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MIZRAHI TEFAHOT BANK LTD

No. with the Registrar of Companies: 520000522

To	<u>Israel Securities Authority</u>	To	<u>Tel Aviv Stock Exchange Ltd</u>	T125 (Public)	Date of transmission: July 22, 2021
	www.isa.gov.il		www.tase.co.il		Ref: 2021-01-121035

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

On July 21, 2021, *S&P Global Rating* published:

A rating report/notice *updated*

A notice regarding rating cessation

1. Rating report or notice

- Corporation's rating: *Other S&P Global Rating A-/A-2 positive*
Comments/Notice summary: *Raised outlook/projection*

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

Date	Rating subject	Rating	Comments/Notice summary
March 18 2021	<i>Mizrahi Tefahot Bank Ltd</i>	<i>Other S&P Global Rating A-/A-2 stable</i>	<i>Initial rating</i>

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

Rating of the corporation's bonds:

Name and type of security	Security number on the stock exchange	Rating company	Current rating	Comments/Notice summary
<i>MizrahiTF \$2031RM</i>	6950836	<i>Other S&P Global Ratings</i>	<i>Other BBB-None/NOO</i>	<i>Rating affirmation</i>

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

Name and type of security	Security number on the stock exchange	Date	Type of rated security	Rating	Comments/Notice summary
<i>MizrahiTF \$2031RM</i>	6950836	<i>March 18 2021</i>	<i>Debentures</i>	<i>Other BBB-None/N OO</i>	<i>Initial rating</i>

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

Attached rating report [GlobalSP isa.pdf](#)

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

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

	Signatory's Name	Position
1	<i>Ofer Horvitz</i>	<i>Other Bank Secretary & Head of the Bank's Headquarters</i>

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

S&P Global Ratings Company has confirmed the bank's long-term issuer credit rating at A-, the bank's short-term issuer credit rating at A-2, and updated the long-term outlook to 'positive'. For further information on said rating, see the attached documenty.

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

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

Form structure revision date: June 15, 2021

Abbreviated Name: Mizrahi Tefahot

Address: 7 Jabotinsky Street, Ramat Gan, 52520 Tel:03-7559720 Fax:03-7559923

E-mail: mangment@umtb.co.il Company website: <https://www.mizrahi-tefahot.co.il>

Previous name of the reporting entity: United Mizrahi Bank Ltd

Name of the person reporting electronically: Horvitz Ofer Position: Bank Secretary Name of Employing Company: Mizrahi Tefahot Bank Ltd

Address: 7 Jabotinsky Street, Ramat Gan, 52520 Tel: 03-7559207 Fax: 03-7559913 E-mail: management@umtb.co.il

Research Update:

Mizrahi Tefahot Bank Outlook Revised To Positive On Resilient Risk Profile And Capital Buffers; Affirmed At 'A-/A-2'

July 21, 2021

Overview

- Mizrahi Tefahot Bank Ltd. (Mizrahi) has maintained sound asset quality and strong capital buffers in the past few years while demonstrating resilience to the economic impact of the COVID-19 pandemic.
- The recently completed merger and ongoing integration of Union Bank will likely further strengthen Mizrahi's creditworthiness, alongside the successful implementation of the bank's new five-year strategy.
- We therefore revised our outlook on Mizrahi to positive from stable and affirmed our 'A-/A-2' ratings on the bank.
- The positive outlook indicates that we could raise our ratings over the next two years if the bank successfully delivers on its commitments under the new strategic plan and improves its product diversification, profitability, and efficiency while maintaining solid credit quality and capital ratios.

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Rating Action

On July 21, 2021, S&P Global Ratings revised its outlook on Israel-based Mizrahi Tefahot Bank Ltd. to positive from stable.

At the same time, we affirmed our 'A-/A-2' long- and short-term issuer credit ratings on the bank.

Rationale

The rating actions stem from our view that Mizrahi could strengthen its business and risk profiles through its merger with Union Bank after demonstrating resilience to the pandemic's impact. We expect the merger with Union Bank to strengthen Mizrahi's brand and domestic

positioning as the third largest bank in Israel. Mizrahi's asset quality metrics and capitalization remained sound despite the pandemic-related economic stress and the consolidation of Union Bank. In 2020, at 9.24%, Mizrahi's return on equity (according to our calculations) exceeded those of domestic and foreign peers. This is despite an elevated cost of risk due to the pandemic (not taking into account the impact of the merger with Union Bank, since Mizrahi's 2020 financials consolidated Union Bank only at the balance-sheet level). Union Bank's merger further boosted Mizrahi's return on equity to 14.15% (according to our calculations) in first-quarter 2021, which is well above that of most peers.

Mizrahi's risk profile compares adequately with higher-rated domestic and global peers'.

During the five years preceding the pandemic, Mizrahi's cost of risk (measured by new loan loss provision to average customer loans) averaged 14 basis points, ranking in the middle of the peer group (a sample of eight banks domiciled in Israel, Czech Republic, and Denmark). At 1.04% of total loans on Dec. 31, 2020, its gross nonperforming assets was the lowest among peers. Given its focus on lending to households, Mizrahi's lending book exhibits lower single-party concentration than domestic peers. Similarly, at about 9.2% of gross loans on the same date, Mizrahi's exposure to real estate and construction was well below domestic peers.

Mizrahi's high capital cushion helped it absorb the negative impact of the pandemic and the merger of Union bank.

Mizrahi's risk-adjusted capital (RAC) ratio dropped to 10.5% at year-end 2020 from 11.6% a year ago, largely reflecting the merger of Union Bank. Our RAC ratios differ from the bank's reported regulatory capital ratios owing to our risk weights for all asset classes. We forecast our RAC ratio for Mizrahi will gradually improve beyond 11% by the end of 2023. In our base-case scenario, we assume a normalization of credit costs starting from this year, coupled with about 6% annual loan growth. The net interest margin should show only a marginal contraction despite current low rates, given higher margins for business lending where the bank plans to expand faster. We assume a gradual resumption of dividend payouts in 2021, eventually increasing to the bank's stated target payout ratio of up to 50%.

The 2021-2025 strategic plan aims at leveraging the Union Bank merger as a platform for rapid growth in business-sector lending while consolidating Mizrahi's leading position among households.

Even after the merger, Mizrahi's loan book remains skewed toward households, with mortgage loans standing at about 64% of gross loans on March 31, 2021. The planned fast lending growth in the middle market and corporate segments (about 8% per annum until 2025) will help the bank diversify its loan and revenue split by customer and product type. We note that this rapid growth could hurt its asset quality should the economic rebound lose momentum, or if Mizrahi compromises its currently prudent lending standards for example, if the pandemic lingers, which is not our base case expectation, however. Yet, even in such an adverse scenario, asset-quality deterioration will be from a very solid base, and the bank has sufficient earnings and capital buffers to absorb elevated losses. Of note, while Mizrahi's mortgage book has performed well so far, we remain cautious regarding the bank's rising exposure to the residential property, especially considering the market's recent heating. We are mindful that a reversal in the current trend--notably prices--could trigger imbalances and higher credit risks for banks.

It remains to be seen when and to what extent expected operational and cost synergies from the merger will materialize.

With a cost to income (C/I) ratio of 54.2% in 2020 (54.6% in 2019), Mizrahi is already one of the most efficient banks in its peer group. In addition, its return on equity averaged 10% in the past four years and exceeded the average of domestic and global peers. The bank's new strategic plan aims at bringing its C/I ratio below 50% by the end of 2025. We view the

plan as somewhat ambitious despite the expected cost synergies from the Union Bank merger. Mizrahi has the lowest headcount among peers but is targeting further savings through reducing the number of Union Bank employees. Additional cost savings will come from a reduction of the branch network as well as from digitalization, which comes with a high price. Mizrahi and its domestic peers have been investing heavily in their IT systems to stave off stiff competition, notably in the retail segment.

We believe integration risks are manageable, given the relatively smaller size of Union Bank.

We see Mizrahi's management team as highly professional and experienced and believe they are capable of successfully completing the merger and integrating Union Bank.

We believe the funding profile of Mizrahi and industrywide is sound, which we also regard as a strength in our Banking Industry Country Risk Assessment (BICRA) for Israel.

In our view, the bank benefits from sound liquidity, supported by its stable and well-diversified domestic funding sources, including a strong retail base. Its key funding and liquidity ratios compare adequately with peers'.

Because we consider Mizrahi a systemically important bank in Israel, our ratings also benefit from expected extraordinary government support for the bank.

We classify Mizrahi as having high systemic importance and consider Israel to be supportive toward the domestic banking sector. This is reflected in our ratings on Mizrahi being one notch above the bank's stand-alone credit profile.

Outlook

The positive outlook on Mizrahi reflects our expectation that the bank is emerging from the pandemic with limited asset quality problems, a strong capital buffer, and improved earnings relative to 2020. In addition, we expect its creditworthiness to benefit from the ongoing integration of recently acquired Union Bank.

Upside scenario

We could raise the ratings by one notch over the next 12-24 months if we conclude that Mizrahi can maintain its solid risk profile and strong capitalization while implementing its new strategic plan, while successfully integrating Union Bank. An upgrade will hinge upon the bank's accelerated growth in new segments not bringing additional risks and remaining supportive to its overall capitalization.

We will monitor the evolution of asset quality, efficiency, and profitability metrics in comparison with those of higher-rated peers' as Mizrahi starts realizing targeted cost synergies after the merger.

Downside scenario

Should the bank fail to maintain its solid risk profile, such that its asset-quality metrics weaken, for example because of higher credit losses than we expect from the anticipated fast growth, we could revise the outlook to stable. An outlook revision could also stem from the bank failing to withstand competitive pressure in Israel and losing market share and revenue, to the detriment of its profitability.

Ratings Score Snapshot

Issuer Credit Ratings	A-/Positive/A-2
SACP	bbb+
Anchor	bbb+
Business position	Adequate (0)
Capital and earnings	Strong (+1)
Risk position	Moderate (-1)
Funding and	Average and (0)
Liquidity	Adequate
Support	+1
ALAC support	0
GRE support	0
Group support	0
Sovereign support	+1
Additional factors	0

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov. 9, 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Banking Industry Country Risk Assessment Update: June 2021, June 29, 2021
- Israel Ratings Affirmed At 'AA-/A-1+'; Outlook Stable, May 14, 2021
- Mizrahi Tefahot Bank Ltd. Assigned 'A-/A-2' Ratings; Outlook Stable, March 18, 2021

- Banking Industry Country Risk Assessment: Israel, July 15, 2020
- Tech Disruption In Retail Banking: The Regulator Is Moving Israeli Banks Into A Digital Future, Feb. 5, 2020

Ratings List

Ratings Affirmed

Mizrahi Tefahot Bank Ltd.

Junior Subordinated	BBB-
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Ratings Affirmed; Outlook Action

	To	From
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Mizrahi Tefahot Bank Ltd.

Issuer Credit Rating	A-/Positive/A-2	A-/Stable/A-2
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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