual early repayment, in each linkage segment and interest type, separately short and long original loan terms.

Early repayment assumptions for deposits and savings plans with early withdrawal options (bearing fixed or variable interest, CPI-linked or non-linked), where interest terms are known in advance, are based on empirical analysis and are reviewed and revised from time to time.

The early repayment assumptions resulted in a NIS 55 million increase in total fair value of assets, and in a NIS 167 million decrease in total fair value of liabilities.

B. Deposits from the public, deposits with banks and loans to Governments, as well as debentures and non-negotiable subordinated notes – the discounted future cash flow method, using interest rates at which, according to Bank management, similar transactions could have been executed on the balance sheet date. For transactions which bear variable interest, the difference between the spread over the variable interest base for the transaction, and the spread for similar transactions upon the balance sheet date is separated. In calculating fair value, this difference is treated as a fixed interest component. For debentures and subordinated notes traded as an asset on an active market, quoted or based on trader quotes for identical liabilities traded as an asset on an active market.

C. Negotiable securities, see Note 1. D.16. to the financial statements.

D. Investments in corporations for which a market value cannot be quoted are not included in this Note at their fair value but rather at cost, (net of impairment provisions) which, in the estimation of management, is not lower than the fair value of the investment.

E. Loans to the public – The fair value of loans to the public is estimated by the present value of future cash flows method, using an appropriate discount rate. For loans which bear variable interest, the difference between the spread over the variable interest base for the transaction, and the spread for similar loans upon the reporting date is separated. In calculating fair value, this difference is treated as a fixed interest component. The balance of the loans was broken down according to the risk level of the individual borrower at the balance sheet date, for which the flows of future receipts (principal and interest) were calculated. The balance of housing loans is divided into homogeneous risk categories.

These receipts were discounted at the interest rates at which the Bank estimates it will be possible to execute similar transactions on the balance sheet date, and which reflects the risk level inherent in the loans for a similar client (for housing loans – a rate which reflects the risk associated with the category).

In certain loans granted by the Bank and a subsidiary at variable interest that changes at a frequency of up to three months, namely housing loans, the carrying value approximates fair value.

F. Impaired debt – fair value is calculated using discount rates that reflects the high credit risk inherent therein. In no case were these discount rates lower than the highest interest rate used by the members of the Bank Group in providing loans on the balance sheet date. The future cash flows of problematic debts were calculated after deducting the provisions for credit losses and after deducting accounting write-offs.

A decrease of 1% in the discount rate affects the fair value of the problematic debts of the Group by NIS 24 million.

G. Off-balance sheet financial instruments in which the balance represents credit risk and contingent liabilities and special commitments – the balance in the financial statements as of the balance sheet date approximates the fair value.

H. Derivatives – see Note 1. D.16. to the financial statements.

I. Financial instruments with original maturity of three months or shorter (other than derivatives and negotiable financial instruments) – the balance on the balance on the financial statements as of the balance sheet date approximates the fair value, subject to changes in credit risk and in Bank margin.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

3) Information on the fair value of financial instruments is presented below:

A. Fair value balances

					December 31, 2016
	Book balance				Fair value
		Level 1[1]	Level 2[1]	Level 3[1]	Total
Financial assets					
Cash and deposits with banks	41,725	6,704	33,804	1,203	41,711
Securities[3]	10,262	7,805	2,434	98	10,337
Securities loaned or purchased in resale agreements	9	9	–	–	9
Loans to the public, net	171,341	331	10,432	[5]160,002	170,765
Loans to Governments	330	–	–	330	330
Investments in associates	35	–	–	35	35
Assets with respect to derivative instruments	3,584	343	1,524	[2]1,717	3,584
Other financial assets	380	–	–	380	380
Total financial assets	[4]227,666	15,192	48,194	163,765	227,151
		–			
Financial liabilities					
Deposits from the public	178,252	331	44,708	135,246	180,285
Deposits from banks	1,537	–	322	1,284	1,606
Deposits from the Government	50	–	–	55	55
Debentures and subordinated notes	27,034	26,043	–	1,617	27,660
Liabilities with respect to derivative instruments	3,566	343	1,385	[2]1,838	3,566
Other financial liabilities	5,019	205	3,715	1,097	5,018
Total financial liabilities	[4]215,458	26,947	50,130	141,138	218,190

(1) Level 1 – Fair value measurement using quoted prices on an active market. Level 2 – Fair value measurement using other significant observed data. Level 3 – Fair value measurement using significant non-observed data.

(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

(3) For more information about the carrying amount and fair value of securities, see Note 12 to the financial statements.

(4) Includes assets and liabilities amounting to NIS 60,183 million and NIS 50,468 million, respectively, whose carrying amount equals their fair value (instruments presented at fair value on the balance sheet). For more information on instruments measured at fair value on recurring basis and on non-recurring basis, see B.-D. below.

(5) Of which embedded derivatives in loans to the public, net amounting to NIS 8 million.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

A. Fair value balances – Continued

					December 31, 2015
	Book				Fair value
	balance	Level 1[1]	Level 2(1)	Level 3(1)	Total
Financial assets					
Cash and deposits with banks	30,489	4,623	23,962	1,898	30,483
Securities[3]	11,845	8,809	2,815	292	11,916
Securities loaned or purchased in resale agreements	71	71	–	–	71
Loans to the public, net	159,204	312	11,041	(5)148,178	159,531
Loans to Governments	316	–	–	316	316
Investments in associates	35	–	–	35	35
Assets with respect to derivative instruments	3,527	565	2,237	(2)725	3,527
Other financial assets	987	580	–	407	987
Total financial assets	(4)206,474	14,960	40,055	151,851	206,866
Financial liabilities					
Deposits from the public	162,380	312	43,565	120,507	164,384
Deposits from banks	1,166	–	313	863	1,176
Deposits from the Government	58	–	–	65	65
Debentures and subordinated notes	23,719	23,132	–	1,262	24,394
Liabilities with respect to derivative instruments	3,634	429	2,387	(2)818	3,634
Other financial liabilities	(6)4,431	121	3,530	(6)780	4,431
Total financial liabilities	(4)195,388	23,994	49,795	124,295	198,084

(1) Level 1 – Fair value measurement using quoted prices on an active market; Level 2 – Fair value measurement using other significant observed data; Level 3 – Fair value measurement using significant non-observed data.

(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

(3) For more information about the carrying amount and fair value of securities, see Note 12 to the financial statements.

(4) Includes assets and liabilities amounting to NIS 50,442 million and NIS 47,044 million, respectively, whose carrying amount equals their fair value (instruments presented at fair value on the balance sheet). For more information on instruments measured at fair value on recurring basis and on non-recurring basis, see B.-D. below.

(5) Of which embedded derivatives in loans to the public, net amounting to NIS 3 million.

(6) Reclassified.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

B. Items measured at fair value:

1. On recurring basis

				December 31, 2016
	Prices quoted on active market (level 1)	Other significant observed data (level 2)	Non-observed significant data (level 3)	Total fair value
Assets				
Securities available for sale				
Debentures				
of Government of Israel	2,606	2,396	–	5,002
Of foreign governments	1,538	–	–	1,538
Of banks and financial institutions in Israel	–	–	–	–
Of banks and financial institutions overseas		19	–	19
Of others overseas	–	19	–	19
Shares	2	–	–	2
Securities held for trading:				–
Debentures of the Government of Israel	348	–	–	348
Securities loaned or purchased in resale agreements	–	–	–	–
Credit with respect to loans to clients	–	–	–	–
Assets with respect to derivative instruments(1)				
Interest contracts:				
NIS / CPI	–	178	205	383
Other	–	507	517	1,024
Currency contracts	75	837	660	1,572
Contracts for shares	268	2	328	598
Commodities and other contracts	–	–	7	7
Other financial assets	–	–	–	–
Other	–	–	8	8
Total assets	4,837	3,958	1,725	10,520
Liabilities				
Deposits with respect to borrowing from clients	–	–	–	–
Securities loaned or acquired in resale agreements	–	–	–	–
Liabilities with respect to derivative instruments(1)				
Interest contracts:				
NIS / CPI	–	137	64	201
Other	–	720	669	1,389
Currency contracts	75	528	790	1,393
Contracts for shares	268	–	311	579
Commodities and other contracts	–	–	4	4
Other financial liabilities	–	–	–	–
Other	–	–	–	–
Total liabilities	343	1,385	1,838	3,566

(1) Fair value measurement of derivatives classified under Level 3 is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

B. Items measured at fair value – continued:

1. On recurring basis

				December 31, 2015
	Prices quoted on active market (level 1)	Other significant observed data (level 2)	Non-observed significant data (level 3)	Total fair value
Assets				
Securities available for sale				
Debentures				
of Government of Israel	3,530	2,716	–	6,246
Of foreign governments	1,664	–	–	1,664
Of banks and financial institutions in Israel	–	–	–	–
Of banks and financial institutions overseas	–	78	196	274
Of others overseas	2	21	–	23
Shares	–	–	–	–
Securities held for trading:				
Debentures of the Government of Israel	222	–	–	222
Securities loaned or purchased in resale agreements	71			71
Credit with respect to loans to clients	312	–	–	312
Assets with respect to derivative instruments[(1)]				
Interest contracts:				
NIS / CPI	–	297	125	422
Other	–	1,143	68	1,211
Currency contracts	127	797	462	1,386
Contracts for shares	438	–	69	507
Commodities and other contracts	–	–	1	1
Other financial assets	580	–	–	580
Other	–	–	3	3
Total assets	6,946	5,052	924	12,922
Liabilities				
Deposits with respect to borrowing from clients	312	–	–	312
Securities loaned or acquired in resale agreements				
Liabilities with respect to derivative instruments[(1)]				
Interest contracts:				
NIS / CPI	–	202	18	220
Other	–	1,541	120	1,661
Currency contracts	89	643	502	1,234
Contracts for shares	340	–	178	518
Commodities and other contracts	–	1	–	1
Other financial liabilities	121	–	–	121
Other	–	–	–	–
Total liabilities	862	2,387	818	4,067

(1) Fair value measurement of derivatives classified under Level 3 is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

B. Items measured at fair value – continued:

2. On non-recurring basis

			December 31, 2016		For the year ended December 31, 2016
			Fair value		
	Level 1[1]	Level 2[1]	Level 3[1]	Total	Losses
Impaired credit whose collection is contingent on collateral	–	–	79	79	19

			December 31, 2015 [2]		For the year ended December 31, 2015
			Fair value		
	Level 1[1]	Level 2[1]	Level 3[1]	Total	Losses
Impaired credit whose collection is contingent on collateral	–	27	[2]144	171	(28)

(1) Level 1 – Fair value measurement using quoted prices on an active market. Level 2 – Fair value measurement using other significant observed data. Level 3 – Fair value measurement using significant non-observed data.

(2) Reclassified.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

C. Change in items measured at fair value on recurrent basis, included in level 3:

	For the year ended December 31, 2016								
		Realized / unrealized gain s(losses) included, net[1]							
	Fair value as of December 31, 2015	In statement of profit and loss	In statement of other comprehensive income under Equity	Acquisitions	Sales	Dispositions	Transfer to level 3	Fair value as of December 31, 2016	Unrealized gain s(losses) with respect to instruments held as of December 31, 2016
Assets									
Securities available for sale									
Debentures:									
Of banks and financial institutions overseas	196	(196)	–	–	–	–	–	–	(196)
Assets with respect to derivative instruments[2][3]	–	–	–	–	–	–	–	–	–
Interest contracts:									
NIS / CPI	125	15	–	–	–	(76)	141	205	235
Other	68	461	–	2	–	(14)	–	517	559
Currency contracts	462	87	–	1,472	–	(1,361)	–	660	416
Contracts for shares	69	161	–	185	–	(87)	–	328	–
Commodities and other contracts	1	5	–	3	–	(2)	–	7	1
Other	3	5	–	–	–	–	–	8	–
Total assets	924	538	–	1,662	–	(1,540)	141	1,725	1,015
Liabilities									
Liabilities with respect to derivative instruments[2][3]									
Interest contracts:									
NIS / CPI	18	1	–	4	–	(7)	48	64	68
Other	120	560	–	4	–	(15)	–	669	799
Currency contracts	502	141	–	1,930	–	(1,783)	–	790	802
Contracts for shares	178	205	–	198	–	(270)	–	311	–
Commodities and other contracts	–	2	–	4	–	(2)	–	4	1
Other	–	3	–	1	–	(4)	–	–	–
Total liabilities	818	912	–	2,141	–	(2,081)	48	1,838	1,670

(1) Realized gains (loss) included on the statement of profit and loss under "Non-interest financing revenues". Unrealized gains and losses included in equity under Adjustments for Presentation of Available-for-Sale Securities at Fair Value under Other Comprehensive Income.

(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

(3) Included in statement of profit and loss under "Non-interest financing revenues".

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

C. Change in items measured at fair value on recurrent basis, included in level 3:

	For the year ended December 31, 2015								
		Realized / unrealized gain s(losses) included, net[1]							
	Fair value as of December 31, 2014	In statement of profit and loss	In statement of other comprehensive income under Equity	Acquisitions	Sales	Dispositions	Transfer to level 3	Fair value as of December 31, 2015	Unrealized gains(losses) with respect to instruments held as of December 31, 2015
Assets									
Securities available for sale									
Debentures:									
Of banks and financial institutions overseas	199	(3)	–	–	–	–	–	196	(3)
Of others overseas	16	(16)	–	–	–	–	–	–	(16)
Assets with respect to derivative instruments[2][3]									
Interest contracts:									
NIS / CPI	119	49	–	13	–	(103)	47	125	108
Other	58	(2)	–	13	–	(1)	–	68	35
Currency contracts	680	131	–	1,298	–	(1,647)	–	462	200
Contracts for shares	120	90	–	148	–	(289)	–	69	–
Commodities and other contracts	–	1	–	1	–	(1)	–	1	
Other	10	(7)	–	–	–	–	–	3	–
Total assets	1,202	243	–	1,473	–	(2,041)	47	924	324
Liabilities									
Liabilities with respect to derivative instruments[2][3]									
Interest contracts:									
NIS / CPI	10	2	–	5	–	(4)	5	18	(16)
Other	173	(51)	–	22	–	(24)	–	120	17
Currency contracts	736	305	–	1,200	–	(1,739)	–	502	(248)
Contracts for shares	117	50	–	169	–	(158)	–	178	–
Other	6	(6)	–	–	–	–	–	–	–
Total liabilities	1,042	300	–	1,396	–	(1,925)	5	818	(247)

(1) Realized gains (loss) included on the statement of profit and loss under "Non-interest financing revenues". Unrealized gains and losses included in equity under Adjustments for Presentation of Available-for-Sale Securities at Fair Value under Other Comprehensive Income.

(2) Fair value measurement is primarily based on use of observed data (market interest rate curves), except for credit quality of counter parties.

(3) Included in statement of profit and loss under "Non-interest financing revenues".

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

D. Additional information about non-observed significant data and valuation techniques used in fair value measurement of items classified at Level 3:

	Fair value as of December 31, 2016	Valuation technique	Non-observed data	Range	Weighted average
Assets with respect to derivative instruments:					
Interest contracts – NIS CPI	85	Cash flows discounting	Inflationary expectations	0.29% – 1.16%	0.53%
Contracts for shares	2	Options pricing model	Standard deviation for shares	71.84% – 71.84%	71.8%
Other	1,638	Cash flows discounting	Counter-party credit quality	0.30% – 3.30%	2.04%
Liabilities with respect to derivative instruments:					
Interest contracts – NIS CPI	20	Cash flows discounting	Inflationary expectations	0.29% – 1.16%	0.47%
Other	1,818	Cash flows discounting	Counter-party credit quality	0.30% – 3.30%	2.08%

	Fair value as of December 31, 2015	Valuation technique	Non-observed data	Range	Weighted average
Securities available for sale:					
CLN	196	Cash flows discounting	Probability of default	0.83%-1.16%	0.92%
Assets with respect to derivative instruments:					
Interest contracts – NIS CPI	73	Cash flows discounting	Inflationary expectations	(0.16%)-(0.14%)	0.02%
Contracts for shares	2	Options pricing model	Standard deviation for shares	29.46% – 95.52%	78.02%
Other	653	Cash flows discounting	Counter-party credit quality	0.30% – 3.10%	1.59%
Liabilities with respect to derivative instruments:					
Interest contracts – NIS CPI	7	Cash flows discounting	Inflationary expectations	(0.16%)-(0.13%)	1.35%
Other	811	Cash flows discounting	Counter-party credit quality	0.30% – 3.10%	1.85%

E. Transfers between Levels 1 and 2 of the fair value hierarchy

There were no transfers from Level 2 and Level 3 to Level 1 during the reported period.

F. Election of fair value option

Due to election of the fair value option, the Bank treats investments in certain debentures at fair value, charging the changes to profit and loss and classifies them under the portfolio held for trading – even though they had not been purchased for this purpose.

Election of the fair value option was made under the following circumstances:

1. Reduce volatility in profit and loss resulting from changes between the original measurement basis of financial instruments designated at the fair value option, and the measurement basis of derivative financial instruments used to manage risks with respect to such investments.
2. Complexity of implementing hedge accounting.
3. More accurate economic presentation of assets managed on fair value basis.

Note 33 – Balances and Estimates of Fair Value of Financial Instruments – continued

Reported amounts (NIS in millions)

The following table lists the fair value of items measured at fair value due to the election of the fair value option:

	Fair value as of December 31, 2016	Gains with respect to changes in fair value for the year ended December 31, 2016
Securities available for sale	–	–

	Fair value as of December 31, 2015	Gains with respect to changes in fair value for the year ended December 31, 2015
Securities available for sale	–	6

Note 34 – Interested and Related Parties

Reported amounts (NIS in millions)

A. Balances

	As of December 31, 2016									
	Interested parties								Related parties owned by the banking corporation	
	Controlling shareholders		Officers[4]		Others[5]		Interested parties upon the transaction date		Jointly-owned associates or investees	
	Balance as of balance sheet date	Highest balance during the year[1]	Balance as of balance sheet date	Highest balance during the year[1]	Balance as of balance sheet date	Highest balance during the year[1]	Balance as of balance sheet date	Highest balance during the year[1]	Balance as of balance sheet date	Highest balance during the year[1]
Assets										
Loans to the public	60	67	34	36	82	184	–	–	–	3
Provision for credit losses	–	–	–	–	2	2	–	–	–	–
Loans to the public, net	60	67	34	36	80	182	–	–	–	3
Investments in associates	–	–	–	–	–	–	–	–	34	36
Liabilities										
Deposits from the public	76	178	53	82	1,367	1,793	–	–	4	17
Shares (included in shareholders' equity)[2]	5,641	5,648	–	–	–	–	–	–	–	–
Credit risk in off-balance sheet financial instruments[3]	5	9	36	37	160	232	–	–	–	–

(1) Based on balances at the end of each month.

(2) The share of interested and related parties in the Bank's capital.

(3) Credit risk in off-balance sheet financial instruments, as calculated for the purposes of per-borrower limitations.

(4) Officers of the Bank (including the President & CEO) and including Board members along with their close family members.

(5) Any corporation in which a person or corporation included in one of these interested party groups has a controlling interest or owns 25% or more of their issued share capital or voting rights thereof, or may appoint 25% or more of their Board members.

										As of December 31, 2015
	Interested parties								Related parties owned by the banking corporation	
	Controlling shareholders		Officers(4)		Others(5)		Interested parties upon the transaction date		Jointly-owned associates or investees	
	Balance as of balance sheet date	Highest balance during the year(1)	Balance as of balance sheet date	Highest balance during the year(1)	Balance as of balance sheet date	Highest balance during the year(1)	Balance as of balance sheet date	Highest balance during the year(1)	Balance as of balance sheet date	Highest balance during the year(1)
	1	1	15	15	163	1,212	–	–	–	5
	–	–	–	–	2	3	–	–	–	–
	1	1	15	15	161	1,209	–	–	–	5
	–	–	–	–	–	–	–	–	36	52
	7	32	65	79	382	852	–	–	3	20
	5,261	5,261	–	–	–	–	–	–	–	–
	–	1	18	19	184	269	–	–	–	–

Note 34 – Interested and Related Parties – Continued

Reported amounts (NIS in millions)

B. Summary of business results with interested and related parties

	For the year ended Dec			
		Interested parties		Related parties owned by the banking corporation
	Controlling shareholders	Officers(1)	Others(2)	Jointly-owned associates or investees
Interest revenues from loans to the public	–	1	9	–
Interest expenses for deposits from the public	–	(1)	(6)	–
Total interest revenues (expenses), net	–	–	3	–
Non-interest financing revenues	–	–	–	–
Operating and other expenses	–	(42)	(3)	–
Total	–	(42)	–	–

C. Remuneration and other benefits to interested parties (by the banking corporation and its investees)

	For the year ended December 31, 2016			
	Officers(1)		Others(2)	
	Total benefits	Total number of beneficiaries	Total benefits	Total number of beneficiaries
Interested party employed by or on behalf of the corporation	35	14	–	–
Board member not employed by or on behalf of the corporation	7	13	–	–
Other interested party not employed by or on behalf of the corporation	–	–	3	4

(1) Officers of the Bank (including the President & CEO) and including Board members along with their close family members.

(2) Any corporation in which a person or corporation included in one of these interested party groups has a controlling interest or owns 25% or more of their issued share capital or voting rights thereof, or may appoint 25% or more of their Board members.

2015				2014			
Interested parties			Related parties owned by the banking corporation	Interested parties			Related parties owned by the banking corporation
Controlling shareholders	Officers(1)	Others(2)	Jointly-owned associates or investees	Controlling shareholders	Officers(1)	Others(2)	Jointly-owned associates or investees
–	–	12	–	–	–	8	–
–	–	(4)	–	–	(1)	(9)	–
–	–	8	–	–	(1)	(1)	–
–	–	–	–	–	–	1	1
–	(50)	(3)	–	–	(58)	(3)	–
–	(50)	5	–	–	(59)	(3)	1

2015				2014			
Officers(1)		Others(2)		Officers(1)		Others(2)	
Total benefits	Total number of beneficiaries	Total benefits	Total number of beneficiaries	Total benefits	Total number of beneficiaries	Total benefits	Total number of beneficiaries
42	14	–	–	51	14	–	–
8	13	–	–	7	13	–	–
–	–	3	5	–	–	3	5

Note 35 – Events after the balance sheet date

On March 20, 2017, after the balance sheet date, the Bank's Board of Directors resolved to distribute dividends amounting to NIS 39.8 million, or 15% of earnings in the fourth quarter of 2016.

The dividends amount is 171.2% of issued share capital, i.e. NIS 0.1712 per NIS 0.1 par value share. The effective date for dividends payment is April 9, 2017 and the payment date is April 26, 2017. The final dividends per share is subject to changes due to realized convertible securities of the Bank. According to accounting rules, this amount will be deducted from retained earnings in the first quarter of 2017.

Note 36 – Condensed financial statements of the Bank[(1)]

A. Statement of profit and loss

Reported amounts (NIS in millions)

	2016	2015	2014
Interest revenues	4,942	4,555	4,962
Interest expenses	1,697	1,487	2,022
Interest revenues, net	3,245	3,068	2,940
Expenses with respect to credit losses	184	200	150
Interest revenues, net after expenses with respect to credit losses	3,061	2,868	2,790
Non-interest revenues			
Non-interest financing revenues	306	290	157
Fees	1,174	1,175	1,144
Other revenues	121	62	33
Total non-interest revenues	1,601	1,527	1,334
Operating and other expenses			
Payroll and associated expenses	1,805	1,697	1,626
Maintenance and depreciation of buildings and equipment	599	602	626
Other expenses	379	455	338
Total operating and other expenses	2,783	2,754	2,590
Pre-tax profit	1,879	1,641	1,534
Provision for taxes on profit	745	656	586
After-tax profit	1,134	985	948
Share in profits of investees, after tax	132	149	144
Net profit	1,266	1,134	1,092

(1) Complete data for the Bank solo is available on the Bank website: www.mizrahi-tefahot.co.il >> about the bank >> investor relations >> financial statements.

Note 36 – Condensed financial statements of the Bank – Continued

B. Balance sheet

Reported amounts (NIS in millions)

	2016	2015
Assets		
Cash and deposits with banks	36,660	24,265
Securities[1]	10,233	11,804
Securities loaned or purchased in resale agreements	9	71
Loans to the public	163,529	152,326
Provision for credit losses	(1,380)	(1,348)
Loans to the public, net	162,149	150,978
Loans to Governments	330	316
Investments in investees	2,786	2,659
Buildings and equipment	1,292	1,344
Assets with respect to derivative instruments	3,584	3,526
Other assets	1,331	1,800
Total assets	218,374	196,763
Liabilities and Equity		
Deposits from the public	182,241	164,208
Deposits from banks	11,398	9,602
Deposits from the Government	30	38
Debentures and subordinated notes	3,270	3,127
Liabilities with respect to derivative instruments	3,565	3,631
Other liabilities[2]	5,156	4,310
Total liabilities	205,660	184,916
Equity	12,714	11,847
Total liabilities and equity	218,374	196,763

(1) Includes: NIS 6,899 million at fair value (December 31, 2015: NIS 8,388 million).
(2) Includes: Provision for credit losses with respect to off balance sheet credit instruments amounting to NIS 108 million (on December 31, 2015: NIS 105 million).

Note 36 – Condensed financial statements of the Bank – Continued

C. Statement of cash flows

Reported amounts (NIS in millions)

	For the year ended December 31,		
	2016	2015	2014
Cash flows provided by current operations			
Net profit	1,266	1,134	1,092
Adjustments			
Share of the Bank in un-distributed (earnings) loss of investees	(132)	(149)	(144)
Depreciation of buildings and equipment	194	196	220
Expenses with respect to credit losses	184	200	150
Loss (gain) from sale of securities available for sale	(58)	(117)	(110)
Loss (gain) from sale of securities held to maturity		–	–
Impairment of securities held for sale		–	2
Realized and unrealized loss (gain) from adjustment to fair value of securities held for trading	(14)	5	(4)
Gain from sale of buildings and equipment	(92)	(36)	(10)
Expenses arising from share-based payment transactions	8	20	40
Deferred taxes, net	(2)	27	26
Change in employee provisions and liabilities	306	(12)	(15)
Effect of changes in exchange rate on cash balances	182	179	(515)
Proceeds from sale of loan portfolios	(45)	(1)	–
Net change in current assets			
Deposits with banks	71	2,134	(10)
Loans to the public	(13,953)	(11,813)	(8,515)
Loans to Governments	(14)	(9)	(2)
Securities loaned or purchased in resale agreements	62	36	(37)
Assets with respect to derivative instruments	(67)	2,068	(1,975)
Securities held for trade	(112)	807	522
Other assets, net	579	193	138
Net change in current liabilities			
Deposits from banks	1,796	1,269	418
Deposits from the public	18,033	12,374	14,078
Deposits from the Government	(8)	(8)	(5)
Securities loaned or sold in conjunction with repurchase agreements	–	(223)	223
Liabilities with respect to derivative instruments	(66)	(2,865)	2,959
Other liabilities	214	(538)	90
Accrual differences included with investment and financing operations	(13)	(268)	(142)
Net cash provided by current operations	8,319	4,603	8,474

Note 36 – Condensed financial statements of the Bank – Continued

C. Statement of cash flows - Continued

Reported amounts (NIS in millions)

	For the year ended December 31,		
	2016	2015	2014
Cash flows provided by investment operations			
Acquisition of debentures held to maturity	–	–	(3,400)
Proceeds from sale of debentures held to maturity	–	–	–
Acquisition of securities available for sale	(6,902)	(10,318)	(12,715)
Proceeds from sale of securities available for sale	7,536	9,470	8,647
Proceeds from redemption of securities available for sale	1,083	401	124
Proceeds from sale of loan portfolios	2,662	590	–
Acquisition of buildings and equipment	(162)	(153)	(232)
Proceeds from sale of buildings and equipment	125	55	21
Proceeds from realized investment in associates	28	19	29
Net cash provided by investment operations	4,370	64	(7,526)
Cash flows provided by financing operations			
Issuance of debentures and subordinated notes	183	417	–
Redemption of debentures and subordinated notes	(38)	(845)	(169)
Dividends paid to shareholders	(186)	(86)	–
Net cash provided by financing operations	(41)	(514)	(169)
Increase (decrease) in cash	12,648	4,153	779
Cash balance at beginning of year	24,141	20,167	20,947
Effect of changes in exchange rate on cash balances	(182)	(179)	515
Cash balance at end of year	36,607	24,141	22,241
Interest and taxes paid / received			
Interest received	4,847	5,149	5,086
Interest paid	2,121	2,387	2,509
Dividends received	9	10	8
Taxes on income received	76	68	79
Taxes on income paid	745	627	705
Appendix A – Non-cash Transactions			
Acquisition of buildings and equipment	13	22	10

Corporate governance, audit, other information about the Bank business and its management

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Corporate governance and audit

Board of Directors and management

Board of Directors

The Bank's members of the board of directors, their principal occupation, and other directorships as of the publication date of these financial statements are presented below:

Moshe Vidman, Chairman(1)(2)	
Membership of Board of Directors' committees	Credit – Chairman; Risks Management – Chairman.
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(3)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party?	No
Start date in office as member of the Bank's Board of Directors	2.8.2010
Education	Undergraduate degree - Economics and Political Science, Hebrew University, Jerusalem. MBA (Financing), Hebrew University, Jerusalem.
Current occupation	Chairman of the Board of Directors, Moshe Vidman Ltd. (owner). Volunteer service: Member, Executive Board of the Jerusalem Foundation (since 2000); Member, Executive Board of Magnes Book Publishers; Member, Board of Trustees of the Hebrew University in Jerusalem (since 1995); Chairman, Hebrew University Assets Ltd. (from 2001 to January 31, 2016).
Previous occupation (in past 5 years, other than current occupation)	Board member: Bank Leumi Le-Israel Ltd.; ICL Ltd.; Dead Sea Works Ltd.; Rotem Amfert Negev Ltd.; Melisaron Ltd.; Elrov Real Estate and Hotels Ltd.; Rosebud Ltd.; Yafora Tavori Ltd.; Ofer Investments Ltd.; Dash Apex Holdings Ltd.; CABM Ltd.; Ofer Development and Investments Ltd.; Ofer Sachaf Ltd.; Ofer Bros. Investments LtdOfer Bros. (Ashkelon Industries) Ltd.; Ofer Bros. ;. Haifa 1974) Ltd.; Ofer Bros. (Jerusalem) Ltd.; Ofer) Bros. Holdings Properties Ltd.; Ofer Centers Ltd.; Ofer Commercial Centers Ltd.; Hof Almog Eilat Ltd.; AABM Ltd.; Ofer Bros. Engineering and Development Ltd.; Ofer Nazareth Industrial Properties Ltd.; Mivnei Oferim Ltd.; Melisa Ltd.; CID Israeli Investments and Development Company Ltd.; Mistletoe Holding BV Ltd.; Ofer Investment Development Energy and Management Ltd.; Ofer Investment Energy Sources Ltd.; Herbert Samuel 10 (Management) Ltd.; Ofer Vacations Tourism Ltd.; Ofer Bros. Holdings (1989) Ltd.; Melifar Shopping Malls Ltd. (in voluntary dissolution); Ofer Commercial Centers Management Maof Ltd. (in voluntary dissolution); Neot Hof Almog 1990 Ltd.; Residence Towers Ltd.; Carmeli - Yuliad Ltd.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) Has "banking experience", pursuant to directives of the Supervisor of Banks.
(2) Serves as Chairman of the Bank Board of Directors as from December 1, 2012.
(3) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Zvi Ephrat[1]	
Membership of Board of Directors' committees	Credit
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	No
Has professional qualifications	Yes
Expert Board member[2]	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	24.1.1995
Education	LL.B. - Hebrew University, Jerusalem; Attorney
Current occupation and in the past 5 years	Senior Partner, J. Gornitzki & Co. – Attorneys at Law;Board member, Ephrat Smith Trust Company; Board member, Ephrat Legal Services
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

Sabina Biran	
Membership of Board of Directors' committees	Audit, Risks Management, Remuneration
External Board member as defined in Proper Banking Conduct Directive 301	Yes
External Board member as defined in the Companies Law	No
Independent Board member	Yes
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member[2]	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	27.2.2012
Education	Undergraduate degree in Political Science and Economics, Haifa University; MBA, Harriett-Watt University; MA studies in Political Studies and International Relations, Tel Aviv University.
Current occupation	Owner and Co-CEO of MVP-B Ltd. Board member of Nova Medical Ltd. (a private company).
Previous occupation (in past 5 years, other than current occupation)	Board member: Shufersal Ltd. (until December 8, 2015).
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) Has "banking experience", pursuant to directives of the Supervisor of Banks.

(2) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Ron Gazit	
Membership of Board of Directors' committees	Risks Management
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	No
Has professional qualifications	Yes
Expert Board member(2)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	14.12.2003
Education	Undergraduate degree (LLB) Law degree, Attorney – Tel Aviv University
Current occupation	Founder of Ron, Gazit, Ruthenberg & Co. - law firm; Board member, Gazit Ruthenberg Trust Company; R. Gazit Attorney (2002).
Previous occupation (in past 5 years, other than current occupation)	Founder and Manager, Ron, Gazit, Ruthenberg & Co. - law firm; Board member, Gover Radio Ltd.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

Avraham Zeldman(1)	
Membership of Board of Directors' committees	Risks Management Committee
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(2)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	26.2.2015
Education	Studied Statistics and Economics, Business Administration at Haifa University (not eligible for degree)
Current occupation	Currently serves as Chairman of the Board of Directors of Fox Wiezel Ltd. (since 2012); Board member of the following companies: A. Zeldman Management Ltd.; Liliot Ltd.; Liliot Bakery Ltd.
Previous occupation (in past 5 years, other than current occupation)	Chairman of the Board of Directors: Bank Leumi LeMashkantaot Ltd.; Leumi Partners Underwriting Ltd.; Leumi Partners Research Ltd.; Leumi Start Ltd.; Leumi Start Management (2000) Ltd. Board member: Paz Oil Ltd.; Partner Communications Ltd.; Electra Consumer Goods 1970 Ltd.; Fox Wiezel Ltd. (2008-2011); Super Pharm Ltd.; Avgol Industries Ltd.; Technorov Ltd.; Archimedes Global Cyprus; Apac Leumi Inc.; Apax Leumi Partners; Keshet Broadcasting Ltd.; CEO, Leumi Partners Ltd.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) Has "banking experience", pursuant to directives of the Supervisor of Banks.
(2) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Nachshon Joav-Asher	
Membership of Board of Directors' committees	Credit
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(1)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	Yes
Start date in office as member of the Bank's Board of Directors	27.2.2012
Education	Academic, undergraduate degree in Economics and Accounting, Tel Aviv University; MBA (specialized in Strategy), Hebrew University, Jerusalem
Current occupation	VP, Finance and Business Development; Central Bottling Company Ltd. (Coca Cola) Board member: Neviot Teva HaGalil Ltd. Dairy Manufacturers Association Ltd. (in voluntary dissolution), Tavor Winery (2005) Ltd., Keshet Broadcasting Ltd., Mira Trading Ltd., TURK TUBORG BIRA VE MALT, SANAYII A.S (Turkey), PAZARLAMA A.S TUBORG (Turkey), (Holland), INTERNATONAL DAIRIES CORPORATION B.V. AL BREWERIES B.V (Holland), UNITED ALBANIAN BREWERIES SH.P.K (Albania).
Previous occupation (in past 5 years, other than current occupation)	Chairman of the Board of Directors, Neviot Teva HaGalil Ltd.; Board member of: Meshek Tzuriel Dairy Ltd.; Mey Galil Ltd.; Central Beverage Distribution Company Ltd.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Mordechai Meir	
Membership of Board of Directors' committees	Audit
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member[(1)]	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	24.12.2008
Education	BA in Accounting and Economics – Tel Aviv University; CPA.
Current occupation	CEO,. Meirav Managers Ltd.; Board member of the following companies: Ofer Investments; Melisa Ltd.; C.A.B.M. Ltd.; Ofer Bros. Foreign Investments Ltd.; Ofer Bros. (Ashkelon Industries) Ltd.; Ofer Bros. (Haifa 1974) Ltd.; Ofer Bros. (Jerusalem) Ltd.; Ofer Centers Ltd.; Ofer Bros. Engineering and Development Ltd.; Mistletoe BV; Ofer Bros. Holdings (1989) Ltd.
Previous occupation (in past 5 years, other than current occupation)	Board member: British Investments Ltd., Ofer Commercial Centers Management Maof Ltd. (in voluntary dissolution), Electric Wires (Properties) Ltd. (in voluntary dissolution), Mey Dal Properties Ltd.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

Jacob Abraham Neyman	
Membership of Board of Directors' committees	Audit Committee, Chair, Remuneration Committee since September 19, 2016, Risks Management Committee.
External Board member as defined in Proper Banking Conduct Directive 301	Yes
External Board member as defined in the Companies Law	Yes
Independent Board member	Yes
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member[(1)]	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	11.4.2013
Education	PhD in Mathematics from Hebrew University, Jerusalem
Current occupation	Professor of Mathematics, Hebrew University, Jerusalem. Board member: A. Neyman Investments Ltd.; A. Neyman Ltd., NAE HOLDINGS LTD. Chairman of the Board of Directors: BIDORBUY.COM, LTD HOLDINGS LTDT.
Previous occupation (in past 5 years, other than current occupation)	–
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Gideon Siterman	
Membership of Board of Directors' committees	Remuneration, Audit, Credit
External Board member as defined in Proper Banking Conduct Directive 301	Yes
External Board member as defined in the Companies Law	Yes
Independent Board member	Yes
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(1)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	07.07.2009
Education	Undergraduate degree in Economics and Accounting, Tel Aviv University; CPA.
Current occupation	Chairman and owner, Pninush Ltd.; Board member of Axiom SL Ltd.
Previous occupation (in past 5 years, other than current occupation)	CEO, Kal Construction Ltd.; Director General, Ministry of Transportation and Road Safety; Board member, Camor Ltd., Chairman, Port of Ashdod
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	Yes

Liora Ofer	
Membership of Board of Directors' committees	Credit
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	No
Has professional qualifications	Yes
Expert Board member(1)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	Board member of Ofer Investments Group companies as listed below, including Ofer Investments Group companies which (directly and indirectly) hold Bank shares.
Start date in office as member of the Bank's Board of Directors	23.1.2006
Education	High school – HaReali HaIvri Haifa
Current occupation	Chair, Melisaron Ltd., Chair, Ofer Investments Ltd. Board memberships: Oro Investments Ltd.; Oro Consulting and Management Ltd.; Helidor Entrepreneurs Ltd.; Ramat Aviv Mall Ltd.; Ofer Bros. Holdings (1989) Ltd.; Ofer Sachaf Ltd.; Ofer Bros. Property Holdings Ltd.; Hof Almog Eilat Ltd.; AABM Ltd., Mivnei Oferim Ltd.,Ofer Development and Investments Ltd.; Ofer Industrial Properties (Nazareth) Ltd., Ofer Commercial Centers Ltd., Ofer Commercial Centers Ltd., CID Israeli Investments and Development Company Ltd.; Neot Hof Almog (1990) Ltd.; Carmeli Yuliad Ltd.; Herbert Samuel 10 (Management) Ltd.; Ofer Investments Energy Sources Ltd.; Ofer Investment Development Energy and Management Ltd.
Previous occupation (in past 5 years, other than current occupation)	Business and corporate management in real estate, investments and other sectors, including Board memberships as listed above.
Family member of another interested party in the corporation	Daughter of Mr. Yuli Ofer (RIP), sister of Mr. Doron Ofer and cousin of Mr. Eyal Ofer
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Jonathan Kaplan	
Membership of Board of Directors' committees	Risks Management
External Board member as defined in Proper Banking Conduct Directive 301	No
External Board member as defined in the Companies Law	No
Independent Board member	No
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(1)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	12.5.2011
Education	Undergraduate degree in Economics and Accounting, Tel Aviv University; CPA; graduate degree in Political Science and National Security, Haifa University; National Security College, Tel Aviv.
Current occupation	Economic Advisor. Board member: Amir Agricultural Marketing and Investments Ltd.; Central Bottling Company Ltd.; International Breweries Ltd.; Novolog PharmUp Marketing (1966) Ltd.
Previous occupation (in past 5 years, other than current occupation)	Board member: Solbar Industries Ltd.; Vilar International Ltd.; Clal Biotechnology Industries Ltd.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	Yes

Osnat Ronen	
Membership of Board of Directors' committees	Credit Committee, Chair, Audit Committee since September 19, 2016, Remuneration Committee.
External Board member as defined in Proper Banking Conduct Directive 301	Yes
External Board member as defined in the Companies Law	Yes
Independent Board member	Yes
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(1)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	23.10.2013
Education	Undergraduate degree in Mathematics and Computer Science, Tel Aviv University. MBA (Financing), Tel Aviv University.
Current occupation	Board member: Partner Communications Ltd.; Fox Wiesel Ltd.; Academic Track, Management College (volunteer Board member); Yisum R&D Corporation of the Hebrew University (volunteer Board member); Perion Network Ltd. (Board member as from December 31, 2015). Founding Partner, Firewind PE.
Previous occupation (in past 5 years, other than current occupation)	Partner, Viola Private Equity. Board member of: Amiad Water Systems Ltd.; Aeronautics Ltd.; Orad High-tech Systems Ltd.; Matomi Media Group Ltd.; Degania Silicon Ltd.; Audiocodes Ltd.; D-Pharm Ltd.; Advisor to Liquidnet Israel.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

Joseph Shachak	
Membership of Board of Directors' committees	Credit, Audit, Remuneration, Risks Management as from January 2, 2017.
External Board member as defined in Proper Banking Conduct Directive 301	Yes
External Board member as defined in the Companies Law	No
Independent Board member	Yes
Has accounting and financial expertise	Yes
Has professional qualifications	Yes
Expert Board member(1)	Yes
Employed by the corporation, subsidiary, affiliate or an interested party	No
Start date in office as member of the Bank's Board of Directors	26.4.2010
Education	Academic, Undergraduate degree in Accounting, Hebrew University, Jerusalem; CPA
Current occupation	Accounting and Financial Advisor to corporations and Boards Board member: Tafron Ltd.; Yogi Consulting and Investments Ltd. - controlling shareholder; Shachak & Co. Assets Ltd. - shareholder; Member, Public Council of the Accounting Standards Board; HaBima National Theater (external Board member), Neve Hon Real Estate Ltd., external Board member of Southern Properties Capital Ltd. (as from November 11, 2016).
Previous occupation (in past 5 years, other than current occupation)	Member, Audit Committee of the Bank of Israel; Board member: Dash Provident Fund Management Ltd., Elul Tamarind Ltd., Psagot Investment House Ltd., Peleg Nia Ltd., Academic Track of the Management College.
Family member of another interested party in the corporation	No
Board member regarded by the corporation as having accounting and financial expertise for meeting the minimum number specified by the Board	No

(1) As this term is defined in the Companies Regulations (Rules for remuneration and expense reimbursement for external board members), 2000.

Board of Directors - continued

During 2016, the Bank Board of Directors held 28 plenary meetings. During this period there were also 66 meetings of Board committees and 5 Board member workshops.

The permanent Board committees are: Audit Committee, Risks Management Committee, Credit Committee and Remuneration Committee.

Presented below are changes during 2016 and through publication of these financial statements:

On March 8, 2016, the General Meeting of Bank shareholders approved the terms of office and employment of Mr. Vidman as Chairman of the Bank’s Board of Directors for a term in office started on December 1, 2015, as stated in an Immediate Report dated March 8, 2016, reference no. 2016-01-002319. This mention constitutes inclusion by way of reference of all information provided in the aforementioned Immediate Report. For more information about approval of terms of office and employment of the Chairman, see Note 22.A.1 to the financial statements.

On that date, the General Meeting of Bank shareholders resolved to amend the Bank’s Bylaws, reducing the Bank's permission to waive liability of its officers for any damage incurred due to any breach of duty of care towards the Bank, so that such waiver would not apply to any breach of duty of care which occurred after December 23, 2015 when making a decision or approving a transaction in which the controlling shareholder of the Bank or any officer of the Bank (including another officer, other than the officer who received the waiver) has a personal interest.

On April 4, 2016, the General Meeting of Bank shareholders approved, after approval by the Bank's Remuneration Committee and Board of Directors, to pay the Chairman of the Board of Directors the amount of NIS 246 thousand (1.35 monthly salaries), which is the full amount with respect to the discretionary portion of the bonus payable to the Chairman of the Board of Directors for 2015, such that the total annual bonus paid to the Chairman of the Board of Directors for 2015 amounted to NIS 764 thousand.

On the same date, the General Meeting of Bank shareholders approved the appointment of Mr. Jacob Abraham Neyman and Mr. Yossi Shachak as external Board members of the Bank for a further 3-year term.

On September 19, 2016, Mr. Avi Zigelman concluded his term in office as external Board member of the Bank. Consequently, the number of Board members having accounting and financial qualifications is 10.

On September 19, 2016, Ms. Osnat Ronen was appointed Chair, Audit Committee - replacing Mr. Avi Zigleman.

On September 19, 2016, Mr. Jacob Abraham Neyman was appointed Chair, Remuneration Committee - replacing Mr. Avi Zigleman.

On September 28, 2016 the General Meeting of Bank shareholders approved the appointment of Ms. Osnat Ronen as external Board member of the Bank for a further 3-year term.

On January 2, 2017, Mr. Joseph Shachak was appointed member of the Risks Management Committee.

Board members having accounting and financial qualifications

The Bank’s Board of Directors prescribed that at least three directors should have accounting and finance skills. In the Board’s opinion, this number enables it to meet all of the obligations imposed on it, especially with respect to its responsibility to examine the financial position of the corporation and to prepare and approve financial statements. The Board has also determined that the Audit Committee would have as members at least 2 Board members having accounting and financial qualifications. Upon publication of these financial statements, there are 10 Board members with accounting and finance skills: Moshe Vidman, Sabina Biran, Avraham Zeldman, Nachshon Yoav-Asher, Mordechai Meir, Jacob Abraham Neyman, Gideon Siterman, Yonatan Kaplan, Osnat Ronen, Joseph Shachak. The Audit Committee includes 7 Board members having accounting and financial qualifications.

Below are the facts related to each of the directors in the Bank named above, and by virtue of which they are to be deemed having accounting and financial skills:

Moshe Vidman

Undergraduate degree in Economics; Graduate degree in Business Administration; specialized in Financing; served as CEO of two industrial companies; Board member at leading companies for over 25 years; member, Finance Committee and Audit Committee, served as Chairman of multiple companies. Serves as Chairman of the Bank Board of Directors.

Board of Directors - continued

Sabina Biran

Undergraduate degree in Political Science and Economics, Haifa University; MBA; served as CEO of two airlines; Board member of private and public companies; formerly - Chairperson of the Board of Directors of an industrial company.

Avraham Zeldman

Studied Statistics and Economics, Business Administration at Haifa University (not eligible for degree). Serves as Chairman of the Board of Directors of a public company. Has served as executive at Bank Leumi, as Chairman of the Board of Directors at Bank Leumi LeMashkantaot and as CEO at Leumi Partners Ltd. Has served as Board member with private and public companies.

Nachshon Yoav-Asher

Undergraduate degree in Economics and Accounting, Tel Aviv University; MBA (specialized in Strategy); CFO, VP, Finance and Business Development; Board member of private and public companies.

Mordechai Meir

BA in Accounting and Economics – Tel Aviv University; CPA. Worked for nine years at Somekh Chaikin as Senior CPA, board member of public companies, consultant to interested parties in public companies. In recent years: CEO of consulting firm, MERAV Management Ltd. - specialized in consulting to and representation of real estate and financial sectors for major corporations and enterprises.

Jacob Abraham Neyman

Professor at Hebrew University, Mathematics Institute (since 1982), Economics Department (1982-1989) and Center for Research into Rationality (since 1990). Has served as Board member of public companies; currently serves as Chairman of the Board of Directors of BIDORBUY.COM.

Gideon Siterman

CPA, former member of Securities Authority, former Director General of the Ministry of Transportation and Chairman, Port of Ashdod, has extensive accounting, economics and financial knowledge.

Jonathan Kaplan

Undergraduate degree in Economics and Accounting, Tel Aviv University; CPA; graduate degree in Political Science and National Security; Economic Advisor; Board member of private and public companies; formerly - Income Tax Commissioner.

Osnat Ronen

Undergraduate degree in Mathematics and Computer Science from Tel Aviv University. MBA (Finance) from Tel Aviv University. Has served as Deputy CEO of investment house; Board member of private and public companies.

Joseph Shachak

Undergraduate degree in Accounting, Hebrew University, Jerusalem; CPA; accounting and financial advisor to private and public companies; Board member of private and public companies; previously - President, Institute of Certified Public Accountants in Israel.

The Bank's Board of Directors thanks the Bank President & CEO, management and employees for their efforts to promote the Bank, the result of their diligent efforts to maintain the Bank's services with due responsibility. The Board of Directors appreciates the constant efforts of the Bank President & CEO, Bank management and Bank employees to expand the business activities and client base.

Executive Management

The following are Executive Management Forum members as of December 31, 2016 with their title and position:

Eldad Fresher	President & CEO	
Menahem Aviv	Vice-President	Manager, Accounting & Financial Reporting Division and Chief Accountant
Israel Engel	Vice-President	Manager, Retail Division
Ayala Hakim		Manager, Mizrahi Tefahot Technology Division Ltd. and CIO
Moshe Lari	Vice-President	Manager, Finance Division and Chief Financial Officer (CFO)
Nisan Levi	Vice-President	Manager, Planning, Operations and Customer Asset Division
Ofir Morad	Vice-President	Manager, Business Banking Division
Dinah Navot	Vice-President	Manager, Marketing, Promotion and Business Development Division
Racheli Friedman	Vice-President	Manager, Legal Division, Chief Legal Counsel
Doron Klauzner	Vice-President	Manager, Risk Control Division and Chief Risk Officer (CRO)
Rita Rubinstein	Vice-President	Manager, Human Resources and Administration Division

Galit Weiser		Chief Internal Auditor; Manager, Internal Audit Division
Maya Feller		Corporate Secretary
Benny Shoukroun		Bank Spokesman

Senior Officers

Below are details of senior officers who are not members of the Bank's Board of Directors:

Eldad Fresher	
Start of term in office	November 3, 2004 (since August 16, 2013 - as Bank President & CEO)
Title	President & CEO
Position held in banking corporation / subsidiary	President & CEO Chairman, Mizrahi Bank Switzerland
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Business Administration – Hebrew University, Jerusalem; MBA – Hebrew University, Jerusalem
Business experience (in past 5 years)	Manager, Financial Division – CFO at Bank Mizrahi Tefahot Ltd.

Menahem Aviv	
Start of term in office	13.4.2005
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Accounting & Financial Reporting Division and Chief Accountant Board member of Mizrahi Tefahot Issue Company Ltd.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Accounting and Economics – Tel Aviv University; MBA – Tel Aviv University; CPA
Business experience (in past 5 years)	Manager, Accounting and Financial Reporting Division and Chief Accountant – Bank Mizrahi Tefahot Ltd.

Israel Engel	
Start of term in office	1.1.2005
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Retail Division Board member of Bank Yahav; Board member of Tefahot Insurance(1)
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Accounting and Economics – Bar Ilan University; MBA (Finance) – Bar Ilan University; CPA
Business experience (in past 5 years)	Manager, Retail Division - Bank Mizrahi-Tefahot Ltd.

(1) Tefahot insurance - Tefahot Insurance Agency (1989) Ltd.

Senior officers - continued

Galit Weiser[1]	
Start of term in office	7.7.2011
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Chief Internal Auditor; Manager, Internal Audit Division Chief Internal Auditor, Bank Yahav and of the following companies: Etgar, Ne'emanut, Mizrahi Tefahot Issuance, Netzivim, Tefahot Insurance[2].
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Accounting and Economics (Hebrew University); graduate degree in Business Administration (Hebrew University), CPA.
Business experience (in past 5 years)	Chief Internal Auditor; Manager, Internal Audit Division

Ayala Hakim	
Start of term in office	1.7.2013
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Mizrahi-Tefahot Technology Division Ltd.; CIO for the Bank
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Accounting and Political Science – Bar Ilan University; Graduate degree in Business Administration – Bar Ilan University;
Business experience (in past 5 years)	Lt. General, Commander, LOTEM unit of IDF Computer Corps

Moshe Lari	
Start of term in office	November 8, 2009 (in current position - since August 16, 2013)
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Financial Division – CFO Chairman, Mizrahi Tefahot Issue Company Ltd.; Board member, Bank Yahav
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Economics and Accounting - Hebrew University, Jerusalem; Graduate degree in Business Administration - Tel Aviv University; CPA
Business experience (in past 5 years)	Manager, Planning, Operations and Customer Asset Division at Bank Mizrahi Tefahot Ltd.

(1) Pursuant to provisions of Section 146(B) of the Companies Law, -1999 - the Internal Auditor is not an interested party of the corporation, an officer or relative there of.

(2) Etgar – Etgar Investment Portfolio Management Company of the Mizrahi Tefahot Group Ltd.
Ne'emanut – Mizrahi Tefahot Trust Company Ltd.
Mizrahi Tefahot Issuance - Mizrahi Tefahot Issue Company Ltd.
Netzivim – Netzivim Assets and Equipment Ltd.
Tefahot insurance - Tefahot Insurance Agency (1989) Ltd.

Senior officers - continued

Nisan Levi	
Start of term in office	2.2.2014
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Planning, Operations and Customer Asset Division Chairman, Tefahot Insurance(1); Chairman, Mizrahi Tefahot Trustees Ltd.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Economics and Accounting - Hebrew University, Jerusalem; Graduate degree in Business Administration - Hebrew University, Jerusalem; CPA
Business experience (in past 5 years)	Manager, Finance Division at Bank Jerusalem Ltd.

Ofir Morad	
Start of term in office	1.1.2014
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Business Banking Division
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Economics and Business Administration; Graduate degree in Industrial Engineering.
Business experience (in past 5 years)	Deputy Manager, Business Banking Division at Bank Mizrahi Tefahot Ltd.

Dinah Navot	
Start of term in office	1.4.2012
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Marketing, Promotion and Business Development Division
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Social Work, Tel Aviv University; graduate degree in Journalism and Media, Bar Ilan University; graduate degree in Social Psychology and Sociology, Bar Ilan University
Business experience (in past 5 years)	Strategic business consulting for organizations, VP, Marketing at HOT Communication Systems

(1) Tefahot insurance - Tefahot Insurance Agency (1989) Ltd.

Senior officers - continued

Racheli Friedman	
Start of term in office	1.1.2015
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Legal Division, Chief Legal Counsel
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate Law degree (LL. B) – Tel Aviv University, Graduate Law degree (LL. M) – Tel Aviv University.
Business experience (in past 5 years)	Chief Legal Counsel at the Bank

Maya Feller	
Start of term in office	20.4.1997
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Corporate Secretary
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree (BA) in Humanities – Tel Aviv University
Business experience (in past 5 years)	Secretary, Bank Mizrahi-Tefahot Ltd.

Doron Klauzner	
Start of term in office	November 8, 2009 (in current position - since January 1, 2014)
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Risks Control Division, CRO.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	Undergraduate degree in Economics and Business Administration - Bar Ilan University
Business experience (in past 5 years)	Manager, Business Banking Division at Bank Mizrahi Tefahot Ltd.

Rita Rubinstein	
Start of term in office	1.1.2007
Title	Vice-President
Position held in banking corporation, subsidiary, affiliate or interested party in the corporation	Manager, Human Resources and Administration Division Chair, Mizrahi-Tefahot Security Services Ltd.; Chair, Netzivim Assets and Equipment Ltd.
Family member of another senior officer or of an interested party in the banking corporation	No
Education	BA in Humanities and Social Sciences – Hebrew University, Jerusalem; MA in Humanities and Social Sciences, Bar Ilan University
Business experience (in past 5 years)	Manager, Human Resources and Administration Division at Bank Mizrahi-Tefahot Ltd.

Internal Auditor

The following is information about the Chief Internal Auditor of the Bank Group, who started in office on July 7, 2011:

Name	Galit Weiser
Start of term in office	July 2011
Education	CPA; undergraduate degree in Accounting and Economics (Hebrew University); graduate degree in Business Administration (Hebrew University).
Experience	Deputy Chief Internal Auditor at Bank Mizrahi Tefahot; previously, Chief Internal Auditor of Bank Tefahot.

Pursuant to provisions of Section 146(B) of the Companies Law, -1999 - the Internal Auditor is not an interested party of the corporation, an officer or relative there of.

Pursuant to provisions of Section 8 of the Internal Audit Act, 1992, the Internal Auditor holds no other position in addition to her position as Chief Internal Auditor, other than as Ombudsman, Internal Auditor of Bank Yahav and Auditor of Bank Mizrahi Tefahot subsidiaries. The Bank's Internal Auditor holds no position outside of the Bank which creates or may create conflict of interest with her position as Internal Auditor. Other than the foregoing, the Internal Auditor has no material business relationships or other material relationships with the Bank or with any related entity thereof.

In conformity with Proper Banking Conduct Directive 307, audit staff are only appointed subject to consent of the Internal Auditor. Audit staff act on behalf of the Internal Auditor for the purpose of internal audit, and are only instructed on audit-related matters by the Internal Auditor. Internal Audit staff do not hold other positions with the banking corporation in addition to internal audit, other than as Ombudsman. Internal Audit staff may only sign on behalf of the banking corporation documents related to audit work or to inquiries from the public. Internal Audit employees are terminated with due process and consent of the Internal Auditor.

As of December 31, 2016, the Internal Auditor is eligible to receive 179,711 options to buy Bank shares. For further details about this allotment, see Note 23 to the financial statements.

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

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

Appointment process – Roles and responsibilities

In June 2011, appointment of the Internal Auditor was confirmed by the Audit Committee and the Board of Directors, based on the Auditor's experience and educational qualifications.

The roles and responsibilities of Internal Audit are listed in the Appointment Letter, which has been discussed and approved by the Bank's Board of Directors, including:

- The authority and ability to initiate audits of all units and existing operations of the Bank, in Israel or overseas, and to demand and receive any document and any information required for discharging their office.
- Employees of the Internal Audit function shall have direct access - for discharging their office - to all records, to any regular or computer-based repository, to any database and work files and to any program of automated data processing, including managerial information and meeting minutes of decision making entities, related to the audit subject.
- Employees of the Audit function may enter any property owned or used by the Bank and to examine it.
- With regard to confidential information by law, the Internal Auditor, their staff and anyone acting on behalf thereof shall be subject to statutory limitations. The Internal Auditor, their staff and anyone acting on behalf thereof must not disclose any document or information obtained in the course of discharging their office - unless such disclosure is required for lawfully discharging their office or if such disclosure is required by any law.

Identity of the Internal Auditor's Supervisor

The Internal Auditor reports to the Chairman of the Board of Directors.

Internal Audit work plan

Internal Audit work is based on a multi-annual audit plan focused on risk for a 4-year period from which an annual work plan is derived. Note that checking of material operations and transactions, including checking of transactions with related parties, are incorporated into the multi-annual work plan of Internal Audit.

Considerations in determining the multi-annual audit plan

- Mapping of activities carried out by different Bank departments according to organizational structure, assignment of potential risk to each activity and setting audit frequency accordingly.
- Risks surveys conducted at the Bank.
- Regulatory requirements arising from directives of the Supervisor of Banks.
- Basel directives and the ICAAP process.
- Current audit reports of the Bank of Israel.
- Findings in audit reports of the Audit Division.
- Decisions of the Audit Committee and the Chairman of the Board of Directors, as well as requests from the Bank President & CEO.

The multi-annual work plan is prepared by the Internal Auditor, brought up for discussion by the Board of Directors' Audit Committee and sent to the Bank President. After discussion and recommendation by the Audit Committee, the plan is submitted for approval by the Board of Directors.

Accordingly, on February 1, 2016, the Board of Directors approved the Internal Audit work plan for 2016-2019.

Considerations in determining the annual audit plan

In addition to the aforementioned considerations, used as basis for determining the multi-annual audit plan from which the annual audit plan is derived, the annual work plan includes additional special tests required of Internal Audit by request of the Supervisor of Banks and the Audit Committee. In addition, the audit refers to issues as requested by Bank management.

Any material changes are brought for approval by the Audit Committee. In case of non-material changes, the Audit Committee is informed after the fact.

Similar to the multi-annual audit plan, the annual audit plan is also prepared by the Internal Auditor and brought for discussion by the Board's Audit Committee. The plan is also submitted to the President. After the Board's Audit Committee recommends approval of the plan, the plan is submitted for approval by the Board of Directors.

Accordingly, on February 1, 2016, the Board of Directors approved the Internal Audit work plan for 2016.

Overseas audits or audits of held corporations

The Bank's Internal Auditor includes in the annual and multi-annual audit program the active corporations held by the Bank, during her tenure as their internal auditor, except for Bank Mizrahi Switzerland, which had its own internal auditor during the reported period. With respect to this company, the Internal Auditor verifies that there is proper internal auditing.

At Bank Yahav, a separate audit plan is submitted to the Bank Yahav Board of Directors.

Scope of employment of the Internal Auditor and their staff

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

The average number of positions reporting to the Internal Auditor is derived from Internal Audit needs, which arise from the multi-annual work plan and from the annual work plan of Internal Audit. The average number of positions in 2016, including internal auditors of subsidiaries and overseas branches is as follows:

In Israel		Outside of Israel
Employees engaged in internal audit	Employees engaged in role of Ombudsman	Employees engaged in internal audit
48(1)	6	2.5(2)

(1) Includes 7 full-time positions for audit at Bank Yahav, including outsourcing at Bank Yahav. In addition, Internal Audit at Bank Mizrahi Tefahot used outsourced services equivalent to 2 full time positions, which are also included.

(2) Includes use of external service providers overseas.

Conducting audits

The Internal Auditor performs the audit based on the generally accepted professional standards.

- Various legal requirements, including provisions of the Internal Audit Act, 1992, Banking Regulations (Internal Audit), 1992 and regulatory authorities' instructions relevant to the audited area, including guidelines and directives of the Supervisor of Banks, including Proper Banking Conduct Directive 307 concerning "Internal Audit function".
- Standards for Professional Engagement in Internal Audit of the Global Institute of Internal Auditors.

The Board of Directors and the Audit Committee believe that audit is conducted in accordance with the aforementioned professional standards so as to achieve the objectives of the internal audit. This is done, *inter alia*, based on annual reporting, semi-annual reporting and work plans of Internal Audit, which include reference to these issues. Furthermore, as needed, an independent external survey is conducted, once every 5 years, of the quality of work of Internal Audit, which is reported to the Audit Committee.

Access to information

The Internal Auditor regularly has complete access to all the information he needed, in conformity with Proper Banking Conduct Directive 307, as stated in Section 9 of the Internal Audit Law, 1992, including constant and direct access to the Bank's IT systems, including financial data. Note that in conducting audits at investees and operations outside of Israel, too, Internal Audit has full access, as noted above, through visits to operation hubs outside of Israel or through receiving material on demand.

Submitting report of Audit findings

The Auditor regularly sends every audit report to the Chairman of the Board of Directors, the chairman of the Audit Committee, the Bank President & CEO and head of the internal audit unit. A copy of each report is also sent to the CRO, Compliance Officer and AML Supervisor, Manager, Risk Control Division and to the Chief Accountant. Audit reports are submitted in writing. Once every six months, the Auditor submits to members of the Audit Committee the list of all reports submitted during the six-month period. All of the reports are discussed in a forum including the division manager and/or official in-charge of the audited unit or activity. The material reports are discussed by a forum headed by the Bank President & CEO. The Chair of the Audit Committee, in consultation with the Internal Auditor, determines the material audit reports to be discussed by the Audit Committee.

On August 7, 2016, a report about the performance of the Internal Audit work plan for the first half of 2016. This report was discussed by the Audit Committee at its meeting held on August 10, 2016. The summary report of Internal Audit in 2016 was distributed on February 16, 2017 and discussed at the Audit Committee meeting held on March 6, 2017. Other major reports were discussed during the year at regular meetings of the Audit Committee.

Assessment of Internal Auditor's activities

The Board of Directors and the Audit Committee believe that the scope, nature, continuity of the activity and the work plan of the Internal Auditor realize the objectives of internal auditing.

Remuneration of the Internal Auditor

Below is information about the salary, benefits, employer contributions and provisions paid or provided for to the Chief Internal Auditor in 2016: Salary amounting to NIS 1,133 thousand, bonuses amounting to NIS 630 thousand (including retention bonus amounting to NIS 172 thousand), social benefits amounting to NIS 400 thousand, bonus with respect to share-based payment amounting to NIS 194 thousand and other benefits valued at NIS 81 thousand. Total remuneration paid or provided for, to the Internal Auditor in 2016 amounted to NIS 2,438 thousand. The outstanding balance of loans at standard terms, as of the end of 2016, amounted to NIS 21 thousand. For more information on officer remuneration policy, see Note 22.A.3.

The Board of Directors believes that the size of remuneration provided to the Internal Auditor should not influence her judgment with respect to his work.

Independent Auditors' Fees[(1)(2)(3)]
(NIS in thousands)

	Consolidated		The Bank	
	2016	2015	2016	2015
For audit activities[(4)]:				
Independent auditors[(5)]	7,027	7,134	6,347	6,444
Other independent auditors	1,236	1,276	396	434
Total	8,263	8,410	6,743	6,878
For tax services[(6)]:				
Independent auditors	–	–	–	–
Other independent auditors	122	128	122	128
For other services:				
Independent auditors[(7)(5)]	1,886	1,860	1,814	1,801
Other independent auditors	740	367	–	–
Total	2,748	2,355	1,936	1,929
Total fees to independent auditors	11,011	10,765	8,679	8,807

(1) Board of Directors' report to the annual general meeting on auditors' fees for audit activities and for other services in addition to the audit, in accordance with Sections 165 and 167 of the Companies Law, 1999.

(2) Independent auditors' fees include payments to partnerships and corporations under their control, as well as payments under the VAT Law.

(3) Includes fees paid and accrued.

(4) Audit of annual financial statements, review of interim financial statements and audit of report adjusted for income tax purposes.

(5) Includes other independent auditors in overseas branches.

(6) Includes payments for preparation of reports adjusted for income tax purposes and reports to tax authorities.

(7) Includes mainly payments for consulting and various services.

Details of senior officer remuneration[1]

(NIS in thousands)

All of 2016										
Details of remunerated party[2]		Remuneration for services rendered[3]						Loans granted at beneficial terms[4]		Loans granted at standard terms
Name	Role	Salary	Bonuses[14]	Social benefit contributions[5]	Share-based payment[6]	Value of additional benefits[7]	**Total**	Balance as of 31.12.2016	Average term to repayment (in years)	
Moshe Vidman[8]	Chairman of the Board of Directors	2,651	–	612	–	133	**3,396**	386	3.3	10
Eldad Fresher[9]	President & CEO	2,385	678	758	449	145	**4,415**	–	–	48
Doron Klauzner[10]	Vice President and Manager, Risks Control Division, CRO	1,136	624	412	191	87	**2,450**	–	–	51
Israel Engel[11]	Deputy President and Manager, Retail Division	1,132	585	406	246	80	**2,449**	–	–	56
Moshe Lari[12]	Deputy President and Manager, Finance Division, CFO	1,135	585	389	246	87	**2,442**	962	11.3	23

All of 2015										
Details of remunerated party[2]		Remuneration for services rendered[3]						Loans granted at beneficial terms[4]		Loans granted at standard terms
Name	Role	Salary	Bonuses[14]	Social benefit contributions[5]	Share-based payment[6]	Value of additional benefits[7]	Total	Balance as of 31.12.2015	Average term to repayment (in years)	
Moshe Vidman[8]	Chairman of the Board of Directors	2,378	1,475	373	–	123	**4,349**	–	–	27
Eldad Fresher[9]	President & CEO	2,384	1,021	901	1,108	145	**5,559**	–	–	32
Racheli Friedman[13]	Chief Legal Counsel; Manager, Legal Division	1,124	526	1,611	418	74	**3,753**	628	3.7	35
Dina Navot[14]	Deputy President and Manager, Marketing, Promotion and Business Development Division	1,136	552	461	610	81	**2,840**	341	4.1	56
Moshe Lari[12]	Deputy President and Manager, Business Division CFO	1,133	560	411	611	82	**2,797**	993	12.8	22

Remarks:

(1) Remuneration is in terms of cost to the Bank and excludes payroll tax.

(2) Remuneration recipients are employed in a full-time position and do not hold Bank equity.

(3) The amounts are included under "salaries and related expenses" in the statement of profit and loss.

(4) The benefit is under the same terms and conditions granted to all Bank employees.

(5) Includes severance pay, pension, study fund, acclimation bonus, paid leave and social security.

(6) For details of share-based payment to the President and to officers, see Note 23 to the financial statements.

(7) Interest relates to loans granted at beneficial terms compared to market terms. There is no interest benefit with respect to deposits. In other banking transactions, the benefits apply to all Bank employees and the amount there of is immaterial.

(8) Mr. Moshe Vidman – On March 8, 2016, the General Meeting of Bank shareholders approved, after approval by the Bank's Remuneration Committee and Board of Directors, the terms of office and employment of Mr. Vidman as Chairman of the Bank Board of Directors pursuant to the approved employment agreement. The employment term is from December 1, 2015 through December 31, 2017 and will be automatically renewed, every year, for one additional year - all subject to provisions of the employment agreement.

Due to enactment of the Executive Remuneration Act, the Bank was required to amend the terms of office and employment of the Chairman of the Board of Directors. On February 14, 2017, the General Meeting of Bank shareholders approved, in line with the resolution by the Board of Directors and after approval by the Remuneration Committee, the terms of office and employment of Mr. Vidman as Chairman of the Bank's Board of Directors in line with a new officer remuneration policy, also approved by the General Meeting on said date, which was made to conform to provisions of the Executive Remuneration Act and with due attention to amendments required by Proper Banking Conduct Directive 301A with regard to remuneration ("the new remuneration policy").

For more information about remuneration of the Chairman of the board of Directors, see Note 22.A.1 to the financial statements. As for bonuses, see details in section (15) below.

(9) Mr. Eldad Fresher – On June 17, 2013, the Bank Board of Directors approved the appointment of Mr. Eldad Fresher as Bank President. Mr. Fresher started in his office as full-time Bank President on August 16, 2013.

On May 4, 2014, the Bank's Board of Directors approved, after approval by the Remuneration Committee, the Bank President's terms of office and employment. On June 10, 2014, these terms of office and employment were approved by the General Meeting of Bank shareholders.

Employment terms of the President & CEO were determined in conformity with the Bank's officer remuneration policy, as adapted to Proper Banking Conduct Directive 301A with regard to remuneration policy of a banking corporation. This policy was approved by the Remuneration Committee, the Bank's Board of Directors and the General Meeting of Bank shareholders.

On February 14, 2017, the General Meeting of Bank shareholders approved, in line with the resolution by the Board of Directors and after approval by the Remuneration Committee, the terms of office and employment of Mr. Fresher as Bank President & CEO, in line with a new officer remuneration policy, also approved by the General Meeting on said date, which was made to conform to provisions of the Executive Remuneration Act and with due attention to amendments required by Proper Banking Conduct Directive 301A with regard to remuneration ("the new remuneration policy").

For more information about remuneration of the Bank President & CEO, see Note 22.A.2 to the financial statements. As for bonuses, see details in section (15) below.

(10) Mr. Doron Klauzner – employed by the Bank under an individual employment contract effective since November 8, 2009 for an unspecified term. Mr. Klauzner's monthly salary is linked to the Consumer Price Index. Upon termination of his employment at the Bank, Mr. Klauzner is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Mr. Klauzner is eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Klauzner shall not be eligible for an acclimation bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under exceptional circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment contract. For officer remuneration policy, see Note 22.A.3 to the financial statements. As for bonuses, see details in section 15 below.

(11) Mr. Israel Engel – employed by the Bank under an individual employment contract effective since June 15, 1999 for an unspecified term. Mr. Engel's monthly salary is linked to the Consumer Price Index. Upon termination of his employment at the Bank, Mr. Engel is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Mr. Engel is eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Engel shall not be eligible for an acclimation bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under exceptional circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment contract. For officer remuneration policy, see Note 22.A.3 to the financial statements. As for bonuses, see details in section 15 below.

(12) Mr. Moshe Larry – employed by the Bank under an individual employment contract effective since November 8, 2009 for an unspecified term. Mr. Larry's monthly salary is linked to the Consumer Price Index. Upon termination of his employment at the Bank, Mr. Larry is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Mr. Larry is eligible to have the Bank, upon termination of his employment, release to him all amounts accumulated on his behalf in the various funds. Notwithstanding the above, Mr. Larry shall not be eligible for an acclimation bonus and release of amounts accumulated on his behalf in the various funds in case of termination of his employment under exceptional circumstances, as stated in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment agreement. For officer remuneration policy, see Note 22.A.3 to the financial statements. As for bonuses, see details in section (15) below.

(13) Ms. Racheli Friedman – employed by the Bank under an individual employment contract effective since January 1, 2015 for an unspecified term. Ms. Friedman's monthly salary is linked to the Consumer Price Index. Upon termination of her employment at the Bank, Ms. Friedman is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever as an officer. Furthermore, Ms. Friedman will be eligible to have the Bank, upon termination of her employment, release to her all amounts accumulated on her behalf in the various funds. Notwithstanding the above, Ms. Friedman shall not be eligible for an acclimation bonus and release of amounts accumulated on her behalf in the various funds in case of termination of her employment under exceptional circumstances, as specified in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment contract. For officer remuneration policy, see Note 22.A.3 to the financial statements. As for bonuses, see details in section 15 below.

(14) Ms. Dina Navot – employed by the Bank under an individual employment contract effective since March 5, 2012 for an unspecified term. Ms. Navot's monthly salary is linked to the Consumer Price Index. Upon termination of her employment at the Bank, Ms. Navot is eligible to receive an acclimation bonus equal to 6 monthly salaries, with no additional benefits whatsoever. Furthermore, Ms. Navot will be eligible to have the Bank, upon termination of her employment, release to her all amounts accumulated on her behalf in the various funds. Notwithstanding the above, Ms. Navot shall not be eligible for an acclimation bonus and release of amounts accumulated on her behalf in the various funds in case of termination of her employment under exceptional circumstances, as specified in the agreement. Each of the parties to the employment contract may terminate the contract with 3 months' prior notice and subject to terms and conditions stated in the employment agreement. For officer remuneration policy, see Note 22.A.3 to the financial statements. As for bonuses, see details in section 15 below.

(15) Bonuses

1.1. Bonus to Chairman of the Board of Directors

In conformity with their terms of office and employment, since 2016 the Chairman of the Board of Directors is not entitled to variable compensation. In 2015, the Chairman of the Board of Directors, the Chairman is entitled, *inter alia*, to an annual monetary bonus equal to 9 monthly salaries at most, based on the eligibility formula approved in conjunction with approval of their terms of employment and office and subject to threshold conditions based on return on equity, overall capital adequacy ratio and core capital adequacy ratio for the Bank for the bonus year. The Chairman of the Board of Directors will also be entitled to an additional deferred bonus, soon after approval of the Bank's 2015 financial statements, equal to up to 9 monthly salaries, subject to threshold conditions based on return on equity and in accordance with an eligibility formula for the deferred bonus - as specified in Appendix II to the Immediate Report concerning approval of terms of employment and office of the Chairman of the Board of Directors.

The eligibility formula for the annual bonus, approved as specified above, is based on three (3) quantitative, company-wide targets which account for up to 85% of the maximum potential bonus: return on equity (weighted at 55% of the maximum potential bonus), ratio of return on Bank share to return of banking index shares and operating efficiency ratio (each weighted at 15% of the maximum potential bonus). The annual bonus formula also includes a discretionary bonus component, accounting for up to 15% of the maximum potential bonus.

With respect to 2015, the Chairman of the Board of Directors is entitled, based on quantitative benchmarks in the eligibility formula for the annual bonus - as specified in Appendix II to the Immediate Report about approval of the terms of employment and office of the Chairman of the Board of Directors, to a bonus amounting to NIS 518 thousand. The Remuneration Committee and the Board of Directors also approved the award of the discretionary component in full (15% of the maximum potential bonus), amounting to NIS 246 thousand, with respect to 2015. Approval of the discretionary component of the annual bonus is subject to approval by the General Assembly of shareholders.

With regard to the aforementioned deferred bonus, the Chairman is eligible to receive a bonus equal to 3.9 salaries with respect to 2013-2015, amounting to NIS 711 thousand.

1.2. Bonus for the President & CEO

According to the remuneration plan of the President & CEO, as specified in the Immediate Report about terms of employment and office of the President & CEO, he will be entitled - in addition to equity-based remuneration awarded to him and the eligibility for which is also conditional - to a monetary bonus capped at NIS 1,517 thousand plus CPI linkage differentials, based on the CPI known on August 16, 2013 ("the maximum monetary bonus") for each calendar year between 2014-2016. This is subject to meeting threshold conditions during the bonus year, based on rates of return on equity, overall capital adequacy ratio and core capital adequacy ratio at the Bank for the bonus years.

Eligibility of the President & CEO to the monetary bonus is contingent, as noted, on threshold conditions and is based on four (4) quantitative, company-wide benchmarks: return on equity, return on Bank share compared to the comparison benchmark, operating efficiency ratio and average ratio of deposits to loans, whose aggregate weighting is 85% of the maximum monetary bonus, as well as a qualitative bonus weighted at 15% of the maximum monetary bonus. For details of threshold conditions for eligibility for the monetary bonus, conditions for eligibility for the monetary bonus, the Board of Directors' authority to reduce the monetary bonus and provisions with regard to reimbursement of the monetary bonus – see Appendix II to the Immediate Report about terms of employment and office of the President & CEO. The annual bonus to which the President & CEO is eligible with respect to quantitative benchmarks for 2016 is NIS 842 thousand (in 2015: NIS 793 thousand). The Bank’s Board of Directors also approved, after approval by the Remuneration Committee, NIS 228 thousand with respect to the qualitative benchmark for 2016 (in 2015: the same), for a total of NIS 1,070 thousand (in 2015: NIS 1,021 thousand). In 2016, once the Executive Remuneration Act became effective, the total bonus to which the Bank President & CEO is eligible, was capped at NIS 678 thousand.

1.3. Bonus for officers and for the Internal Auditor

On June 19, 2014, the Bank’s Board of Directors approved, after approval by the Remuneration Committee, and in line with the officer remuneration policy, approved on June 10, 2014 by the General Meeting of shareholders, a remuneration plan for officers concerning, *inter alia*, award of equity-based remuneration and monetary remuneration ("variable remuneration"). Eligibility for variable remuneration is contingent on threshold conditions, identical to those listed in the Immediate Report about terms of employment and office of the President & CEO and is also based on four (4) quantitative company-wide benchmarks, identical to those in the remuneration plan of the President & CEO, whose aggregate weighting is 80% of the maximum monetary bonus, as well as two qualitative benchmarks weighted at 10% each. The qualitative benchmarks refer to achievement by each officer of individual targets specified for them at the start of the year, as well as to evaluation of the officer's overall performance, at the discretion of the President & CEO - to be brought for approval by the Remuneration Committee and by the Board of Directors. As for the Chief Internal Auditor, evaluation of her achievement of her individual targets and evaluation of her performance would be by the Audit Committee, after receiving the recommendation of the Chairman of the Board of Directors - to be brought for approval by the Remuneration Committee and by the Board of Directors. The Bank’s Board of Directors, after approval by the Remuneration Committee and after receiving evaluations by the President & CEO and by the Chairman of the Board of Directors, as the case may be, as specified above, approved the eligibility rate of the officers and the Chief Internal Auditor with respect to the qualitative benchmarks (which also apply to the eligibility rate with respect to this component in equity-based remuneration).

Transactions with controlling shareholders and related parties

On August 6, 2008, the amendment to the Securities Regulations (Periodic and Immediate Reports), 1970 became effective ("the Amendment"), whereby, inter alia, a reporting corporation is required to issue an Immediate Report with regard to "details of a transaction with a controlling shareholder, or which the controlling shareholder has a personal interest in its confirmation, including highlights of the transaction or contract, details of the organ which confirmed the transaction and its summary reasons for the confirmation; in this paragraph, "transaction" excludes a transaction which the most recent financial statements classify transactions of its type as immaterial."

Banks have been exempted from immediate reporting of non-extraordinary banking transactions, provided they specify criteria for extraordinary and negligible transactions.

The Audit Committee of the Board of Directors has previously approved criteria for unusual and immaterial transactions, which the Committee ratified on February 6, 2017, as follows:

Transaction other than a banking transaction

Definition of "immaterial transaction":

A transaction other than a banking transaction, conducted in the normal course of business at market terms and conditions, and which meets one or more of the following criteria, is an immaterial transaction:

In this section, "transaction" means a transaction with a controlling shareholder, or a transaction in which a controlling shareholder has a personal interest.

A. Transaction for sale of retail products in the normal course of Bank business and at market conditions, amounting up to NIS 1.5 million per transaction, or a continuous transaction as stated above (multiple, essentially identical transactions with the same company), whose aggregate amount over one calendar year is up to 0.1% of supervisory capital, after adjustments and deductions, as defined in Proper Banking Conduct Directive 202 (hereinafter - "supervisory capital"). This amount will not apply to individual transactions whose amount is under NIS 25 thousand each.

B. Transaction for provision of services, including in the field of TV advertising, in the normal course of Bank business and at market conditions, amounting up to 0.1% of supervisory capital, or a continuous transaction as stated above (multiple, essentially identical transactions with the same company), whose aggregate amount over one calendar year is up to .0.75% of total annual operating and other expenses by the Bank's most recent annual financial statements. This amount will not apply to individual transactions whose amount is under NIS 25 thousand each.

C. Transactions involving leasing of space, in the normal course of Bank business and at market conditions, approved in a single calendar year and amounting up to 0.1% of supervisory capital.

D. Any other transaction in the normal course of Bank business and at market conditions, where the total amount for such a transaction type in a single calendar year is up to 0.1% of supervisory capital. This amount will not apply to individual transactions whose amount is under NIS 25 thousand each.

Banking transaction

Definition of "unusual transaction" - a transaction other than at market conditions or not in the normal course of business or a material transaction.

A banking transaction which meets one of the following criteria shall be deemed to be, for this matter, a "material transaction":

A. **Indebtedness transaction** - an indebtedness transaction (after deductions, as specified in Proper Banking Conduct Directive no. 312), which results in total indebtedness of any group of controlling shareholders exceeding 5% of supervisory capital, or a transaction which results in the increase in indebtedness of an individual borrower from among the controlling shareholders exceeding 2% of supervisory capital. If multiple indebtedness transactions are approved for the same borrower in a single calendar year, these indebtedness transactions shall be measured in aggregate. Any specific provision for doubtful debts, or write-off of any amount with regard to indebtedness of a controlling shareholder or a corporation affiliated with it, shall be deemed to be a material transaction. Measurement of total indebtedness, for this matter, shall be separate for the Wertheim Group and for the Ofer Group.

"**Group of controlling shareholders**" - a controlling shareholder, as defined in the Securities Law, together with corporations affiliated there with, as the term "affiliated person" is defined in Proper Business Conduct of Directive 312, and together with relatives of controlling shareholders included in the group.

B. **Deposits** - receipt of deposit from a controlling shareholder shall be deemed to be a material transaction if, consequently, total deposits from the same group of controlling shareholders would exceed 2% of total deposits at the Bank. Receipt of deposit from a company which is an "affiliated person" of the controlling shareholder, and which is not a company controlled by it, shall be deemed to be a material transaction if, consequently, total deposits from that company, on a consolidated basis, would exceed 2% of total deposits at the Bank. Total deposits at the Bank will be calculated based on the most recent annual financial statements published by the Bank prior to the transaction date.

C. **Transaction in securities or in foreign currency (other than an indebtedness transaction or deposit transaction, as stated above)** - a transaction in securities or in foreign currency where the annual commission charged with respect there to does not exceed 2% of total annual operating revenues of the Bank (less revenues from investment in shares), based on the most recent annual financial statement published by the Bank prior to the transaction date.

D. **Other transactions** - any other transaction for provision of financial and banking services, the revenues from which to the Bank exceed 0.1% of the Bank's total supervisory capital.

Any temporary, immaterial deviation for a period of up to 30 days would not change classification of the transaction as an immaterial transaction, and disclosure of such deviation would be provided in the annual report.

"Market terms" - terms which are not preferable to those at which similar transactions are made by the Bank with individuals or corporations which are not controlling shareholders of the Bank, or in transactions in which the controlling shareholder has no personal interest . Market terms with regard to banking transactions are compared to terms of similar transactions of similar volume at the Bank, as used for review of transactions with affiliated persons in accordance with Proper Banking Conduct Directive 312, with Bank clients who are not affiliated persons, or are not entities where the controlling shareholder has a personal interest in transactions there with; market conditions with regard to transactions other than banking transactions are compared to conditions of similar transactions made by the Bank with suppliers and/or with regard to offers from other suppliers reviewed prior to deciding to make the commitment. In cases where the Bank has no similar transactions, market conditions are to be compared with regard to similar transactions made in the market, provided that such transactions are made in the normal course of business and that such transactions have a market in which similar transactions are made.

Indebtedness transactions to which Proper Banking Conduct Directive 312 does not apply - as for Indebtedness transactions to which Proper Banking Conduct Directive 312 does not apply, should the Bank become aware of any such transaction, the Bank commits to bring any such transaction for approval pursuant to Proper Banking Conduct Directive 312 and to provide disclosure of it in the Bank's annual financial statements. The definition of "immaterial transaction" and "unusual transaction" with regard to these transactions would be similar to the aforementioned definitions by the Bank.

Below is summary data with regard to banking transactions with controlling shareholders (NIS in millions):

A. Indebtedness transactions

					December 31, 2016
Group of controlling shareholders	Loan balance on balance sheet	Unutilized facility	Risk assets due to derivatives activity	Guarantees provided by the Bank to secure credit of controlling shareholder or its affiliated party	Total indebtedness[1]
Wertheim Group and private companies it controls	60	5	–	–	65
Relatives of Wertheim Group	–	–	–	–	–
Total - Wertheim Group	60	5	–	–	65
Ofer Group and private companies it controls	14	15	–	–	29
Relatives of Ofer Group and private companies it control	82	16	–	13	111
Reporting entities controlled by relatives of Ofer Group					
Oil Refineries Ltd.	–	85	–	–	85
Israel Chemicals Ltd.	–	3	14	–	17
Gadiv Petrochemical Industries Ltd.	–	27	–	–	27
Rotem Amfert Negev Ltd.	–	1	–	–	1
Total - Ofer Group	96	147	14	13	270

					December 31, 2015
Group of controlling shareholders	Loan balance on balance sheet	Unutilized facility	Risk assets due to derivatives activity	Guarantees provided by the Bank to secure credit of controlling shareholder or its affiliated party	Total indebtedness[1]
Wertheim Group and private companies it controls	–	–	–	–	–
Relatives of Wertheim Group	10	8	–	–	18
Total - Wertheim Group	10	8	–	–	18
Ofer Group and private companies it controls					
Relatives of Ofer Group	77	72	12	14	175
Reporting entities controlled by relatives of Ofer Group					
Oil Refineries Ltd.	77	78	–	–	155
Israel Chemicals Ltd.	–	–	–	–	–
Carmel Ulpinim Ltd.	–	–	–	–	–
Total - Ofer Group	154	150	12	14	330

(1) Indebtedness as defined in Proper Conduct of Banking Businesses regulation 312, after set off of allowed deductions.

B. Deposits

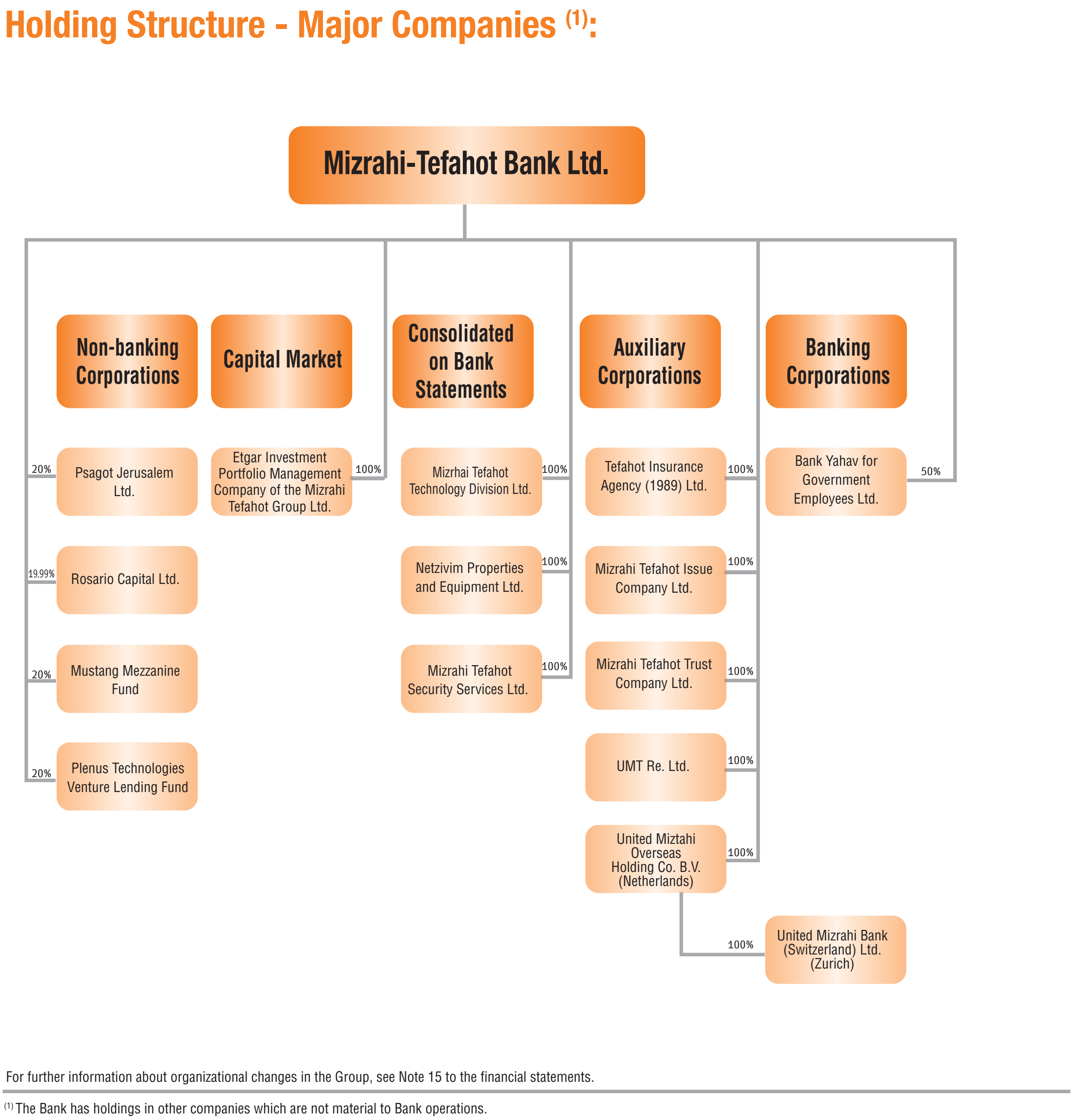
Group of controlling shareholders	Balance as of December 31, 2016	Highest balance in 2016
Wertheim Group and private companies it controls	61	156
Relatives of Wertheim Group and private companies it controls	–	–
Reporting entities controlled by relatives of Wertheim Group	–	–
Total - Wertheim Group	61	156
Ofer Group and private companies it controls	15	22
Relatives of Ofer Group and private companies it control	100	206
Reporting entities controlled by relatives of Ofer Group		
Oil Refineries Ltd.	195	380
Israel Corporation Ltd.	1,071	1,203
Israel Chemicals Ltd.	1	2
Gadish Petrochemical Industries Ltd.	2	4
Total - Ofer Group	1,384	1,819

Group of controlling shareholders	Balance as of December 31, 2015	Highest balance in 2015
Wertheim Group and private companies it controls	–	–
Relatives of Wertheim Group and private companies it controls	3	19
Reporting entities controlled by relatives of Wertheim Group		
Amot Investments Ltd.	3	5
Total - Wertheim Group	6	24
Ofer Group and private companies it controls	6	30
Relatives of Ofer Group and private companies it control	103	241
Reporting entities controlled by Ofer Group		
Meliseron Ltd.	–	–
Reporting entities controlled by relatives of Ofer Group		
Oil Refineries Ltd.	78	78
Israel Corporation Ltd.	195	501
Israel Chemicals Ltd.	–	–
Carmel Ulpinim Ltd.	1	10
Total - Ofer Group	383	860

To the best of the Bank's knowledge, transactions with affiliated persons were executed in the ordinary course of business, at market terms and under terms similar to those of transactions effected with unrelated entities.

Other information about the Bank and its management

Major holding structure[1] of Mizrahi Tefahot Group



(1) The Bank has holdings in other companies which are not material for Bank business.

See Note 15 to the financial statements for details.

Summary of key data by Group structure

	As of December 31, 2016							
	Operations in Israel			Operations overseas				
	Standard banking			Standard banking			Inter-	Total
	The Bank	Subsidiaries	Other	The Bank	Subsidiaries	Other	company	consolidated
Highlights of statement of profit and loss								
Net profit attributable to shareholders of the Bank	1,051	85	95	83	(6)	–	(42)	1,266
Interest revenues, net	3,100	493	31	145	8	–	1	3,778
Expenses with respect to credit losses	181	16	–	3	–	–	–	200
Non-interest revenues	2,243	137	129	1	8	–	(656)	1,862
Of which: Fees	1,167	135	108	13	16	–	(6)	1,433
Operating and other expenses	3,371	476	32	55	20	–	(655)	3,299
Of which: Payroll and associated expenses	1,768	232	20	37	12	–	2	2,071
Highlights of balance sheet								
Cash and deposits with banks	220,643	14,502	24,607	2,709	582	–	(221,318)	41,725
Securities	9,099	29	–	1,134	–	–	–	10,262
Loans to the public, net	159,179	8,931	–	2,970	261	–	–	171,341
Deposits from banks	195,723	33	–	1,911	1	–	(196,131)	1,537
Deposits from the public	177,705	20,273	–	4,779	493	–	(24,998)	178,252
Debentures and subordinated notes	3,270	793	23,544	–	–	–	(573)	27,034

	As of December 31, 2015							
	Operations in Israel			Overseas activity[1]				
	Standard banking			Standard banking			Inter-	Total
	The Bank	Subsidiaries	Other	The Bank	Subsidiaries	Other	company	consolidated
Highlights of statement of profit and loss								
Net profit attributable to shareholders of the Bank	927	120	84	59	4	–	(60)	1,134
Interest revenues, net	2,963	431	28	105	6	–	1	3,534
Expenses with respect to credit losses	200	11	–	–	–	–	–	211
Non-interest revenues	2,165	205	118	15	20	–	(665)	1,858
Of which: Fees	1,168	135	100	12	17	–	(6)	1,426
Operating and other expenses	3,349	433	30	58	21	–	(665)	3,226
Of which: Payroll and associated expenses	1,658	212	22	39	12	–	1	1,944
Highlights of balance sheet								
Cash and deposits with banks	185,326	14,299	21,579	2,297	592	–	(193,604)	30,489
Securities	10,727	31	–	1,077	10	–	–	11,845
Loans to the public, net	148,183	7,943	–	2,795	283	–	–	159,204
Deposits from banks	169,971	74	–	2,633	41	–	(171,553)	1,166
Deposits from the public	160,970	19,415	–	3,553	488	–	(22,046)	162,380
Debentures and subordinated notes	3,127	550	20,592	–	–	–	(550)	23,719

(1) Includes effect of exchange rate differences.

Controlling shareholders

To the best of the knowledge of the Bank and the Board of Directors, the holding interests of controlling shareholders of the Bank, as of December 31, 2016, are as follows:

	Holder	No. of shares	% of capital and voting rights
Wertheim Group	M.W.Z. (Holdings) Ltd.(1)	20,585,785	8.87
	F & W (Registered Partnership)(2)	30,172,844	13.00
	Total - Wertheim Group	50,758,629	21.87
Ofer Group	C.A.B.M. Ltd.(3)	7,193,594	3.10
	L.A.B.M. (Holdings) Ltd.(4)	7,814,717	3.37
	A.A.B.M. Ltd.(5)	15,428,435	6.65
	Ofer Investments Ltd.(6)	14,291,819	6.16
	Ofer Sahaf Ltd.(7)	7,477,642	3.22
	Total - Ofer Group	52,206,207	22.50
	Total holdings by controlling shareholders	102,964,836	44.37
Total shares issued by the Bank		(8)232,068,508	100.00

(1) A private company owned by David Wertheim (63%) and by Drorit Wertheim (37%).

(2) A registered partnership owned (1%) by Mr. David Wertheim and Ms. Drorit Wertheim (at a ratio of 63% and 37%, respectively) and by MWZ (99%).

(3) A private company wholly-owned and controlled by Ofer Development and Investments Ltd., a private company, the shares of which are held by Ofer Holdings Properties Ltd. (89.1%) and by Nazareth Industrial Properties (10.9%). Nazareth Industrial Properties Ltd. is a private company wholly-owned and controlled by Ofer Development and Investments Ltd. Ofer Holdings Properties Ltd. is a private company wholly-owned and controlled by Ofer Holdings (1989) Ltd. ("Ofer Holdings"). Ofer Holdings is a private company held by the Yehuda (Yuli) Ofer RIP estate (36.67%), Liora Ofer (15%), Doron Ofer (15%) and L.I.N. (Holdings) Ltd. (33.33%) (see also footnotes 4 and 6 below).

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

(5) A private company wholly-owned and controlled by Ofer Brothers Holdings Properties Ltd., a private company wholly-owned and controlled by Ofer Holdings (see also footnote 3 above).

(6) A private company, the shares of which are held by Leora Ofer (51.67%), Doron Ofer (15%) and L.I.N. (33.33%) (see also footnote 4 above).
Prior to the death of Mr. Yuli Ofer RIP, he together with his children, Liora Ofer and Doron Ofer, were the controlling shareholders of Ofer Investments and Ofer Holdings. Upon the death of Mr. Yuli Ofer RIP on September 11, 2011, his shares of Ofer Investments and Ofer Holdings became part of his estate.
On December 18, 2013, the Family Affairs Court issued an order to execute the will of Mr. Yuli Ofer RIP. On January 30, 2014, an appeal of the aforementioned verdict was filed with the Tel Aviv-Yafo District Court as an Appellate Court for Civil Appeals. On November 16, 2015, the District Court unanimously rejected the aforementioned appeal and the order to execute the will became conclusive.
As the Bank was informed by Ofer Investments, further to the notice from Administrators of the Estate of Mr. Juli Ofer RIP (hereinafter: "the Estate Administrators") to Ofer Investments and following resolutions by the Family Court with regard to distribution of assets in the estate of Mr. Juli Ofer RIP, on September 28, 2016 the shareholder registry of Ofer Investments was revised, so that Ms. Liora Ofer was registered as holder of Ofer Investments shares held by Mr. Juli Ofer RIP (accounting for 36.67% of the share capital of Ofer Investments). Therefore, the holdings in Ofer Investments as of this date are as follows: Liora Ofer: 51.67%; Doron Ofer: 15%; L.I.N. (Holdings) Ltd.: 33.33%.
They further noted that, as informed by the Estate Administrators, the Estate Administrators would continue, at this time, to hold the shares held by Mr. Juli Ofer RIP in Ofer Holdings (which constitute 36.67% of Ofer Holdings' share capital). Upon receiving confirmation from the Bank of Israel, the shareholder registry of Ofer Holdings would be revised, so that Ms. Liora Ofer would be registered as holder of Ofer Holdings shares held by Mr. Juli Ofer RIP.

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

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

Shareholder agreements

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

Ofer Group

On January 17, 2013 the Bank received notice from Ofer Investments Ltd. (hereinafter: "Ofer Investments") with regard to a permit dated January 15, 2013 given by the Governor of the Bank of Israel, for holding control and means of control over the Bank by Ofer Group (as defined in the control permit - i.e. Eyal Ofer, Doron Ofer, Liora Ofer and the estate of Juli Ofer RIP managed by temporary estate administrators, Attorneys Zvi Ephrat and Reuven Bachar) and by Wertheim Group (i.e. Mr. Moshe Wertheim), pursuant to the Banking Act (Licensing), 1981 (hereinafter: "the new permit"). On this matter, see report issued by the Bank on January 17, 2013 (reference 2013-01-016320). This mention constitutes inclusion by way of reference of all information provided in the aforementioned report.

Through the receipt date of the new permit, Ofer Group held Bank shares (controlling interest shares and non-controlling interest shares) through Ofer Investments and its subsidiaries, and through L.I.N. (Holdings) Ltd. (hereinafter: "L.I.N") and its subsidiary. Upon receiving the new permit, the outline of change in the Bank holding structure came into effect, referring only to holding of Bank shares by Ofer Investments, to separation of holding of controlling interest shares of the Bank from other operations of Ofer Investments, including holding of real estate properties (hereinafter: "new structure change"). The new structure change includes transfer of controlling interest shares of the Bank (indirectly held by Ofer Investments) to be indirectly held by a sister company of Ofer Investments, Ofer Holdings (1989) Ltd. (hereinafter: "Ofer Holdings"). Resulting from the new structure change, Ofer Investments would continue to hold ordinary Bank shares (not part of the controlling interest), directly and through a subsidiary. For more information see footnote 6 to the above table showing control of the Bank Group.

New co-operation agreement between individuals of Ofer Group and corporations under their control -

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

The notice from Ofer Investments to the Bank further indicated that Ofer Investments and Ofer Sahaf Ltd. (who would continue to hold non-controlling interest Bank shares) have committed, in the new co-operation agreement, to act pursuant to provisions of the control permit, as these may be from time to time, if applicable to them, including to only exercise voting rights with respect to Bank shares they hold in accordance with the decision made with regard to exercise of voting rights with respect to controlling interest Bank shares. Moreover, these companies committed that, should their shares be offered in future to the public, their aforementioned commitment would be reflected in the prospectus to be made public. For more information see footnote 6 to the above table showing control of the Bank Group.

Wertheim Group

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

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

On January 18, 2015, the Bank received notice from Mr. Wertheim, whereby a letter, received on January 15, 2015 from the Supervisor of Banks at the Bank of Israel, indicates that for legal and procedural reasons, the Supervisor of Banks is unable to recommend that the Governor of the Bank of Israel grant the requested permit. However, since receiving said letter, negotiations are ongoing with Bank of Israel to arrange this matter.

On August 31, 2016, Mr. Moshe (Mosie) Wertheim passed away.

On December 27, 2016, the Governor of the Bank of Israel, Dr. Karnit Flug, informed Mr. David Wertheim and Ms. Drorit Wertheim that the control permit at the Bank awarded to Mr. Moshe Wertheim RIP is no longer valid and that provisions of said control permit shall apply to Mr. David Wertheim and Ms. Drorit Wertheim as from the date of the Governor's notice, as if they had held the means of control over the Bank pursuant to a valid control and holding permit. According to the Governor's notice, Mr. David Wertheim and Ms. Drorit Wertheim would be regarded, *mutatis mutandis*, as replacing Mr. Moshe Wertheim RIP with regard to the voting agreement. For more information about the Governor's notice received by the Bank, see the report issued by the Bank on December 28, 2016 (reference no. 2016-01-092391).

The shareholders agreement signed by Mr. David Wertheim and Ms. Drorit Wertheim and companies controlled there by which hold Bank shares and are part of the controlling block at the Bank, MWZ and F&W, on June 26, 2015, governs the relations of Mr. David Wertheim and Ms. Drorit Wertheim in the holding companies and, indirectly, their exercise of their means of control over the Bank. The shareholders agreement stipulates various arrangements and principles. As for the control agreement with Ofer Group, the shareholders agreement stipulates that the representative of Wertheim Group at the Bank would be appointed by the MWZ Board of Directors, by simple majority. The parties also agreed how they would decide on their nominees for office of Bank Board member (other than external Board members); in conformity with the current holdings of the parties in the holding companies, David Wertheim may nominate most of the Wertheim Group nominees for office of Bank Board member and Drorit Wertheim may nominate the remaining ones. For more information, see report by the Bank dated January 5, 2017, reference: 2017-01-002452).

Fixed assets and installations

The amortized cost of buildings and real estate for the Bank Group (including installations and leasehold improvements), net of provision for impairment, as of December 31, 2016 amounts to NIS 872 million, compared to NIS 915 million at the end of 2015.

In 2017, no unusual investments are expected in fixed assets and in plant (buildings, land, equipment, furniture and automobiles).

For more information about fixed assets for the Group, see Note 16 "Buildings and equipment" on the financial statements.

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

For more information about investments and expenses with respect to IT, see chapter "Analysis of composition of assets, liabilities, capital and capital adequacy" in the Report of the Board of Directors and Management.

For more information about replacement of the core banking system at Bank Yahav, see chapter "Significant developments in IT" of the Report of the Board of Directors and Management.

Intangible assets

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

The Bank has acted extensively to develop its technological capabilities, in response to evolution of its business and in order to achieve the strategic plan.

The balance of discounted software development cost is included on the financial statements under "Buildings and equipment".

For more information about treatment of software development costs on the financial statements, including their useful life, see Note 1.D. 8. to the financial statements.

For more information about investments and expenses with respect to IT, see chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management.

For more information about replacement of the core banking system at Bank Yahav, see chapter "Significant developments in IT" of the Report of the Board of Directors and Management.

Human Resources

Bank organizational structure

The Bank organizational structure is intended to support achievement of Bank objectives and realization of its business plan. The organizational structure is based on divisions and other departments, reporting to the Bank President & CEO (except for the Internal Audit Division, which reports to the Chairman of the Board of Directors), as follows:

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

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

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

Information Technology Division – in charge of information technology, including pursuant to requirements of Proper Banking Conduct Directive 357, through the Mizrahi-Tefahot Technology Division Ltd., a wholly-owned subsidiary of the Bank.

Planning, Operations and Customer Asset Division – The division includes the Process Engineering Division, responsible, *inter alia*, for back-office banking operations and the Planning & Economics Division, which is also responsible for supervision and control of subsidiaries. The division is also responsible for Bank insurance business (including: banking insurance as well as officer and director insurance), insurance incidental to mortgages and the clearinghouse. The division also includes the departments which provide pension consulting and financial consulting services offered to clients. The division is also responsible for subsidiaries operating in the capital market, including: Etgar Investment Portfolio Management Company of the Mizrahi Tefahot Group Ltd., Mizrahi-Tefahot Trust Company Ltd. and the provident fund sector.

Risk Control Division – this division includes the various risk control departments at the Bank (including: market, interest, liquidity, credit and derivatives risk), which also manages the operational risk at the Bank. This division is in charge of information security issues. The Division includes the Bank's Chief Compliance Officer as well as the Analysis Department, tasked with formulating independent recommendations with regard to extending credit as well as opinions with regard to associated risk.

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

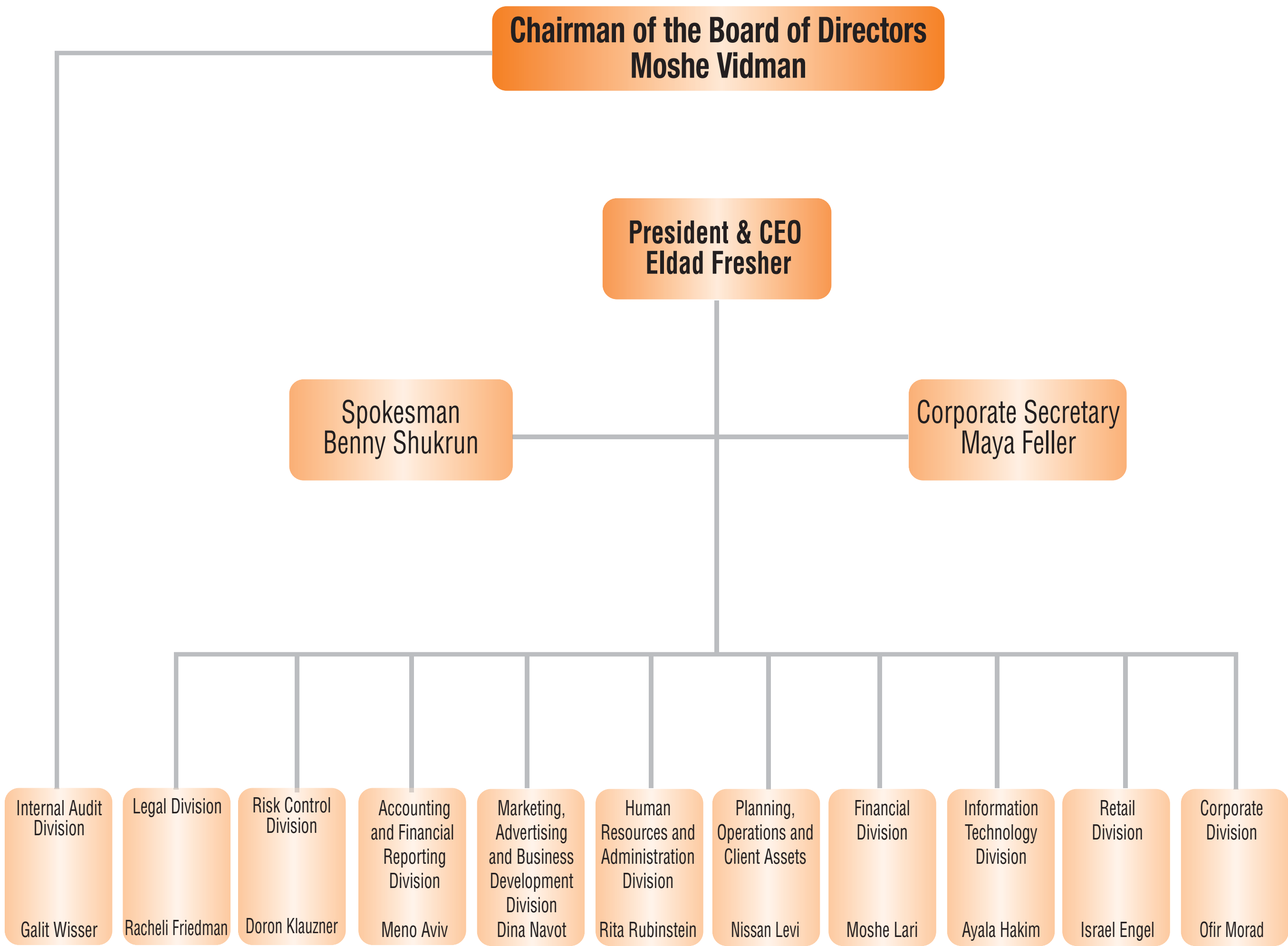
Marketing, Advertising and Business Development Division – This division consolidates activities relating to advertising, marketing, and development of financial products that the Bank markets to customers.

Accounting & Financial Reporting Division – in charge of preparing the Bank's public financial statements, reporting to statutory authorities and to management, taxation, main ledger, accounting, treasury and payroll department. The Division is also responsible for credit classification and for determining the provision for credit losses.

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

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

Organizational Chart of the Bank



Human Resource Division Policy

Bank management regards all Bank employees and managers as a key component for achieving its business strategy and business growth targets. This commitment is reflected by implementation of three key principles in Bank operations:

- Creating a respectful work environment - The Bank regards its employees and managers as partners in the Bank's success and therefore strives to promote them and to create a supportive work environment.
- Caring for employee rights - The Bank ensures the rights of all employees, as well as their right to join a labor union. The Bank offers its employees better working conditions than required by labor laws.
- Caring for employee welfare – Employee welfare is managed as follows: Creating welfare support for Bank employees and their families, an extensive healthcare plan for employees, an organizational culture which supports recognition and allows for optional leisure activities - based on the understanding that such balance generates value for both the employee and the Bank.

The Bank regularly promotes equal opportunity in the work place. This is based on recognizing the ultimate importance of the value of equality. The Bank does not discriminate against any employee by religion, ethnicity, race, gender nor any other attributes.

Significant developments

- For more information about the streamlining plan, see chapter "Significant Events in the Bank Group's Business" of the Report of the Board of Directors and Management and Notes 22 and 25 to the financial statements.
- As part of the Bank's strategy of expansion in certain demographic segments, focused on the Arab segment and on the Jewish Orthodox segment, the Bank has acted to recruit employees from these demographics.
- As part of our commitment to equal opportunity and in preparation for implementing the Employment of Persons with Disabilities Act, a policy on this matter was approved and is being implemented by the Bank.
- As part of the Bank's concern for employee health, eligibility for medical check-ups and funding for such check-ups has been extended to all employees aged 40 or over.

Staff – general information

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

						2016
	At the Bank	Overseas branches	Total for the Bank	Subsidiaries in Israel	Overseas subsidiaries	Total for the Group
Number of full-time equivalent positions as of December 31, 2015	5,072	64	5,136	982	23	6,141
Number of full-time employees based on monthly average	5,078	64	5,142	938	23	6,103

						2015
	At the Bank	Overseas branches	Total for the Bank	Subsidiaries in Israel	Overseas subsidiaries	Total for the Group
Number of full-time equivalent positions as of December 31, 2015	5,040	61	5,101	923	23	6,047
Number of full-time employees based on monthly average	4,982	60	5,042	895	24	5,961

Below is the distribution of number of positions in the Group by operating segment(1)(2):

		As of December 31
Operating segment	2016	2015
Households	3,718	3,675
Private banking	129	130
Small business	1,156	1,108
Commercial banking	254	263
Business banking	551	526
Financial management	333	345
Total	6,141	6,047

(1) Composition is by operating segments based on management approach. See Note 29 to the financial statements for details.
(2) Including Head Office employees that are allocated pro-rata to the various segments.

Human resource management

Bank management regards all Bank employees and managers as a key component for achieving its business strategy and growth objectives for operations and profitability. Human resources at the Bank are managed on two levels:

- Caring for the individual includes: recruitment, on-boarding and during the employee's service life time, through retirement.
- Human resources are developed during regular work, through individual and group training and development processes.

The Bank invests in development of its human resources, by training for skills related to banking, regulatory affairs, new behavioral and managerial skills, as well as by preservation of existing knowledge and skills. This is done through training activities throughout the employee's time with the organization, from starting in their new role, through promotion tracks, completing and expanding academic education and enrichment through external seminars.

In 2016, the Training Center continued to deploy the "Learning organization" concept – whereby managers and employees regard learning as an on-going task carried out at their workstation as well. Unit managers lead organizational change and are responsible for their employees' professional skills through personal mentoring. The Bank applies diverse learning methods: in-person training at the Training Center, individual / training at departments, in-person learning at departments (during team meetings), eLearning, professional and managerial mentoring, videos, games etc.

The Bank's Organizational Development and Training Division applies diverse tools to develop intra-organizational communication channels in general and conducting evaluation and feedback processes, with each employee given personal feedback for their performance over the past year.

Training expenses in 2016 amounted to NIS 14 million, compared to NIS 10 million in the previous year.

In 2016, all Bank employees attended training (in-person and online), for a total of 35,275 training days, compared to 31,191 training days in 2015.

For more information about human resource management, see also the 2015 Corporate Governance Report on the Bank website.

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

Collective labor relations

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

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

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

C. **Bank Mizrahi Tefahot Ltd. Technology Division Employee Committee** – the organization authorized to sign, together with the MAOF trade union, on behalf of Bank Mizrahi Tefahot Ltd. Technology Division employees (a subsidiary wholly owned and controlled by the Bank), any collective bargaining agreements applicable to company employees (except for Technology Division employees employed under individual employment contracts).

D. **Bank Yahav employee representatives** - empowered to sign on behalf of Bank Yahav employees any collective bargaining agreements applicable to Bank Yahav employees.

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

Overview

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

Salary agreements

For more information about salary agreements, see chapter "Significant developments in human resources and administration" of the Report of the Board of Directors and Management .

Salary update method

Salaries of most Bank employees (except for a small number of employees employed under individual contracts signed by them and by the Bank - see chapter Individual Employment Contracts below) are updated based on three key components:

- Components which are updated regularly at rates and in the manner prescribed from time to time, in negotiations of labor agreements The major component is the basic salary. In addition, other increments derived from the basic salary are updated, primarily the seniority increment, which is updated at the start of each year by an increasing percentage, as employee seniority increases. The seniority increment reaches 4% per year (of the basic salary), for an employee with over 26 years' service with the Bank.
- Components updated in accordance with changes in the Consumer Price Index.
- Components linked to changes in external tariffs.

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

Special payments

In addition to the regular salary elements, the Bank pays to its employees, as stipulated in the labor constitution, a one-time grant upon reaching seniority of thirteen years and eighteen years. The Bank's financial statements include a provision for these obligations, according to an actuarial calculation that is based on past experience and the probability that on the date of record, the employee will still be employed by the Bank.

The Bank also provides individual compensation tools, through which the personal compensation of each and every employee is carried out. These compensation tools are selective and are based on specific assessments of the direct managers of the Bank's employees in the different segments regarding the performance of every employee. Personal promotion is achieved primarily via promotion in rank and in the bonus component, about which Bank management decides each year and these decisions are approved by the Board of Directors. Decisions relating to the extent of personal promotion and bonus or grant are not derived from provisions of labor agreements, but are influenced by the assessment of the employee performance, the Bank's situation and profitability in the relevant period.

Special collective bargaining agreement

On April 11, 2006, the employee union and the Bank signed a special collective bargaining agreement, effective through December 31, 2010. On September 16, 2009, this collective bargaining agreement was extended through December 31, 2015.

Highlights of this agreement include extension of the "employment constitution", avoidance of labor unrest and voluntary retirement program.

The Bank and the employee union are in negotiations to renew the payroll agreement for 2016-2020.

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

Overview – Wage Agreements

On June 16, 2014, a wage agreement was concluded with the Manager Council for the period 2013-2017. The agreement primarily includes a gradual increase in management fee by 2% per annum for 2014-2017, linkage of vacation pay rates to the CPI, inclusion of vacation pay as part of the basis for contribution to study fund, extension of the agreements on other matters and ensuring labor unrest is avoided through December 31, 2017.

Individual employment contracts

The labor agreements signed in the Bank in the years 1995, 1998, 2003 and 2006, stipulated that the Bank will be permitted to enter into individual employment contracts with senior employees, as defined in the agreements, as well as several individual employment contracts with certain officers. Some of the senior employees employed under individual employment contracts are eligible, in the event of termination by the Bank, to severance bonuses based on their period of service with the Bank, in addition to other amounts and benefits accrued to their credit in various funds. The financial statements include a provision for the severance bonuses accrued through the balance sheet date. See Note 22 to the financial statements for additional information.

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

Employment terms of employees of Mizrahi Tefahot Technology Division Ltd. (hereinafter: "the Technology Division" or "the Company") are arranged in the labor constitution that was signed in 1989 and in a series of agreements signed by the Technology Division Employee Council, the Labor Union and the Technology Division over the years.

Employees of the Technology Division have their pay linked to the pay for Bank employees.

Significant Agreements

A. Employment agreements signed with the Employee Council, the Manager and Authorized Signatory Association and the Technology Division Employee Committee. For more information see chapter "Human Resources" above.
B. Indemnification letters. For more information see Note 26.C. 4-9) to the financial statements.
C. Agreement with Israel Credit Cards Ltd. (hereinafter: "CAL") and with Diners Club Israel Ltd., a company controlled by CAL, for joint issue of Visa, MasterCard and Diners Club debit cards, including Bank-branded cards, to be distributed by the Bank to its clients. For more information see Note 26.C.13 to the financial statements.
D. Bank Yahav contracting with an international company for creating a core banking system and receiving outsourced services for such system. For more information see chapter "Significant developments in IT" in the Report by the Board of Directors and Management.
E. Directed loans to Ministry of Construction and Housing eligible borrowers. For more information see chapter "Household segment" in the Report of the Board of Directors and Management.
F. Small business tender. For more information see chapter "Small businesses segment" in the Report of the Board of Directors and Management.
G. Tender for management of deposit funds for overseas workers. For more information see chapter "Household segment" in the Report of the Board of Directors and Management.
H. Sale of assets and liabilities in mortgage portfolio – For more information see chapter "Significant Events in the Bank Group's Business" in the Report of the Board of Directors and Management.

Legislation and Supervisory Regulation of Bank Group Operations

Laws and regulations

Remuneration of officers in financial corporations act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016

On April 12, 2016, the Remuneration of officers in financial corporations act (Special permission and non-allowance of expenses for tax purposes with respect to excessive remuneration), 2016 was made public. The Act, whose provisions with regard to contracts approved prior to its publication date would apply as from six months after said publication date, contracting with a senior officer or employee of a financial corporation with regard to their terms of office or employment, which include remuneration for which the forecasted expenses, as calculated as of the approval date, in conformity with GAAP, would exceed NIS 2.5 million per year, is subject to special approval proceedings (including approval by the General Meeting of Bank shareholders by a special majority). The Act also stipulates that a pre-condition for approval of contracting with such employee is that the ratio of the aforementioned anticipated expense to the expense for the lowest remuneration of a full-time position paid by the financial corporation, directly or indirectly, to any employee of the corporation, must be less than 35.

The Act further stipulated an amendment to the Income Tax Ordinance, whereby the cost of payroll for any officer or employee of the financial corporation, in excess of the adjusted cap of NIS 2.5 million per year, would not be deductible from the taxable income of the financial corporation, so that the adjusted cap threshold, as noted above, would be decreased by the amount of any expenses in excess of this cap. The Act further stipulates that for calculation of the cost of payroll, as noted above, any expense with respect to retirement bonus would be deemed to have been expended in equal annual installments over the years in service for which such expense is payable.

The Act stipulates mandatory reporting by financial corporations to the Taxes Authority, for any officer or employee whose cost of payroll exceeds NIS 2.5 million.

Given the uncertainty with regard to interpretation of the law with respect to past employee rights and in order to allow Bank officers additional time to review the legal status, the Bank's Board of Directors resolved on June 20, 2016, after approval by the Remuneration Committee and recommendation by the Audit Committee with regard to the Chief Internal Auditor, to waive part of the notice period to which the Bank is entitled from the President and other officers reporting there to, including the Chief Internal

Auditor, with regard to termination of their employment by the Bank, so that the notice period would be of 45 days instead of 3 months (and for one officer - instead of 6 months) according to their employment contracts - provided that such notice be given to the Bank by end of 2016. It was further stipulated that as from January 1, 2017, the notice period would once again be of 3 or 6 months, as the case may be.

On September 21, 2016, the Bank's Board of Directors, following a resolution by the Remuneration Committee, resolved that as a consequence of implementation of the statutory provisions, the Chairman of the Board of Directors and the Bank President & CEO would not be eligible for remuneration for which the expected cost would exceed the maximum specified in section 2(a) of the Act - NIS 2.5 million. This applies for an interim period, from October 12, 2016 (the effective start date of the Remuneration Act, with regard to such contracts) or from a later date to be specified for this matter in conformity with the Supreme Court ruling (if any), whichever is later, through the date of approval of terms of office and employment for the Bank President and for the Chairman of the Board of Directors by the qualified organs of the Bank which terms are in compliance with provisions of the Remuneration Act. For the period ended October 11, 2016, the terms of employment of the Chairman of the Bank Board of Directors and of the Bank President & CEO remain in effect as prior to the effective start date of the Remuneration Act.

The Banking Association and the Insurance Companies Association filed an appeal with the Supreme Court with regard to validity of the aforementioned statutory provisions, against the Knesset, the Minister of Finance and others. On July 27, 2016, the Supreme Court issued a temporary injunction against the defendants, instructing them to provide justification with regard to provisions of the Act by August 29, 2016. The Court also left in place an interim order issued on July 11, 2016, whereby employees of banking corporations who would resign within 45 days from a decision on this appeal or rescinding of the interim order, would not forfeit their rights with regard to termination of employment.

On September 29, 2016, a verdict was issued on appeal, which stipulated, *inter alia*, that the required remedies with regard to provisions of sections 2(b), 4(1) and 6(a) of the Act being constitutional have been rejected and further stipulates that the ratio cap would only apply to expected remuneration expenses with respect to future work. The interim injunction issued on July 11, 2016 was extended through January 1, 2017.

Terms of office and employment of the Bank Chairman of the Board of Directors and the Bank President & CEO, which have been adapted to limitations set forth in the Remuneration Act (i.e. the ratio of their anticipated remuneration expense, as defined in the Act, to the expense for the lowest remuneration of a full-time position paid by the Bank, directly or indirectly, must be less than 35), have been approved by the General Meeting of shareholders on February 14, 2017.

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

The Income Tax Ordinance Amendment Law (Amendment no. 227), 2016 and Income Tax Regulations (Implementation of the FATCA Agreement), 2016

On July 14, 2016, the Income Tax Ordinance Amendment Law(Amendment no. 227), 2016 ("the Act") was made public. This Law was designed to enable Israel to implement the FATCA agreement and other "implementation agreements", as defined in the Law (agreements for implementation of information exchange pursuant to an international agreement, based on the procedure for automated information exchange for financial accounts, issued by the OECD). Highlights of the Law are as follows:

The Law stipulates that financial institutions should demand information from account holders, or from prospective account holders, including entities and controlling shareholders and carry out checks to verify their identity and tax residency, or their citizenship for the purpose of implementation of the FATCA agreement or any other implementation agreement, in conformity with directives to be stipulated by the Minister of Finance.

According to the Law, a financial institution should deliver to the Taxes Authority Manager ("the Manager") information about clients and accounts which the Manager should deliver to a tax authority in a foreign country, as stipulated in regulations by the Minister of Finance.

The Law authorizes the Minister of Finance to specify directives with regard to notice to be given by an Israeli financial institution to clients where information about such clients and accounts held thereby is expected to be delivered to the Manager for delivery to a foreign tax authority. The Law also authorizes the Minister of Finance to specify conditions upon which the financial institution would close accounts opened after June 30, 2014, for which the financial institution was unable to obtain certifications or documents.

The Law stipulates that the Manager may impose monetary sanctions on any financial institution or person who have failed to conduct authentication as required by the Act or have failed to deliver information, or have delivered partial information, to the Manager about accounts managed with the financial institution.

The Income Tax Ordinance Amendment Law (Amendment no. 227), 2016 also includes amendments to the Prohibition of Money Laundering Act.

The Law is effective as from the date of publication of relevant regulations Income Tax Regulations (Implementation of the FATCA Agreement), 2016 were issued on August 4, 2016. The regulations refer, *inter alia*, to issues addressed by the Law: Due diligence to be conducted by the financial institution, account classification and reporting by the financial institution to the Manager, as well as specification of transition provisions with regard to recognizing an entity as a public institution by a reporting Israeli financial institution for the purpose of implementation of these regulations. The Hebrew version of the FATCA Agreement was enclosed as Addendum I to the regulations.

On September 12, 2016, the Supreme Court resolution in case no. 8886/15, Overseas Republicans in Israel *et al v.* Government of Israel, stipulated that no information would be provided to US authorities with regard to anyone whose account has been classified as "Reportable" and fewer than 30 days have elapsed since notifying them of this fact, or if such notification has been given and reservations have been made about the notification, for as long as a response to the reservations is still pending.

The Bank applies provisions of the Act, regulations and Court rulings in conformity with the schedules stipulated in the FATCA agreement, in the Supervisor of Bank's directives and in the Act.

Prohibition of Money Laundering Act (Amendment no. 14) – addition of tax violations as original violations

The Amendment was published on April 7, 2016 and became effective on October 7, 2016. As part of the fight against tax evasion, Israel has joined other countries in defining in statute severe tax violations as "original violations" with regard to the Prohibition of Money Laundering Act ("the Act"). This list includes violations of the Income Tax Ordinance, VAT Law and Land Taxation Law (Capital Gain and Purchase Taxation) which were made under aggravated circumstances (over a certain threshold, or with sophistication, or with relation to criminal or terror organizations, or made by a person other than the taxable person. These conditions should not affect the Bank's preparations).

After this Amendment, any action involving property or monies related to or arising from the aforementioned tax violations constitutes an action involving prohibited property and money laundering.

The Amendment has created a legal infrastructure for indictment and conviction of tax evaders and those who knowingly assist them (such as attorneys, bookkeepers and bankers) in money laundering violations - as well as authority to exercise enforcement pursuant to the Act and regulatory supervisory provisions and imposing of monetary sanctions - also for activity related to tax violations. The Bank is preparing to take action with all its clients, in order to ensure that funds deposited with or transferred through the Bank are reported to the tax authorities.

The Dodd-Frank Wall Street Reform and Consumer Protection Act and the European Market Infrastructure Regulation (EMIR).

In 2012, rules were published governing application of the Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted in the USA in 2010 (hereinafter: "the reform").

The reform is designed, *inter alia*, to mitigate credit risk in trading on the OTC derivatives market, systemic risk arising there and increase transparency of this market.

The reform stipulates, inter alia, that transactions are to be settled by a central clearing house to consist of large, major banks which would guarantee each party's compliance with their obligations, binding procedures concerning collateral are to be specified, and all swap transactions made are to be reported to central information repositories, which would store this information and make it accessible to all market players.

The reform classified financial entities by scope of trading and imposes obligations based on this classification (swap dealer, MSP - Major Swap Participants etc.)

The rules specified in the reform apply to US entities and to non-US entities which conduct transactions of significant volume (as defined in the reform) with US entities. In view of the reform, such entities would not be able to conduct transactions involving the types of derivatives included in the Act with other financial entities (even those not subject to the Act, such as the Bank) - unless they comply with provisions of the Act.

Provisions of the Act gradually became effective, and today many transactions in OTC derivatives with US banks and with banks which are Swap Dealers or MSPs, require compliance with provisions of the Act, including with regard to settlement.

The Bank is preparing to apply the relevant provisions of the reform so as to be able to conduct transactions involving OTC derivatives with entities subject to the Act.

Concurrently with the Dodd Frank reform launched in the USA, a similar reform was launched in Europe - European Market Infrastructure Regulation ("EMIR")

The EMIR reform, similar to the Dodd Frank reform, calls for mandatory central settlement, increased collateral requirements and reporting of executed transactions to designated data repositories.

The EMIR reform applies to all financial entities in the EU and therefore should impact Bank operations involving derivatives - since the Bank has significant business with European banks. Some provisions of this reform are in effect (such as: the mandatory reporting provisions) and the central settlement provisions which became effective gradually for entities such as the Bank, as from December 21, 2016 with mandatory settlement of transactions dated from May 31, 2016 through the settlement date (December 21, 2016) – the Front loading directive. The Bank is applying the reform provisions applicable to the Bank in conformity with the schedule stipulated in legislation and is preparing for settlement of transactions where the other party to the transaction is subject to regulation. The Bank has contracted settlement agreements with clearinghouse members, which would allow the Bank to settle transactions which require settlement in a central clearinghouse.

Along with rules applicable to transactions subject to central settlement, the regulations also stipulate new, binding rules with regard to margins (Variation Margin and Initial Margins) for transactions which would not be settled. In this area, too, there are parallels in the USA and in Europe, which should result in rules of conduct for the derivatives market (both for transactions to be settled and for transactions which would not be settled) being uniform and supervised by the relevant regulators. Provisions with regard to Variation Margin should become effective for regulated entities such as the Bank as from March 1, 2017. The Bank is preparing in conformity with the schedules stipulated by regulations.

The Volcker Rule

US legislation, applicable to relevant financial corporations, such as the Bank, which includes certain restrictions on "proprietary trading" of "financial instruments" and investments in "covered funds", as these terms are defined in legislation. This legislation is part of the Dodd Frank reform, designed to maintain stability of the US financial system and to preclude speculative transactions, such as those which contributed to the financial crisis of 2008.

The Bank has reviewed the legislation and the applicable activity, is acting to apply the legislation and revise Bank policy accordingly.

Credit Data Act, 2016

On April 12, 2016, the Act was made public, to become effective on October 12, 2018 if not delayed (to April 12, 2020 at the latest).

The aforementioned act reforms the market for credit data service. When this act would become effective, the Credit Data Service Act, 2002 would be rescinded.

This act is relevant for the Bank, both due to the Bank being an "information source", required to provide credit data for Bank clients to a central information repository to be created for this purpose at the Bank of Israel and due to the Bank being a "credit data user", authorized to receive credit data from the credit bureaus.

Key provisions of the act include:

A client may ask the Bank of Israel to exclude their credit data from the repository. A client may not file such a request if credit data has been provided by an information source to the repository, which clearly indicate that the client has failed to make payments they have committed to.

Credit data for a client would only be provided to a credit provider (such as the Bank) if:

- The credit provider needs the credit data for contracting a credit transaction with that client or to ensure fulfillment of conditions of such transaction;
- The client has explicitly consented for credit data about them, included in the repository, to be provided to the credit bureau for the purpose of compiling a credit report to be provided to the credit provider.

A credit provider may ask the credit bureau to provide an indication as to whether credit should be extended to the client for contracting a credit transaction with this client - provided that they have informed the client of this fact in advance.

As part of the Bank's preparations for implementation of this act, the Bank is currently gathering information to be provided to the Bank of Israel repository.

Electronic Settlement of Checks Act, 2016 (Legislation Register 2528)

The Act was published on February 10, 2016 and was to have become effective on August 10, 2016. Since banks require time for preparations to apply the Act, two major stages for implementation have been specified: The first stage, starting on November 8, 2016, allows inter-bank settlement of checks deposited using a cell phone. The second stage, which refers to settlement of all checks denominated in NIS, is to be put in place in the third quarter of 2017.

The Act is designed to transition from physical settlement of checks to electronic settlement. The objective of electronic settlement is to streamline the check settlement process, reduce cost of check transportation and eliminate the need for retaining the checks in physical storage for seven years. Note that electronic settlement only applies to checks deposited for collection with the collecting bank or transferred for collection at the collecting bank in a computer file, rather than in physical format. For computer-based checks (including on cellular devices) transferred for collection, these are only checks made (in writing or in printed letters) to the payee only and which may not be endorsed to another.

Since checks are settled electronically and the drawee bank does not physically "see" the check, the collecting bank is responsible for careful verification of the checks, ensuring that no prohibited changes were made to them, including verification of endorsements, their correctness and validity.

Computer output of the scan would constitute admissible evidence to proof the veracity of its content in any legal proceeding. The Governor of the Bank of Israel will specify rules and provisions with regard to computer scanning of checks, producing the computer check output and rules for mandatory retention of computer checks.

The Governor, with consent of the Minister of Public Security, will determine the duration for retention of the actual checks by the bank.

The bank is liable to their client for any damage which may be incurred due to failure to retain the actual check.

Banking Decree (Customer Service) (Supervision of Standard Reporting Service Requested by the Client), 2016

The Decree was made public on July 19, 2016 and became effective on August 1, 2016. According to the Decree, a "Standard Reporting Service Requested by the Client" (section 2(a)(4)(a) of the price list for individuals / small businesses) is considered a supervisable service and the commission may not exceed NIS 15 (compared to NIS 36 at the Bank, prior to the Decree becoming effective). Application of this decree has no material impact on the Bank's financial statements.

Banking Rules (Customer Service) (Commissions) (Amendment), 2016

The amendment to the rules was made public on July 19, 2016 and became effective on August 2, 2016. According to the amendment, the Bank should assign, by its own initiative, any client who is a senior citizen or a person with disabilities, to the basic commission track if charged for basic transactions (transactions by teller and transactions by direct channel) an amount higher than the basic commission track cost in any month during the fiscal year.

No commission may be charged to any client for six months after they have closed their account, other than for delivery of one copy of notice sent by media to the client pursuant to the law during the six months prior to the account closing. Application of this amendment has no material impact on the Bank's financial statements.

Increased Competition and Reduced Concentration in Israeli Banking Act (Legislation Amendments), 2017

The Act was approved on January 27, 2017 and would become effective gradually. The Act aims to increase competition in the financial system through various means: The Bank may be required, as from July 31, 2018, to sell to other financial institutions computer services primarily used by the Bank. Moreover, for two years starting on the 4th anniversary of the effective start date of the Act, the Bank may be prohibited from operating the issue of credit cards. As from March 31, 2017, no bank shall unreasonably deny a borrower's request for consent to an additional, inferior lien on any asset in favor of another creditor. The second lien may only be exercised with the bank's consent, which may not be unreasonably denied. As from July 31, 2018, a client may ask the bank for information about the balance in their checking account be given to a financial institution for extending credit, daily or less frequently. As from January 31, 2019, before the bank would contract a credit card agreement with a client, the bank must provide to the customer information about all issuers who have a distribution agreement with the bank with regard to their credit cards.

The bank would allow the client, or anyone duly registered in a registry as cost comparison service provider, and authorized by the client, to view online financial information about the client, using a special password, which would allow viewing only, as from the effective start date of regulations governing the information transfer, but no later than six months after the effective start date of the Act.

Evaluation of effect of the Act on the Bank:

- Credit cards
  - Separation of control and ownership by large banks (banks with total balance sheet assets, on consolidated basis, exceeding 20% of total balance sheet assets for the Israeli banking system) from credit card companies may result in higher supply of consumer credit. However, demand for consumer credit may grow concurrently, hence the effect on the cost of borrowing is unclear at this stage.
  - Re-structuring of the credit card market should increase marketing efforts of credit card companies in issuing and distribution of credit cards. Conversely, restrictions imposed on major banks with regard to these matters may contribute to Mizrahi Tefahot's business in the household segment.
- Additional lien on property – banking corporations would not be allowed to refuse a borrower's request to pledge an additional lien on a property, which is lower-ranked, in favor of another creditor. This may result in increased credit risk for such borrowers.
- Provision and operation of IT services – financial institutions may apply to banks which operate IT services to acquire such IT services. Mizrahi Tefahot Group would consider the option to leverage the infrastructure of Bank Yahav's core system in order to provide IT services to other banks and financial institutions.
- Credit card settlement – currently, the settlement market is exclusively controlled by the credit card companies. Recommendations of the committee and Bank of Israel directives should contribute to increased competition for credit card settlement, thanks to removal of barriers with regard to capital, technology and regulation. Due to these changes, which may lead to introduction of new clearing houses, the Bank would consider the option of co-operations with regard to settlement.
- Information services and activity initiation – consumer side – statutory provisions may result in reduction of information gaps and increase in consumers' ability to make choices among different financial alternatives. Empowering consumers increases the importance of added value provided to clients with regard to professional service and a personal approach. Mizrahi Tefahot Group acts to establish itself as a leader in the retail segment through, *inter alia*, reinforcing synergies with Bank Yahav to create a two-pronged strategy: service-oriented and price-oriented.

Note that at this early stage, the impact of the Act on business results cannot be estimated.

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

Change in VAT rate and corporate tax rate

On January 4, 2016, the Knesset approved by second and third readings, a proposed bill stipulating a decrease in the corporate tax rate to 25%, effective as from January 1, 2016.

On December 21, 2016, the Knesset Plenum approved by second and third readings, the proposed Economic Streamlining Act, 2016. The Act stipulates that the corporate tax rate would be reduced in 2017 by 1% and as from 2018 – by 2%, so that in 2017 it would be 24% and as from 2018 – 23%.

Proposed legislation

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

Circulars and Public Reporting Regulations

Improved usefulness of public reports by banking corporations for 2016

On February 12, 2017, the Supervisor of Banks issued a circular concerning improved usefulness of public reports by banking corporations for 2016. For more information about the Supervisor of Banks' directive on improved usefulness of public reports by banking corporations for 2016, see Note 1.C. 6) to the financial statements.

Streamlining operations of the banking system in Israel – setting a multi-annual streamlining plan subject to capital adequacy relief

On January 12, 2016, the Supervisor of Banks issued a letter with regard to streamlining operations of the banking system in Israel. According to the letter, the bank Board of Directors should set a multi-annual streamlining plan (hereinafter: "the streamlining plan").

The streamlining plan should stipulate specific action for the next five years and streamlining principles for the longer term. The plan should reflect long-term commitment to streamlining and to current, active expense management in line with the current economic and technological environment.

The streamlining plan would include well-defined interim targets, annual or more frequent, as well as means of monitoring and supervision by the Board of Directors over achievement of the plan and interim targets.

Any bank which heads a banking group would set a streamlining plan which takes into account streamlining at group level.

In order to promote the implementation of a streamlining plan, the Supervisor would allow the banking corporation capital adequacy relief, as stated below, subject to the following conditions:

- The bank has a streamlining plan associated with specific cost (cost which the banking corporation would bear to carry out the multi-year plan, such as for a multi-year voluntary retirement program or changes to lines of business);
- The bank has demonstrated, to the Supervisor's satisfaction, that such relief would be used to carry out the streamlining plan and would not be used for any other purpose; and
- The bank has achieved interim streamlining targets. Banks which fail to achieve the streamlining targets would no longer be able to benefit from such relief.

In conformity with the foregoing, banks which meet the aforementioned conditions, would be allowed a delay in achieving the capital adequacy targets specified for them by the Supervisor of Banks. The relief would be equal to the effect of expected decrease in regulatory capital, upon plan approval, with respect to the aforementioned specific cost. The delay would by for up to five years, on a straight line basis.

The accounting treatment of long-term streamlining including a voluntary retirement program

US GAAP, which have been adopted as part of the Public Reporting Regulations, specify the situations when the effect of an update to liabilities with respect to employee rights are charged to Other Comprehensive Income and those when it is charged to the Statement of Profit and Loss.

Accordingly, in many cases a bank is required to recognize the effect of an update to employee retirement and severance pay liabilities, due to specific actions included in he streamlining plan for the subsequent five years and principles for streamlining over the longer term, under "Actuarial gain and loss" charged to Other Comprehensive Income. Such gains and losses would be charged to the statement of profit and loss over the average service term of the employees.

Banks are required to maintain a liability with respect to employee rights, reflecting the estimates excess bonuses to be paid to employees under the streamlining plan for the subsequent five years and over the longer term, in future. This estimate is often based on data with regard to excess bonuses actually paid in the past, adjusted for circumstances upon the report date. Although estimated retirement over the longer term is based on actual past experience, adjusted for the streamlining principles specified for the longer term, banks are not required to assume that the excess bonuses expected over the subsequent five years necessarily represent the excess bonuses expected over the longer term.

On December 27, 2016, the Bank’s Board of Directors approved the streamlining plan recommended by Bank management, whereby early retirement would be possible for 300 employees in 2017-2021, at improved conditions.

Bank management is in negotiations with the employee union with regard to the retirement program and as a first step, has started implementation of the plan in the Technology Division Ltd., pending agreement with the employee union at the Bank.

The cost of update to the actuarial liability with respect to the streamlining plan, recorded on the financial statements as of December 31, 2016, amounts to NIS 286 million; the cost net of tax, amounting to NIS 188 million, was charged to equity (under Other Comprehensive Income).

In conformity with the Supervisor of Banks' letter dated January 12, 2016, with regard to operating streamlining of the Israeli banking system, the Supervisor of Banks allowed capital relief with respect to this plan. The Bank applies this capital relief so that supervisory capital used to calculate capital adequacy would be adjusted (increased) and the capital effect of the streamlining (a decrease by 0.14%) would be applied on a straight line basis as from 2017, over a five-year period.

See Notes 22 and 25 to the financial statements for further information.

Bank's credit rating

On January 4, 2017, Standard & Poor's Ma'alot (hereinafter: "Ma'alot") confirmed the Bank's issuer rating of ilAAA with a Stable rating outlook.

The rating of subordinated notes issued by Tefahot Issuance is one rank below the issuer rating, i.e. rated ilAA+. These subordinated notes qualify as Tier II capital under transitional provisions of Basel III.

The subordinated capital notes, which qualify as Tier II equity in conformity with transitional provisions of Basel III, are rated ilA+.

The negotiable contingent subordinated notes (CoCo), which qualify as Tier II equity in conformity with provisions of Basel III, are rated ilAA-.

On June 30, 2015, Moody's rating agency confirmed the Bank's long-term deposit rating at A2 and raised the outlook from Negative to Stable.

Operating segments

On November 3, 2014, the Supervisor of Banks issued an update to the Public Reporting Directives concerning supervisory operating segments. According to the directive, the Bank is required to provide, on its financial statements, disclosure with regard to supervisory operating segments in conformity with a uniform, comparable layout specified by the Supervisor of Banks; attribution to supervisory operating segments is typically determined by the client's turnover (annual sales or annual revenues).

The disclosure outline for supervisory operating segments includes the following segments:

Individuals, micro and small businesses, medium businesses, large businesses, institutional entities and financial management. The Bank's overseas operations should be presented separately.

Supervisory operating segments

Supervisory operating segments include operating segments for individuals and operating segments for business clients other than individuals (including institutional investors and financial management of the Bank).

Individuals are defined as persons with no indebtedness to the Bank or whose indebtedness is classified as indebtedness of "individuals - housing loans and others", in conformity with definitions of credit risk classification by economic sector.

Below is brief description of supervisory operating segments:

Households – individuals, other than private banking clients, as noted below.

Private banking – individuals who manage a financial asset portfolio in excess of NIS 3 million.

Small and micro businesses – businesses with turnover amounting up to NIS 50 million.

Medium businesses – businesses with turnover higher than NIS 50 million and lower than NIS 250 million.

Large businesses – businesses with turnover higher than NIS 250 million

Institutional investors – the segment primarily includes provident funds, pension funds, study funds, mutual funds, ETFs, insurance companies and stock exchange members who manage client portfolios, as defined by the Supervisor of Banks.

Financial management – includes trading operations, asset and liability management and non-banking investments.

Overseas operations – the aforementioned operating segments are divided into operations in Israel and operations overseas; operations overseas are presented separately and are divided into operations of individuals and business operations only.

Financial information in the Report by the Board of Directors and Management is included in conformity with definitions of supervisory operating segments.

In addition, the financial statements include - in Note 12 to the financial statements - disclosure with regard to "Operating segments in conformity with management approach".

An operating segment in conformity with management approach is a Bank component with operations which may derive revenues and incur expenses which meet the following criteria:

- Its operating results are regularly reviewed for the purpose of decision making about resource allocation and for performance evaluation.
- Separate financial information is available with regard to it.

In fact, the supervisory operating segments and "Operating segments in conformity with management approach" are correlated. However, there are some differences in client attribution to segments and in how decisions are made. Therefore, at this stage, the financial statements also include reporting of operating results in conformity with "management approach", as noted above.

A summary of these differences are as follows:

- The Bank's operating segments by "management approach" are based on client attribution to the organizational structure responsible in the past period. However, client attribution to supervisory operating segments is based on uniform definitions specified by the Supervisor of Banks, as noted above.
- There is a strong correlation between attributes specified by management for client attribution to the responsible division and the supervisory definitions.

- However, according to "management approach", in some cases the final client attribution may be based on other parameters, such as: specialization of a certain unit in activity types of clients or past experience working with the client, which result in business and service-related advantages to client attribution to the specific division or being part of the same borrower group.
- Other differences are reflected in the Bank's definition of Private Banking, how institutional investors are handled, business operations attributed to the Financial Management Division and other differences arising from the aforementioned definitions.
- The difference in definitions is reflected in particular in these segments:
  - Individual clients with a financial asset portfolio at the Bank of less than NIS 3 million, classified to the private banking segment in the disclosure about operating segments in conformity with management approach, were classified to the household segment in the disclosure about supervisory operating segments.
  - Micro and small businesses, classified to the private banking segment in the disclosure about operating segments in conformity with management approach, based on their attribution to the organizational unit in charge, were classified to the business segment in the disclosure about supervisory operating segments, in conformity with the aforementioned definitions.
  - Business clients, classified to the business segment or to the commercial segment in the disclosure about operating segments in conformity with management approach, based on their attribution to the organizational unit in charge, were classified to the micro and small businesses segment in the disclosure about supervisory operating segments, in conformity with the aforementioned definitions.
  - Institutional investors classified to the business segment or to the financial management segment in the disclosure about operating segments in conformity with management approach, were classified to the institutional investor segment in the disclosure about supervisory operating segments.
  - Business and individual clients at overseas branches classified into the various operating segments in conformity with management approach, are classified into the overseas operations segment in the disclosure of supervisory operating segments.

Exceptions for classification of business clients by turnover

According to the Bank of Israel Q&A File, the Bank classified business clients to operating segments other than by turnover, in the following cases:

- When the Bank has no information about the revenues of a business client and client indebtedness is smaller than NIS 300 thousand, the client is classified to the appropriate supervisory operating segment based on the client's total financial assets with the Bank. Such classification would be in accordance with the aforementioned categories for revenues, with total financial assets multiplied by 10 for the purpose of such classification.
- When the Bank is of the opinion that the volume of revenues of a business client are not indicative of their total operations and the client's total assets on the balance sheet exceed NIS 100 million, the Bank classifies such client to the Large Businesses segment. Such classification is used, for example, in the real estate sector. When total assets on the balance sheet amount to less than NIS 100 million and the revenues are not indicative, as noted above, the client is typically classified as follows:

  Small and micro businesses – total assets on client balance sheet amount up to NIS 50 million.

  Medium businesses – businesses where total assets on the client balance sheet amount to between NIS 50 million and NIS 215 million.

  Large business es– businesses where total assets on the client balance sheet exceeds NIS 215 million.

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

- Credit interest revenues and deposit interest expenses are directly attributed to the client. For credit, expense set at cost of capital raised (transfer cost) is attributed to clients, against an inter-segment credit to the Financial Management segment. Each segment is also charged any excess premium inherent in the cost of raising qualified equity instruments for capital adequacy. This is based on the capital attributed for segment operations. For deposits, revenue set at cost of capital raised is attributed to clients, against an inter-segment debit to the Financial Management segment. Transfer prices for loans and deposits are similar. Each of the segments is credited for capital attributed to operations there of, against a debit to the Financial Management segment. Capital consumption is measured by the average risk-free assets managed by the segment.
- When calculating risk assets attributed to each segment, any off-balance sheet credit exposures are "converted" to credit equivalent using coefficients specified in directives on measurement of capital adequacy.
- For derivative instrument operations, profits are attributed to the client at the spread incorporated in the price of the derivative instrument quoted to the client. Gains arising from changes to fair value of derivatives is attributed to Financial Management.
- Gains and losses from Bank investment in securities and from strategic positions are attributed to Financial Management.
- Expenses with respect to credit losses are directly attributed to clients on behalf of whom they were made.
- Commissions and other revenues are specifically attributed to clients.
- Payroll expenses, building maintenance and other expenses specifically attributed to Bank branches are attributed to branch clients using loading factors which reflect the client operations and the number of transactions in their account. Later on, an additional (inter-segment) settlement takes place, which attributes some of the direct expenses of the branch to clients in non-retail operating segments.

  Intersegment settlement reflects the fact that branches also serve non-retail clients. This settlement is presented under inter-segment expenses / revenues in the Note.
- Payroll expenses of headquarters staff, maintenance and other expenses not specifically related to branches, are loaded on clients based on appropriate load bases which take into account the ratio of the expense for the segment.

  Certain headquarters expenses may sometimes be attributed to a specific operating segment and may sometimes be attributed based on the current estimate of resources allocated to each operating segment.
- When headquarters expenses may not be attributed, they are assigned by weighted business and IT transactions, as noted above In this regard, IT expenses directly associated with specific operating segments are attributed to these segments and other IT expenses are assigned to operating segments based on headcount.
- Provision for tax on operating profit is attributed to clients, is9 pro-rated in accordance with the effective tax rate and accounting for tax impact referring to specific segments and not to all Bank operations.
- Return on equity is calculated as the ratio of net profit to attributed equity. Equity is attributed based on the average risk assets of the customers.
- Balance sheet and assets-under-management balances are specifically attributed to clients.
- Fixed assets are attributed based on appropriate ratios.

Household segment

For more information about the supervisory definition, concise description of segment attributes (under management approach) and differences between management approach and the supervisory definition, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Products and services

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

Banking and finance

Most of the services are provided within this framework

- **Credit and debitory accounts:** The credit limits for debitory account activity are determined according to the client's needs, his income level and Bank judgment, based on factors including economic models. In accordance with Proper Conduct of Banking Business Directive 325, clients are not allowed to exceed their determined credit limit.
- **Investments:** Providing investment-related services to customers, such as: Various deposits for different terms.
- **Loans:** General-purpose loans which include, inter alia, loans not intended for home purchase secured by pledging a lien on a residential property, and other loans for various terms and under different conditions.
- **Financing automobile purchases:** Operations providing loans for purchasing new automobiles from importers, where the Bank cooperates with multiple auto importers.

Mortgages

Major services related to mortgages:

Loans out of Bank funds – Loans out of Bank funds and at its risk, are extended for purchase / construction / expansion / renovation of real estate, as well as general-purpose loans secured by a lien on a residential apartment. The loans are issued for long terms of up to 30 years, considering the loan type and borrower repayment capacity.

The Bank extends credit in different linkage segments and offers a "combined mortgage" – a loan composition that combines various linkage segments and interest types. The combined mortgage enables the Bank to manage risk while maintaining profitability and allowing clients to diversify risk.

In 2016, loans in the non-linked segment increased. Moreover, in view of the downward trend in Bank of Israel interest and the low interest rate, the share of loans bearing fixed interest in the CPI-linked and non-linked track increased.

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

Services in conjunction with the Ministry of Construction and Housing Assistance Program – Beyond the banking activity of granting credit, the Bank acts as an extension of the State in servicing eligible Ministry of Construction and Housing recipients. These services include loans within the Ministry of Construction and Housing's assistance program, including location-based loans and contingent grants. In this area, the Bank is involved, in addition to the ordinary banking services, in the array of administrative aspects required for services to Ministry of Construction and Housing eligible participants, such as issuance of eligibility certificates. The decision as to which bank to apply for their eligibility is up to clients who take out a mortgage. Interest on loans extended as part of assistance programs is set by the Housing Loan Act.

In addition to ordinary loans in conjunction with the Assistance Program, there is an arrangement for providing loans, the objective of which is to encourage the purchase of new homes in certain communities that the State has an interest in populating ("location-based loans") as well as special assistance provided to those buying an apartment under the "Buyer price" program.

Contracting by the Bank and the State for extending loans as part of assistance programs, including the consideration payable to the Bank, is governed by two agreements dated 2004 and 2008. These agreements are extended annually.

Bank revenues from all loans to eligible borrowers under State responsibility in 2016 amounted to NIS 41 million, compared to NIS 54 million in 2015 and to NIS 56 million in 2014.

For details of the agreement between the Ministry of Finance and banks, for provision of loans to eligible borrowers with low point rating out of Bank funds and under Bank responsibility, see Note 26.C.18.

Insurance marketing (insurance incidental to mortgages)

The vast majority of borrowers are insured by life insurance policies related to the loan, and the properties serving as collateral are insured by property insurance.

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

Some borrowers choose to obtain insurance coverage through the Bank's insurance agency while others make other insurance arrangements.

In order to maintain the required separation between mortgage and insurance operations, clients are required, in order to purchase insurance from the Bank's insurance agency, to directly contact the insurance agency, also by using special phones connected directly to the insurance agency, which have been placed in Bank branches.

Bank revenues from insurance incidental to mortgages (in NIS millions):

	2016	2015	2014
Life insurance	96	93	96
Property insurance	15	15	21
Total revenues from sale of insurance	111	108	117

Life insurance – The increase in life increase revenues in 2016 is primarily due to portfolio growth.

Property insurance – In 2016, the portfolio grew and resulted in increased revenues. Conversely, reduction of the commission payable to the insurance agency and reduction of property insurance premiums for clients, as stipulated by the Ministry of Finance, resulted in a decrease in revenues, so that in 2016, total revenues amounted to NIS 15 million, similar to 2015.

Capital market

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

Credit cards

Credit cards are one of the key means of payment in the economy. As part of the activities with clients in the household segment, the clients a range of credit cards are offered. The Bank offers its clients all types of credit cards available in Israel, acting in this area with credit card companies Isracard, CAL and Leumi Card. The Bank offers its clients credit cards that are issued by these companies when opening a private account in the Bank, according to the client's request. The Bank also has several products in the credit card sector:

"The Card": A Mizrahi-Tefahot credit card which also serves as the Bank's own client loyalty club. The Card provides unique promotions and activity focused on consumer and banking benefits.

For more information about the agreement with CAL group, *inter alia*, with regard to issuance of the branded credit card, see Note 26.C.13 to the financial statements.

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

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

"Free Student" credit card: This card provides students with general-purpose credit. Credit on this credit card may be used within 3 years and bears attractive interest on the amount actually utilized; credit repayment is flexible; and early repayment at no cost to the client is allowed.

Unique services provided by the Bank to segment clients

The key unique service offered by the Bank is Hybrid Banking, which allows clients easy, direct access to a personal banker using a range of readily available technologies. As part of the Hybrid Banking campaign, the call center became a banking center, composed of 13 clusters. Later on, branch teams have been formed - each of which is assigned to 8-9 branches in various regions. These teams are an integral part of the branches to which they are assigned. Accordingly, Bank clients can reach their banker at the branch, or one of the branch team members, by using various communication channels during 12 hours of business, from 8am to 8pm. Moreover, under the household segment, the Bank offers its clients services which express the advantages of the combination of products offered by the Bank to its clients as described above. The Bank offers various benefits in current accounts and credit of clients who take out mortgages, in order to encourage the mortgage clients to maintain their current account in the Bank. The Bank also offers mortgage-related benefits to clients with current accounts in the Bank, in order to encourage these clients to take out mortgages through the Bank. The applicable benefits have also been applied to Bank Yahav clients, based on their activity and attributes.

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

"Priority Account": Personalized banking assistance.

"Executive Account": The unique "Executive Account" brand, launched in 2007, offers premium service to individuals on account management, banking value propositions, financial benefits and non-banking services. Clients may use professional advisors for financial, pension and mortgage advisory services.

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

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

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

Major markets and distribution channels

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

The Bank has mortgage marketers operating across Israel, based on geography. The role of these marketers is to identify target audiences in their geographic territory, to increase the exposure of such audiences to Bank products and services and to maximize the marketing potential of such audiences. Marketers give the Bank an edge in the market while making the client the focal point, in line with the Bank's strategy in recent years.

Marketers operate in four major areas:

- Direct activity with real estate players – to obtain potential clients.
- Activity with end clients – proactive contract with potential mortgage and checking account clients.
- Synergetic activity with individual clients – to realize the potential synergy of mortgage clients.
- Synergetic activity with business clients and MM clients - businesses, plants, employee unions etc.

Bank branches – the Group operates 184 business centers, branches, affiliates and representative offices across the country, including 45 Yahav branches. In conformity with the Bank's growth strategy, the expansion of the branch network continues, primarily in business-rich environments and in towns of two distinct demographics where the Bank seeks growth – the Arab segment and the Jewish Orthodox segment.

Direct channels: In conformity with the Bank's unique Hybrid Banking concept, which links direct channels and the client's personal banker, the Bank operates these main direct channels:

– Banking Center: The branch team at the banking center provides backup to branch bankers, assisting with transactions and providing information to Bank clients, as part of the integrated Hybrid service offered to clients. This service is provided 24 hours a day (except for weekends and holidays).

  The banking center provides sale of instant loan services, standing orders and credit cards as well as client preservation for non-bank credit cards.

– Mortgage center: This center is at the core of the mortgage segment, providing clients with a range of activities related to mortgages, including filing applications and providing advice on housing loans, receiving payments for existing loans and making arrangements and payments for loans in arrears.

  The Hybrid Banking service for mortgages was expanded in 2015 to all Bank branches.

– Sales center: Intended to support the selling capabilities of Bank branches, as part of marketing campaigns to recruit clients, who are referred directly to the sales center, or by means of sales calls. In addition, the sales center handles sales of credit cards, re-financing mortgages from other banks for Bank clients, sale of car loans and preventing churn.

  In 2017, the Bank is expected to intensify the mortgage refinancing operations for commercial clients, activities designed to prevent churn, reactivation of open but inactive accounts and will improve performance across its operations by better interfacing with Bank branches.

– Investment center: This center provides rapid, professional response to capital market clients for investment transactions and advice, from 7am to midnight, along with training of investment advisors to be assigned to branches. The center also recruits new clients for savings, focusing on maximizing performance of investment campaigns. The center operates an affiliate of the trading room, providing Bank clients with service concerning foreign currency and foreign securities.

– On line service: Allows clients to receive banking information and execute transactions in your account for a range of banking products available to Bank clients at a reduced cost. This service is available 24 hours a day.

  In 2016, the Bank launched a new website for mortgages and upgraded the application for existing clients. Data for the mortgage segment is presented using an advanced, convenient interface for clients. Clients who enroll in this service can now obtain valuable information, including: detailed information about the mortgage loan (including graphics), details of properties pledged to secure the loan, mortgage loan repayment history, details of life and property insurance as entered in the Bank's system, comprehensive environmental information, apartment price lists and market analysis from the MADLAN website. Clients can also produce for themselves useful documents and forms, directly from the website.

  The new website offers a secure correspondence service for clients in the process of obtaining a mortgage. This services improves the service experience and reinforces the personal connection between mortgage clients and the personal banker who handles their application. The service allows for close assistance to clients throughout the process, through mortgage origination, expanded communication channels, including a means for easy and convenient document transfer between the client and the banker at the branch.

  In 2017, the Bank anticipates extending the digital services offered to business clients.

– Cell phone application: Allows clients to obtain banking information and conduct transactions by means of cellular browsing using smart phones.

  In 2016, the Bank expanded the feature of check deposit on your cell phone, to include checks drawn on other banks.

- "Tefahot to Home" app: In 2016, the Bank launched an advanced app for clients interested in obtaining a mortgage. This app provides: assistance in creating a financing plan to buy your home, comprehensive, current information about different neighborhoods, including recent transactions, data about apartment prices, rental yields, social benchmarks, education quality etc., an option for clients to photograph and document apartments, a user-friendly mortgage calculator and a service offering correspondence with a mortgage banker.

- Notification Box service: Receiving Bank notifications of account activity in a personal notification box via the Bank's website.
- Cell phone service: Disseminating banking and financial information through cell phones.
- IVR service: This service, available 24 hours a day, is provided to clients who authenticate using their personal password to obtain computer-based information in response to frequently-asked queries.

Business Strategy

Service strategy at Bank Mizrahi Tefahot is based on the understanding that personal, human contact with a banker offering a high level of professional service is at the core of client needs. The Bank's branch network is a key component in creating that personal contact with the banker – and must be supported by a current, efficient digital technology environment.

The Bank sees the importance of further development of the household segment and intends to maintain and establish its leadership position in the retail sector. The key goals in the household segment and the resultant business strategy are presented below:

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

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

Competition in the segment and changes to it

Banking and Finance, credit cards and the capital market

The number of competitors in the household segment is the number of banks operating in the economy, with the focus on the five commercial bank groups. In recent years, the retail banking market sees strong competition among banks. Generally, one can state that the retail banking products offered by the different banks are similar, and therefore, competition focuses on the quality of service, the rates of the margins and commissions paid by the clients.

In 2016, branch closures and elimination of teller positions at branches of some banks continued, with clients referred to digital solutions. Consequently, in August 2016 the Knesset enacted the Banking Act (Licensing) (Amendment no. 22), 2016, whereby any banking corporation seeking to close a permanent branch would be required to obtain permission from the Supervisor of Banks after filing a written justification and application to do so.

In addition to the inter-bank competition, intensified efforts are discerned by non-banking entities (mainly insurance companies, credit card companies) that also approach this population segment with offers to provide credit. The credit card companies, together with retail chains and other entities, are also taking measures to issue credit cards directly to clients, not through a bank. See below regarding barriers to entry and exit.

In the capital market sector, the competitors also include private investment houses, in addition to insurance companies.

In January 2017, the Knesset enacted the Increased Competition and Reduced Concentration in Israeli Banking Act. This legislation includes separation of control over credit card companies by the two top banks, including provisions and fledgling protection for the credit card companies to be separated; provisions with regard to creating IT infrastructure and mandatory sale of IT services and operation thereof, as well as leasing of real estate used for IT services and operation thereof, used primarily by the bank; provisions whereby a clearing house would be required to allow settlement by a guest clearing house, in conformity with rules to be specified by the Governor of the Bank of Israel with consent of the Minister of Finance and provisions with regard to guest clearing house and bundled clearing house. Additional provisions enacted relate to a service for comparison of financial costs.

Mortgages

Most of the mortgage activity in Israel is conducted through ten banks operating in this field. For dozens of years, the Bank has been the leader in the mortgage sector, in terms of the volume of loans issued and the balance of the loans portfolio. Based on Bank of Israel data, the Group's share of provision of housing loans (for residential purpose), out of Bank funds as well as loans guaranteed by the State, reached 35% at the end of 2015, compared to 34% at the end of 2014. The Bank's major competitors are Bank Leumi and Bank Hapoalim.

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

Private Banking Segment

For more information about the supervisory definition, concise description of segment attributes (under management approach), differences between management approach and the supervisory definition, markets, distribution methods and business strategy, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Products and services

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

- **Banking and finance** – A wide range of banking and finance products are offered to this segment’s clients, in addition to ordinary banking services, while formulating an investment strategy suitable for each client, tailored to his character and special needs, as well as an array of advanced investment products.

- **Capital market** – this product includes client operations in the capital market, including buying, selling and custodial services of various securities, and provision of services with respect to securities (receipt of interest, dividends, benefits etc.) This also includes mutual fund distribution services.
- **Credit cards** – the Bank offers to segment clients a range of exclusive credit cards issued by Israeli credit card companies.

Competition in the segment and changes to it

The concept of the unique services defined by the Bank as "private banking" prevails throughout the global and international banking system, and also in Israel. However, it should be noted that the criteria that determine whether one belongs to this segment, the service approach and its specific nature change, and do not rest on identical principles in all the banks. Also, accordingly, the volume of the Bank's activities in this segment relative to its competitors is not known, and public information is not available about the proportionate share in the private banking system of the different banks.

In addition to local banks, there is competition in this segment from foreign banks and non-banking entities, such as investment houses, types of funds (from Israel and overseas) and insurance companies.

In order to deal with current competition in this segment, the Bank invests substantial resources in the professional training of its employees, in providing high quality service and in maintaining strong ties with the client, in the organization of professional conferences for the segment's select clients, in introduction of specialized and unique products to the segment's clients, and in efforts to identify and attract new clients on a regular basis.

Micro and Small Business Segment

For more information about the supervisory definition, concise description of segment attributes (under management approach), differences between management approach and the supervisory definition, markets and distribution methods, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Products and services

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

Banking and finance

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

Loans for various purposes: Business loans, loans against the discounting of checking, credit vouchers etc.

Import / export activities: Foreign currency operations, adaptation of credit facilities to the nature of the client's activities using technological means, such as: on line Electronic Data Interchange (EDI).

Investments: Diverse operations related to investments, such as deposits of various types and for various terms.

Management of checking account facilities: The facilities are determined according to the client's needs, turnover and judgment of the Bank.

Capital market

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

Credit cards

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

Loans for small businesses, guaranteed by the State

In May 2016, Bank Mizrahi Tefahot launched its financial partnership with HaPhoenix and with Altshuler Shacham, selected as one of the winning bidders in a tender to provide loans to small and medium businesses, guaranteed by the State, by providing loans in a range of tracks under this heading.

Business Strategy

Increasing focus and expanding operations in business segments, including the micro and small business segment is at the heart of the Bank's business strategy. This is done while constantly assessing risk and controls at the client, segment and economy levels.

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

Increasing marketing activity vis-à-vis clients, while segmenting the clients by occupation, size of operation and individual needs.

Maximize potential profitability for each client by adopting a comprehensive view of client activity, creating a comprehensive relationship based on credit products and marketing of other products – depending on client attributes.

Expanded activity in State fund for small and medium businesses.

Expand geographic deployment of services provided to segment clients.

Competition in the segment and changes to it

Competition in the small business segment is primarily within the banking system. However, over the past years, public action was taken to reinforce the market share of non-bank credit providers (such as institutional investors, non-bank credit cards and other financing companies) by including institutional investors in a new tender issued by the State Fund for Small and Medium Business. The Bank's principal methods for dealing with the competition are active marketing, personal ties with the client, providing personal service and comprehensive professional solutions for the full range of client financial needs.

Medium business segment

For more information about the supervisory definition and differences between management approach and the supervisory definition, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Brief description of segment attributes (using "management approach")

The medium business segment primarily includes medium-sized private and public companies (Middle Market), with total indebtedness between NIS 6 and 25 million.

This segment operates across all economic sectors, primarily industry, commerce and services, construction and real estate.

Clients in this segment are primarily served by the Bank's Business Division, primarily by the Business Sector, operating three business centers nation-wide, with additional service provided by the Bank's extensive branch network.

Each center has the professional resources required to address all client needs. These centers operate in co-ordination with the Bank's branch network, which handles operating aspects of client activity. Thus, clients enjoy personal, professional service which provides a response to all their banking needs, as well as benefit from the extensive branch network.

Segment clients primarily operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector. These clients, too, enjoy service at the branch convenient to them, with regard to operating aspects as well as the specialized, professional service of the construction and real estate sector.

Clients in this segment use a range of banking services, associated with a relatively high ratio of required collateral compared to Business Banking segment clients.

Clients are mostly active on the local market. However, clients also conduct foreign trade transactions (import / export) of significant volume.

Major markets and distribution channels

The segment primarily engages in marketing and distribution using three business hubs operating under the Business Division, as well as business centers and Bank branches throughout Israel. Client relations management and recruiting of new clients are conducted by special professionals at the business centers, who are in charge of this and are in constant contact with clients.

Operations in this segment include development of marketing and business operations based on understanding client needs and customizing comprehensive banking solutions to these needs; providing professional, rapid and efficient service; offering a range of products and solutions customized for client needs with controlled management of risk arising from segment operations, including by specifying financial covenants to monitor clients' financial robustness.

Clients may also use the direct banking channels and customary banking channels.

Business Strategy

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

The Bank intends to continue significantly expanding operations in this segment, primarily by recruiting new clients and expanding banking services to current clients and to clients for which the Bank is a secondary bank.

Competition in the segment and changes to it

Segment clients conduct their financial activity primarily within the banking system, so that competition for this client segment is significant, since all banks compete for this target audience. Non-banking finance providers have a smaller share of this segment, mostly in the factoring business and in credit card companies.

The Bank considers expansion of this segment's business to be an important major objective and therefore invests resources in handling these companies by providing comprehensive, professional solutions for client needs, maintaining a personal relationship and providing fast, efficient service.

Large business segment

For more information about the supervisory definition and differences between management approach and the supervisory definition, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Brief description of segment attributes (using "management approach")

The segment specializes in providing complete banking and financing services to the largest companies, in a range of sectors, with total indebtedness exceeding NIS 25 million per client.

The major sectors served are: industry, commerce, construction and real estate.

This segment includes market-leading clients with large-scale operations, some of which are multi-nationals or companies with local operations which address overseas markets.

Segment clients are served under responsibility of the Bank's Business Division, primarily by the Large Corporation Sector.

Segment clients operating in the real estate sector are served by the Construction and Real Estate sector of the Business Division, which specializes in provision of dedicated services to this sector.

All clients receive additional (operating) service from the Bank's extensive branch network in Israel and overseas.

In its activities in this segment, the Bank emphasizes expansion of the current client base and improved profitability through expansion of activity in financing areas with very high profitability relative to capital, such as trading room transactions, including transactions in derivatives and other products provided to clients by the trading room.

Products and services

Segment clients are offered a range of banking and finance products, including: Various types of credit – on call, short-, medium- and long-term loans, guarantees, international trade transactions (financing for credit insurance, import, export and documentary credit) as well as factoring. These services are provided with support from a specialized sector at the Bank, which can customize for each client the products relevant for their business and attributes, financing through organizing or participating in syndications, financing of infrastructure projects, mergers and acquisitions as well as transactions involving derivative instruments.

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

Credit to large corporations in Israel and overseas

The Bank provides banking services to multi-national clients based in Israel.

In this context, the Bank provides foreign currency, foreign trade and factoring services as well as service at the Bank's overseas branches.

Products related to real estate

In this sector, the Bank offers loans to finance the purchase and construction of real estate, mainly residential construction products in areas of high demand, while insisting on the applications of tests prescribed in order to maintain the quality of the loan portfolio, and these include ties with customers having financial strength and stability, transactions characterized by favorable safety cushions for the Bank, and management using methods that reduce the risk.

The main services provided to clients of the real estate sector are:

- **Credit for construction** - in this sector, the Bank provides credit, in particular short- and medium-term loans, used to finance land acquisition and investment in construction, as well as various types of bank guarantees.
- **Financing for construction projects** - construction project financing is a unique service, provided by the Bank exclusively to clients in this sector. Within this framework, the client is offered a package of financial and banking services, suited to the specific needs of each project and based on its characteristics. This includes allotment of credit facilities for land acquisition, construction loans, financial guarantees, performance guarantees and guarantees to home buyers in projects. The Bank issues construction financing mainly by the closed financial support method, in which the Bank

channels the financing sources, including the buyers' monies deposited with it, in a manner that advances completion of the project.

- **Purchase groups** - a purchase group is a collection of individuals, gathered for the purpose of jointly acquiring land and buying construction services on said land. Alternatively, existing land owners join forces to jointly construct, by ordering construction services.

The Bank provides dedicated financing for projects of this type, and assists them from preliminary stages of forming the group, through completion of construction.

Arranging and leading syndications - The Bank sees an objective in expansion of its business in initiating, leading, organizing and managing syndication transactions - to help turn the Bank into a major player in the business credit market. To this end, the Bank has established a department specialized in leading and participating in syndication transactions. By leading and organizing syndication transactions, the Bank provides a solution for businesses requiring significant credit while maintaining risk within the Bank's risk appetite.

Major markets and distribution channels

The main marketing and distribution parties in this segment are the managers and client managers in the Business Banking Division, supported by the Bank's branches and business centers.

In order to provide an optimal response to segment client needs, the servicing of major business banking clients in this segment was placed under the Corporation Sector of the Bank's Business Division, divided into departments and teams having specific industry specialization. The teams work in cooperation with professional Bank departments involved in factoring, foreign trade, capital market, trading room operations etc. – in order to provide a comprehensive solution for client needs.

Operations in this segment include providing fast and effective professional services that offers a comprehensive solution adapted for all of the client's banking needs. This is done while by a variety of innovative financial products and solutions.

These operations are backed by a strong capacity for analysis of client needs and their financial standing, as well as identifying risk associated with client relationships due, *inter alia*, to anticipated changes in the economy and in the client sector.

Business Strategy

The Bank's business strategy for the large business segment is designed to increase the number of clients and to expand business with existing clients. This is to be done while maximizing the economic potential of the capital by focusing on activities having high profitability relative to the capital needed for them, through, inter alia, the following activities:

Implement an approach based on total outlook on the business client, leveraging credit products and offering other products to establish a comprehensive client relationship.

Segment business clients by size, sector of operation and other attributes in order to optimally specify their business needs and to provide an appropriate, professional solution.

Given the legal complexity of transactions in recent years, *inter alia* in combination projects and in urban renewal projects (evacuation-construction schemes and National Zoning Plan 38), these require custom specialization.

Emphasis on profitability and return on uses.

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

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

Competition in the segment and changes to it

Competition in the business banking segment is with large and mid-sized banks in Israel, and occasionally with overseas banks, and for some services – the entire capital market. In recent years, institutional investors and insurance companies have expanded their business with such clients, by focusing on providing significant long-term credit.

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

The Bank's main methods for dealing with the competition are to provide professional service that is fast and effective, while offering optimal solutions for the customer's needs in a diverse array of its financial activities. As well as customizing complex financial solutions in response to client needs.

As part of its operations in this segment, the Bank places emphasis on the best possible personal service to the business client and adapting it to the client's needs according to his unique characteristics, while focusing on industry expertise and providing specific professional advice in specialty areas.

Similar to competition for corporate financing, the competition for providing banking services to construction and real estate clients has seen non-banking entities enter into this area, as well. These entities have started providing assistance to projects on their own, without cooperation with any banks.

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

Institutional investor segment

For more information about the supervisory definition, concise description of segment attributes (under management approach), differences between management approach and the supervisory definition, products and services, markets, distribution methods and business strategy, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Competition in the segment and changes to it

With regard to providing execution services on the Tel Aviv Stock Exchange to institutional investors, there is significant competition between local banks and stock exchange members.

As for transactions involving derivatives, there is also competition with foreign banks with which some institutional investors have opened direct accounts.

Financial Management Segment

For more information about the supervisory definition, concise description of segment attributes (under management approach), differences between management approach and the supervisory definition, products and services, major markets and distribution methods, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Business Strategy

Asset and liability management operations have the key objective of active management of exposure to market risk and of the debenture portfolio, aimed at optimal management of financing profitability, while maintaining appropriate, controlled exposure to market- and liquidity risk, which reflects the Bank's risk appetite, subject to limits specified by decisions of the Board of Directors and management.

The main activity in the debenture portfolio is efficient management of Bank liquidity in NIS and in foreign currency, compared to an alternative, risk-free investment. The policy on excess liquidity management is based on requirements for liquidity risk management, in conformity with Proper Conduct of Banking Business Directive no. 342 and Proper Banking Conduct Directive 221 – liquidity coverage ratio. (For more information about the liquidity model and restrictions imposed by management and by the Board of Directors, see chapter "Risk overview" of the Report of the Board of Directors and Management and the Detailed Risks Management Report on the Bank website). Threshold criteria were also prescribed for nostro debenture activity, based on the credit risk inherent in the portfolio's activity, to diversify investments and to increase the liquidity there of. Debenture operations are subject to compliance with credit limits specified by the Bank for countries, banks and companies - with the bulk of these operations involving risk exposure to the State of Israel.

As for management of market risk exposure, the Bank actively manages the negotiable portfolio in order to generate gain at the specified risk level. The bank portfolio is regularly managed and monitored in order to improve interest revenues, subject to the risk appetite. The volume of activity and risk must meet the market risk exposure limits prescribed by the Board of Directors and management. For more information about risk limitations and management of market risk exposure, see the Detailed Risks Management Report on the Bank website.

The segment also acts to raise financial sources as needed for Bank operations, while complying with liquidity ratio targets and capital ratio targets, as per decisions of the Board of Directors. This would be achieved by raising deposits with different linkage bases and for different terms, and by issuing subordinated notes and contingent subordinated notes (Tier II capital). For more information see chapter "Developments in financing sources" and chapter "Developments in capital structure" of the Report of the Board of Directors and Management.

One of the tools used by the segment in managing liquidity and exposure to market risk is the issuance of subordinated notes, inter alia, through the subsidiary, Mizrahi-Tefahot Issuance Company Ltd., as provided below in the chapter "Developments in capital structure" of the Report of the Board of Directors and Management.

The segment includes the Bank’s trading room operations in financial and capital markets. These operations include market making in all standard derivative instruments trading over-the-counter in Israel and back-to-back trading in complex derivative instruments. The trading room also serves major local and foreign clients trading in securities in stock exchanges in Israel and overseas. The Bank strives to position itself as a leader in the OTC market in Israel, while maintaining the risk level specified in Bank policy and adapting operations to local and global regulation. Furthermore, the Bank constantly strives to expand its operations by expanding the client base and intensifying business activity and client relationships, inter alia, by improving cooperation between Bank departments operating within the trading room, development of new transaction types and investing in acquiring professional knowledge.

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

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

Competition in the segment and changes to it

The financial management segment includes operations of the trading room. This area faces a high level of competition with the primary competitors: Israel's top four bank groups, as well as foreign banks.

Operating results of overseas operations

For more information about the supervisory definition, concise description of segment attributes (under management approach), differences between management approach and the supervisory definition, markets and distribution methods, see chapter "Supervisory operating segments" of the Report of the Board of Directors and Management.

Products and services

Details of the affiliates and their business are as follows:

Swiss subsidiary – UMB (Switzerland) Ltd. – specializes in private banking services and in extending loans for purchase of real estate in Israel. The subsidiary operates through one branch and is owned by the wholly-owned Bank holding company incorporated in Holland – UMOHC B.V. (hereinafter: ("the holding company"). The Swiss subsidiary is subject to the regulatory laws in Switzerland.

Bank's overseas branches – Overseas branches offer their customers banking services, in accordance with the local laws and regulations. The branches are subject to the local and Israeli regulation.

- **Los Angeles Branch:** The branch is primarily engaged in commercial banking, participating in syndicated loans and receiving deposits. Deposits with this branch are insured by the Federal Deposit Insurance Corporation(FDIC). The branch's clients are local, Israeli and international clients.
- **London Branch:** The branch is engaged mainly in business banking, including participation in loan syndicates, financing of foreign trade, credit, receiving deposits, foreign currency trade and providing private banking services, excluding advisory service on securities. The branch's clients are local, Israeli and international clients.

International private banking branches in Israel – The Bank operates four special branches, located in Jerusalem, Tel Aviv, Netanya and Ashdod, serving foreign resident and new immigrant clients. These branches provide full banking services to their clients, primarily private banking. The branches are under supervision by supervisory entities and relevant authorities in Israel and report to the Private Banking and International Operations sector.

Representative offices - The major activities of representative offices are marketing of Bank services and representation of the Bank overseas. The Bank operates representative offices in Mexico, Uruguay and Germany. The Bank has decided to close its representative offices in Uruguay.

Major markets and distribution channels

The major markets are local clients, mostly from the Jewish community, located in countries where the Bank's overseas affiliates do business, as well as clients resident in Israel whose financial and business needs include banking services provided overseas.

Major distribution channels include participation in professional conferences in countries where the affiliates are located, local advertising to the Jewish community, marketing of the Bank by Bank representatives among the local Jewish community and referrals from current clients.

Business Strategy

The Bank's overseas affiliates operate in a competitive environment of local and international banks operating in the same country, but are focused on providing banking services on a more limited scale, compared to local and international banks. Competition is focused on service quality, response time and maximizing the client-Bank relationship. Each international operations affiliate has a unique target audience. Critical success factors are based on providing fast, personal service at an international level. Service provided to clients is based on understanding their personal needs and providing individual solutions based on intensive knowledge of local markets in order to find the appropriate range of products.

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

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

International operations involve several unique risk factors:

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

Each overseas affiliate operates subject to local laws and regulations, and is regularly assisted by local legal counsel who specialize in banking operations applicable for each affiliate. The Bank has also established and maintains a supervisory and control process over operations of its affiliates, through relevant risk managers at the Bank in Israel, as well as using external professional consultants on behalf of the Bank in Israel.

Competition in the segment and changes to it

In recent years, competition with affiliates of Israeli banks overseas has diminished. Furthermore, global regulatory changes have resulted in a change in business focus and changes to client preferences.

Addendums to annual financial statements

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Addendum 1 – Revenue and Expense Rates – of the Bank and its Subsidiaries[1]

For the year ended December 31,

Reported amounts (NIS in millions)

A. Average balances and interest rates - assets

	2016			2015			2014		
	Average balance[2]	interest revenues	Revenue rate	Average balance[2]	interest revenues	Revenue rate	Average balance[2]	interest revenues	Revenue rate
			In %			In %			In %
Interest-bearing assets									
Loans to the public [3]									
In Israel	161,072	[7]5,011	3.11	149,239	4,585	3.07	140,363	[7]5,026	3.58
Outside of Israel	3,195	146	4.57	2,665	106	3.98	2,305	103	4.47
Total	164,267	5,157	3.14	151,904	4,691	3.09	142,668	5,129	3.60
Loans to the Government									
In Israel	187	3	1.60	288	9	3.13	303	9	2.97
Outside of Israel	151	7	4.64	–	–	–	–	–	–
Total	338	10	2.96	288	9	3.13	303	9	2.97
Deposits with banks									
In Israel	685	1	0.15	1,745	3	0.17	1,841	8	0.43
Outside of Israel	308	4	1.30	427	3	0.70	296	5	1.69
Total	993	5	0.50	2,172	6	0.28	2,137	13	0.61
Deposits with central banks									
In Israel	30,702	26	0.08	20,357	21	0.10	21,614	108	0.50
Outside of Israel	3,925	20	0.51	3,319	8	0.24	1,535	–	–
Total	34,627	46	0.13	23,676	29	0.12	23,149	108	0.47
Securities loaned or purchased in resale agreements									
In Israel	88	–	–	174	–	–	199	1	0.50
Outside of Israel	–	–	–	–	–	–	–	–	–
Total	88	–	–	174	–	–	199	1	0.50
Debentures held to maturity and available for sale [4]									
In Israel	7,925	71	0.90	11,799	150	1.27	7,294	62	0.85
Outside of Israel	1,084	18	1.66	1,137	17	1.50	1,105	16	1.45
Total	9,009	89	0.99	12,936	167	1.29	8,399	78	0.93
Debentures held for trading[5]									
In Israel	355	4	1.13	326	4	1.23	1,149	9	0.78
Outside of Israel	–	–	–	–	–	–	–	–	–
Total	355	4	1.13	326	4	1.23	1,149	9	0.78
Total interest-bearing assets	209,677	5,311	2.53	191,476	4,906	2.56	178,004	5,347	3.00
Receivables for credit card operations	3,136			3,030			2,914		
Other non-interest bearing assets[6]	4,022			4,625			5,693		
Total assets	216,835			199,131			186,611		
Total interest-bearing assets attributable to operations outside of Israel	8,663	195	2.25	7,548	134	1.78	5,241	124	2.37

See remarks below.

Addendum 1 – Revenue and Expense Rates – of the Bank and its Subsidiaries[1] – continued

For the year ended December 31,

Reported amounts (NIS in millions)

B. Average balances and interest rates - liabilities and equity

	2016			2015			2014		
	Average balance[2]	Interest expenses	Revenue rate	Average balance[2]	Interest expenses	Revenue rate	Average balance[2]	Interest expenses	Revenue rate
			In %			In %			In %
Interest-bearing liabilities									
Deposits from the public									
In Israel									
On-call	8,013	24	0.30	6,295	8	0.13	5,204	5	0.10
Term deposits	119,220	991	0.83	114,058	932	0.82	118,599	1,359	1.15
Outside of Israel									
On-call	628	–	–	758	–	–	6	–	–
Term deposits	4,166	30	0.72	2,216	22	0.99	3,358	29	0.86
Total	132,027	1,045	0.79	123,327	962	0.78	127,167	1,393	1.10
Deposits from the Government									
In Israel	53	2	3.77	58	2	3.45	58	3	5.17
Outside of Israel	–	–	–	–	–	–	–	–	–
Total	53	2	3.77	58	2	3.45	58	3	5.17
Deposits from banks									
In Israel	822	12	1.46	828	12	1.45	1,381	17	1.23
Outside of Israel	6	–	–	–	–	–	152	1	0.66
Total	828	12	1.45	828	12	1.45	1,533	18	1.17
Securities loaned or sold in conjunction with repurchase agreements									
In Israel	–	–	–	116	–	–	93	–	–
Outside of Israel	–	–	–	–	–	–	–	–	–
Total	–	–	–	116	–	–	93	–	–
Debentures and subordinated notes									
In Israel	25,092	472	1.88	21,652	392	1.81	18,752	556	2.97
Outside of Israel	–	–	–	–	–	–	–	–	–
Total	25,092	472	1.88	21,652	392	1.81	18,752	556	2.97
Other liabilities									
In Israel	105	2	1.90	349	4	1.15	380	2	0.53
Outside of Israel	–	–	–	–	–	–	–	–	–
Total	105	2	1.90	349	4	1.15	380	2	0.53
Total interest-bearing liabilities	158,105	1,533	0.97	146,330	1,372	0.94	147,983	1,972	1.33
Non-interest bearing deposits from the public	37,442			30,788			19,035		
Payables for credit card transactions	3,136			3,030			2,914		
Other non-interest bearing liabilities[8]	5,203			7,126			5,939		
Total liabilities	203,886			187,274			175,871		
Total equity resources	12,949			11,857			10,740		
Total liabilities and equity resources	216,835			199,131			186,611		
Interest margin			1.56			1.62			1.67
Net return[9] on interest-bearing assets									
In Israel	201,014	3,613	1.80	183,928	3,422	1.86	172,763	3,281	1.90
Outside of Israel	8,663	165	1.90	7,548	112	1.48	5,241	94	1.79
Total	209,677	3,778	1.80	191,476	3,534	1.85	178,004	3,375	1.90
Total interest-bearing liabilities attributable to operations outside of Israel	4,800	30	0.63	2,974	22	0.74	3,516	30	0.85

See remarks below.

Addendum 1 – Revenue and Expense Rates – of the Bank and its Subsidiaries[1] – continued

For the year ended December 31,

Reported amounts (NIS in millions)

C. Average balances and interest rates - additional information about interest-bearing assets and liabilities attributed to operations in Israel

			2016			2015			2014
	Average balance[2]	Interest revenues (expenses)	Revenue (expense) rate	Average balance[2]	Interest revenues (expenses)	Revenue (expense) rate	Average balance[2]	Interest revenues (expenses)	Revenue (expense) rate
			In %			In %			In %
Israeli currency - non-linked									
Total interest-bearing assets	138,152	3,620	2.62	117,783	3,453	2.93	105,258	3,397	3.23
Total interest-bearing liabilities	98,553	(620)	(0.63)	85,504	(557)	(0.65)	86,640	(781)	(0.90)
Interest margin			1.99			2.28			2.33
Israeli currency – linked to the CPI									
Total interest-bearing assets	50,921	1,202	2.36	52,518	1,019	1.94	53,845	1,505	2.79
Total interest-bearing liabilities	36,983	(682)	(1.84)	37,147	(626)	(1.69)	37,594	(987)	(2.63)
Interest margin			0.52			0.25			0.16
Foreign currency (including Israeli currency linked to foreign currency)									
Total interest-bearing assets	11,941	294	2.46	13,627	300	2.20	13,660	321	2.35
Total interest-bearing liabilities	17,769	(201)	(1.13)	20,705	(167)	(0.81)	20,233	(174)	(0.86)
Interest margin			1.33			1.39			1.49
Total - operations in Israel									
Total interest-bearing assets	201,014	5,116	2.55	183,928	4,772	2.59	172,763	5,223	3.02
Total interest-bearing liabilities	153,305	(1,503)	(0.98)	143,356	(1,350)	(0.94)	144,467	(1,942)	(1.35)
Interest margin			1.57			1.65			1.67

See remarks below.

Addendum 1 – Revenue and expense rates of the Bank and of its subsidiaries[(1)]
For the year ended December 31,
Reported amounts (NIS in millions)

D. Analysis of change in interest revenues and expenses

	2016 compared to 2015			2015 compared to 2014		
	Increase (decrease) due to change[(10)]			Increase (decrease) due to change[(10)]		
	Quantity	Price	Net change	Quantity	Price	Net change
Interest-bearing assets						
Loans to the public						
In Israel	368	58	426	273	(714)	(441)
Outside of Israel	24	16	40	14	(11)	3
Total	392	74	466	287	(725)	(438)
Other interest-bearing assets						
In Israel	14	(96)	(82)	12	(22)	(10)
Outside of Israel	5	16	21	11	(4)	7
Total	19	(80)	(61)	23	(26)	(3)
Total interest revenues	411	(6)	405	310	(751)	(441)
Interest-bearing liabilities						
Deposits from the public						
In Israel	55	20	75	(27)	(397)	(424)
Outside of Israel	11	(3)	8	(3)	(4)	(7)
Total	66	17	83	(30)	(401)	(431)
Other interest-bearing liabilities						
In Israel	57	21	78	42	(210)	(168)
Outside of Israel	–	–	–	–	(1)	(1)
Total	57	21	78	42	(211)	(169)
Total interest expenses	123	38	161	12	(612)	(600)

(1) Information in these tables is after effect of hedging financial derivative instruments.
(2) Based on balances at start of the months (in Israeli currency, non-linked segment - based on daily balances).
(3) Before deduction of average balance sheet balance of provisions for credit losses. Includes impaired debt not accruing interest revenues.
(4) From the average balance of debentures available for sale, for the one-year periods ended December 31, 2016, 2015 and 2014, we deducted (added) the average balance of unrealized gains (losses) from adjustment to fair value of debentures available for sale, included in equity under Other Comprehensive Income, under "Adjustments with respect to presentation of securities available for sale at fair value", amounting to NIS 3 million, NIS 2 million and NIS 9 million, respectively.
(5) From the average balance of debentures held for trading, for the one-year periods ended December 31, 2016, 2015 and 2014, we added (deducted) the average balance of unrealized gains (losses) from adjustment to fair value of debentures held for trading, amounting to NIS 2 million, NIS (4) million and NIS (33) million, respectively.
(6) Includes derivative instruments, other non-interest bearing assets, net of provision for credit losses.
(7) Commissions amounting to NIS 271, 456 and 417 million were included in interest revenues for the one year periods ended December 31, 2016, 2015 and 2014, respectively.
(8) Includes derivative instruments.
(9) Net return - net interest revenues divided into total interest-bearing assets.
(10) The change attributed to change in quantity was calculated by multiplying the new price by the change in quantity. The change attributed to change in price was calculated by multiplying the old quantity by the change in price.

Addendum 2 – Multi-period information

Consolidated Statement of Profit and Loss – Multi-period information

For the years ended December 31, 2012 – 2016

Reported amounts (NIS in millions)

	2016	2015	2014	2013	2012
Interest revenues	5,311	4,906	5,347	6,442	6,591
Interest expenses	1,533	1,372	1,972	2,978	3,377
Interest revenues, net	3,778	3,534	3,375	3,464	3,214
Expenses with respect to credit losses	200	211	173	288	276
Interest revenues, net after expenses with respect to credit losses	3,578	3,323	3,202	3,176	2,938
Non-interest revenues					
Non-interest financing revenues	295	358	173	14	95
Fees	1,433	1,426	1,395	1,458	1,452
Other revenues	134	74	44	27	26
Total non-interest revenues	1,862	1,858	1,612	1,499	1,573
Operating and other expenses					
Payroll and associated expenses	2,071	1,944	1,866	1,823	1,704
Maintenance and depreciation of buildings and equipment	693	692	715	690	670
Other expenses	535	590	458	438	433
Total operating and other expenses	3,299	3,226	3,039	2,951	2,807
Pre-tax profit	2,141	1,955	1,775	1,724	1,704
Provision for taxes on profit	833	761	657	593	594
After-tax profit	1,308	1,194	1,118	1,131	1,110
Share in profit (loss) of associates, after tax	–	–	5	(4)	–
Net profit:					
Before attribution to non-controlling interests	1,308	1,194	1,123	1,127	1,110
Attributable to non-controlling interests	(42)	(60)	(31)	(44)	(50)
Attributable to shareholders of the Bank	1,266	1,134	1,092	1,083	1,060
Earnings per share[(1)]					
Basic earnings per share (in NIS):					
Total net profit attributable to shareholders of the Bank	5.46	4.90	4.74	4.74	4.70
Diluted earnings per share (in NIS):					
Total net profit attributable to shareholders of the Bank	5.46	4.89	4.71	4.71	4.67

(1) Share of NIS 0.1 par value each.

Addendum 2 – Multi-period information

Consolidated Balance Sheet – Multi-period information

As of December 31, 2012 – 2016

Reported amounts (NIS in millions)

	2016	2015	2014	2013	2012
Assets					
Cash and deposits with banks	41,725	30,489	26,798	26,060	16,671
Securities	10,262	11,845	14,259	7,000	9,041
Securities loaned or acquired in resale agreements	9	71	107	70	207
Loans to the public	172,779	160,604	148,912	139,880	130,244
Provision for credit losses	(1,438)	(1,400)	(1,343)	(1,315)	(1,593)
Loans to the public, net	171,341	159,204	147,569	138,565	128,651
Loans to Governments	330	316	307	305	317
Investments in associates	34	36	52	60	60
Buildings and equipment	1,585	1,583	1,570	1,536	1,548
Intangible assets and goodwill	87	87	87	87	87
Assets with respect to derivative instruments	3,584	3,527	5,602	3,606	3,518
Other assets	1,498	2,000	2,162	2,256	2,032
Total assets	230,455	209,158	198,513	179,545	162,132
Liabilities and Equity					
Deposits from the public	178,252	162,380	152,379	141,244	128,499
Deposits from banks	1,537	1,166	1,258	2,041	1,694
Deposits from the Government	50	58	55	62	107
Securities loaned or sold in conjunction with repurchase agreements	–	–	223	–	–
Debentures and subordinated notes	27,034	23,719	20,580	16,443	14,039
Liabilities with respect to derivative instruments	3,566	3,634	6,497	3,538	3,773
Other liabilities	6,692	5,786	6,217	6,058	4,849
Total liabilities	217,131	196,743	187,209	169,386	152,961
Shareholders' equity **attributable to shareholders of the Bank**	12,714	11,847	10,797	9,681	8,730
Non-controlling interests	610	568	507	478	441
Total equity	13,324	12,415	11,304	10,159	9,171
Total liabilities and equity	230,455	209,158	198,513	179,545	162,132

Addendum 3 – Multi-quarter information

Consolidated Statement of Profit and Loss by Quarter - for 2016

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest revenues	1,254	1,601	1,588	868
Interest expenses	306	545	574	108
Interest revenues, net	948	1,056	1,014	760
Expenses with respect to credit losses	81	59	57	3
Interest revenues, net after expenses with respect to credit losses	867	997	957	757
Non-interest revenues				
Non-interest financing revenues (expenses)	119	40	69	67
Fees	356	360	352	365
Other revenues	14	20	11	89
Total non-interest revenues	489	420	432	521
Operating and other expenses				
Payroll and associated expenses	566	508	520	477
Maintenance and depreciation of buildings and equipment	171	177	171	174
Other expenses	132	130	145	128
Total operating and other expenses	869	815	836	779
Pre-tax profit	487	602	553	499
Provision for taxes on profit	212	218	200	203
After-tax profit	275	384	353	296
Share in net profits of associates, after tax	(1)	1	–	–
Net profit:				
Before attribution to non-controlling interests	274	385	353	296
Attributable to non-controlling interests	(9)	(12)	(13)	(8)
Attributable to shareholders of the Bank	265	373	340	288
Earnings per share[(1)]				
Basic earnings per share (in NIS)				
Total net profit attributable to shareholders of the Bank	1.14	1.61	1.47	1.24
Diluted earnings per share (in NIS)				
Total net profit attributable to shareholders of the bank	1.14	1.61	1.47	1.24

(1) Share of NIS 0.1 par value each.

Addendum 3 – Multi-quarter information

Consolidated Statement of Profit and Loss by Quarter - for 2015 – continued

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest revenues	1,010	1,495	1,851	550
Interest expenses	190	562	769	(149)
Interest revenues, net	820	933	1,082	699
Expenses with respect to credit losses	75	61	40	35
Interest revenues, net after expenses with respect to credit losses	745	872	1,042	664
Non-interest revenues				
Non-interest financing revenues (expenses)	127	151	(45)	125
Fees	355	350	365	356
Other revenues	35	8	10	21
Total non-interest revenues	517	509	330	502
Operating and other expenses				
Payroll and associated expenses	499	487	492	466
Maintenance and depreciation of buildings and equipment	169	175	174	174
Other expenses	151	159	159	121
Total operating and other expenses	819	821	825	761
Pre-tax profit	443	560	547	405
Provision for taxes on profit	197	213	204	147
After-tax profit	246	347	343	258
Share in net profit (loss) of associates, after tax	–	1	–	(1)
Net profit:				
Before attribution to non-controlling interests	246	348	343	257
Attributable to non-controlling interests	(6)	(32)	(13)	(9)
Attributable to shareholders of the Bank	240	316	330	248
Earnings per share[1]				
Basic earnings per share (in NIS)				
Total net profit attributable to shareholders of the Bank	1.04	1.36	1.43	1.06
Diluted earnings per share (in NIS)				
Total net profit attributable to shareholders of the Bank	1.03	1.36	1.42	1.05

(1) Share of NIS 0.1 par value each.

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Addendum 3 – Multi-quarter information

Consolidated balance sheet as of the end of each quarter in 2016

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Assets				
Cash and deposits with banks	41,725	40,753	36,842	38,193
Securities	10,262	9,407	8,419	9,013
Securities loaned or purchased in resale agreements	9	16	46	151
Loans to the public	172,779	170,024	166,914	163,451
Provision for credit losses	(1,438)	(1,404)	(1,399)	(1,378)
Loans to the public, net	171,341	168,620	165,515	162,073
Loans to the Government	330	353	363	323
Investments in associates	34	34	35	36
Buildings and equipment	1,585	1,537	1,545	1,546
Intangible assets and goodwill	87	87	87	87
Assets with respect to derivative instruments	3,584	3,267	3,460	3,922
Other assets	1,498	1,446	1,446	1,465
Total assets	230,455	225,520	217,758	216,809
Liabilities and Equity				
Deposits from the public	178,252	173,748	169,621	165,001
Deposits from banks	1,537	1,255	1,183	1,416
Deposits from the Government	50	53	53	55
Debentures and subordinated notes	27,034	27,253	24,337	26,859
Liabilities with respect to derivative instruments	3,566	3,520	3,787	4,878
Other liabilities	6,692	6,365	5,806	5,928
Total liabilities	217,131	212,194	204,787	204,137
Equity attributable to equity holders of the Bank	12,714	12,726	12,384	12,098
Non-controlling interests	610	600	587	574
Total equity	13,324	13,326	12,971	12,672
Total liabilities and equity	230,455	225,520	217,758	216,809

Addendum 3 – Multi-quarter information

Consolidated balance sheet as of the end of each quarter in 2015 – continued

Reported amounts (NIS in millions)

	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Assets				
Cash and deposits with banks	30,489	26,720	25,318	25,455
Securities	11,845	11,306	15,833	13,802
Securities loaned or purchased in resale agreements	71	100	–	300
Loans to the public	160,604	159,382	153,688	152,049
Provision for credit losses	(1,400)	(1,386)	(1,371)	(1,355)
Loans to the public, net	159,204	157,996	152,317	150,694
Loans to the Government	316	287	273	299
Investments in associates	36	39	38	45
Buildings and equipment	1,583	1,543	1,545	1,544
Intangible assets and goodwill	87	87	87	87
Assets with respect to derivative instruments	3,527	4,780	4,478	5,694
Other assets	2,000	2,108	1,875	3,052
Total assets	209,158	204,966	201,764	200,972
Liabilities and Equity				
Deposits from the public	162,380	158,107	153,736	153,002
Deposits from banks	1,166	1,298	1,903	1,472
Deposits from the Government	58	62	60	59
Securities loaned or sold in conjunction with repurchase agreements	–	–	–	240
Debentures and subordinated notes	23,719	23,196	22,648	20,804
Liabilities with respect to derivative instruments	3,634	4,527	5,350	7,260
Other liabilities	5,786	5,598	6,271	6,587
Total liabilities	196,743	192,788	189,968	189,424
Equity attributable to equity holders of the Bank	11,847	11,616	11,266	11,033
Non-controlling interests	568	562	530	515
Total equity	12,415	12,178	11,796	11,548
Total liabilities and equity	209,158	204,966	201,764	200,972

Addendum 4 – Additional information

Subsidiaries in which the Bank holds less than 50% of means of control

Had the Bank not consolidated the financial statements of Bank Yahav, the consolidated financial statements (excluding Bank Yahav) would have been similar to the Bank's (solo) financial statements as presented in Note 36 to the financial statements, except for the following material changes:

Balance sheet highlights (as of December 31, 2016)

- The balance of investment in associates would have been lower by NIS 1.6 billion.
- The balance of deposits from the public would have been lower by NIS 24.3 billion.
- The balance of debentures and subordinated notes would have been higher by NIS 23.5 billion.

Profit and loss highlights (for 2016)

- Total non-interest revenues would have been higher by NIS 130 million.
- The share of net profit of associates, after tax effect, would have been lower by NIS 90 million.

Glossary and index of terms included on the annual financial statements

Below is a summary of terms included on the financial statements and and index for these terms

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

Term	Explanation	Location on the financial statements
Basel Committee	The Basel Committee is a forum for cooperation on matters of bank supervision. The Committee's objectives are to increase understanding in key supervision issues and to improve the quality of supervision over banking corporations around the world. The Committee is mostly known for the international standards on capital adequacy, core principles for effective supervision over banks and for coordination between different countries in order to create cross-border supervision over banks world-wide.	This term appears multiple times.
Basel II	A framework for assessment of capital adequacy and risks management, published in its final version by the Basel Committee on Bank Supervision in 2006.	This term appears multiple times.
Basel III	A framework for assessment of capital adequacy and risks management, initially published by the Basel Committee on Bank Supervision in 2010.	This term appears multiple times.
Business continuity	A situation where the Bank operates continuously and with no disruption.	Chapter "Risks overview" and chapter "Overview, targets and strategy" of the Report of the Board of Directors and Management
Compliance and regulatory risk	The risk of imposition of legal or regulatory sanctions, material financial loss or impact to Bank image, which the Bank may incur due to its failure to comply with compliance provisions (such as: statutory provisions, regulation, standards and conduct commonly expected from the corporation).	Chapter "Overview, targets and strategy", chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management
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.	Chapter "Risks Overview" in the Report of the Board of Directors and Management Term included in Notes to the financial statements
Credit rating (score)	A credit rating is a score assigned to a borrower, as part of assessment of its capacity to fulfill its obligations when due and in full.	Chapter "Risks overview" of the Report of the Board of Directors and Management - term included in Notes to the financial statements
Credit risk	Credit risk is the risk that a borrower or counter-party of the Bank would not fulfill its obligations towards the Bank.	This term appears multiple times.

Term	Explanation	Location on the financial statements
Credit Valuation Adjustment risk (CVA)	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).	Term included in Notes to the financial statements
Cross-border risk	The risk of financial loss (including due to legal proceedings, fines or sanctions imposed by statutory authorities or others in Israel and in other countries) and of impact to reputation, arising from the Bank's failure to comply with statutory provisions originating in other countries – whether provisions binding on the Bank or provisions which are not binding, but failure to comply with them may cause the Bank to incur damage, or from overseas activities of Bank clients in contravention of any statutory provisions.	Chapter "Overview, targets and strategy", chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management
Economic value approach - EVE - Economic Value of Equity	The economic value approach to analysis and estimation of the effect of changes in interest rates on the fair value of assets, liabilities and off-balance sheet positions of the Bank.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
External credit rating agencies	Rating agencies which provide external credit ratings and recognized by the Supervisor of Banks, in conformity with specified qualification requirements. Qualified external credit rating agencies are: S&P, Moody's and Fitch.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Financing risk	Financing risk, or funding liquidity risk, is the risk that the corporation would not be able to efficiently service its cash flows and collateral needs, both expected and unexpected, both present and future, without this affecting its day-to-day operations or its financial standing.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Inflation risk	Exposure to loss due to the effect of changes in the Consumer Price Index on profit or capital of the corporation, including through effect on off-balance sheet items.	Chapter "Risks Overview" of the Report of the Board of Directors and Management

Term	Explanation	Location on the financial statements
Interest risk	The risk to Bank profit (change in revenues) or 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).	Chapter "Overview, targets and strategy" and chapter "Risks overview" in the Report of the Board of Directors and Management
KPIs – Key performance indicators	Key performance indicators, used as a tool to formulate insights about the status of process execution across the Bank.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
KRI - Key risk indicators	Key risk indicators are risk benchmarks and/or statistical benchmarks used to monitor key factors associated with key risks factors at the banking corporation, in order to try and diagnose risk materialization, as early as possible.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Legal risk	Legal risk is part of operating risk and includes the risk of loss due to exposure to fines, lawsuits and/or punitive action due to breach of contract or disagreements. Legal risk includes risks arising from legal exposure due to Bank conduct with its various interested parties (such as: clients, suppliers and other third parties).	Chapter "Overview, targets and strategy", chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management
Liquidity risk	The risk to profit and stability of the banking corporation, due to its inability to satisfy its liquidity requirements.	Chapter "Overview, targets and strategy", chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management
Loan to Value (LTV) ratio	The ratio between the approved facility when extended and the asset value.	This term appears multiple times.
Market risk	This is the risk of loss in 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).	This term appears multiple times.
Minimum capital ratio	This ratio reflects the minimum supervisory capital requirement which the Bank is required to maintain in conformity with Proper Banking Conduct Directive 201.	Chapter "Overview, targets and strategy" in the Report of the Board of Directors and Management Term included in Notes to the financial statements

Term	Explanation	Location on the financial statements
Operating risk	The risk of loss due to inappropriateness or failure of internal processes, people and systems or due to external events. This risk is inherent in all products, activities, processes and systems.	This term appears multiple times.
Pillar 1	The first pillar of the Basel II project, includes calculation of minimum capital requirements with respect to credit risk (including counter-party risk), market risk (negotiable portfolio only) and operating risk.	Chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management
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.	Chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management
Reputation risk	Reputation is a set of concepts, ideas and beliefs by interested parties about the corporation, based on their experience and expectations. Reputation risk is the risk to corporate profit, stability or capacity to achieve its objectives, due to impact to reputation which may arise from practices applied by the corporation, its financial standing or negative publicity (whether true or false).	Chapter "Overview, targets and strategy" and chapter "Risks overview" in the Report of the Board of Directors and Management
Risk	Risk is the potential (likelihood) of impact to capital, profit, stability of the corporation or its capacity to achieve its business objectives.	This term appears multiple times.
Risk appetite	A decision made by the Bank with regard to the risk level which the banking corporation is willing to assume, given the risk / reward attributes.	Chapter "Overview, targets and strategy", chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management
Risk assets	These consist of credit risk, operating risk and market risk, calculated using the standard approach as stated in Proper Banking Conduct Directives 201-211.	This term appears multiple times.

Term	Explanation	Location on the financial statements
Risk profile	Assessment of the aggregate risk inherent in exposures and business operations of the Bank at a certain point in time.	Chapter "Overview, targets and strategy", chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management
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 sent to the Board of Directors quarterly.	Chapter "Overview, targets and strategy" and chapter "Risks overview" in the Report of the Board of Directors and Management
Risks management framework	A framework for risks management, which includes policy, procedures, measurement, risk appetite and controls for risks management.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Standard approach	An approach used to calculate the required capital with respect to credit risk, market risk or operating 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.	Chapter "Explanation and analysis of results and business standing", chapter "Risks overview" and chapter "Policies and critical accounting estimates" Term included in Notes to the financial statements
Strategic risk	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.	Chapter "Risks overview" and chapter "Overview, targets and strategy" of the Report of the Board of Directors and Management
Stress tests	A title for various methods used to assess the financial standing of a banking corporation under a scenario.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Supervisory capital (total capital)	Supervisory capital consists of two tiers: – Tier I equity , which includes Tier I shareholder equity and additional Tier I equity. – Tier II equity. As defined in Proper Banking Conduct Directive 202 "Measurement and capital adequacy – supervisory capital".	Chapter "Overview, targets and strategy" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management - term included in Notes to the financial statements

Term	Explanation	Location on the financial statements
Three lines of defense	The risks management concept is divided into three lines of defense: First line – risks takers: Business line management is responsible for identification, assessment, measurement, monitoring, mitigation and reporting of the inherent risks. It is also responsible for management of an appropriate control environment for risk management. Second line – risk controllers: The risks management function is tasked with complementing the risks management activities by the line of business. Responsible, *inter alia*, for planning and development of a risks management framework and for challenging risks management by the lines of business. Third line – Internal Audit conducts an independent review and challenges the controls, processes and systems used for risks management.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
VaR	A model used to estimate overall exposure to diverse market risk factors. The VaR (Value at Risk) obtained by the model is a statistical estimate of the maximum expected loss for the Bank due to materialization of market risks factors in a given time period at a pre-determined statistical confidence level.	Chapter "Risks Overview" of the Report of the Board of Directors and Management

2. Terms with regard to banking and finance

Term	Meaning	Report chapter
Asset and Liability Management (ALM)	A technique applied by organizations to align the composition of assets and liabilities in order to ensure an adequate return on equity. This means management of risks arising from gaps between the composition of assets and liabilities, at the business level. This includes processes for management of market and liquidity risks, setting shadow pricing etc.	Chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management – term included in Notes to the financial statements
Average effective duration	The average term to maturity of debentures. Measured in years, by weighting principal and interest payments for the debenture over its term to final maturity. The average effective duration of a debenture reflects the financial instrument's sensitivity to changes in interest rates. Average effective duration is calculated as the ratio between the weighted average debenture payouts to its price.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Banking portfolio / non-negotiable portfolio	The banking portfolio, which is the Bank's primary activity, consists of all transactions not included in the negotiable portfolio, including financial derivatives used to hedge the banking portfolio.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Credit control	A review process designed to assess performance of the team involved in extending credit and the overall status of the credit portfolio. This process is retroactively conducted by the Bank's Credit Control Department; the review includes a review of rating reliability and appropriateness of classification and provision.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Debt under restructuring	Problematic debt under restructuring is defined as debt for which, for economic or legal reasons related to financial difficulties of the debtor, the Bank has made a concession by way of modification to terms and conditions of the debt, designed to make it easier for the debtor to make cash payments in the near term (reduction or postponement of cash payments due from the debtor), or by way of receiving other assets as debt repayment (in whole or in part).	Chapter "Overview, targets and strategy" and chapter "Risks overview" of the Report of the Board of Directors and Management - term included in Notes to the financial statements
Debt under special supervision	Debt under special supervision is debt with potential weaknesses, which require special attention by Bank management. Should these weaknesses not be addressed, the likelihood of debt repayment may deteriorate.	Chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management Term included in Notes to the financial statements

Term	Meaning	Report chapter
Derivatives	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.	This term appears multiple times.
Financial covenants	Covenants agreed between lender and borrower in the loan contract, which specify suspensive conditions for extending credit, such as achieving certain financial ratios. Occasionally, a breach of such condition may give cause to demand immediate repayment of the credit.	Chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management
Financial project assistance	A method for financial project assistance (closed assistance) is a financing method where the borrower expects to be repaid primarily from expected project receipts, which are both the repayment source and the collateral for exposure. As part of this method, the financed projects are closely monitored.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
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 Banking Conduct Directive 314 on problematic debt in housing loans.	This term appears multiple times.
Inferior debt	Inferior debt is debt insufficiently secured by collateral or by debtor repayment capacity, and for which the Bank may incur a loss if faults are not corrected, including debt over NIS 700 thousand which is 60-89 days in arrears.	Chapter "Explanation and analysis of results and business standing" and chapter "Risks overview" in the Report of the Board of Directors and Management Term included in Notes to the financial statements
Loan repayment to income ratio	The ratio between monthly payment and available monthly income. This ratio is a benchmark used for assessment of the current repayment capacity of the borrower over the term of the loan.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
Minimum liquidity coverage ratio	The ratio of liquidity cushion to net forecasted cash outflows for the next month, under various scenarios.	Chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management

Term	Meaning	Report chapter
Negotiable portfolio	The Bank's negotiable portfolio includes the portfolios managed as market maker in the trading room, as well as portfolios of securities held for trade and transactions in derivatives conducted as part of a specific market strategy, managed by Financial Management under specific limitations on exposure and profitability.	Chapter "Risks Overview" of the Report of the Board of Directors and Management
OTC - Over the Counter	Transaction involving financial instruments which is conducted over the counter and not on a stock exchange.	Chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management - term included in Notes to the financial statements
Problematic debt	Debt classified under one of the following negative classifications: special supervision, inferior or impaired.	This term appears multiple times.
Provision for credit losses	A provision designed to cover expected credit losses in the Bank's credit portfolio. These losses reflects the net write-off amount which is likely to materialize for a loan or loan group, given the facts and circumstances as of the evaluation date.	This term appears multiple times.

2. Terms with regard to regulatory directives

Term	Meaning	Report chapter
FATCA - Foreign Accounts Tax Compliance Act	The US Foreign Accounts Tax Compliance Act stipulates mandatory reporting to the US tax authority (IRS) of accounts held by US persons with foreign financial institutions (outside the USA).	Chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management
LCR – Liquidity Coverage Ratio	Liquidity Coverage Ratio is defines 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.	Chapter "Risks overview" and chapter "Explanation and analysis of results and business standing" of the Report of the Board of Directors and Management

3. Other terms

Term	Meaning	Report chapter
Corporate governance	The ensemble of relations between management, the Board of Directors, shareholders and interested parties which form the structure used to determine Bank objectives and the means to achieve and to monitor these objectives. Corporate governance also supports definition of roles and responsibilities as well as the decision-making process.	This term appears multiple times.

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