Bank Hapoalim

Report on Risks

Pillar 3 Disclosure and Additional Information Regarding Risks

as at March 31, 2019

Q1

bank hapoalim

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This is a translation of the Hebrew report and has been prepared for convenience only.
In case of any discrepancy, the Hebrew version will prevail.

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Report on Risks

We are honored to present the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at March 31, 2019 (hereinafter: the "Report on Risks" or the "Report").

The information in this Report, as required by the reporting directives of the Bank of Israel, includes disclosure requirements issued by the Basel Committee and risk disclosure requirements based on other sources, including disclosure requirements issued by the Financial Stability Forum (FSF) and disclosure requirements issued by a task force established by the Financial Stability Board (FSB) in order to improve risk disclosure at banking corporations.

The activity of the Isracard Group has been classified as a "discontinued operation" since the financial statements for the second quarter of 2018. The data of the Isracard Group are therefore not presented in most of the detailed information below, including restatement of comparative periods (except where otherwise noted). For further details, see Note 1E to the Condensed Financial Statements as at March 31, 2019.

This Report on Risks is published within the Financial Statements of Bank Hapoalim B.M., and contains extensive information regarding the management of risks and capital. This report should be perused in conjunction with the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018; the Annual Financial Statements for 2018; and the Condensed Financial Statements as at March 31, 2019.

Sincerely yours,

Oded Eran	**Ari Pinto**	**Amir Bachar**
Chairman of the	President and	Senior Deputy Managing Director
Board of Directors	Chief Executive Officer	Chief Risk Officer

Tel Aviv, May 28, 2019

A. Introduction

A.1. Forward-looking information

Most of the information in this report that does not refer to historical facts (even if it is based on processing of historical data) constitutes forward-looking information, as defined in the Securities Law, 1968. The actual results of the Bank may differ materially from those included in forward-looking information, including, among other factors, as a result of changes in capital markets in Israel and globally, macro-economic changes, changes in geopolitical conditions, regulatory changes, accounting changes, changes in taxation rules, and other changes not under the Bank's control, which may lead to the failure of estimates to materialize and/or to changes in the Bank's business plans. Forward-looking information is marked by words or phrases such as "forecast," "plan," "objective," "risk estimate," "scenario," "stress scenario," "risk assessment," "correlation," "distribution," "we believe," "expect," "predict," "estimate," "intends," "plans," "aims," "may change," "should," "can," "will," or similar expressions. Such forward-looking expressions involve risk and uncertainty, because they are based on management's estimates regarding future events, which include changes in the following parameters, among others: economic conditions, public tastes, interest rates in Israel and overseas, inflation rates, new legislation and regulation in the area of banking and the capital market, exposure to financial risks, the financial stability of borrowers, the behavior of competitors, aspects related to the Bank's image, technological developments, manpower-related matters, and other areas that affect the activity of the Bank and the environment in which it operates, the materialization of which is uncertain by nature.

This information reflects the Bank's current viewpoint with regard to future events, which is based on estimates, and is therefore subject to risks and uncertainty, as well as to the possibility that expected events or developments may not materialize at all or may only partially materialize, or even that actual developments may be the opposite of expectations.

The information presented below is based, among other things, on information known to the Bank and based, among other things, on publications by various entities, such as the Central Bureau of Statistics, the Ministry of Finance, the Bank of Israel, the Ministry of Housing, and other entities that publish data and estimates regarding the Israeli and global capital markets.

A.2. Disclosure declaration

Pursuant to the instructions of the Bank of Israel, the disclosure declarations in the periodic financial report of the Bank are also valid for the Report on Risks – Pillar 3 Disclosure and Additional Information Regarding Risks. Within the discussions of the condensed financial statements of the Bank, the Board of Directors of the Bank approved the publication of the Report on Risks – Pillar 3 Disclosure and Additional Information Regarding Risks as at March 31, 2019.

B. Principal supervisory ratios, risk-management review, and weighted risk-adjusted assets

B.1. Principal supervisory ratios

Table B-1: Principal supervisory ratios

	On a consolidated basis, as at				
	March 31, 2019	December 31, 2018	September 30, 2018	June 30, 2018	March 31, 2018
	NIS millions				
Available capital					
Common equity Tier 1 capital	**38,903**	38,004	38,112	37,178	36,637
Common equity Tier 1 capital before effect of transitional directives(1)	**38,484**	37,547	37,617	36,645	36,065
Tier 1 capital	**39,636**	38,981	39,089	38,155	37,614
Tier 1 capital before effect of transitional directives(1)	**38,484**	37,547	37,617	36,645	36,065
Total capital	**49,072**	49,023	49,723	48,771	46,630
Total capital before effect of transitional directives(1)	**44,158**	*43,284	*43,301	*42,297	39,863
Risk-weighted assets					
Total risk-weighted assets (RWA)	**339,691**	340,597	336,678	333,206	331,539
Total risk-weighted assets (RWA) before effect of transitional directives(1)	**340,277**	341,236	337,370	333,951	332,337
Capital-adequacy ratios according to the directives of the Banking Supervision Department					
Common equity Tier 1 capital ratio	**11.45%**	11.16%	11.32%	11.16%	11.05%
Common equity Tier 1 capital ratio before effect of transitional directives(1)	**11.31%**	11.00%	11.15%	10.97%	10.85%
Tier 1 capital ratio	**11.67%**	11.44%	11.61%	11.45%	11.35%
Tier 1 capital ratio before effect of transitional directives(1)	**11.31%**	11.00%	11.15%	10.97%	10.85%
Total capital ratio	**14.45%**	14.39%	14.77%	14.64%	14.06%
Total capital ratio before effect of transitional directives(1)	**12.98%**	*12.68%	*12.83%	*12.67%	11.99%
Common equity Tier 1 capital ratio required by the Banking Supervision Department(2)	**10.24%**	10.24%	10.24%	10.23%	10.23%
Available common equity Tier 1 capital ratio beyond the requirement of the Banking Supervision Department(2)	**1.21%**	0.92%	1.08%	0.93%	0.82%
Leverage ratios according to the directives of the Banking Supervision Department					
Total exposures	**523,012**	518,980	512,146	516,190	509,845
Total exposures before effect of transitional directives(1)	**523,246**	519,236	512,423	516,488	510,164
Leverage ratio	**7.58%**	7.51%	7.63%	7.39%	7.38%
Leverage ratio before effect of transitional directives(1)	**7.35%**	7.23%	7.34%	7.10%	7.07%

* Restated.

(1) Before the effect of the transitional directives, including the effect of the adoption of US GAAP on employee benefits, and before the effect of Efficiency Plan Adjustments.

(2) Including a capital requirement at a rate representing 1% of the balance of housing loans at the dates of the financial statements.

Table B-1: Principal supervisory ratios (continued)

	For the three months ended				
	March 31, 2019	December 31, 2018	September 30, 2018	June 30, 2018	March 31, 2018
Liquidity coverage ratio according to the directives of the Banking Supervision Department					
Total high-quality liquid assets	**109,781**	106,375	109,043	110,310	108,529
Total net cash outflows	**87,721**	88,515	89,726	89,479	91,418
Liquidity coverage ratio (in %)	**125%**	120%	122%	123%	119%

B.2. Risk assessment and management

The Bank performs comprehensive examinations to assess the risks to which it is exposed and to estimate the materiality of such risks. Within the ICAAP (the Internal Capital Adequacy Assessment Process), the Bank defined the following risks as material risks: credit risk, concentration risk, market risk, investment risk, operational risk (including IT risk and cyber risk), counterparty risk, interest-rate risk in the banking book, liquidity risk, reputational risk, strategic and competitive risk, regulatory risk, and compliance risk. Other risks to which the Bank is exposed are handled directly as part of the management of its business: legal risk, economic risk, and environmental risk.

Risk management is performed based on a global view of the Bank's activity in Israel and of activity at the Bank's branches abroad, with due attention to the activity of subsidiaries with exposure significant for the Group. The subsidiaries are instructed to manage risks based on the risk strategy and policy of the Group, with adjustments according to the circumstances, which are reported to the parent company. Risks are managed separately by each company in the Bank Group, according to policy formulated by each company's board of directors. The Bank manages the various risks while using hedges for some risks. The Supervisor of Banks has set forth guidelines concerning risk management in the Proper Conduct of Banking Business Directives. The directives detail the requirements of the Supervisor for the management of the various risks to which a banking corporation is exposed, and stipulate fundamental principles for the management and control of risks, including suitable involvement in and thorough understanding of risk management by the board of directors of the banking corporation, the management of risks by a risk manager who is a member of the board of management, the employment of tools for the identification and measurement of risks, and the creation of means for supervision and control, including the existence of an independent risk-control function. The Bank operates in accordance with the guidelines of the Supervisor of Banks.

The Chief Risk Officer (CRO) and the member of the Board of Management responsible for the Risk Management Area is Dr. A. Bachar.

Financial risks are managed by designated members of the Board of Management and under their responsibility.

The principal members of the Board of Management responsible for managing credit risks are the Head of Corporate Banking, Mr. T. Cohen, and the Head of Retail Banking, Mr. R. Stein.

The member of the Board of Management responsible for managing market, investment, and liquidity risks and the Head of Financial Markets and International Banking is Mr. Y. Antebi.

Legal risk is managed by Attorney Y. Almog, Chief Legal Advisor.

Technological risk, including cyber risk, is managed by Ms. E. Ben-Zeev, Head of Information Technology.
Operational risk, excluding legal risk and technological risk, is managed by each member of the Board of Management in the area of activity for which he or she is responsible.
For details and more extensive information regarding risk management governance, including the control approach, the responsible parties, and the committees of the Board of Directors and Board of Management relevant to risk management, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018.

B.3. Top and emerging risks

Based on the recommendations of the FSB (Financial Stability Board), a top risk is defined as a development currently occurring in the business environment of the Bank that may adversely affect the Bank's results over the course of the coming year. By contrast, with respect to an emerging risk, there is greater uncertainty regarding the timing of materialization of the risk as an occurrence with a material effect on the strategy of the Bank.
The management of risks at the Bank Group is described extensively in the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018.
The Board of Management and Board of Directors of the Bank discussed the effect of the top and emerging risks described below on the Bank; from time to time, they examine the need to adjust business strategy to such developments.

- **Compliance risk:** Pursuant to Proper Conduct of Banking Business Directive 308, compliance risk also includes risks related to the fairness of the Bank towards its customers, conflicts of interest, the prohibition of money laundering and financing of terrorism, provision of advice to customers, protection of privacy (excluding information-technology aspects), taxation aspects relevant to products or services for customers, or directives of a similar nature. The materialization of this risk globally is reflected in the continuing investigations of banks around the world, and the fines imposed on them in connection with the violation of laws or regulations, such as in the areas of assisting tax evasion, the prevention of terrorism financing, money laundering, and investigations of corruption. The Bank Group's business with American customers and the issue of FIFA are under investigation by United States government agencies. The Bank estimates that the aggregate total to be paid by the Bank Group in connection with the investigation of the Bank Group's business with American customers is likely to be significantly higher than the amount of the existing provision in the financial statements. Very significant fines may adversely affect the results of the Bank. At this time, it appears that a resolution or resolutions with the United States Department of Justice regarding this matter may be in the form of a deferred prosecution agreement or a plea agreement. The type of resolution, if attained, may also affect the Bank, in that a severe resolution may cause damage to the Bank's business. For details regarding the investigations of the United States authorities, see Note 10D and 10E to the Condensed Financial Statements as at March 31, 2019.

- **Macro-economic environment:** The activity of the Bank is dependent on the business environment, in Israel and globally. The condition of the global economy; significant changes in monetary policies and interest-rate curves; market volatility; changes in prices of financial assets in Israel and worldwide, and in real-estate prices; and the economic, political, and security situation in Israel and in the region have the potential to affect the activity of the Bank. The Bank's multi-annual strategic plan includes certain assumptions regarding the macro-economic environment, taking into consideration the existing risks in the global and Israeli economy, and balances risk and return considerations.
- **Regulatory environment in Israel and overseas:** International regulatory reforms have implications for the business of the Bank, in Israel and globally. In Israel, several regulatory initiatives have been formulated over the last few years, with the primary aim of increasing competition in the banking system in Israel; several additional regulatory initiatives are in the process of being generated. The regulatory initiatives and trends, and specifically the mandatory separation of the Bank from its credit-card companies and the significant changes in this area of activity, as well as the mobility of bank accounts and open API, may affect the banking system in general and the Bank in particular. At this stage, it is too early to estimate and assess the effect thereof on the Bank. For details regarding the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel, 2017, see Note 16 to the Condensed Financial Statements as at March 31, 2019.
- **Information security and cyber incident risk:** Increasing cyber threats to financial institutions have led to the channeling of resources in the banking industry to cope with this risk. The Bank applies frequent controls in all channels in order to prevent harmful penetration, activation of malicious software, and information leakage. The lines of defense consist of a large number of advanced information-security systems, deployed internally in the Bank's network as well as externally as a perimeter defense.
- **Competitive and strategic risk:** New competition from technological entities, new technologies, changes in customer behavior, and new business models in the financial sphere have the power to significantly affect the banking system, in Israel and worldwide, alongside the other regulatory and competitive changes in this field. The Bank works to update its strategic plan, while taking action in the areas of innovation, technology, the structure of its operations, and more, in order to respond to all such threats.

For details regarding legal proceedings, see Note 10 to the Condensed Financial Statements as at March 31, 2019.

B.4. Review of weighted risk-adjusted assets

Table B-2: Review of weighted risk-adjusted assets

		Risk-weighted assets		Minimum capital requirements*
		March 31, 2019	December 31, 2018	**March 31, 2019**
		NIS millions		
1	Credit risk (standardized approach)**	**293,179**	292,367	**40,283**
6	Counterparty credit risk (standardized approach)	**5,585**	6,949	**767**
10	Credit valuation adjustment (CVA)	**3,047**	3,327	**419**
15	Settlement risk	**-**	-	**-**
16	Securitization exposures (standardized approach)	**133**	143	**18**
25	Amounts below deduction thresholds (subject to 250% risk weight)	**10,464**	10,114	**1,437**
	Total credit risk	**312,408**	312,900	**42,924**
20	Market risk (standardized approach)	**2,998**	3,429	**412**
24	Operational risk	**24,285**	24,268	**3,337**
27	Total	**339,691**	340,597	**46,673**

* Capital requirements according to the minimum required total capital ratio, plus a capital requirement reflecting 1% of the balance of housing loans at the reporting date, at a rate of 13.74%.

** Credit risk does not include counterparty credit risk, adjustment in respect of credit risk, settlement risk, securitization exposures, and amounts below the deduction thresholds.

C. Capital and leverage

C.1. Composition of capital

Table C-1: Composition of supervisory capital

		March 31, 2019	March 31, 2018	December 31, 2018
		NIS millions		
	Common equity Tier 1 capital			
	Common equity Tier 1 capital – instruments and retained earnings			
1	Ordinary share capital issued by the banking corporation and premium on ordinary shares included in common equity Tier 1 capital	**8,153**	8,148	8,135
2	Retained earnings, including dividends proposed or declared after the balance sheet date	**31,368**	28,849	30,565
3	Accumulated other comprehensive income and disclosed retained earnings	**(1,040)**	(913)	(1,156)
5	Ordinary shares issued by subsidiaries of the banking corporation which were consolidated and are held by a third party (non-controlling interests)	**43**	49	40
6	Common equity Tier 1 capital before supervisory adjustments and deductions	**38,524**	36,133	37,584
	Common equity Tier 1 capital – supervisory adjustments and deductions			
10	Deferred tax assets, realization of which depends on future profitability of the banking corporation, excluding deferred tax assets arising from timing differences	**39**	40	34
11	Total accumulated other comprehensive income in respect of cash-flow hedges of items not presented in the balance sheet at fair value	**(1)**	(1)	(1)
14	Unrealized profits and losses resulting from changes in the fair value of liabilities due to changes in the own credit risk of the banking corporation	**2**	4	4
16	Investment in own ordinary shares held directly or indirectly (including commitments to purchase shares under contractual agreements)	**-**	25	-
21	Deferred tax assets arising from timing differences in amounts exceeding 10% of common equity Tier 1 capital	**-**	-	-
26	Additional supervisory adjustments and deductions established by the Banking Supervision Department	**(419)**	(572)	(457)
26C	Of which: additional supervisory adjustments to common equity Tier 1 capital	**(419)**	(572)	(457)
26C	Of which: in respect of the efficiency plan	**(419)**	(572)	(457)
26C	Of which: in respect of wage tax	**-**	-	-
28	Total supervisory adjustments and deductions in common equity Tier 1 capital	**(379)**	(504)	(420)
29	Common equity Tier 1 capital	**38,903**	36,637	38,004

Table C-1: Composition of supervisory capital (continued)

		March 31, 2019	March 31, 2018	December 31, 2018
		NIS millions		
	Additional Tier 1 capital			
	Additional Tier 1 capital – instruments			
33	Additional Tier 1 capital instruments issued by the corporation, which are eligible for inclusion in supervisory capital during the transitional period	**733**	977	977
36	Additional Tier 1 capital before deductions	**733**	977	977
	Additional Tier 1 capital – deductions			
43	Total deductions from additional Tier 1 capital	**-**	-	-
44	Additional Tier 1 capital	**733**	977	977
45	Tier 1 capital	**39,636**	37,614	38,981
	Tier 2 capital			
	Tier 2 capital – instruments and provisions			
47	Tier 2 capital instruments issued by the corporation, which are eligible for inclusion in supervisory capital during the transitional period	**45**	136	57
48	Tier 2 capital instruments issued by subsidiaries of the banking corporation to third-party investors	**5,535**	5,092	6,074
49	Of which: Tier 2 capital instruments issued by subsidiaries of the banking corporation and held by third-party investors, which are gradually deducted from Tier 2 capital	**3,717**	5,092	4,251
50	Collective allowances for credit losses before the effect of related tax	**3,856**	3,788	3,911
51	Tier 2 capital before deductions	**9,436**	9,016	10,042
	Tier 2 capital – deductions			
57	Total supervisory adjustments to Tier 2 capital	**-**	-	-
58	Tier 2 capital	**9,436**	9,016	10,042
59	Total capital	**49,072**	46,630	49,023
	Risk-weighted assets			
	Total risk-weighted assets according to the requirements prior to the adoption of Directive 202, in accordance with Basel 3	**339,204**	330,870	339,973
	Of which: credit risk assets	**311,921**	302,399	312,276
	Of which: market risk assets	**2,998**	4,692	3,429
	Of which: operational risk assets	**24,285**	23,779	24,268
60	Total risk-weighted assets	**339,691**	331,539	340,597

Table C-1: Composition of supervisory capital (continued)

		March 31, 2019	March 31, 2018	December 31, 2018
		NIS millions/percent		
	Capital ratios and capital preservation cushions			
61	Common equity Tier 1 capital	**11.45%**	11.05%	11.16%
62	Tier 1 capital	**11.67%**	11.35%	11.44%
63	Total capital	**14.45%**	14.06%	14.39%
	Minimum requirements established by the Banking Supervision Department			
69	The required minimum common equity Tier 1 capital ratio is 10%. A capital requirement at a rate representing 1% of the balance of housing loans at the dates of the financial statements was added to this ratio.	**10.24%**	10.23%	10.24%
71	The required minimum total capital ratio is 13.5%. A capital requirement at a rate representing 1% of the balance of housing loans at the dates of the financial statements was added to this ratio.	**13.74%**	13.73%	13.74%
	Amounts below the deduction threshold (before risk weighting)			
72	Investments in the capital of financial corporations which do not exceed 10% of the ordinary share capital issued by the financial corporation and which are below the deduction threshold	**1,474**	2,211	1,802
73	Investments in the capital of financial corporations which exceed 10% of the ordinary share capital issued by the financial corporation and which are below the deduction threshold	**671**	602	656
75	Deferred tax assets arising from timing differences, below the deduction threshold	**3,749**	3,590	3,645
	Ceiling for inclusion of provisions in Tier 2			
76	Provision qualifying for inclusion in Tier 2, with reference to exposures under the standardized approach, before application of the ceiling	**3,856**	3,989	3,919
77	Ceiling for inclusion of provision in Tier 2 under the standardized approach	**3,905**	3,788	3,911
	Capital instruments not qualifying as supervisory capital, which are subject to the transitional directives			
82	Present ceiling amount for instruments included in additional Tier 1 capital subject to the transitional directives	**733**	977	977
83	Amount deducted from additional Tier 1 capital due to the ceiling	**1,126**	1,425	887
84	Present ceiling amount for instruments included in Tier 2 capital subject to the transitional directives	**4,577**	6,102	6,102
85	Amount deducted from Tier 2 capital due to the ceiling	**-**	-	-

C.2. Capital adequacy

C.2.a. Capital-adequacy target

Pursuant to the circular of the Banking Supervision Department concerning minimum capital ratios, the Bank, as a banking corporation of significant importance (a banking corporation whose total balance sheet assets on a consolidated basis constitute at least 20% of the total balance sheet assets of the banking system in Israel), is required to maintain a minimum common equity Tier 1 capital ratio of 10% and a minimum total capital ratio of 13.5%. A capital requirement at a rate representing 1% of the balance of housing loans at the dates of the financial statements was added to the minimum capital ratios.

Accordingly, the minimum common equity Tier 1 capital ratio and the minimum total capital ratio of the Bank required by the Banking Supervision Department, on a consolidated basis, based on data as at March 31, 2019, stand at 10.24% and 13.74%, respectively.

Pursuant to a resolution of the Board of Directors of the Bank, the target common equity Tier 1 capital ratio is 10.75% as of December 31, 2017.

C.2.b. Planning and management of capital by the Bank

Issuance of subordinated notes with a loss-absorption mechanism

In April 2019, the Bank issued a series of subordinated notes, in the amount of approximately NIS 0.5 billion, which constitute part of the Tier 2 capital of the Bank. For details regarding issues of subordinated notes by Hapoalim Hanpakot, see Note 9J to the Condensed Financial Statements as at March 31, 2019.

Early redemption of capital notes in Tier 1 capital

The Bank carried out full early redemption of the subordinated notes in Series B in February 2019, in the amount of NIS 582 million.

Buybacks by banking corporations

In February 2019, the Banking Supervision Department issued a circular updating Proper Conduct of Banking Business Directive 332, "Buybacks by Banking Corporations," according to which banks will be able to perform buybacks of securities that they issue, subject to the fulfillment of certain conditions. Until now, the existing directive prohibited banks from performing buybacks, other than in exceptional cases, whereas the Companies Law permits buybacks, subject to fulfillment of conditions for distribution.

The circular establishes conditions under which banking corporations can perform buybacks of securities that they issue, including the following, among other matters:

- The approval of the Banking Supervision Department for the buyback, based on a buyback plan presented by the bank, is required.
- The volume of the buyback in each plan shall not exceed 3% of the issued and paid-up share capital of the banking corporation.
- The banking corporation shall act in accordance with the safe-harbor protection mechanism published by the Israel Securities Authority, to ensure that it has legal protection against allegations of use of insider information.
- The buyback offer shall not be directed to a particular group of shareholders (except in the case of a shareholder who is a qualifying customer, as defined in the directive).
- The buyback plan shall be approved by the board of directors of the bank.

As a result of the sale of approximately 65% of the shares of Isracard in the second quarter of 2019 (see Note 17 to the Condensed Financial Statements), the Bank accumulated additional capital surplus in the amount of approximately NIS 1.3 billion. Further to the coordination with the Banking Supervision Department, the Board of Directors of the Bank instructed the Board of Management to formulate a plan for a buyback of shares of the Bank against this capital surplus, to be executed over a period of time, subject to the directives of the law and of the Banking Supervision Department on this matter. The implementation, volume, and terms of the plan are subject to resolution and approval by the Board of Directors of the Bank.

C.2.c. Implementation of regulatory directives with an effect on measurement and capital-adequacy matters

Sale of Isracard

In accordance with the requirements of the Law for Increasing Competition and Reducing Concentration in the Banking Market in Israel (Legislative Amendments), 2017 (the "Law for Increasing Competition"), and the publication of the prospectus for a public sale offering of the shares of Isracard, the Bank sold approximately 65.2% of the capital of Isracard in a public sale offering on April 8, 2019. The effect of the sale is estimated at an increase of approximately 0.4% in the common equity Tier 1 capital ratio and in the total capital ratio. For details regarding the holdings of the Bank in the Isracard Group, see the section "Controlled companies in Israel" in the Report of the Board of Directors and Board of Management as at March 31, 2019.

Improving operational efficiency

In January 2016, the Banking Supervision Department issued a letter on the subject, "Improving the operational efficiency of the banking system in Israel" (the "Efficiency Directive"). Pursuant to the Efficiency Directive, the boards of directors of banking corporations shall formulate a multi-year plan to improve efficiency. Banking corporations that meet the conditions established in the directive will be granted a relief allowing them to spread the effects of the plan over a period of up to five years in a straight line, for the purposes of the calculation of capital-adequacy ratios and of the leverage ratio. In October 2016, the Board of Directors of the Bank approved an efficiency plan at an estimated cost in the amount of NIS 762 million, net of tax effect, which was allocated to capital. The effect of the costs of the efficiency plan on the ratio of common equity Tier 1 capital to risk components, estimated at approximately 0.14% as at March 31, 2019, are being allocated in equal parts over five years, beginning in 2017.

Further to the Efficiency Directive, in June 2017, the Banking Supervision Department issued a letter entitled, "Improving the operational efficiency of the banking system in Israel – efficiency in the area of real estate," which encourages banking corporations to also examine, in addition to improved efficiency in personnel expenses, the possibility of reducing real-estate and maintenance costs of headquarters and management units, including through a reexamination of the geographical location of such units (hereinafter: "Real-Estate Efficiency").

In order to encourage the implementation of a plan for Real-Estate Efficiency, the Banking Supervision Department will approve reliefs for the banks in the area of capital adequacy.

The Banking Supervision Department has extended the period for implementation of the efficiency plan until December 31, 2019.

The subsidiary of the Bank in Turkey

In January 2019, a letter was received from the Bank of Israel concerning the subsidiary of the Bank in Turkey, Bank Pozitif. In the letter, the Bank of Israel stated that the activity of the Bank in Turkey exposes it to significant risks, and therefore, until the realization of the full holdings of the Bank in Bank Pozitif, the Bank is required to increase the risk weighting rates of risk-adjusted assets in respect of this activity, in the calculation of the consolidated capital ratio only, as follows:

- Beginning January 1, 2020, risk-adjusted assets in respect of the activity of Bank Pozitif will be weighted at a rate of at least 300%.
- Beginning January 1, 2021, the risk-adjusted assets will be weighted at a rate of at least 600%.

The Bank is examining possibilities for the sale of its full holdings, and in accordance with its strategic plan, has decided to gradually reduce the credit portfolio.

The effect of this instruction on the common equity Tier 1 capital ratio, based on data as at March 31, 2019, is a decrease of approximately 0.05%, under the assumption of weighting of the risk-adjusted assets at 300%, and a decrease of approximately 0.12%, under the assumption of weighting of the risk-adjusted assets at 600%.

C.2.d. Basel 3 directives

The Basel 3 directives took effect on January 1, 2014. Implementation is gradual, in accordance with the transitional directives established in Proper Conduct of Banking Business Directive 299, "Capital Measurement and Adequacy – Supervisory Capital – Transitional Directives." In accordance with the transitional directives, capital instruments that no longer qualify as supervisory capital were recognized as of January 1, 2014, up to a ceiling of 80% of their balance in the supervisory capital as at December 31, 2013; this ceiling is being lowered by an additional 10% in each subsequent year, until January 1, 2022. Accordingly, the ceiling for instruments qualifying as supervisory capital was 40% in 2018, and stands at 30% in 2019.

C.3. Leverage ratio

The Bank applies Proper Conduct of Banking Business Directive 218, "Leverage Ratio" (hereinafter: the "Directive"). The Directive establishes a simple, transparent, non-risk-based leverage ratio, which serves as a complementary measurement to risk-based capital requirements, and which is designed to limit the accumulation of leverage at banking corporations.

The leverage ratio is expressed as a percentage, and is defined as the ratio of the capital measurement to the exposure measurement. Capital, for the purpose of measurement of the leverage ratio, is Tier 1 capital, as defined in Proper Conduct of Banking Business Directive 202, taking into consideration the transitional arrangements that have been established. The total exposure measurement is the total of balance sheet exposures, exposures to derivatives and to securities financing transactions, and off-balance sheet items.

Table C-2: Comparison of balance sheet assets to exposure measurement, for the purposes of the leverage ratio

	March 31, 2019	March 31, 2018	December 31, 2018
	NIS millions		
Total consolidated assets as per published financial statements	**465,778**	448,195	460,926
Adjustment for investments in banking, financial, insurance, or commercial entities that are consolidated for accounting purposes but outside the scope of regulatory consolidation	**-**	-	-
Adjustment for fiduciary assets recognized in the balance sheet pursuant to the Public Reporting Directives, but excluded from the leverage ratio exposure measurement	**-**	-	-
Adjustments for derivative financial instruments	**(658)**	(1,423)	333
Adjustments for securities financing transactions	**-**	-	-
Adjustments for off-balance sheet items	**54,763**	60,004	54,608
Other adjustments	**3,129**	3,069	3,113
Exposure for the purposes of the leverage ratio	**523,012**	509,845	518,980

Table C-3: Leverage ratio disclosure

	March 31, 2019	March 31, 2018	December 31, 2018
	NIS millions/percent		
On-balance sheet exposures			
On-balance sheet items (excluding derivatives and securities financing transactions, but including collateral)	**457,986**	438,423	452,831
Asset amounts deducted in determining Tier 1 capital	**(39)**	(40)	(34)
Total on-balance sheet exposures (excluding derivatives and securities financing transactions)	**457,947**	438,383	452,797
Derivative exposures			
Replacement cost associated with all derivatives transactions	**4,818**	5,970	5,717
Add-on amounts for potential future exposure associated with all derivatives transactions	**6,153**	6,808	6,704
Gross-up for collateral provided in respect of derivatives deducted from balance sheet assets pursuant to the Public Reporting Directives	**-**	-	-
Deductions of receivables assets for cash variation margin provided in derivatives transactions	**(1,383)**	(2,051)	(1,554)
Exempted central counterparty leg of client-cleared trade exposures	**-**	-	-
Adjusted effective notional amount of written credit derivatives	**-**	123	-
Adjusted effective notional offsets and add-on deductions for written credit derivatives	**-**	-	-
Total derivative exposures	**9,588**	10,850	10,867
Securities financing transaction exposures			
Gross securities financing transaction assets (with no recognition of netting), after adjusting for sale accounting transactions	**714**	608	708
Netted amounts of cash payables and cash receivables of gross securities financing transaction assets	**-**	-	-
Central counterparty credit risk exposure for securities financing transaction assets	**-**	-	-
Agent transaction exposures	**-**	-	-
Total securities financing transaction exposures	**714**	608	708
Other off-balance sheet exposures			
Off-balance sheet exposure at gross notional amount	**185,035**	179,901	185,688
Adjustments for conversion to credit equivalent amounts	**(130,272)**	(119,897)	(131,080)
Off-balance sheet items	**54,763**	60,004	54,608
Capital and total exposures			
Tier 1 capital*	**39,636**	37,614	38,981
Total exposures*	**523,012**	509,845	518,980
Leverage ratio			
Leverage ratio pursuant to Proper Conduct of Banking Business Directive 218	**7.58%**	7.38%	7.51%
Minimum leverage ratio required by the Banking Supervision Department	**6.00%**	6.00%	6.00%

* These data also include Efficiency Plan Adjustments, established based on the letter of the Banking Supervision Department of January 12, 2016, "Improvement of the operational efficiency of the banking system in Israel." The effect of the costs of the efficiency plan on the leverage ratio as at March 31, 2019, estimated at approximately 0.08%, is allocated in equal parts over five years, beginning in 2017.

D. Credit risk

Credit risk is the risk that a borrower or debtor may default on obligations to the Bank under a credit agreement.

The credit portfolio is a major component of the asset portfolio of the Bank Group; therefore, deterioration in the stability of the various borrowers may have an adverse effect on the Group's asset value and profitability.

Activities that create credit risk include:

- **Balance sheet exposures –** Present liabilities to the Bank, such as credit and mortgages to the public, credit to banks and deposits with banks, credit to governments, investment in bonds (corporate and other), and the balance sheet part (market value) of derivatives and financial instruments.
- **Off-balance sheet exposures –** Potential (unrealized) liabilities to the Bank, such as guarantees, unutilized commitments to grant credit, unutilized credit facilities, and potential liabilities arising from changes in the value of transactions in derivative financial instruments. The credit risk arising from transactions in derivative financial instruments is counterparty risk – the risk that the counterparty to the transaction will default before the final settlement of cash flows in the derivatives transaction. Counterparty risk is addressed separately in Section E, below.

Another risk arising from the portfolio of credit exposures is concentration risk. Concentration risk arises from non-optimal diversification of specific risks in the credit portfolio, such that the credit portfolio is insufficiently diversified across the various risk factors; for example, when the credit portfolio is composed of a small number of borrowers (name concentration) or has a high degree of exposure to a particular economic sector (sector concentration).

In accordance with the reporting directives of the Bank of Israel, this section contains items to which the Basel credit-risk framework applies, pursuant to Proper Conduct of Banking Business Directive 203, unless explicitly noted otherwise.

D.1. Credit quality of credit exposures

Table D-1: Credit risk indicators[1]

	As at	
	March 31, 2019	December 31, 2018
Balance of impaired credit to the public, as a percentage of the balance of credit to the public*	**1.04%**	0.95%
Balance of unimpaired credit to the public, in arrears of 90 days or more, as a percentage of the balance of credit to the public*	**0.31%**	0.28%
Allowance for credit losses in respect of credit to the public, as a percentage of the balance of credit to the public*	**1.33%**	1.31%
Collective allowance for credit losses, as a percentage of the balance of credit to the public*	**1.11%**	1.14%
Allowance for credit losses in respect of credit to the public, as a percentage of the balance of impaired credit to the public*	**128.17%**	138.11%
Allowance for credit losses in respect of credit to the public, as a percentage of the balance of impaired credit to the public plus the balance of credit to the public in arrears of 90 days or more*	**99.09%**	106.49%
Problematic credit risk in respect of the public, as a percentage of total credit risk in respect of the public*	**1.98%**	1.89%
Provision (income) for credit losses as a percentage of the average recorded balance of credit to the public	**(2)0.17%**	0.22%
Net charge-offs in respect of credit to the public as a percentage of the average recorded balance of credit to the public	**(2)0.17%**	0.20%
Net charge-offs in respect of credit to the public as a percentage of the allowance for credit losses in respect of credit to the public	**(2)12.86%**	14.58%

* Before deduction of the allowance for credit losses.
(1) Does not include the data of the Isracard Group, which constitutes a discontinued operation.
(2) Calculated on an annualized basis.

Portfolio quality analysis

In the first quarter of 2019, increases were recorded in the balance of impaired credit to the public, as a percentage of the balance of credit to the public; problematic credit risk in respect of the public, as a percentage of total credit risk in respect of the public; and the allowance for credit losses in respect of credit to the public, as a percentage of the balance of credit to the public. This increase followed a downward trend over a long period; the allowance for credit losses in respect of credit to the public as a percentage of the balance of credit to the public decreased moderately over the last five quarters, and the two other indicators showed volatility with no clear trend. It is therefore too early to determine whether the change this quarter represents a reversal of the trend.

The balance of unimpaired credit to the public, in arrears of 90 days or more, as a percentage of the balance of credit to the public also rose during the quarter, but this figure is characterized by volatility, and no upward trend is apparent relative to previous quarters.

Some indicators of credit risk decreased:

- The provision (income) for credit losses as a percentage of the average recorded balance of credit to the public.
- Net charge-offs in respect of credit to the public, as a percentage of the average recorded balance of credit to the public.
- The collective allowance for credit losses, as a percentage of the balance of credit to the public.

The improvements in the indicators of provision and charge-offs was influenced, among other factors, by the measures taken by the Bank to improve the quality of the portfolio of credit to private individuals.

With regard to other indicators that refer to only to the risk in the portfolio of credit for private individuals, see Table D-7, below.

Table D-2: Credit quality of credit exposures

		March 31, 2019			
		Gross balances		Allowances for credit losses or impairment	Net balances
		Impaired or in arrears of 90 days or more	Others		
		NIS millions			
1	Debts, excluding bonds	**4,126**	**389,690**	**665**	**393,151**
2	Bonds	**-**	**58,520**	**-**	**58,520**
3	Off-balance sheet exposures	**-**	**185,109**	**74**	**185,035**
4	Total	**4,126**	**633,319**	**739**	**636,706**

		March 31, 2018			
		Gross balances		Allowances for credit losses or impairment	Net balances
		Impaired or in arrears of 90 days or more	Others		
		NIS millions			
1	Debts, excluding bonds	3,139	375,313	536	377,916
2	Bonds	-	50,033	-	50,033
3	Off-balance sheet exposures	-	180,002	101	179,901
4	Total	3,139	605,348	637	607,850

		December 31, 2018			
		Gross balances		Allowances for credit losses or impairment	Net balances
		Impaired or in arrears of 90 days or more	Others		
		NIS millions			
1	Debts, excluding bonds	3,934	394,373	594	397,713
2	Bonds	-	47,860	-	47,860
3	Off-balance sheet exposures	-	185,769	81	185,688
4	Total	3,934	628,002	675	631,261

For details regarding changes in the inventory of impaired debts, see Table 3-3 in the section "Review of risks" in the Report of the Board of Directors and Board of Management as at March 31, 2019.

D.2. Credit risk in respect of exposures to borrowers and to groups of borrowers

Table D-3: Details of balances of balance sheet credit and off-balance sheet credit risk to borrowers whose indebtedness exceeds NIS 1,200 million, by sector of the economy

	March 31, 2019			
	Number of borrowers	Balance sheet credit risk	Off-balance sheet credit risk	Total
		NIS millions		
Economic sector				
Industry	**3**	**959**	**4,625**	**5,584**
Construction and real estate – construction	**-**	**-**	**-**	**-**
Construction and real estate – real-estate activities	**-**	**-**	**-**	**-**
Electricity and water supply	**1**	**1,273**	**1,757**	**3,030**
Financial services	**5**	**5,030**	**4,411**	**9,441**
Total	**9**	**7,262**	**10,793**	**18,055**

	December 31, 2018			
	Number of borrowers	Balance sheet credit risk	Off-balance sheet credit risk	Total
		NIS millions		
Economic sector				
Industry	3	877	5,164	6,041
Construction and real estate – construction	-	-	-	-
Construction and real estate – real-estate activities	1	756	647	1,403
Electricity and water supply	1	1,276	2,315	3,591
Financial services	3	3,077	2,571	5,648
Total	8	5,986	10,697	16,683

Credit risk in respect of exposure to borrower groups

The Bank conducts monitoring and control processes in order to examine compliance with the limits set forth in Directive 313 with regard to exposure to the indebtedness of borrower groups. As at the reporting date, the Bank is in compliance with the limits.

Table D-4: Details of credit risk balances for each group of borrowers whose net indebtedness on a consolidated basis exceeds 15% of the capital of the banking corporation (as defined in Directive 313)

	Balance sheet credit risk[(1)]	Off-balance sheet credit risk[(1)]	Of which: off-balance sheet credit risk in respect of derivative instruments[(2)]	Gross indebtedness[(3)]	Deductions[(4)]	Net indebtedness[(5)]	Percentage of regulatory capital
	NIS millions						
Borrower group A	3,821	3,059	456	6,891	22	6,869	17.62%

(1) After deduction of the balance of charge-offs and the allowance for credit losses calculated on an individual basis.
(2) Off-balance sheet credit risk in respect of derivative instruments, as calculated for the purposes of the limits on indebtedness of borrowers and of borrower groups.
(3) This amount includes third-party guarantees outside the group.
(4) Deductions permitted under Directive 313, mainly including deposits deposited at the Bank, bonds issued by the State of Israel, and deductible indemnity letters of the State of Israel or financial institutions.
(5) The data presented above represent exposure to borrower groups, and are stated after the permitted deductions pursuant to Directive 313, and after deduction of the allowance for credit losses calculated on an individual basis. These data are therefore not comparable with data regarding borrowers' indebtedness provided in other disclosures in the report.

D.3. Risks in the housing loan portfolio

Table D-5: Development of the balance in the housing credit portfolio, by linkage base and as a percentage of the balance in the credit portfolio of the Bank

	Unlinked segment				CPI-linked segment				Foreign-currency segment		Total	
	Fixed interest rate		Floating interest rate		Fixed interest rate		Floating interest rate		Floating interest rate			
	Balance in NIS millions	Rate in %	Balance in NIS millions	Rate in %	Balance in NIS millions	Rate in %	Balance in NIS millions	Rate in %	Balance in NIS millions	Rate in %	Recorded debt balance in NIS millions	Rate of change during the period
March 31, 2019	**15,004**	**18.0%**	**31,928**	**38.4%**	**13,560**	**16.3%**	**22,320**	**26.8%**	**336**	**0.4%**	**83,148**	**2.1%**
Dec. 31, 2018	14,503	17.8%	31,060	38.1%	13,539	16.6%	21,984	27.0%	368	0.5%	81,454	9.3%
Dec. 31, 2017	12,455	16.7%	28,022	37.6%	12,988	17.4%	20,619	27.7%	437	0.6%	74,521	7.6%

Risk quantification and measurement – housing credit portfolio

The Bank routinely monitors developments in the housing credit portfolio, and applies various measures to manage risk. Housing credit risks are examined individually, based on the policies and objectives established in the risk appetite set for housing credit, from the level of the individual transaction to an overview of the housing credit portfolio of the Bank.

Risk hedging: The Bank manages and hedges risk, among other means, through limits on various segments, as established in policy discussions of the Board of Management and the Board of Directors, overseen and led by the Risk Management Area. The limits address LTV rates, repayment capability, distribution of credit products in the portfolio, volume of problematic debt, loan durations, geographical distribution, rate of arrears, etc. These indicators are also monitored in comparison to the data of the banking system as a whole. The Bank tracks conditions and changes in macro-economic indicators in general, and in the business environment of the industry in particular. Certain events require a reexamination of policy, such as a sharp increase in the floating interest rate or in inflation, an increase in unemployment in the Israeli economy, or a material change in housing prices.

Data are reported on a monthly basis in an Area-level risk forum headed by the Head of Retail Banking, and on a quarterly basis as part of the report on developments in the credit portfolio and in credit risk to the Board of Management and Board of Directors.

The Bank uses a statistical model to measure the probability of default and the expected loss in the mortgage portfolio. In addition, stress scenarios are applied to the mortgage portfolio, and the effect on the portfolio and on the Bank as a whole is analyzed. These scenarios include a sharp decline in prices of homes, an increase in the interest rate, and an increase in the unemployment rate. In addition, insurance arrangements are in place (life insurance and building insurance).

Table D-6: Details of characteristics of housing credit granted by the Bank – percentage of total new loans executed

	For the three months ended				
	March 31, 2019	December 31, 2018	September 30, 2018	June 30, 2018	March 31, 2018
Characteristics					
Financing rate over 60%	**38.1%**	34.5%	34.2%	31.2%	29.6%
Ratio of repayment to income greater than 40% (for purchases of homes and in monthly payments)	**0.0%**	0.2%	0.1%	0.1%	0.0%
Percentage with floating interest rates varying at a frequency of less than 5 years	**31.5%**	30.3%	32.5%	32.6%	31.5%
Percentage with floating rates	**59.2%**	57.9%	59.5%	60.1%	58.1%
Percentage of all-purpose loans	**6.0%**	6.3%	6.2%	5.7%	6.2%
Loans for investment purposes as a percentage of total purchases of homes	**9.7%**	10.2%	9.0%	9.3%	10.8%
Principal planned for repayment after age 67 (excluding investments)	**6.9%**	7.3%	7.3%	7.0%	7.1%
Average original term to maturity of loans for purchases of homes, in years (excluding bridge loans)	**24.7**	24.6	24.6	24.5	23.9

Balances at the end of the period rose in the first quarter of 2019. The upward trend in the percentage of credit granted with a financing rate greater than 60% continued. The percentage of floating-rate loans rose. The percentage of credit granted with payments at a rate higher than 40% of income fell to a near-zero rate. The percentage of credit granted with principal scheduled for repayment after the age of 67 (excluding investments), loans for investment purposes as a percentage of total purchases of homes, and the percentage of all-purpose loans decreased.

The average term to maturity of loans for purchases of homes (excluding bridge loans) has continued to increase.

D.4. Credit to private individuals (excluding housing)

Table D-7: Balance of credit to private individuals in Israel*

	Balance as at		Change	
	March 31, 2019	December 31, 2018		
	NIS millions			%
Balance sheet				
Negative balance in current accounts	**3,887**	3,892	(5)	(0.13%)
Loans[1]	**29,225**	29,791	(566)	(1.90%)
Of which: bullet and balloon loans	**98**	114	(16)	(14.04%)
Credit for purchases of motor vehicles[2]	**4,036**	4,375	(339)	(7.75%)
Debtors in respect of credit-card activity	**4,830**	4,905	(75)	(1.53%)
Total balance sheet credit risk	**41,978**	42,963	(985)	(2.29%)
Off-balance sheet				
Off-balance sheet credit risk	**21,029**	20,368	661	3.25%
Total credit risk	**63,007**	63,331	(324)	(0.51%)

* Does not include the data of the Isracard Group, which constitutes a discontinued operation.
(1) Excluding loans for purchases of motor vehicles.
(2) Including loans granted for the purchase of motor vehicles or with a lien on a motor vehicle.

Table D-8: Information regarding problematic debts in respect of private individuals in Israel

	Balance as at		Change	Percentage of total balance sheet credit risk	
				As at	
	March 31, 2019	December 31, 2018		**March 31, 2019**	December 31, 2018
	NIS millions				
Problematic credit risk	**854**	873	(2.18%)	**2.03%**	2.03%
Of which: impaired credit risk	**709**	694	2.16%	**1.69%**	1.62%
Debts in arrears of more than 90 days	**85**	107	(20.56%)	**0.20%**	0.25%
Net charge-offs for the period	**93**	473	[1](21.35%)	[1]**0.89%**	1.10%
Allowance for credit losses	**866**	892	(2.91%)	**2.06%**	2.08%

(1) Calculated on an annualized basis.

In the first quarter of 2019, the balance of loans to private individuals in Israel, including credit for the purchase of motor vehicles, decreased by 2.6%. Total balance sheet credit risk decreased by 2.3%.

Most indicators of portfolio quality show an improvement in this quarter. The rate of problematic credit risk remained stable, and the rate of impaired credit risk rose, but the other indicators point to improvement. The percentage of debts in arrears of more than 90 days decreased from 0.25% in December 2018 to 0.20% in March 2019. The rate of net charge-offs decreased significantly, from 1.10% in December 2018 to 0.89% in March 2019, indicating the effect of the measures taken by the Bank to improve the quality of underwriting in credit for private individuals. The rate of the allowance for credit losses also decreased slightly.

For additional information regarding the risk of credit to private individuals, see the section "Review of risks" in the Report of the Board of Directors and Board of Management as at March 31, 2019.

D.5. Leveraged financing

Data regarding credit risks of leveraged financing follow. The disclosure focuses on exposures of leveraged borrowers/transactions where the credit balance exceeds the amount of 0.5% of Tier 1 capital.

Table D-9: The Bank's exposures to leveraged financing, by economic sector of the borrower

	March 31, 2019			
	Number of borrowers	Balance sheet credit balance	Off-balance sheet credit balance	Total
		NIS millions		
Economic sector of the borrower				
Construction and real estate – construction	**1**	**252**	**-**	**252**
Construction and real estate – real-estate activities	**1**	**121**	**96**	**217**
Mining and quarrying	**2**	**1,347**	**22**	**1,369**
Information and communications	**1**	**266**	**-**	**266**
Commerce	**2**	**588**	**35**	**623**
Total	**7**	**2,574**	**153**	**2,727**

	December 31, 2018			
	Number of borrowers	Balance sheet credit balance	Off-balance sheet credit balance	Total
		NIS millions		
Economic sector of the borrower				
Construction and real estate – construction	1	257	-	257
Construction and real estate – real-estate activities	2	658	534	1,192
Mining and quarrying	2	1,361	38	1,399
Information and communications	1	266	-	266
Commerce	3	741	170	911
Industry	1	225	-	225
Total	10	3,508	742	4,250

D.6. Credit risk mitigation: standardized approach disclosures

Table D-10: Credit risk mitigation

		March 31, 2019								
		Unsecured	Secured							
		Total balance sheet balance	Total balance sheet balance	Of which: amount secured	Of which: by collateral		Of which: by financial guarantees		Of which: by credit derivatives	
					Balance sheet balance	Of which: amount secured	Balance sheet balance	Of which: amount secured	Balance sheet balance	Of which: amount secured
		NIS millions								
1	Debts, excluding bonds	**372,233**	**20,918**	**14,215**	**12,278**	**5,983**	**8,640**	**8,232**	**-**	**-**
2	Bonds	**58,520**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
3	Total	**430,753**	**20,918**	**14,215**	**12,278**	**5,983**	**8,640**	**8,232**	**-**	**-**
4	Of which: impaired or in arrears of 90 days or more	**3,401**	**21**	**6**	**21**	**6**	**-**	**-**	**-**	**-**

		March 31, 2018								
		Unsecured	Secured							
		Total balance sheet balance	Total balance sheet balance	Of which: amount secured	Of which: by collateral		Of which: by financial guarantees		Of which: by credit derivatives	
					Balance sheet balance	Of which: amount secured	Balance sheet balance	Of which: amount secured	Balance sheet balance	Of which: amount secured
		NIS millions								
1	Debts, excluding bonds	358,201	19,715	13,936	11,207	6,060	8,508	7,876	-	-
2	Bonds	50,033	-	-	-	-	-	-	-	-
3	Total	408,234	19,715	13,936	11,207	6,060	8,508	7,876	-	-
4	Of which: impaired or in arrears of 90 days or more	2,604	61	14	61	14	-	-	-	-

		December 31, 2018								
		Unsecured	Secured							
		Total balance sheet balance	Total balance sheet balance	Of which: amount secured	Of which: by collateral		Of which: by financial guarantees		Of which: by credit derivatives	
					Balance sheet balance	Of which: amount secured	Balance sheet balance	Of which: amount secured	Balance sheet balance	Of which: amount secured
		NIS millions								
1	Debts, excluding bonds	377,488	20,225	13,779	11,841	5,993	8,384	7,786	-	-
2	Bonds	47,860	-	-	-	-	-	-	-	-
3	Total	425,348	20,225	13,779	11,841	5,993	8,384	7,786	-	-
4	Of which: impaired or in arrears of 90 days or more	3,358	62	45	62	45	-	-	-	-

Table D-11: Standardized approach – exposures by asset type and risk weight[(1)(2)]

		March 31, 2019								
		0%	20%	35%	50%	60%	75%	100%	150%	Total amount of credit exposures (after CCF and after CRM)
		NIS millions								
1	Sovereigns, central banks thereof, and national monetary authority	**112,825**	**4,386**	**-**	**69**	**-**	**-**	**308**	**43**	**117,631**
2	Public-sector entities (PSE) other than the central government	**2,241**	**306**	**-**	**4,395**	**-**	**-**	**-**	**-**	**6,942**
3	Banks (including multilateral development banks (MDB))	**540**	**17,282**	**-**	**6,973**	**-**	**-**	**72**	**-**	**24,867**
5	Corporations	**-**	**5,363**	**-**	**2,280**	**-**	**-**	**108,026**	**-**	**115,669**
6	Retail exposures to individuals	**-**	**-**	**-**	**-**	**-**	**64,908**	**-**	**-**	**64,908**
7	Loans to small businesses	**-**	**-**	**-**	**-**	**-**	**9,795**	**-**	**-**	**9,795**
8	Secured by a residential property	**-**	**-**	**27,779**	**22,763**	**5,273**	**23,509**	**3,532**	**-**	**82,856**
9	Secured by commercial real estate	**-**	**-**	**-**	**-**	**-**	**-**	**57,446**	**-**	**57,446**
10	Loans in arrears	**-**	**-**	**-**	**-**	**-**	**-**	**1,273**	**1,891**	**3,164**
11	Other assets*	**3,000**	**-**	**-**	**-**	**-**	**-**	**8,336**	**688**	**12,024**
11A	* Of which: in respect of shares	**-**	**-**	**-**	**-**	**-**	**-**	**1,419**	**457**	**1,876**
12	Total	**118,606**	**27,337**	**27,779**	**36,480**	**5,273**	**98,212**	**178,993**	**2,622**	**495,302**

(1) The balances in the disclosure include balance sheet and off-balance sheet balances reflecting credit risk, excluding amounts of deferred taxes and investments in financial corporations below deduction thresholds (which are subject to a risk weight of 250%), exposures in respect of counterparty credit risk, and securitization exposures.
(2) The balances reflect the supervisory exposure amounts net of allowances and charge-offs, after credit conversion factors and after credit risk mitigation methods.

Table D-11: Standardized approach – exposures by asset type and risk weight[1][2] (continued)

		March 31, 2018								
		0%	20%	35%	50%	60%	75%	100%	150%	Total amount of credit exposures (after CCF and after CRM)
		NIS millions								
1	Sovereigns, central banks thereof, and national monetary authority	108,084	4,770	-	-	-	-	453	-	113,307
2	Public-sector entities (PSE) other than the central government	2,189	572	-	4,192	-	-	-	-	6,953
3	Banks (including multilateral development banks (MDB))	292	13,510	-	4,347	-	-	96	-	18,245
5	Corporations	-	10,673	-	3,241	-	-	105,293	27	119,234
6	Retail exposures to individuals	-	-	-	-	-	65,965	-	-	65,965
7	Loans to small businesses	-	-	-	-	-	10,857	-	-	10,857
8	Secured by a residential property	-	-	27,310	19,371	-	25,483	3,536	-	75,700
9	Secured by commercial real estate	-	-	-	-	-	-	52,171	-	52,171
10	Loans in arrears	-	-	-	-	-	-	1,060	1,440	2,500
11	Other assets*	3,517	-	-	-	-	-	8,503	627	12,647
11A	* Of which: in respect of shares	-	-	-	-	-	-	1,625	440	2,065
12	Total	114,082	29,525	27,310	31,151	-	102,305	171,112	2,094	477,579

(1) The balances in the disclosure include balance sheet and off-balance sheet balances reflecting credit risk, excluding amounts of deferred taxes and investments in financial corporations below deduction thresholds (which are subject to a risk weight of 250%), exposures in respect of counterparty credit risk, and securitization exposures.
(2) The balances reflect the supervisory exposure amounts net of allowances and charge-offs, after credit conversion factors and after credit risk mitigation methods.

Table D-11: Standardized approach – exposures by asset type and risk weight(1)(2) (continued)

		December 31, 2018								
		0%	20%	35%	50%	60%	75%	100%	150%	Total amount of credit exposures (after CCF and after CRM)
		NIS millions								
1	Sovereigns, central banks thereof, and national monetary authority	110,991	5,169	-	71	-	-	343	41	116,615
2	Public-sector entities (PSE) other than the central government	2,210	407	-	4,614	-	-	-	-	7,231
3	Banks (including multilateral development banks (MDB))	700	13,459	-	5,138	-	-	72	-	19,369
5	Corporations	-	5,993	-	2,437	-	-	112,778	-	121,208
6	Retail exposures to individuals	-	-	-	-	-	64,412	-	-	64,412
7	Loans to small businesses	-	-	-	-	-	9,656	-	-	9,656
8	Secured by a residential property	-	-	27,717	22,003	3,755	23,971	3,644	-	81,090
9	Secured by commercial real estate	-	-	-	-	-	-	54,660	-	54,660
10	Loans in arrears	-	-	-	-	-	-	1,231	1,957	3,188
11	Other assets*	3,166	-	-	-	-	-	8,060	640	11,866
11A	* Of which: in respect of shares	-	-	-	-	-	-	1,103	410	1,513
12	Total	117,067	25,028	27,717	34,263	3,755	98,039	180,788	2,638	489,295

(1) The balances in the disclosure include balance sheet and off-balance sheet balances reflecting credit risk, excluding amounts of deferred taxes and investments in financial corporations below deduction thresholds (which are subject to a risk weight of 250%), exposures in respect of counterparty credit risk, and securitization exposures.
(2) The balances reflect the supervisory exposure amounts net of allowances and charge-offs, after credit conversion factors and after credit risk mitigation methods.

E. Counterparty credit risks

Counterparty risk is defined at the Bank, according to the definition in Proper Conduct of Banking Business Directive 203, as the credit risk arising from transactions in derivative financial instruments. The risk is that the counterparty to the transaction will default before the final settlement of cash flows in the transaction. The market value of the transaction may be positive or negative for any of the parties to the transaction; the market value is not certain, and may change over time and according to movements in the underlying market-risk factors.

Table E-1: Analysis of exposure to counterparty credit risk based on the supervisory approach

		March 31, 2019				March 31, 2018			
		Replacement cost	Potential future exposure	EAD after CRM	RWA	Replacement cost	Potential future exposure	EAD after CRM	RWA
		NIS millions							
1	Present exposure method	**2,000**	**5,913**	**7,913**	**5,111**	3,490	6,544	10,034	6,878
3	Comprehensive approach to credit risk mitigation (for securities financing transactions (SFT))	**-**	**-**	**-**	**-**	-	-	-	-
6	Total	**2,000**	**5,913**	**7,913**	**5,111**	3,490	6,544	10,034	6,878

		December 31, 2018			
		Replacement cost	Potential future exposure	EAD after CRM	RWA
		NIS millions			
1	Present exposure method	2,886	6,383	9,269	6,449
3	Comprehensive approach to credit risk mitigation (for securities financing transactions (SFT))	-	-	-	-
6	Total	2,886	6,383	9,269	6,449

Table E-2: Capital allocation in respect of adjustment of revaluation to credit risk

		March 31, 2019		March 31, 2018		December 31, 2018	
		EAD after CRM	RWA	EAD after CRM	RWA	EAD after CRM	RWA
		NIS millions					
3	Total portfolios in respect of which CVA is calculated according to the standardized approach	**7,913**	**3,047**	10,034	4,008	9,269	3,327

F. Market risk

Market risk is the risk of loss or decline in value as a result of change in the economic value of a financial instrument, or of a particular portfolio, due to changes in prices, rates, spreads, and other market parameters. This includes:

- **Interest-rate risk –** The risk of loss or decline in value as a result of changes in interest rates in the various currencies;
- **Currency risk –** The risk of loss as a result of changes in exchange rates;
- **Inflation risk –** The risk of loss as a result of changes in the curve of CPI expectations;
- **Share price risk –** The risk of loss as a result of changes in stock prices or in stock indices;
- **Credit spread risk –** The risk of loss as a result of change in the spread between the yield to maturity of corporate bonds traded in the markets and the relevant risk-free interest rate;
- **Volatility risk –** The risk of loss as a result of changes in the volatility rates quoted in the market;
- **Basis spread risk –** The risk of loss as a result of changes in the spreads between different interest-rate curves or different interest bases.

The main risk factors to which the Bank is exposed are NIS interest rates in the linked and unlinked segments, inflation, the NIS/USD exchange rate, and spreads between different interest-rate curves.

For more extensive information regarding market risks and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

F.1. Market risk in the trading book

Table F-1: Market risk according to the standardized approach

The Bank is required to allocate capital in respect of market risk assets, on the basis of a standardized model defined by the Bank of Israel. The regulatory capital adequacy is calculated for interest-rate and share risks in the trading book alone, as defined above, and for currency risks in the banking book and in the trading book.

		March 31, 2019	March 31, 2018	December 31, 2018
		Risk-adjusted assets in NIS millions		
	Direct products			
1	Interest-rate risk (general and specific)	**2,174**	2,959	2,302
2	Share position risk (general and specific)	**20**	88	82
3	Exchange-rate risk	**213**	913	738
4	Commodity risk	**-**	-	-
	Options			
5	Simplified approach	**-**	-	-
6	Delta-plus approach	**591**	732	307
7	Scenario approach	**-**	-	-
8	Securitization	**-**	-	-
9	Total	**2,998**	4,692	3,429

F.2. Interest-rate risk in the banking book

Interest-rate risk in the banking book refers to the potential effect of changes in the various interest-rate curves on the economic value of the Bank (i.e. change in the present value of assets and liabilities) and/or on net interest income (accounting income sensitivity). The risk emerges during the routine and proactive banking activity of the Bank, as a result of the provision of routine services to the general public and to the business and financial sectors, and from other activities; this includes interest-rate exposure arising from the management of the investment portfolio. The risk arises from differences in the structure of assets and liabilities – gaps between segments, durations, interest bases, interest-rate renewal dates, and more. Limits apply at the Bank both to the sensitivity of economic value and to the sensitivity of income (including financial subsidiaries under the Bank's management and subsidiaries with exposure significant for the Group) to scenarios of change in the shekel, CPI-linked, and foreign-currency interest-rate curves.

Table F-2: Adjusted* net fair value of the financial instruments of the Bank and its consolidated companies**

	March 31, 2019			December 31, 2018		
	NIS	Foreign currency	Total	NIS	Foreign currency	Total
	NIS millions					
Adjusted net fair value*	**32,913**	**1,198**	**34,111**	32,971	1,120	34,091
Of which: banking book	**32,540**	**1,093**	**33,633**	32,822	741	33,563

* Net fair value of financial instruments, excluding non-monetary items and after the effect of employee benefit liabilities and attribution of on-demand deposits to the periods.

** Includes balances attributed to a discontinued operation.

For further details regarding assumptions used to calculate the fair value of financial instruments, see Note 17 to the Condensed Financial Statements.

Table F-3: Effect of scenarios of changes in interest rates on the adjusted* net fair value of the Bank and its consolidated companies**

	March 31, 2019			December 31, 2018		
	NIS	Foreign currency	Total	NIS	Foreign currency	Total
	NIS millions					
Parallel changes						
1% parallel increase	**538**	**223**	**761**	415	211	626
Of which: banking book	**505**	**282**	**787**	441	227	668
1% parallel decrease	**(569)**	**(208)**	**(777)**	(389)	(270)	(659)
Of which: banking book	**(540)**	**(196)**	**(736)**	(446)	(238)	(684)
Non-parallel changes						
Steepening(1)	**(23)**	**82**	**59**	(201)	119	(82)
Flattening(2)	**151**	**(61)**	**90**	124	(32)	92
Increase in short-term interest rate	**351**	**(25)**	**326**	122	178	300
Decrease in short-term interest rate	**(369)**	**34**	**(335)**	(278)	(207)	(485)

* Net fair value of financial instruments, excluding non-monetary items and after the effect of employee benefit liabilities and attribution of on-demand deposits to the periods.

** Includes balances attributed to a discontinued operation.

(1) Steepening – decrease in the short-term interest rate and increase in the long-term interest rate.

(2) Flattening – increase in the short-term interest rate and decrease in the long-term interest rate.

This table presents the change in the adjusted net fair value of all of the financial instruments under the assumption that the noted change occurs in all interest rates, in all linkage segments.

Table F-4: Sensitivity of the economic capital of the Bank to parallel changes in interest-rate curves (theoretical change in economic value as a result of each scenario)

	March 31, 2019			December 31, 2018		
	Unlinked NIS	CPI-linked NIS	Foreign currency	Unlinked NIS	CPI-linked NIS	Foreign currency
	NIS millions					
Parallel changes						
1% parallel increase	**197**	**(476)**	**258**	239	(506)	275
1% parallel decrease	**(181)**	**556**	**(279)**	(242)	592	(297)

The above table presents an analysis of the sensitivity of the Bank's economic value to changes in interest-rate curves, based, among other factors, on the discounting of expected cash flows by interest-rate curves that do not take into account the credit risk spread of the counterparty, with the use of internal models for some products. This differs from a fair-value calculation, which is based on factors including the discounting of expected cash flows by an interest rate reflecting the risk level inherent in the financial instrument, taking into consideration liabilities to employees, which are not used by the Bank in the management of economic value sensitivity.

Table F-5: Effect of scenarios of changes in interest rates on interest income*

	March 31, 2019			December 31, 2018		
	Interest income	Non-interest financing income	Total	Interest income	Non-interest financing income	Total
	NIS millions					
Parallel changes						
1% parallel increase	**850**	**521**	**1,370**	838	522	1,360
Of which: banking book	**850**	**505**	**1,355**	838	552	1,390
1% parallel decrease	**(680)**	**(576)**	**(1,256)**	(596)	(563)	(1,159)
Of which: banking book	**(680)**	**(546)**	**(1,226)**	(596)	(575)	(1,171)

* Does not include the data of the Isracard Group, which constitutes a discontinued operation.

Income sensitivity in the table above was calculated according to the management approach, which includes assumptions regarding models of current-account balances and the change in spreads of deposits with changes in the interest rate, in some of the scenarios, and involves the use of interest-rate floors. The sensitivity of the trading book was calculated using the MTM approach.

F.3. Share and credit spread risk – investment risk

Investment risk is defined at the Bank as exposure to the stock market, to credit spreads, and to credit risk in the bond and stock markets in the banking book of the Group (as a result of holdings in these products, the Bank may also be exposed to interest-rate risks and/or currency risks and/or liquidity risks, which are managed separately). According to the definition at the Bank, Israeli government bonds in NIS and in foreign currency and government bonds of the country in which a branch/subsidiary operates, held by the branch/subsidiary, do not bear investment risk, and are therefore not included in the measurement of investment risk at the Bank.

For more extensive information regarding investment risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018; the Annual Financial Statements for 2018; and the Condensed Financial Statements as at March 31, 2019.

G. Liquidity risk

Liquidity risk – Liquidity risk is defined as present or future risk to the stability and profits of the Bank arising from an inability to sustain the cash flow required for its needs. Liquidity risk at the Bank is examined from a broader perspective, encompassing the ability to repay liabilities on schedule, including during times of stress, without damage to routine operations within the business plans of the Bank and without incurring exceptional losses.

Refinancing risk – The risk of inability to raise new resources to replace resources that have matured, or the risk that the reissue may be performed at durations and terms that damage the Bank's net interest income. This risk is managed as part of liquidity risk. In light of the financing sources of the Bank, the Bank does not view this risk as a material risk in its own right. The Bank accords high importance to raising resources that are stable and highly diversified.

Table G-1: Liquidity coverage ratio – limited banking corporation and consolidated subsidiaries, for the three-month period

	For the quarter ended March 31, 2019*	
	Total unweighted value**	Total weighted value***
Total high-quality liquid assets		
Total high-quality liquid assets (HQLA)		**109,781**
Cash outflows		
Retail deposits from individuals and from small business customers, of which:	**199,076**	**15,148**
Stable deposits	**64,572**	**3,229**
Less stable deposits	**94,389**	**10,716**
Deposits for a period greater than 30 days (Section 84 of Proper Conduct of Banking Business Directive 221)	**40,115**	**1,203**
Unsecured wholesale financing, of which:	**111,114**	**70,477**
Operational deposits (all counterparties) and deposits in networks of cooperative banks	**1,817**	**454**
Non-operational deposits (all counterparties)	**108,300**	**69,026**
Unsecured debts	**997**	**997**
Secured wholesale financing	**3**	**-**
Additional liquidity requirements, of which:	**119,329**	**26,120**
Outflows related to derivative exposure and other collateral requirements	**17,713**	**16,182**
Outflows related to loss of funding on debt products	**-**	**-**
Credit and liquidity facilities	**101,616**	**9,938**
Other contractual funding obligations	**15,299**	**15,299**
Other contingent funding obligations	**54,076**	**1,813**
Total cash outflows		**128,857**
Cash inflows		
Secured lending (e.g. reverse repos)	**725**	**725**
Inflows from fully performing exposures	**31,739**	**24,627**
Other cash inflows	**20,242**	**15,784**
Total cash inflows	**52,706**	**41,136**

	Total adjusted value****
Total high-quality liquid assets (HQLA)	**109,781**
Total net cash outflows	**87,721**
Liquidity coverage ratio (%)	**125%**

* Includes balances attributed to a discontinued operation.

** Unweighted values were calculated as outstanding balances maturing or callable within 30 days (for inflows and outflows), based on an average of daily observations.

*** Weighted values were calculated after the application of respective haircuts or inflow and outflow rates (for inflow and outflow), based on an average of daily observations. The number of observations used to calculate the averages in the reported quarter is 63.

**** Adjusted values were calculated after the application of: (1) haircuts and inflow and outflow rates; and (2) any applicable caps (i.e. caps on level 2B and level 2 assets for HQLA and a cap on inflows).

Table G-1: Liquidity coverage ratio – limited banking corporation and consolidated subsidiaries, for the three-month period (continued)

	For the quarter ended March 31, 2018*	
	Total unweighted value**	Total weighted value***
Total high-quality liquid assets		
Total high-quality liquid assets (HQLA)		108,529
Cash outflows		
Retail deposits from individuals and from small business customers, of which:	186,550	14,541
Stable deposits	60,600	3,030
Less stable deposits	89,774	10,426
Deposits for a period greater than 30 days (Section 84 of Proper Conduct of Banking Business Directive 221)	36,176	1,085
Unsecured wholesale financing, of which:	114,794	75,171
Operational deposits (all counterparties) and deposits in networks of cooperative banks	1,673	418
Non-operational deposits (all counterparties)	112,105	73,737
Unsecured debts	1,016	1,016
Secured wholesale financing	51	-
Additional liquidity requirements, of which:	106,592	22,302
Outflows related to derivative exposure and other collateral requirements	14,973	13,240
Outflows related to loss of funding on debt products	-	-
Credit and liquidity facilities	91,619	9,062
Other contractual funding obligations	14,341	14,341
Other contingent funding obligations	57,857	1,894
Total cash outflows		128,249
Cash inflows		
Secured lending (e.g. reverse repos)	588	588
Inflows from fully performing exposures	31,068	23,733
Other cash inflows	16,831	12,510
Total cash inflows	48,487	36,831

	Total adjusted value****
Total high-quality liquid assets (HQLA)	108,529
Total net cash outflows	91,418
Liquidity coverage ratio (%)	119%

* Includes balances attributed to a discontinued operation.

** Unweighted values were calculated as outstanding balances maturing or callable within 30 days (for inflows and outflows), based on an average of daily observations. The number of observations used to calculate the averages in the reported quarter is 62.

*** Weighted values were calculated after the application of respective haircuts or inflow and outflow rates (for inflow and outflow), based on an average of daily observations.

**** Adjusted values were calculated after the application of: (1) haircuts and inflow and outflow rates; and (2) any applicable caps (i.e. caps on level 2B and level 2 assets for HQLA and a cap on inflows).

Table G-1: Liquidity coverage ratio – limited banking corporation and consolidated subsidiaries, for the three-month period (continued)

	For the quarter ended December 31, 2018*	
	Total unweighted value**	Total weighted value***
Total high-quality liquid assets		
Total high-quality liquid assets (HQLA)		106,375
Cash outflows		
Retail deposits from individuals and from small business customers, of which:	195,062	15,032
Stable deposits	63,494	3,175
Less stable deposits	93,346	10,710
Deposits for a period greater than 30 days (Section 84 of Proper Conduct of Banking Business Directive 221)	38,222	1,147
Unsecured wholesale financing, of which:	107,845	69,011
Operational deposits (all counterparties) and deposits in networks of cooperative banks	1,738	435
Non-operational deposits (all counterparties)	105,776	68,245
Unsecured debts	331	331
Secured wholesale financing	8	-
Additional liquidity requirements, of which:	118,042	27,613
Outflows related to derivative exposure and other collateral requirements	19,765	17,957
Outflows related to loss of funding on debt products	-	-
Credit and liquidity facilities	98,277	9,656
Other contractual funding obligations	15,827	15,827
Other contingent funding obligations	55,580	1,834
Total cash outflows		129,317
Cash inflows		
Secured lending (e.g. reverse repos)	894	894
Inflows from fully performing exposures	29,486	22,556
Other cash inflows	21,795	17,352
Total cash inflows	52,175	40,802

	Total adjusted value****
Total high-quality liquid assets (HQLA)	106,375
Total net cash outflows	88,515
Liquidity coverage ratio (%)	120%

* Includes balances attributed to a discontinued operation.

** Unweighted values were calculated as outstanding balances maturing or callable within 30 days (for inflows and outflows), based on an average of daily observations.

*** Weighted values were calculated after the application of respective haircuts or inflow and outflow rates (for inflow and outflow), based on an average of daily observations. The number of observations used to calculate the averages in the reported quarter is 64.

**** Adjusted values were calculated after the application of: (1) haircuts and inflow and outflow rates; and (2) any applicable caps (i.e. caps on level 2B and level 2 assets for HQLA and a cap on inflows).

The average ratio during the quarter (the average of the daily observations) is 125%, consolidated, and 122% for the stand-alone banking corporation, while the minimum requirement is 100%. This ratio increased during the quarter, in comparison to the preceding quarter. The increase in the ratio mainly resulted from an increase in retail deposits. There is some volatility from day to day during the month, and some interchange between NIS and foreign currency, mainly due to activity in derivatives.

The liquid assets of the Bank mainly consist of Israeli government bonds in NIS and in foreign currency, US government bonds in foreign currency, and deposits with central banks (the Bank of Israel and the Federal Reserve). Part of the liquid assets are held by the Bank, and part are held by the subsidiaries. The Bank takes into consideration possible restrictions on the transfer of liquidity between some subsidiaries and the Bank itself, particularly banking subsidiaries overseas. Accordingly, some of the subsidiaries hold liquid assets for times of crisis (or a credit line from the parent company), according to need, and the Bank does not rely on these assets. The Bank manages the liquidity coverage ratio, and accordingly its liquid assets, with a separation of NIS and foreign currencies. For details of liquid assets by level, see the table below. The Board of Directors of the Bank has adopted an internal limit stricter than the regulatory LCR requirement, both for the stand-alone banking corporation and consolidated.

The main source of funding of the Bank is deposits from retail customers and small businesses in Israel, which generate low liquidity risk relative to other resources. In addition, the Bank obtains financing through issues, deposits from corporate and financial companies, and more. Funding in foreign currency includes deposits of private customers and corporate clients in Israel, foreign residents, Israeli companies abroad, issues of CDs and other instruments secured by the FDIC in the United States, and additional resources. Deposits from corporate and financial entities with a maturity date of up to one month are subject to high outflow coefficients, pursuant to the directive, and therefore have a relatively large contribution to cash outflow. The Bank monitors the concentration of funding sources, in various breakdowns, in both NIS and foreign currency, and complies with the internal limits in this area. The Bank does not rely on funding from the capital market as a major financing source.

Derivatives create a large inflow and a large outflow, and lead to redirection of liquid assets and net cash outflow between NIS and foreign currency, but their net contribution in all currencies is low. In the calculation of liquid assets, the Bank does not include collateral which it is required to deposit against derivatives activity; volatility in the volume of this deposit is taken into consideration, as required in the directive.

Liquidity and refinancing risks are managed based on a global view of the Bank's activity in Israel, at its overseas branches, and at subsidiaries with significant liquidity risk for the Group. Liquidity risk at the Bank, in foreign currency and in NIS, is managed and controlled routinely at the Asset and Liability Management Division, in accordance with Group policy, with the aim of ensuring the ability to cope competitively even in exceptional supply and demand situations in the financial markets. Current liquidity management is under the responsibility of the Asset and Liability Management Division, and is executed through NIS and foreign-currency liquidity units, and through corresponding units at the subsidiaries. Reports to Board of Management committees are submitted on a monthly basis; reports to Board of Directors committees are submitted on a quarterly basis. Additional reports to internal functions for monitoring and management purposes are submitted more frequently. The business plan of the Bank takes expected business changes, future liquidity requirements, and future liquidity risks into consideration, in order to ensure that the Bank continues to comply with all limits. The Market and Liquidity Risk Management Department in the Risk Management Area routinely monitors liquidity using internal and environmental parameters, independently reports the risk level to the committees of the Board of Management and the Board of Directors, and challenges the parameters in the various models related to liquidity.

Table G-2: Details of liquid assets, by level, as required in the Basel directives

	Balance as at March 31, 2019	**Average in the quarter ended March 31, 2019**
	NIS millions	
Level 1 assets	**105,803**	**108,157**
Level 2A assets	**1,293**	**1,296**
Level 2B assets	**347**	**328**
Total HQLA	**107,444**	**109,781**

	Balance as at March 31, 2018	Average in the quarter ended March 31, 2018
	NIS millions	
Level 1 assets	102,333	107,796
Level 2A assets	561	557
Level 2B assets	153	176
Total HQLA	103,047	108,529

	Balance as at December 31, 2018	Average in the quarter ended December 31, 2018
	NIS millions	
Level 1 assets	105,564	105,039
Level 2A assets	1,181	1,030
Level 2B assets	315	306
Total HQLA	107,060	106,375

For additional information regarding liquidity risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

H. Operational risk

Operational risk is defined as the risk of loss that may be caused by failed or faulty internal processes, human actions, system malfunctions, or external events. The definition includes legal risk, but does not include strategic risk or reputational risk. Failures related to one of the aforesaid factors may cause damage to profitability. The Bank operates control units, including Information Systems Security and Cyber Defense, Business Continuity, Security, the Compliance Officer, and Anti-Money Laundering and Terrorism Financing Prevention, as well as comprehensive procedures and systems in areas related to banking activity, management of human resources, process control, emergency operation, and more.

For additional information regarding operational risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

I. Compliance risk

Compliance risk is the risk of imposition of a legal or regulatory sanction, material financial loss, or reputational damage which the banking corporation may suffer as a result of a failure to comply with the compliance directives, as defined in Proper Conduct of Banking Business Directive 308.

Pursuant to Proper Conduct of Banking Business Directive 308, compliance risk also includes risks related to the fairness of the Bank towards its customers, conflicts of interest, the prohibition of money laundering and financing of terrorism (including with respect to tax laws), provision of advice to customers, securities enforcement, protection of privacy (excluding information-technology aspects), the US FATCA directives and the international CRS directives, and taxation aspects relevant to products or services for customers, or directives of a similar nature. Compliance risk also includes the reputational risk that accompanies failure to comply with such directives.

Imposition of monetary sanctions by the Supervisor of Banks: Over the last few months, there has been an increase in instances of monetary sanctions imposed on banks and credit-card companies (including the Bank and Isracard) by the Banking Supervision Department, in cases in which, according to the position of the Banking Supervision Department, flaws or deficiencies have been discovered in the conduct of the financial institutions. For more detailed and extensive information, see Section 5.2, "Other matters," in the Corporate Governance Report.

For additional information regarding compliance risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

J. Legal risk

Legal risk includes, among other matters, legal claims, rulings, inability to enforce contracts, and exposure to fines, penalties, or punitive damages as a result of supervisory actions and private settlements that may disrupt or adversely affect the activity of the Bank Group. The Group has a structure of internal and external legal counsel in order to contend with this risk.

For additional information regarding legal risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018; the Annual Financial Statements for 2018 and Note 25 to the Annual Financial Statements for 2018; and Note 10 to the Condensed Financial Statements as at March 31, 2019.

K. Reputational risk

Reputational risk is defined as present or future risk of damage to income or capital as a result of a negative image in the eyes of relevant stakeholders, such as customers, parties to transactions, shareholders, investors, or regulatory agencies. This risk, which usually accompanies other activities and other risks, may materialize in various ways, such as customer departures, new regulation, and more.

For additional information regarding reputational risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

L. Regulatory risk

Regulatory risk is risk to the Group's income and/or capital arising from legislative processes and/or draft directives of various regulatory agencies that cause changes in the Group's business environment. Such changes may occasionally influence the Group's ability to offer certain services, and/or may obligate the Group to carry out technological and other investments at considerable cost, while disrupting schedules for development of other planned services.

For additional information regarding regulatory and legislative risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

For details regarding material regulatory initiatives with an effect on the activity of the Bank during the reported period, see Note 16 to the Condensed Financial Statements as at March 31, 2019.

M. Economic risk

Risk factors in the economic environment are identified by the Economics Department, which tracks current economic and financial data in Israel and worldwide and professionally evaluates the implications of the data. The department maps potential risks in the economy and in the financial markets, and reports to the relevant teams and committees.

For additional information regarding economic risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

For details regarding conditions in the Israeli and global economy, see the section "Economic review" in the Report of the Board of Directors and Board of Management as at March 31, 2019.

N. Strategic risk

Strategic risk is material present or future risk to profits, capital, reputation, or status that may be caused by changes in the business environment; faulty business decisions; improper implementation of strategy or business decisions; or failure to respond to changes in the industry (e.g. competitors' actions), the economy, or technology. Strategic risk is also a function of the congruence of the organization's strategic objectives with its environment, adaptation of the business plans that it develops to achieve these objectives, resource allocation, and quality of implementation. As such, this risk constitutes forward-looking information.

For additional information regarding strategic risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.

O. Environmental risk

Environmental risk to the Bank is the risk of loss as a result of directives related to the protection of the environment and the enforcement thereof, which may materialize if the Bank bears direct responsibility for an environmental hazard, including the possibility that the Bank may be required to remove an environmental hazard, or may be liable to a third party in respect of an environmental hazard, or as a result of the impairment of realized collateral. This risk may also materialize indirectly as a result of the deterioration of the financial condition of another entity due to environmental costs stemming from directives related to the protection of the environment. Reputational risk may also materialize as a result of the association of the Bank to a party causing environmental damage.

For additional information regarding environmental risk and the management thereof, see the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2018, and the Annual Financial Statements for 2018.