

Bank Hapoalim

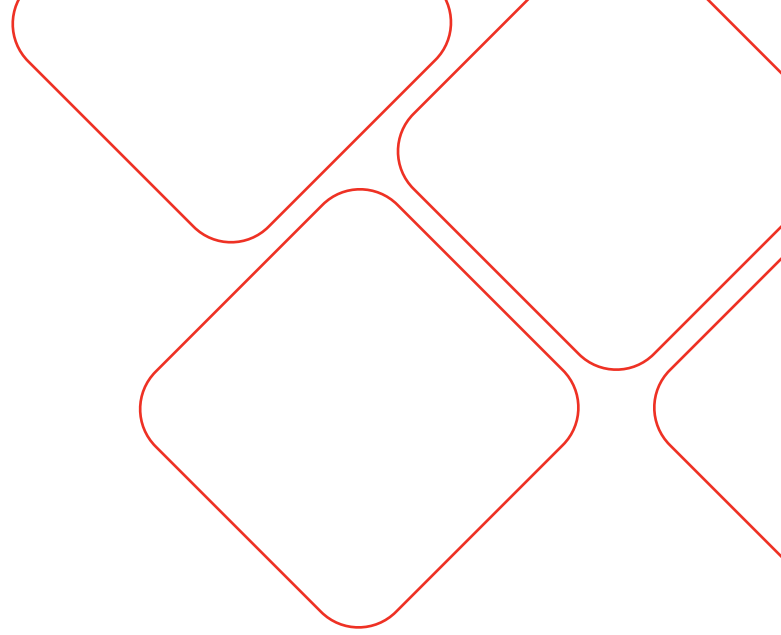
Report on Risks

Pillar 3 Disclosure and Additional

Information Regarding Risks

as at June 30, 2023





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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 June 30, 2023.

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.

This Report on Risks is published within the financial reporting of Bank Hapoalim B.M., and contains 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, 2022, and the Condensed Financial Statements as at June 30, 2023.

Sincerely yours,

Ruben Krupik

Chairman of the
Board of Directors

Dov Kotler

President and
Chief Executive Officer

Merav Ben Shushan Cohen

Senior Deputy Managing Director,
Chief Risk Officer

Tel Aviv, August 13, 2023

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, macroeconomic 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 Construction and 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. As part of the discussions of the 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 June 30, 2023.

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				
	June 30, 2023	March 31, 2023	December 31, 2022	September 30, 2022	June 30, 2022
NIS millions					
Available capital					
Common equity Tier 1 capital	49,449	48,241	46,745	45,262	44,446
Common equity Tier 1 capital before effect of transitional directives ⁽¹⁾	49,160	47,935	46,330	44,830	43,996
Tier 1 capital	49,449	48,241	46,745	45,262	44,446
Tier 1 capital before effect of transitional directives ⁽¹⁾	49,160	47,935	46,330	44,830	43,996
Total capital	63,061	61,704	61,094	58,514	57,619
Total capital before effect of transitional directives ⁽¹⁾	62,777	61,408	60,704	58,103	57,218
Risk-weighted assets					
Total risk-weighted assets (RWA)	429,440	424,532	415,577	407,914	398,865
Total risk-weighted assets (RWA) before effect of transitional directives ⁽¹⁾	429,815	425,346	417,603	409,587	402,830
Capital-adequacy ratios according to the directives of the Banking Supervision Department					
Common equity Tier 1 capital ratio	11.51%	11.36%	11.25%	11.10%	11.14%
Common equity Tier 1 capital ratio before effect of transitional directives ⁽¹⁾	11.44%	11.27%	11.09%	10.95%	10.92%
Tier 1 capital ratio	11.51%	11.36%	11.25%	11.10%	11.14%
Tier 1 capital ratio before effect of transitional directives ⁽¹⁾	11.44%	11.27%	11.09%	10.95%	10.92%
Total capital ratio	14.68%	14.53%	14.70%	14.34%	14.45%
Total capital ratio before effect of transitional directives ⁽¹⁾	14.61%	14.44%	14.54%	14.19%	14.20%
Common equity Tier 1 capital ratio required by the Banking Supervision Department ⁽²⁾	10.23%	10.23%	10.23%	10.23%	10.23%
Available common equity Tier 1 capital ratio beyond the requirement of the Banking Supervision Department ⁽²⁾	1.28%	1.13%	1.02%	0.87%	0.91%
Leverage ratios according to the directives of the Banking Supervision Department					
Total exposures	738,952	738,726	737,115	732,928	720,777
Total exposures before effect of transitional directives ⁽¹⁾	739,102	738,885	737,330	733,152	721,069
Leverage ratio	6.69%	6.53%	6.34%	6.18%	6.17%
Leverage ratio before effect of transitional directives ⁽¹⁾	6.65%	6.49%	6.28%	6.11%	6.10%

(1) Before the effect of adjustments for efficiency plans; before the effect of adjustments in respect of current expected credit losses; and before the effect of adjustments in respect of high-risk loans for land acquisition.

(2) Including a capital requirement at a rate representing 1% of the balance of housing loans at the dates of the financial statements, excluding housing loans for which a relief was granted under the Temporary Order.

Table B-1: Principal supervisory ratios (continued)

	Average for the three months ended				
	June 30, 2023	March 31, 2023	December 31, 2022	September 30, 2022	June 30, 2022
Liquidity coverage ratio according to the directives of the Banking Supervision Department					
Total high-quality liquid assets	175,609	173,662	179,514	189,487	195,054
Total net cash outflows	138,971	136,279	147,712	150,828	154,857
Liquidity coverage ratio (in %)	126%	127%	122%	126%	126%
	On a consolidated basis, as at				
	June 30, 2023	March 31, 2023	December 31, 2022	September 30, 2022	June 30, 2022
Net stable financing ratio according to the directives of the Banking Supervision Department					
Total available stable financing	407,381	410,435	412,150	397,965	403,331
Total required stable financing	326,541	323,578	316,321	312,819	305,916
Net stable financing ratio (%)	125%	127%	130%	127%	132%

B.2. Risk assessment and management

The Bank performs a comprehensive examination to assess the risks to which it is exposed and to determine the materiality of such risks. Within the ICAAP (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, compliance risk, and model 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 (including climate risk).

The risk-management strategy of the Bank Group is designed to support the achievement of the strategic objectives of the Group as a whole, while identifying and quantifying risks, establishing risk ownership, and maximizing business value, taking into consideration costs in terms of risk, by every responsible function at all levels of the organization. Risk management at the Bank is based on a uniform methodology, from a comprehensive perspective, adapted to regulatory requirements, with the aim of supporting risk-taking in an informed manner in order to maximize the Group's profitability at a risk level aligned with its risk appetite.

B.2.a. Risk management structure and organization

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 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 hedging some risks. The Banking Supervision Department has set forth guidelines concerning risk management in the Proper Conduct of Banking Business Directives. The directives detail the requirements of the Banking Supervision Department 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 Banking Supervision Department.

The Chief Risk Officer (CRO) and the member of the Board of Management responsible for the Risk Management Division is Ms. M. Ben Shushan Cohen.

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. I. Furman, and the Head of Retail Banking, Ms. D. Raviv.

The member of the Board of Management responsible for managing market, investment, and liquidity risks is the Head of Financial Markets and International Banking, 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, 2022](#).

B.3. Severity of risk factors

Table B-2: Severity of risk factors

	Risk factor	Risk effect
Financial risks		
1.	Credit risk (including counterparty risk)	Medium
1.1.	Of which: risk in respect of the quality of borrowers and/or collateral	Medium
1.2.	Of which: risk in respect of sector concentration/exposure to credit in the construction and real-estate sectors*	Medium
1.3.	Of which: risk in respect of concentration of borrowers/borrower groups	Medium
2.	Market risk	Low-Medium
2.1.	Of which: interest-rate risk	Low-Medium
2.2.	Of which: inflation risk/exchange-rate risk	Low
3.	Share price and credit spread risk	Low-Medium
4.	Liquidity risk	Low-Medium
Operational and legal risks		
5.	Operational risk	Medium
5.1.	Of which: cyber risk	Medium
5.2.	Of which: IT risk	Medium
6.	Legal risk	Low-Medium
Other risks		
7.	Reputational risk	Low-Medium
8.	Strategic and competitive risk	Medium
9.	Regulatory and legislative risk	Medium
10.	Economic risk – condition of the Israeli economy**	Medium-High
11.	Economic risk – condition of the global economy	Medium
12.	Compliance risk	Medium
13.	Model risk	Medium

* This risk factor reflects the effect of the increasing growth in credit to the construction and real-estate sector and its effect on risk in the portfolio.

** The risk level was raised in light of the potential aggregate effect of the developments in the local and global economy, including the effects of the high inflation and ensuing monetary tightening, the forecasts of a global economic slowdown, and the impacts of the progression of the legislative procedures on judicial matters in the absence of a broad consensus, on the credit rating of the state, combined with proposed regulatory changes, particularly in the area of banking. For further details, also see [the section "Top and emerging risks,"](#) below.

B.4. 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.

Risk management at the Bank Group is described extensively later in this report.

The Board of Management and Board of Directors of the Bank have 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.

- **Macroeconomic 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 macroeconomic environment, taking into consideration the existing risks in the global and Israeli economy, and balances risk and return considerations.

The Bank estimates that a combination of economic and political factors are currently increasing the economic risks to which it is exposed. In early August, the credit-rating agency Fitch downgraded the debt rating of the United States government from AAA to AA+. The downgrade was attributed to the ongoing deterioration in the fiscal position of the United States and an expected deceleration of growth. In Israel, legislation promoted by the government aimed at implementing changes of the judicial system has led to a broad wave of public and social protests. During the second quarter, negotiations were held between the coalition and some opposition parties in an attempt to reach agreements, but the talks were unsuccessful. In July, as part of the planned changes in the judicial system, the Knesset passed an amendment to the Basic Law: The Judiciary, limiting the reasonableness doctrine. The process of passing the law was accompanied by broad social protests. After the law passed, several leading global financial bodies, including the credit-rating agencies Moody's and S&P, issued reviews warning of the economic impacts of continued legislation of changes to the judicial system without a broad consensus. One of the main risk areas, also noted by the credit-rating agency Moody's, is the local high-technology industry. Amid the global circumstances and the political and legal uncertainty, capital raising by these companies dropped sharply in the first half of this year. According to the estimates of the Bank, the risk of a downgrade of the credit rating outlook of the State of Israel, and subsequently possibly a downgrade of its actual rating by the rating agencies, has increased.

The foregoing may lead to other potential effects, such as a decrease in foreign investments in Israel, an increase in country risk and the yield curve, damage to the GDP, and more. Accordingly, further legislative proceedings without a broad consensus, social instability, and the possibility of a downgrade of Israel's debt rating have the potential to negatively affect the Israeli economy, the customers of the Bank, and the Bank itself.

We estimate that the real-estate sector presents another risk. The rising interest rates have led to a sharp decrease in purchases of new homes in Israel. Although construction starts have also started to fall, an increase in the number of unsold new homes is still apparent. Data from the Central Bureau of Statistics point to a slight decrease of 1.6% in prices of new homes thus far. Note that these data do not weigh in benefits sometimes granted at the time of purchase; therefore, actual decreases in prices may be greater. A decrease is also evident in prices of land, and some land sale tenders have closed without bids. While global inflation has started to fall, it is still high and remains far from the inflation targets of the central banks; the central banks are applying tight policies. Globally, rising interest rates have led to adjustments of financial and non-financial asset prices; the prevailing market assessment is now that global growth will slow considerably in the coming quarters. The war in Ukraine continues, and presents another ongoing risk, although the impacts on the European economy thus far have been more moderate than previously estimated. The increase in interest rates of the central banks in Israel and the United States has the potential to contribute positively to the results of operations of the Bank. However, a prolonged high interest-rate environment, combined with a decline in tax revenues and a higher budget deficit, may, among other matters, raise the risks of recession, lead to changes in asset prices (including financial and real-estate assets), lower the level of liquidity in the economy, affect the condition of customers of the Bank, and, accordingly, have a negative effect on the results of operations and profits of the Bank. Note that the rapid rise in interest rates in the first quarter led to liquidity shortages among commercial banks, mainly in the United States. This trend halted in the second quarter.

- **Information-security risk and cyber incidents:** 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. These 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. Note that the transition of employees to remote work, transition to cloud computing, and increased digitization of the activity of the Bank, including an increase in remote work with customers, concurrently with an increase in threats and attempted attacks on the Bank and its customers, have intensified the risk. The Bank is taking action to mitigate this risk.
- **Regulatory environment in Israel and overseas:** Local and international regulatory reforms have implications for the business of the Bank, in Israel and overseas. In Israel, several regulatory initiatives have been formulated over the last few years, primarily concerned with increasing competition in the banking system in Israel; additional regulatory initiatives are in the process of being generated, some of which concern direct intervention in prices and interest rates in the banking industry. Proposals and suggested measures include the intention of the Ministry of Finance to impose a tax on excess profits; the announcement of the Competition Authority regarding the possibility of declaring the banks a concentration group; directives regarding the proposal of the Ministry of Finance to create a default deposit; direct legislative intervention in interest rates on deposits, current accounts, and mortgages through private bills; and draft legislative amendments proposed by the Israel Securities Authority concerning the exclusion of money-market funds from the Advising Law and creation of money-market funds with similar characteristics to deposits. For further details, see [the section "Regulatory initiatives" in the Corporate Governance Report](#). The regulatory initiatives and trends may adversely affect the banking system in general and the Bank in particular. At this stage, it is too early to estimate the effects of these changes, if they occur, on the Bank. Further, these effects may not be immediate; instead, there may be slower, prolonged effects derived from processes of gradual change in the Bank's environment (customers, market players, etc.), alongside the gradual preparations of the Bank for the necessary adaptation of its operations.

- **Competitive and strategic risk:** Competition from big tech companies (Apple, Google, Amazon, and others), fintech companies, and digital banks, alongside the entry of new technologies, changes in customer behavior, and new business models in the financial sphere, may significantly affect the banking system, in Israel and worldwide, in the medium to long term. Concurrently, regulatory and competitive changes in the domestic arena, with an emphasis on measures aimed at increasing competition in the banking industry, bank account switching, and open banking, as well as competition in the business sector, may affect the business results of the Bank, including its credit spreads. The Bank recently formulated a comprehensive strategic plan for the period through 2026, encompassing, among other matters, action in the areas of the core activities of the Bank, innovation, technology, the structure of operations, and more, in order to respond to such threats.
- **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 (including international sanctions), 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 on the global level is reflected in the continuing investigations of banks around the world and in 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.
- **Environmental risk:** Around the world, the understanding has grown in recent years that the materialization of environmental risks and climate risks may cause harm to the economy, and, in extreme cases, may cause significant damage to banks and to the financial system, as a result of the materialization of financial and non-financial risks in the long term. These effects may also be expressed within other risks to which the banking corporation is exposed in the course of its activity, such as credit risk (through the effect on the financial resilience of borrowers and the value of collateral), market and investment risk, operational risk, legal risk, reputational risk, and more. These risks, particularly climate risks and the impact of processes of transition to a low greenhouse-gas emissions economy, have unique characteristics of uncertainty. At this stage, it is too early to estimate the potential long-term effects of these changes on the Bank.

For details regarding legal proceedings, see [Note 10 to the Condensed Financial Statements](#).

For details regarding material regulatory initiatives with an effect on the activity of the Bank during the reported period, see [the Corporate Governance Report](#).

B.5. Discontinuation of publication of the LIBOR interest rates

As of the end of 2021, the publication of the LIBOR interest rates in four currencies (euro, British pound, yen, and Swiss franc) has been discontinued. The LIBOR rates for the US dollar continued to be published until the end of June 2023. The LIBOR rates served as the basis for calculation of interest rates applicable to financial products denominated in or linked to principal foreign currencies with floating rates. As part of the intention to establish alternative benchmark rates for the relevant currencies, global institutions such as ISDA (International Swaps and Derivatives Association) and ARRC (Alternative Reference Rate Committee) have formulated alternatives to these interest rates, new legal language, and proposals for substitution mechanisms. The change affects the banking industry, globally and in Israel.

In accordance with the recommendation of the international committees, the rates of addition to interest rates for the conversion of financial instruments based on these rates were determined in March 2021, according to the ISDA resolutions. The Bank prepared for the substitution of the reference rate for the financial products it offers to customers. The Bank has adapted its technological systems to the new interest rates and mechanisms.

As of January 1, 2022, the reference rates for current-account products and revolving overdrafts have been replaced with the new reference rates. For loans based on the reference rates the publication of which has been discontinued, the Bank acted to replace the legal agreements with the customers and convert all of the products (balance sheet and off-balance sheet), within the change in reference rates.

By June 30, 2023, the reference rates for most of the products had been substituted. In a small number of products, the change will be applied at the first interest-rate update after June 30, 2023. The Bank is continuing to monitor the international publications, and will act with the aim of reducing the risks arising from the interest-rate substitution process.

For additional details, see [Note 1C to the Condensed Financial Statements](#).

B.6. Review of weighted risk-adjusted assets

Table B-3: Review of weighted risk-adjusted assets

	Risk-weighted assets		Minimum capital requirements*
	June 30, 2023	March 31, 2023	June 30, 2023
	NIS millions		
1 Credit risk (standardized approach)**	374,332	371,309	50,535
6 Counterparty credit risk (standardized approach)	9,091	8,855	1,227
10 Credit valuation adjustment (CVA)	4,757	4,572	642
15 Settlement risk	-	-	-
16 Securitization exposures (standardized approach)	13	13	2
25 Amounts below deduction thresholds (subject to 250% risk weight)	8,798	8,533	1,188
Total credit risk	396,991	393,282	53,594
20 Market risk (standardized approach)	4,957	5,180	669
24 Operational risk	27,492	26,070	3,711
27 Total	429,440	424,532	57,974

* Capital requirements according to the minimum required total capital ratio, at a rate of 13.5%.

** 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

	June 30, 2023	June 30, 2022	December 31, 2022	
	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	8,225	8,212	8,212
2	Retained earnings, including dividends proposed or declared after the balance sheet date	43,948	38,750	41,346
3	Accumulated other comprehensive income and disclosed retained earnings	(2,831)	(2,745)	(3,056)
6	Common equity Tier 1 capital before supervisory adjustments and deductions	49,342	44,217	46,502
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	4	16	4
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	26	19	17
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	(137)	(264)	(264)
26C	Of which: additional supervisory adjustments to common equity Tier 1 capital	(137)	(264)	(264)
26C	Of which: in respect of the efficiency plans	(106)	(176)	(141)
26C	Of which: in respect of wage tax	-	-	-
26C	Of which: in respect of the business of the corporation with related persons	130	158	123
26C	Of which: in respect of expected credit losses	(183)	(274)	(274)
26C	Of which: in respect of non-accruing housing loans	22	28	28
28	Total supervisory adjustments and deductions in common equity Tier 1 capital	(107)	(229)	(243)
29	Common equity Tier 1 capital	49,449	44,446	46,745
45	Tier 1 capital	49,449	44,446	46,745

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

	June 30, 2023	June 30, 2022	December 31, 2022	
	NIS millions/percent			
Tier 2 capital				
Tier 2 capital – instruments and provisions				
46	Instruments issued by the banking corporation (not included in Tier 1 capital) and premium on such instruments	5,492	4,381	5,281
48	Tier 2 capital instruments issued by subsidiaries of the banking corporation to third-party investors	3,158	4,149	4,236
50	Collective allowances for credit losses before the effect of related tax	4,962	4,643	4,832
51	Tier 2 capital before deductions	13,612	13,173	14,349
Tier 2 capital – deductions				
57	Total supervisory adjustments to Tier 2 capital	-	-	-
58	Tier 2 capital	13,612	13,173	14,349
59	Total capital	63,061	57,619	61,094
Risk-weighted assets				
	Total risk-weighted assets according to the requirements prior to the adoption of Directive 202, in accordance with Basel 3	428,929	397,515	415,256
	Of which: credit risk assets	396,480	370,068	386,229
	Of which: market risk assets	4,957	3,795	4,007
	Of which: operational risk assets	27,492	23,652	25,020
60	Total risk-weighted assets	429,440	398,865	415,577
Capital ratios and capital preservation cushions				
61	Common equity Tier 1 capital	11.51%	11.14%	11.25%
62	Tier 1 capital	11.51%	11.14%	11.25%
63	Total capital	14.68%	14.45%	14.70%
Minimum requirements established by the Banking Supervision Department				
69	The required minimum common equity Tier 1 capital ratio is 10%. A capital requirement is added to this ratio at a rate representing 1% of the balance of housing loans at the dates of the financial statements, excluding housing loans for which a relief was granted under the Temporary Order.	10.23%	10.23%	10.23%
71	The required minimum total capital ratio is 13.5%.	13.50%	13.50%	13.50%
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	586	538	480
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	111	108	105
75	Deferred tax assets arising from timing differences, below the deduction threshold	3,558	3,463	3,436
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	5,893	4,749	5,198
77	Ceiling for inclusion of provision in Tier 2 under the standardized approach	4,962	4,643	4,832

C.2. Capital adequacy

C.2.a. The Bank's approach to capital-adequacy assessment

The Bank applies capital measurement and adequacy directives based on the Basel directives, as published by the Banking Supervision Department.

The capital measurement and adequacy directives are based on three pillars:

- Pillar 1 – Includes the manner of calculation of the supervisory minimum capital requirements in respect of credit risks, operational risk, and market risk.
- Pillar 2 – Sets the forth internal processes (the ICAAP – Internal Capital Adequacy Assessment Process) used by banks to assess the required capital in respect of risks in aggregate, including those not covered by Pillar 1 (such as credit concentration, interest-rate risk in the banking book, liquidity risks, settlement risks, and strategic risks), as well as a review process performed by the Banking Supervision Department.
- Pillar 3 – Market discipline; this pillar requires quantitative and qualitative disclosure within the report to the public on the risks to which the bank is exposed, in order to estimate the extent of the bank's exposure to risk factors.

The Basel Committee on Banking Supervision is applying updates to the framework for capital-adequacy measurement, sometimes referred to as "Basel 4." Significant updates have been established in connection with the method of calculating risk-adjusted assets in respect of which capital requirements are required to be calculated in Pillar 1. The standards included in the update are expected to be implemented in the European Union in 2025.

In accordance with its policy of adopting prevalent international standards, the Banking Supervision Department has adopted the directives of the Basel Committee of 2017 on the subject of the calculation of credit requirements in respect of operational risk. On December 29, 2022, the Banking Supervision Department issued a draft update of Proper Conduct of Banking Business Directive 206, "Capital Measurement and Adequacy – Operational Risk." The draft establishes an updated definition for the calculation of the capital allocation in respect of operational risk, such that it is based, among other things, on components of the business indicator described in the draft and on an internal loss multiplier based on the average historical losses of the banking corporation. Pursuant to the draft, implementation of the directive will begin on January 1, 2026.

C.2.b. Capital-adequacy target and capital planning and management

Pursuant to the directives of the Banking Supervision Department, the Bank, as a banking corporation of significant importance (a banking corporation whose total balance sheet assets on a consolidated basis constitute at least 24% 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 10.0% and a minimum total capital ratio of 13.5%. A capital requirement is added to the common equity Tier 1 capital ratio at a rate representing 1% of the balance of housing loans at the dates of the financial statements, excluding housing loans for which a relief was granted under the Temporary Order aimed at coping with the coronavirus crisis. 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, as at June 30, 2023, stand at 10.23% and 13.50%, respectively.

The common equity Tier 1 capital target established by the Bank takes into consideration, among other matters, the results of the internal processes of the Bank for determining capital targets, including the results of internal stress tests run by the Bank, and the outcomes of discussions held with the Banking Supervision Department regarding the specific risk attributes of the Bank, within the most recent supervisory review process and the most recent uniform stress tests performed.

In order to comply with the capital-adequacy target and manage capital effectively, capital planning is performed at the Bank based on the work plan of the Bank and on regulatory directives, which are translated into risk-adjusted assets and changes in the various tiers of capital, while maintaining safety margins. Various sensitivity tests are applied within the planning of capital and capital ratios. The Bank also routinely monitors actual results as compared to planning, and the gaps between results and planning, and, as necessary, examines the actions needed in order to comply with the established capital targets. As part of the establishment of the internal capital targets of the Bank, as detailed below, the policy of the Bank is to maintain capital adequacy at a level higher than the minimum ratio required by the Banking Supervision Department, and not lower than the level of capital adequacy required to cover the risks as assessed in the Internal Capital Adequacy Assessment Process (ICAAP). Within the ICAAP, the Bank examines the effect of stress scenarios on capital-adequacy ratios; accordingly, plans are in place for preparedness to return to regulatory capital adequacy in the case of a such a stress event.

Based on the processes of establishment of internal capital targets of the Bank and the results of the internal discussions held with the Banking Supervision Department (as described above), the Board of Directors of the Bank set an internal target for the common equity Tier 1 capital ratio at a rate of no less than 10.5%.

The Bank manages its capital-adequacy ratio with the aim of complying with the minimum capital requirements of the Banking Supervision Department and with the internal target, while maintaining safety margins.

The capital of the Bank and the volume of risk-adjusted assets are subject to changes, due to the following factors, among others:

- Effects of changes in the interest rate on capital reserves from bonds available for sale.
- Effects of changes in the CPI and in exchange rates on asset balances.
- Actuarial changes resulting from changes in the interest rate for the calculation of the Bank's liabilities, or other actuarial assumptions.

The sensitivity of the capital reserve in respect of bonds available for sale, net, after tax effect, to a theoretical increase of 1% in the risk-free yield curve and in the credit risk spread is estimated at a decrease in the amount of approximately NIS 0.7 billion and approximately NIS 0.7 billion, respectively. By contrast, the sensitivity of the capital reserve arising from adjustments for actuarial changes, net, after tax effect, to a theoretical increase of 1% in the discount rate is estimated at an increase in the amount of approximately NIS 0.2 billion. Capital requirements in respect of the exposures of the Bank to the government of Israel, Israeli banks, institutional entities, and public-sector entities are derived from the rating of the State of Israel.

The direct effect of a downgrade of the credit rating of the State of Israel by Standard & Poor's Rating Group, if it occurs, would lead to a reduction of 0.23% and 0.29% in the Tier 1 capital ratio and the total capital ratio, respectively.

Dividends

Dividend distribution by the Bank is subject to tests and limits set forth in the Companies Law and in the directives of the Banking Supervision Department, including Proper Conduct of Banking Business Directive 331. Any distribution and the rate thereof are subject to a specific resolution of the Board of Directors of the Bank, based on its judgment at the date of the distribution, taking into account the directives of all laws, any constraints on distribution, and business considerations, including the strategy of the Bank.

The dividend distribution policy of the Bank is to distribute up to 40% of quarterly net operating profit.

On May 22, 2023, the Board of Directors of the Bank declared the distribution of dividends in the amount of NIS 803 million, which constituted approximately 40% of the net profit of the Bank for the first quarter of 2023, paid on June 14, 2023.

At the date of approval of these financial statements, with due attention to the financial results, the capital needs of the Bank, and the aforesaid distribution policy, the Board of Directors of the Bank resolved to declare the distribution of dividends in the amount of NIS 769 million, constituting approximately 40% of the net profit of the Bank for the second quarter of 2023, to be paid on September 6, 2023.

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

Improving operational efficiency

The circulars of the Banking Supervision Department grant reliefs to banks that apply improvements in efficiency, with respect to personnel and to real estate.

The total volume of the personnel efficiency plan from 2020 to which the reliefs apply is NIS 352 million, net of tax effect.

The effect of the aforesaid plans was recorded to capital, and, for the purposes of calculation of the capital ratio and leverage ratio, deducted from supervisory capital over a period of five years from the date of beginning of implementation of each plan.

The remaining effect of the reliefs in respect of the efficiency plans on the common equity Tier 1 capital ratio is estimated at approximately 0.02% as at June 30, 2023.

The subsidiary of the Bank in Turkey

The Bank Group holds 100% of the share capital of Bank Pozitif, in Turkey, which is engaged in corporate banking. In accordance with the strategy of the Bank, the Bank is acting to sell its holding in Bank Pozitif. Accordingly, the Bank is working to gradually reduce the credit portfolio of Bank Pozitif.

On March 30, 2023, the Bank entered into an agreement for the sale of its holding in Bank Pozitif, for a consideration primarily consisting of repayment of credit granted to Bank Pozitif at the time of completion of the transaction. The regulatory approvals required for the transaction have been received, and the Bank is working towards its completion. If the transaction is completed, no material effect on the financial statements of the Bank is expected.

In accordance with the requirement of the Banking Supervision Department, risk-adjusted assets in respect of the subsidiary were weighted at a rate of 300%.

The Bank also has a credit line for Bank Pozitif, which was granted at an interest rate below market terms, taking into consideration the position of the Turkish regulator regarding the pricing of the credit line, and the challenging condition of the Turkish economy and of Bank Pozitif. In accordance with a requirement of the Banking Supervision Department in Israel, due to the aforesaid pricing, the balance of the credit line was deducted from supervisory capital. The credit line was renewed in November 2022, in the amount of approximately USD 35 million, for the earlier of twelve months or until the date when the Bank ceases to be a shareholder of Bank Pozitif. As at the end of June 2023, approximately USD 20 million of the credit line is utilized. The aforesaid effects, in total, on the common equity Tier 1 capital ratio of the Bank as at June 30, 2023, amount to a reduction of 0.05%.

Notes with a loss-absorption mechanism

For additional information regarding the subordinated notes, see [Note 9J to the Condensed Financial Statements](#).

Circular updating Proper Conduct of Banking Business Directive 203, "Capital Measurement and Adequacy – Standardized Approach – Credit Risk"

A circular updating Proper Conduct of Banking Business Directive 203, "Capital Measurement and Adequacy – Standardized Approach – Credit Risk," was issued on May 22, 2022. Pursuant to the circular, loans designated for the acquisition of land for the purpose of development or construction at a rate exceeding 80% of the value of the acquired asset (LTV) are added to the list of loans risk weighted at 150%, with the exception of loans for the acquisition of agricultural land with no planning horizon or intention to apply for a change in designation. The effect of the circular was spread over equal quarterly installments, from September 30, 2022, to implementation of the full effect on June 30, 2023. A questions and answers document was released on January 26, 2023, containing clarifications regarding the implementation of the circular.

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 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 is the total of balance sheet exposures, exposures to derivatives and to securities financing transactions, and off-balance sheet items.

On November 15, 2020, the Banking Supervision Department issued a circular, as a temporary order, updating Proper Conduct of Banking Business Directive 250 concerning the leverage ratio. Banking corporations must maintain a leverage ratio of no less than 4.5% on a consolidated basis. Banking corporations whose total balance sheet assets on a consolidated basis constitute 24% or more of the total balance sheet assets in the banking system (the Bank is such a banking corporation) must maintain a leverage ratio of no less than 5.5% (instead of 6.0% prior to the relief).

The period of the relief has been extended until December 31, 2023; after that date, the requirement is to return to the leverage ratio required prior to the Temporary Order (6.0%) within two quarters.

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

	June 30, 2023	June 30, 2022	December 31, 2022
	NIS millions		
Total consolidated assets as per published financial statements	668,784	651,598	665,353
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	2,173	(7,772)	801
Adjustments for securities financing transactions	-	-	-
Adjustments for off-balance sheet items	68,922	72,713	70,140
Other adjustments	(927)	4,238	821
Exposure for the purposes of the leverage ratio	738,952	720,777	737,115

Table C-3: Leverage ratio disclosure

	June 30, 2023	June 30, 2022	December 31, 2022
	NIS millions/percent		
On-balance sheet exposures			
On-balance sheet items (excluding derivatives and securities financing transactions, but including collateral)	627,724	625,907	628,537
Asset amounts deducted in determining Tier 1 capital	(4)	(16)	(4)
Total on-balance sheet exposures (excluding derivatives and securities financing transactions)	627,720	625,891	628,533
Derivative exposures			
Replacement cost associated with all derivatives transactions	5,931	5,852	5,142
Add-on amounts for potential future exposure associated with all derivatives transactions	21,091	11,932	17,491
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	-	(3,174)	-
Exempted central counterparty leg of client-cleared trade exposures	-	-	-
Adjusted effective notional amount of written credit derivatives	-	-	-
Adjusted effective notional offsets and add-on deductions for written credit derivatives	-	-	-
Total derivative exposures	27,022	14,610	22,633
Securities financing transaction exposures			
Gross securities financing transaction assets (with no recognition of netting), after adjusting for sale accounting transactions	15,288	7,563	15,809
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	15,288	7,563	15,809
Other off-balance sheet exposures			
Off-balance sheet exposure at gross notional amount	211,002	220,819	210,369
Adjustments for conversion to credit equivalent amounts	(142,080)	(148,106)	(140,229)
Off-balance sheet items	68,922	72,713	70,140
Capital and total exposures			
Tier 1 capital*	49,449	44,446	46,745
Total exposures*	738,952	720,777	737,115
Leverage ratio			
Leverage ratio pursuant to Proper Conduct of Banking Business Directive 218	6.69%	6.17%	6.34%
Minimum leverage ratio required by the Banking Supervision Department in the period of the Temporary Order	5.50%	5.50%	5.50%
Minimum leverage ratio required by the Banking Supervision Department after the end of the Temporary Order	6.00%	6.00%	6.00%

* These data include adjustments in respect of the efficiency plans, in accordance with the directives of the Banking Supervision Department (see [Note 9H to the Condensed Financial Statements](#)). The effect of the relief in respect of the efficiency plans on the leverage ratio as at June 30, 2023, estimated at an additional future decrease of approximately 0.01%, is recorded in equal parts over five years, from their inception date until December 31, 2024. In addition, the data include adjustments in respect of the effect of the implementation of accounting principles concerning current expected credit losses, which are to be gradually reduced until December 31, 2024. The effect of the relief in respect of current expected credit losses as at June 30, 2023, is estimated at an additional future decrease of approximately 0.03%.

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

The Bank has implemented United States generally accepted accounting principles concerning current expected credit losses (CECL) as of January 1, 2022, prospectively.

Table D-1: Credit risk indicators

	As at							
	June 30, 2023				December 31, 2022			
	Commercial	Private individuals – housing loans	Private individuals – other	Total	Commercial	Private individuals – housing loans	Private individuals – other	Total
Analysis of quality of credit to the public								
Non-accruing credit as a percentage of the balance of credit to the public	0.98%	0.54%	0.63%	0.81%	1.15%	0.45%	0.60%	0.87%
Balance of credit to the public, non-accruing or past due by 90 days or more, as a percentage of the balance of credit to the public	1.10%	0.54%	0.77%	0.89%	1.17%	0.45%	0.72%	0.89%
Problematic credit as a percentage of the balance of credit to the public	2.38%	0.54%	1.91%	1.75%	2.24%	0.45%	1.90%	1.63%
Credit not at credit execution rating as a percentage of the balance of credit to the public	4.70%	1.09%	9.31%	3.94%	5.10%	1.02%	9.44%	4.16%
Analysis of provision for credit losses in the reported period								
Provision for credit losses as a percentage of the average balance of credit to the public	0.43%	0.11%	0.98%	0.38%	(0.08%)	0.06%	0.11%	(0.02%)
Net charge-offs as a percentage of the average balance of credit to the public	0.06%	0.02%	0.31%	0.07%	(0.05%)	-	0.07%	(0.03%)
Analysis of allowance for credit losses in respect of credit to the public								
Total allowance for credit losses* as a percentage of credit to the public	2.25%	0.45%	2.99%	1.74%	2.17%	0.41%	2.64%	1.64%
Allowance for credit losses in respect of credit to the public, as a percentage of the balance of credit to the public	1.88%	0.42%	2.90%	1.50%	1.80%	0.38%	2.55%	1.41%
Allowance for credit losses as a percentage of the balance of non-accruing credit to the public	191.0%	78.1%	463.5%	185.2%	156.4%	83.8%	427.1%	160.7%
Allowance for credit losses as a percentage of the balance of credit to the public, non-accruing or past due by 90 days or more	170.8%	78.1%	374.5%	168.2%	154.2%	83.8%	353.2%	156.9%
Ratio of allowance for credit losses to net charge-offs	34.8	21.0	9.4	23.1	(34.6)	243.5	39.0	(58.3)

* Including the allowance in respect of off-balance sheet balances.

Note:

The rates calculated above refer to provisions in respect of credit to the public only, without credit losses in respect of banks and governments. Credit to the public – before deduction of the allowance for credit losses.

Portfolio quality analysis

Most credit risk indicators have worsened somewhat. However, the indicators do not point unequivocally to worsening at this stage; some are influenced by the increase in the collective allowance, in which the Bank reflected the forecast of changes in macroeconomic variables. The increases in the interest rate and the rise in inflation, combined with the growing uncertainty regarding economic conditions in the coming period, may lead to an increase in the risk level in this portfolio.

The following credit risk indicators increased (worsened) in the first half of 2023, compared with the end of 2022:

- Problematic credit as a percentage of the balance of credit to the public, for the Bank as a whole and for each sub-segment, as shown in the table above.
- The provision for credit losses as a percentage of the average balance of credit to the public, for the Bank as a whole and for each of the sub-segments, as shown in the table above.
- Net charge-offs as a percentage of the average balance of credit to the public, for the Bank as a whole and for each sub-segment, as shown in the table above.
- The allowance for credit losses as a percentage of the balance of credit to the public and the overall allowance for credit losses (including the allowance in respect of off-balance sheet balances) as a percentage of credit to the public, for the Bank as a whole and for each sub-segment, as shown in the table above.

The following credit risk indicators decreased (improved) in the first half of 2023, compared with the end of 2022:

- Non-accruing credit as a percentage of the balance of credit to the public, for the Bank as a whole and in the commercial segment, despite an increase in the housing loan and private individual segments.
- Credit not at credit execution rating as a percentage of the balance of credit to the public, for the Bank as a whole and for the sub-segments, as shown in the table above, with the exception of the housing loan segment, which increased.

The balance of credit to the public, non-accruing or past due by 90 days or more, as a percentage of the balance of credit to the public, showed no change in comparison to the end of 2022, despite an increase in the housing loan and private individual segments.

Table D-2: Credit quality of credit exposures

		June 30, 2023			
		Gross balances		Allowances	Net
		Non-accruing or past due by 90 days or more	Others	for credit losses or impairment	balances
		NIS millions			
1	Debts, excluding bonds	3,620	419,659	6,118	417,161
2	Bonds	-	128,232	25	128,207
3	Off-balance sheet exposures	714	209,244	980	208,978
4	Total	4,334	757,135	7,123	754,346
<hr/>					
		June 30, 2022			
		Gross balances		Allowances	Net
		Non-accruing or past due by 90 days or more	Others	for credit losses or impairment	balances
		NIS millions			
1	Debts, excluding bonds	3,350	389,935	5,134	388,151
2	Bonds	-	77,725	11	77,714
3	Off-balance sheet exposures	769	218,270	854	218,185
4	Total	4,119	685,930	5,999	684,050
<hr/>					
		December 31, 2022			
		Gross balances		Allowances	Net
		Non-accruing or past due by 90 days or more	Others	for credit losses or impairment	balances
		NIS millions			
1	Debts, excluding bonds	3,527	410,005	5,564	407,968
2	Bonds	-	103,369	17	103,352
3	Off-balance sheet exposures	813	208,507	935	208,385
4	Total	4,340	721,881	6,516	719,705

For further details, see [Table 3-4: Additional information regarding changes in non-accruing credit to the public, in the Report of the Board of Directors and Board of Management.](#)

D.2. Credit risk exposures

D.2.a. Details of exposures by economic sector

Table D-3: Details of exposures by economic sector in Israel

	June 30, 2023									
	Total credit risk ⁽¹⁾			Debts ⁽²⁾ and off-balance sheet credit risk (excluding derivatives) ⁽³⁾					Credit losses for the three-month period ended June 30, 2023 ⁽⁴⁾	
	Total	Credit execution rating ⁽⁵⁾	Problematic ⁽⁶⁾	Total	Of which: debts ⁽²⁾	Problematic ⁽⁶⁾	Non-accruing	Provision (income) for credit losses	Net charge-offs	Allowance for credit losses
NIS millions										
In respect of borrower activity in Israel										
Public – commercial										
Agriculture	3,240	3,103	22	3,235	2,718	22	2	(1)	(2)	48
Mining and quarrying	1,474	955	516	1,361	885	516	498	(2)	-	183
Industry	32,148	31,313	463	31,372	16,560	461	186	(1)	(3)	337
Construction and real estate – construction ⁽⁷⁾	102,350	99,722	1,788	102,119	49,092	1,788	613	(22)	15	797
Construction and real estate – real-estate activities	40,386	39,800	113	40,091	33,055	113	54	127	(6)	766
Electricity and water supply	14,625	14,200	291	14,064	8,909	291	106	20	6	522
Commerce	39,116	37,466	637	38,986	29,543	637	359	82	22	386
Hotels, hospitality, and food services	11,732	10,877	496	11,700	9,972	496	104	84	3	265
Transportation and storage	12,128	11,252	478	12,021	8,883	475	189	32	7	379
Information and communications	7,384	6,901	151	7,291	5,208	151	133	(22)	(14)	130
Financial services	54,727	54,628	25	39,871	30,917	25	8	51	6	228
Other business services	16,957	15,818	192	16,788	11,010	192	90	30	17	259
Public and community services	8,993	8,326	382	8,975	6,684	382	364	109	12	346
Total commercial ⁽⁸⁾	345,260	334,361	5,554	327,874	213,436	5,549	2,706	487	63	4,646
Private individuals – housing loans	136,131	134,732	687	136,131	129,156	687	687	74	13	575
Private individuals – other	54,885	51,479	672	54,879	34,941	672	220	171	53	1,045
Total public – activity in Israel	536,276	520,572	6,913	518,884	377,533	6,908	3,613	732	129	6,266
Banks in Israel ⁽⁹⁾	1,250	1,250	-	900	182	-	-	1	-	2
Israeli government	93,270	93,270	-	1,389	1,385	-	-	-	-	-
Total activity in Israel	630,796	615,092	6,913	521,173	379,100	6,908	3,613	733	129	6,268

(1) Balance sheet credit risk and off-balance sheet credit risk,⁽³⁾ including in respect of derivative instruments. Includes debts,⁽²⁾ bonds, securities borrowed or purchased under agreements to resell, assets in respect of derivative instruments, and credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness, in the amount of NIS 379,100; 91,394; 1,071; 2,781; and 156,450 million, respectively.

(2) Credit to the public, credit to governments, and deposits with banks (excluding deposits with the Bank of Israel), excluding bonds, securities borrowed or purchased under agreements to resell, and assets in respect of activity in the Maof market (presented under the item "other assets").

(3) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness.

(4) Including in respect of off-balance sheet credit instruments (presented in the balance sheet under the item "other liabilities").

(5) Credit risk for which the credit rating at the date of the report is congruent with the credit rating for the execution of new credit, according to the policy of the Bank.

(6) Balance sheet and off-balance sheet non-accruing, substandard, or special mention credit risk.

(7) Including balance sheet credit risk in the amount of approximately NIS 526 million and off-balance sheet credit risk in the amount of approximately NIS 630 million extended to certain purchasing groups currently in the process of construction.

(8) The balance of commercial debts includes the balance of housing loans, in the amount of approximately NIS 82 million, of commercial borrowers, or extended to purchasing groups currently in the process of construction.

(9) Excluding cash balances of the Bank and deposits with the Bank of Israel, and before deducting the allowance for credit losses.

Table D-3: Details of exposures by economic sector in Israel (continued)

	December 31, 2022									
	Total credit risk ⁽¹⁾			Debts ⁽²⁾ and off-balance sheet credit risk (excluding derivatives) ⁽³⁾						
	Total	Credit execution rating ⁽⁵⁾	Problematic ⁽⁶⁾	Total	Of which: Problematic ⁽⁶⁾ debts ⁽²⁾	Non-accruing	Credit losses for the year ended December 31, 2022 ⁽⁴⁾			
Provision (income) for credit losses							Net charge-offs	Allowance for credit losses		
NIS millions										
In respect of borrower activity in Israel										
Public – commercial										
Agriculture	3,393	3,261	23	3,380	2,820	23	3	(25)	(37)	48
Mining and quarrying	1,754	1,138	612	1,754	1,142	612	610	(533)	-	184
Industry	31,481	30,570	487	30,919	16,637	485	157	70	(23)	335
Construction and real estate – construction ⁽⁷⁾	101,927	99,490	1,007	101,819	47,152	1,007	610	(165)	(79)	834
Construction and real estate – real-estate activities	36,900	36,325	109	36,643	30,844	109	72	173	(56)	635
Electricity and water supply	13,714	13,249	291	13,127	7,175	291	107	49	39	512
Commerce	39,133	37,566	582	38,954	28,179	582	242	(23)	5	323
Hotels, hospitality, and food services	11,567	10,353	182	11,546	9,999	182	117	(7)	(6)	185
Transportation and storage	12,891	11,944	529	12,794	8,853	526	237	121	12	358
Information and communications	7,551	6,866	144	7,501	5,213	144	131	31	(11)	142
Financial services	51,736	51,521	29	38,237	27,684	29	22	(128)	(4)	184
Other business services	17,243	15,949	252	17,106	11,298	252	116	84	13	247
Public and community services	9,089	8,403	407	9,083	6,801	407	387	57	6	246
Total commercial ⁽⁸⁾	338,379	326,635	4,654	322,863	203,797	4,649	2,811	(296)	(141)	4,233
Private individuals – housing loans	134,643	133,342	572	134,643	127,527	572	572	72	2	515
Private individuals – other	52,896	49,437	670	52,892	35,054	670	211	40	22	927
Total public – activity in Israel	525,918	509,414	5,896	510,398	366,378	5,891	3,594	(184)	(117)	5,675
Banks in Israel ⁽⁹⁾	1,391	1,391	-	1,206	255	-	-	1	-	1
Israeli government	68,613	68,613	-	771	768	-	-	-	-	-
Total activity in Israel	595,922	579,418	5,896	512,375	367,401	5,891	3,594	(183)	(117)	5,676

(1) Balance sheet credit risk and off-balance sheet credit risk, ⁽³⁾ including in respect of derivative instruments. Includes debts⁽²⁾, bonds, securities borrowed or purchased under agreements to resell, assets in respect of derivative instruments, and credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness, in the amount of NIS 367,401; 67,788; 316; 2,468; and 157,949 million, respectively.

(2) Credit to the public, credit to governments, and deposits with banks (excluding deposits with the Bank of Israel), excluding bonds, securities borrowed or purchased under agreements to resell, and assets in respect of activity in the Maof market (presented under the item "other assets").

(3) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness.

(4) Including in respect of off-balance sheet credit instruments (presented in the balance sheet under the item "other liabilities").

(5) Credit risk for which the credit rating at the date of the report is congruent with the credit rating for the execution of new credit, according to the policy of the Bank.

(6) Balance sheet and off-balance sheet non-accruing, substandard, or special mention credit risk.

(7) Including balance sheet credit risk in the amount of approximately NIS 447 million and off-balance sheet credit risk in the amount of approximately NIS 628 million extended to certain purchasing groups currently in the process of construction.

(8) The balance of commercial debts includes the balance of housing loans, in the amount of approximately NIS 72 million, of commercial borrowers, or extended to purchasing groups currently in the process of construction.

(9) Excluding cash balances of the Bank and deposits with the Bank of Israel, and before deducting the allowance for credit losses.

Table D-3: Details of exposures by economic sector in Israel (continued)

	June 30, 2023									
	Total credit risk ⁽¹⁾			Debts ⁽²⁾ and off-balance sheet credit risk (excluding derivatives) ⁽³⁾						
	Total credit risk ⁽¹⁾	Of which: credit execution rating ⁽⁵⁾	Of which: problematic credit risk ⁽⁴⁾	Total	Of which: Problematic ⁽⁶⁾ debts ⁽²⁾	Non-accruing	Credit losses for the three-month period ended June 30, 2023 ⁽⁴⁾			
Provision (income) for credit losses							Net charge-offs	Allowance for credit losses		
NIS millions										
In respect of borrower activity overseas										
Public – commercial										
Agriculture	178	178	-	178	178	-	-	-	-	1
Mining and quarrying	739	739	-	350	72	-	-	(10)	-	4
Industry	3,773	3,632	65	2,379	1,404	65	-	1	6	24
Construction and real estate	14,453	13,022	746	14,389	9,359	745	327	32	-	556
Electricity and water supply	1,284	1,245	-	877	265	-	-	-	-	5
Commerce	3,542	3,443	98	3,290	2,685	98	34	(9)	-	26
Hotels, food services, and hospitality	4,283	3,648	168	4,283	3,216	168	-	18	-	117
Transportation and storage	1,110	1,075	35	791	678	35	-	2	-	16
Information and communications	3,046	2,986	60	2,612	2,052	60	14	2	-	19
Total financial services	14,492	14,488	-	5,614	4,646	-	-	(5)	(4)	12
Other business services	1,545	1,328	216	1,542	1,064	216	-	(1)	-	15
Public services	2,922	2,921	-	2,760	2,369	-	-	(1)	-	21
Total commercial	51,367	48,705	1,388	39,065	27,988	1,387	375	29	2	816
Private individuals – housing loans	676	656	11	676	626	11	11	-	-	5
Private individuals – other	222	218	-	222	76	-	-	1	1	1
Total public – activity overseas	52,265	49,579	1,399	39,963	28,690	1,398	386	30	3	822
Banks overseas ⁽⁷⁾	24,399	24,395	-	14,318	13,798	-	-	(1)	-	9
Governments overseas	25,471	25,211	-	1,737	1,691	-	-	2	-	24
Total activity overseas	102,135	99,185	1,399	56,018	44,179	1,398	386	31	3	855
Total in Israel and overseas	732,931	714,277	8,312	577,191	423,279	8,306	3,999	764	132	7,123

(1) Balance sheet credit risk and off-balance sheet credit risk,⁽³⁾ including in respect of derivative instruments. Includes debts,⁽²⁾ bonds, securities borrowed or purchased under agreements to resell, assets in respect of derivative instruments, and credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness, in the amount of NIS 44,179; 36,838; 597; and 20,521 million, respectively.

(2) Credit to the public, credit to governments, and deposits with banks, excluding bonds, securities borrowed or purchased under agreements to resell, and assets in respect of activity in the Maof market (presented under the item "other assets").

(3) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness, excluding in respect of derivative instruments.

(4) Including in respect of off-balance sheet credit instruments (presented in the balance sheet under the item "other liabilities").

(5) Credit risk for which the credit rating at the date of the report is congruent with the credit rating for the execution of new credit, according to the policy of the Bank.

(6) Balance sheet and off-balance sheet non-accruing, substandard, or special mention credit risk.

(7) Excluding cash balances of the Bank, and before deducting the allowance for credit losses.

Table D-3: Details of exposures by economic sector in Israel (continued)

	December 31, 2022										
	Total credit risk ⁽¹⁾			Debts ⁽²⁾ and off-balance sheet credit risk (excluding derivatives) ⁽³⁾						Credit losses for the year ended December 31, 2022 ⁽⁴⁾	
	Total credit risk ⁽¹⁾	Of which: credit execution rating ⁽⁵⁾	Of which: problematic credit risk ⁽⁶⁾	Total	Of which: debts ⁽²⁾	Problematic ⁽⁶⁾	Non-accruing	Provision (income) for credit losses	Net charge-offs	Allowance for credit losses	
NIS millions											
In respect of borrower activity overseas											
Public – commercial											
Agriculture	164	164	-	164	164	-	-	-	-	1	
Mining and quarrying	763	763	-	369	64	-	-	2	-	12	
Industry	3,940	3,924	16	2,609	1,662	16	-	(19)	(3)	17	
Construction and real estate	13,650	12,019	838	13,546	9,781	837	558	96	16	527	
Electricity and water supply	1,177	1,130	-	762	179	-	-	(5)	-	4	
Commerce	3,667	3,627	41	3,332	2,705	41	41	23	(2)	37	
Hotels, food services, and hospitality	3,747	2,840	635	3,747	2,978	635	6	8	-	107	
Transportation and storage	1,024	932	70	787	678	70	29	7	-	29	
Information and communications	2,583	2,570	13	2,214	1,821	13	13	1	2	18	
Total financial services	10,062	10,060	1	4,480	3,782	1	1	(12)	-	12	
Other business services	1,535	1,314	222	1,536	1,091	222	-	9	8	16	
Public services	2,861	2,858	2	2,673	2,323	2	2	10	-	23	
Total commercial	45,173	42,201	1,838	36,219	27,228	1,837	650	120	21	803	
Private individuals – housing loans	631	614	9	631	578	9	9	(1)	-	4	
Private individuals – other	220	213	1	220	78	1	-	-	1	1	
Total public – activity overseas	46,024	43,028	1,848	37,070	27,884	1,847	659	119	22	808	
Banks overseas ⁽⁷⁾	27,239	27,238	-	17,608	16,837	-	-	9	-	10	
Governments overseas	25,760	25,669	-	1,541	1,410	-	-	21	-	22	
Total activity overseas	99,023	95,935	1,848	56,219	46,131	1,847	659	149	22	840	
Total in Israel and overseas	694,945	675,353	7,744	568,594	413,532	7,738	4,253	(34)	(95)	6,516	

(1) Balance sheet credit risk and off-balance sheet credit risk,⁽³⁾ including in respect of derivative instruments. Includes debts⁽²⁾, bonds, securities borrowed or purchased under agreements to resell, assets in respect of derivative instruments, and credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness, in the amount of NIS 46,131; 35,581; 582; 285; and 16,444 million, respectively.

(2) Credit to the public, credit to governments, and deposits with banks, excluding bonds, securities borrowed or purchased under agreements to resell, and assets in respect of activity in the Maof market (presented under the item "other assets").

(3) Credit risk in off-balance sheet financial instruments, as calculated for the purpose of the limit on borrower indebtedness, excluding in respect of derivative instruments.

(4) Including in respect of off-balance sheet credit instruments (presented in the balance sheet under the item "other liabilities").

(5) Credit risk for which the credit rating at the date of the report is congruent with the credit rating for the execution of new credit, according to the policy of the Bank.

(6) Balance sheet and off-balance sheet non-accruing, substandard, or special mention credit risk.

(7) Excluding cash balances of the Bank, and before deducting the allowance for credit losses.

Table D-4: Exposure of the Bank Group to foreign financial institutions⁽¹⁾

	June 30, 2023			December 31, 2022		
	Balance sheet credit risk ⁽²⁾	Present off-balance sheet credit risk ⁽³⁾	Total present credit risk	Balance sheet credit risk ⁽²⁾	Present off-balance sheet credit risk ⁽³⁾	Total present credit risk
NIS millions						
External credit rating⁽⁴⁾						
AAA to AA-	5,903	6,388	12,291	4,906	11,504	16,410
A+ to A-	9,298	14,818	24,116	8,178	10,719	18,897
BBB+ to BBB-	84	32	116	101	96	197
BB+ to B-	2	10	12	5	-	5
Lower than B-	-	-	-	-	-	-
Unrated	123	69	192	339	66	405
Total present credit exposures to foreign financial institutions	15,410	21,317	36,727	13,529	22,385	35,914

- (1) Foreign financial institutions include: banks, investment banks, broker/dealers, insurance companies, institutional entities, and entities controlled by such entities, but do not include credit exposure to foreign financial institutions backed by government guarantees.
- (2) Deposits with banks, credit to the public, investments in bonds, securities borrowed or purchased in agreements to resell, and other balance sheet risk in respect of derivative instruments.
- (3) Mainly guarantees and commitments to grant credit.
- (4) According to the lowest of the long-term foreign-currency credit ratings assigned by one of the major rating agencies – S&P and Moody's.

In the course of its routine business operations, the Bank Group is exposed to risk arising from credit exposures to foreign financial institutions.

This risk arises from the range of activities conducted with the financial institutions, such as transactions carried out at the Bank's dealing rooms (deposits of foreign-currency balances and derivatives), purchases of bonds issued by such institutions, foreign-trade transactions, capital-market activity, and credit insurance through foreign insurance companies. The exposure to foreign financial institutions is influenced both by the financial robustness of each institution and by the risk in the political and economic environment in which it operates. It is emphasized that most of the credit exposures of the Bank Group are to financial institutions located in developed markets in Western Europe and North America, rated investment grade or higher.

Note that the rapid rise in interest rates over the last year led to liquidity shortages among commercial banks, mainly in the United States, in the first quarter of 2023. This trend halted in the second quarter of 2023. The crisis, which peaked in the first quarter of 2023, appears to be centered on American regional banks, where concerns have arisen following the collapse of SVB (Silicon Valley Bank), which led to significant withdrawals of money by customers. The exposures of the Bank to global banks are focused on large, top-tier banks rated investment grade. The same is true for the Bank's exposures to American banks. The Bank does not have, and did not have at the time of the collapses/bailouts, exposures to the American banks that have failed or been bailed out in recent months (SVB, Signature Bank, and First Republic Bank). The Bank has negligible exposure to a small number of regional banks in the United States.

In the ordinary course of its business, the Bank regularly applies monitoring and controls with respect to developments that may affect the ability of the financial institutions with which it conducts activity to meet their obligations. Concurrently, measures are applied in order to minimize credit risk.

The exposure of the Bank Group to foreign financial institutions totaled approximately NIS 36.7 billion on June 30, 2023, an increase of approximately NIS 0.8 billion, compared with approximately NIS 35.9 billion at the end of 2022. This increase mainly resulted from an increase in the amount of approximately NIS 1.9 billion in balance-sheet exposure, mainly as a result of an increase in securities of foreign financial institutions. An offsetting effect of a decrease of approximately NIS 1.1 billion in off-balance sheet exposure was recorded as a result of a decrease in guarantees and credit facilities provided to financial institutions. Approximately 99.1% of the exposure to foreign financial institutions is to financial institutions rated A- or higher. The Bank Group's exposure to foreign financial institutions is distributed as follows: 36.3% in banks and bank holding companies, 58.6% in insurance companies, and 5.1% in another financial institution. The exposure of the Bank Group is to foreign financial institutions operating in Western European countries (67.7%), the United States (26.1%), and South and East Asian countries (6.2%).

D.3. Additional information regarding exposures to credit risks

D.3.a. Construction and real estate

Activity in the construction and real-estate sectors slowed considerably in first half of the year. According to data from the Central Bureau of Statistics, the volume of transactions in new and preowned homes decreased steeply in January-May, by approximately 44% year-on-year, and the inventory of unsold homes grew.

Interest-rate increases have reduced households' ability to buy homes and lowered purchases by investors. Data of the Central Bureau of Statistics indicate a cumulative decrease of 1.6% in prices of new homes since September 2022, and a slight decrease of 0.6% in the index of overall prices of homes in the last two months. These data do not weigh in benefits sometimes granted at the time of purchase; therefore, actual decreases in prices may be greater. A decrease is apparent in the number of land auctions of the Israel Land Administration in the first half of 2023, along with a low number of bidders. Auctions of land for rental housing reflect a significant decrease in the value of land in this segment.

The growth of the portfolio slowed significantly in 2022, compared with the preceding year. With the changes in the economic environment, the increase in the interest rate, and the decrease in the volume of transactions, measures were taken in 2022 and 2023 to apply stricter credit underwriting rules in this sector. The Bank is operating within its credit risk management limits, while examining risk-adjusted profitability. The Bank is continuing to examine the potential implications of the changes in the economic environment, and the potential effect of the continued increase in the interest rate and inflation, and will perform additional required adjustments as necessary. The Bank reflects expected economic conditions and portfolio data in determining the appropriate collective allowance for the construction and real-estate sector.

Table D-5: Segmentation of credit risk in the construction and real-estate sectors, by customers' principal area of activity

	Balance as at June 30, 2023			Total credit risk
	Balance sheet credit risk	Off-balance sheet credit		
	Loans ⁽¹⁾	Unutilized credit facilities	Guarantees	
	NIS millions			
Corporate Banking Division				
Construction for commerce and services	2,636	645	317	3,598
Construction for industry	167	16	39	222
Housing construction	32,257	17,907	⁽¹⁾ 19,602	69,766
Yield-generating properties	28,840	5,925	777	35,542
Other	10,027	8,092	4,673	22,792
Corporate Banking Division total	73,927	32,585	25,408	131,920
Retail Banking Division	8,436	1,693	687	10,816
Total activity in Israel	82,363	34,278	26,095	142,736
<hr/>				
	Balance as at December 31, 2022			Total credit risk
	Balance sheet credit risk	Off-balance sheet credit		
	Loans ⁽¹⁾	Unutilized credit facilities	Guarantees	
	NIS millions			
Corporate Banking Division				
Construction for commerce and services	2,734	793	499	4,026
Construction for industry	361	86	45	492
Housing construction	30,677	17,591	⁽¹⁾ 21,537	69,805
Yield-generating properties	26,365	4,607	796	31,768
Other	9,156	7,278	4,877	21,311
Corporate Banking Division total	69,293	30,355	27,754	127,402
Retail Banking Division	8,836	1,852	737	11,425
Total activity in Israel	78,129	32,207	28,491	138,827

(1) Includes balance sheet and off-balance sheet credit risk in respect of which insurance was acquired, mainly from foreign insurance companies, for the portfolio of credit for land. For further details, see [the Report on Risks as at June 30, 2023](#).

Overall credit risk in the construction and real-estate sectors in Israel totaled approximately NIS 143 billion as at June 30, 2023. The total balance of risk of credit to the public in the construction and real-estate sectors in Israel increased by approximately 2.8% in the first six months of 2023. Most of the exposure is at the Corporate Banking Division (mid-sized and large customers), at approximately 92% of total credit risk in the construction and real-estate sectors in Israel.

Exposure to companies operating primarily in the residential construction industry at the Corporate Banking Division constitutes approximately 53% of the exposure of the division to the construction and real-estate sector. Most financing for companies in this industry consists of financing of land for housing and financing of residential construction projects nationwide. Exposure to companies operating in the industries of construction of buildings for commerce and services, construction for industry, and yield-generating properties for rent at the Corporate Banking Division constitutes approximately 30% of the exposure of the division to the construction and real-estate sector.

Table D-6: Analysis of credit quality in the construction and real-estate sectors

	Balance as at		Change
	June 30, 2023	December 31, 2022	
	NIS millions		
Credit risk at credit execution rating			
Non-problematic credit risk	139,522	135,815	2.7%
Credit risk not at credit execution rating			
Problematic accruing	1,234	434	184.3%
Non-accruing	667	682	(2.2%)
Problematic credit risk not at execution rating	1,901	1,116	70.3%
Non-problematic credit risk not at execution rating	1,313	1,896	(30.7%)
Total credit risk not at credit execution rating	3,214	3,012	6.7%
Total	142,736	138,827	2.8%

Total credit risk not at credit execution rating increased by 6.7% in the first six months of 2023. Total credit risk not at credit execution rating as a percentage of total credit risk increased from 2.17% in 2022 to 2.25% in the first six months of 2023. Problematic debt as a percentage of total credit risk increased from 0.80% in 2022 to 1.33% in the first six months of 2023, and non-accruing debt as a percentage of total credit risk decreased from 0.49% in 2022 to 0.47% in the first six months of 2023.

The increase in the percentage of balances not at credit execution rating, and particularly the significant increase in the percentage of problematic debt, was influenced by the changes in the economic environment. These changes point to an increase in the probability of worsening in these sectors, and accordingly, of a possible continued increase in the level of borrowers' credit risk in this area.

Table D-7: Credit risk in the real-estate sector at the Corporate Banking Division in Israel, by financing rate (LTV) and absorption capacity⁽¹⁾

	Balance as at June 30, 2023				
	Land	Real estate in construction processes ⁽²⁾	Completed properties	Other	Total
	NIS millions				
Financing rate⁽³⁾					
Up to 45%	2,063	-	5,454	-	7,517
Over 45% up to 65%	7,295	-	8,436	-	15,731
Over 65% up to 80%	16,250	-	6,846	-	23,096
Over 80%	2,722	-	631	-	3,353
Absorption capacity⁽⁴⁾					
Up to 25%	-	270	-	-	270
Over 25% up to 50%	-	12,533	-	-	12,533
Over 50% up to 75%	-	8,024	-	-	8,024
Over 75%	-	23,266	-	-	23,266
Projects not yet started	-	10,693	-	-	10,693
Other⁽⁵⁾					
	-	-	-	27,437	27,437
Total Corporate Banking Division credit risk	28,330	54,786	21,367	27,437	131,920

(1) Segmentation was performed according to an analysis of the source of repayment of each credit, as presented and approved during the underwriting process.

(2) "Real estate in construction processes" includes all projects under construction in the various segments (residential, offices, commerce, etc.), including construction of properties designated for rental. This segment includes purchasing groups; projects for which a financing agreement has been signed, but financing has not commenced due to non-attainment of preliminary conditions; land where development has started; and balances of Sale Law guarantees in the process of cancellation in respect of completed projects.

(3) The financing rate is the ratio of the monetary credit at the report date to the present value of the existing collateral at the report date before the effect of haircuts. Financing rates do not weigh in risk hedging of credit balances backed by insurance acquired from reinsurers.

(4) The absorption capacity of the projects is the maximum possible rate of decline in the value of the asset as completed without the Bank incurring losses from the projects. The absorption capacity is based on the last known report at the report date, and does not weigh in risk hedging of balances secured by insurance acquired from reinsurers.

(5) "Other credit" is any credit that does not meet the definitions of one of the segments listed above. This item includes, for example, financing of infrastructure projects (PPP); financing against collateral other than real estate (such as deposits, shares, floating liens, third-party guarantees, and more); current credit against financial robustness; and more.

Table D-7: Credit risk in the real-estate sector at the Corporate Banking Division in Israel, by financing rate (LTV) and absorption capacity⁽¹⁾ (continued)

	Balance as at December 31, 2022*				
	Land	Real estate in construction processes ⁽²⁾	Completed properties	Other	Total
	NIS millions				
Financing rate⁽³⁾					
Up to 45%	2,316	-	5,250	-	7,566
Over 45% up to 65%	6,422	-	7,523	-	13,945
Over 65% up to 80%	15,241	-	5,801	-	21,042
Over 80%	3,733	-	812	-	4,545
Absorption capacity⁽⁴⁾					
Up to 25%	-	865	-	-	865
Over 25% up to 50%	-	8,075	-	-	8,075
Over 50% up to 75%	-	6,906	-	-	6,906
Over 75%	-	27,237	-	-	27,237
Projects not yet started	-	9,109	-	-	9,109
Other⁽⁵⁾					
	-	-	-	28,112	28,112
Total Corporate Banking Division credit risk	27,712	52,192	19,386	28,112	127,402

* Reclassified.

(1) Segmentation was performed according to an analysis of the source of repayment of each credit, as presented and approved during the underwriting process.

(2) "Real estate in construction processes" includes credit for projects in various stages of progress, such as purchasing groups; projects for which a financing agreement has been signed, but financing has not commenced due to non-attainment of preliminary conditions; land where development has started; and balances of Sale Law guarantees in the process of cancellation in respect of completed projects.

(3) The financing rate is the ratio of the monetary credit at the report date to the present value of the existing collateral at the report date before the effect of haircuts. Financing rates do not weigh in risk hedging of credit balances backed by insurance acquired from reinsurers.

(4) The absorption capacity of the projects is the maximum possible rate of decline in the value of the asset as completed without the Bank incurring losses from the projects. The absorption capacity is based on the last known report at the report date, and does not weigh in risk hedging of balances secured by insurance acquired from reinsurers.

(5) "Other credit" is any credit that does not meet the definitions of one of the segments listed above. This item includes, for example, financing of infrastructure projects (PPP); financing against collateral other than real estate (such as deposits, shares, floating liens, third-party guarantees, and more); current credit against financial robustness; and more.

Credit at financing rates greater than 80% constitutes approximately 6.7% of the total balance of completed properties and land at the Corporate Banking Division on June 30, 2023, compared with 9.7% on December 31, 2022. Credit with absorption capacity of up to 25% for real estate in construction processes constitutes approximately 0.6% of the total balance of real estate in construction processes at the Corporate Banking Division (excluding projects not yet started) on June 30, 2023, compared with 2.0% on December 31, 2022.

The main change in the composition of financing rates and absorption capacity in the first six months of the year is an increase in the amount of NIS 4,458 million in projects with absorption capacity of 25% to 50%. This change mainly resulted from the commencement of financing of new projects. In addition, a decrease in the amount of NIS 3,971 million occurred in projects with absorption capacity over 75%, mainly as a result of the completion of construction of projects.

Note that on May 22, 2022, the Banking Supervision Department issued an update of Directive 203 pursuant to which loans designated for the acquisition of land for the purpose of development or construction at a rate exceeding 80% of the value of the acquired asset (LTV) would be added to the list of debts risk weighted at 150%, excluding loans for the acquisition of agricultural land with no planning horizon or intention to apply for a change in designation, and excluding loans for the acquisition of land for the borrower's own use where the borrower is not categorized as being in the economic sector of construction and real estate, according to the sector classifications in Directive 831 concerning reporting on economic sectors. A questions and answers document was released on January 26, 2023, containing clarifications regarding the implementation of the circular. For additional information, see [Note 9K to the Condensed Financial Statements](#).

Management of credit risk in the construction and real-estate sectors

Exposure to the area of construction and real estate constitutes a substantial portion of the credit portfolio. The Bank monitors developments in credit to the construction and real-estate sectors, and applies various measures to manage the risk. Real-estate credit risks are examined individually, based on the policies and objectives established in the risk appetite that has been set, from the level of the individual transaction to an overview of the portfolio of credit for the construction and real-estate sectors at the Bank.

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 Division, in addition to the regulatory limit established by the Bank of Israel. On January 7, 2021, the Bank of Israel issued additional adjustments of Proper Conduct of Banking Business Directive 250 (Temporary Order on Coping with the Coronavirus Crisis), which also addresses Proper Conduct of Banking Business Directive 315, "Industry Indebtedness Limit." The update stated that the limit on credit for the construction and real-estate sector, excluding indebtedness for national infrastructures, would rise from 20% to 22% of total indebtedness of the public, and the limit on credit for the construction and real-estate sector would rise from 24% to 26% of total indebtedness of the public. The period of the relief was extended to 24 months from December 31, 2025, provided that the rate does not exceed the rate on December 31, 2025, or the rate of the industry limit as established in Proper Conduct of Banking Business Directive 315, whichever is higher. As part of its management of exposure to this sector and compliance with the limit in this sector, the Bank uses tools such as syndication and the acquisition of insurance from rated foreign insurance companies recognized for the reduction of indebtedness pursuant to Proper Conduct of Banking Business Directive 313. Beginning in the second half of 2021, the Bank expanded its use of insurance policies. In the first quarter of 2023, the Bank continued to expand the land insurance policies that protect the Bank against credit losses in respect of the portfolio of loans granted to customers of the Corporate Banking Division of the Bank that are secured by a lien on land. In addition, the Bank uses insurance policies for Sale Law guarantees that protect the Bank against losses in respect of Sale Law guarantees issued in real-estate projects of customers of the Corporate Banking Division financed by the Bank. These insurance policies allow the Bank to reduce its exposure to the construction and real-estate sector (for further details, see [Note 10A\(4\) to the Condensed Financial Statements](#)). The Bank may take additional measures in the future to continue to manage this limit and the exposure to this sector.

The underwriting process for new credit in this sector is performed according to a formalized credit policy for the various types of financing in the industry, such as financing of land, financing of residential construction, and financing of construction and yield generation of yield-generating properties. The policy encompasses qualitative and quantitative criteria such as rate of equity capital, maximum LTV, minimum coverage ratio, and absorption capacity. These criteria are adapted to the type of financed asset, and are used to set the boundaries of risk appetite in this sector. New credit is underwritten with the establishment of risk-adjusted profitability. Within the monitoring of the portfolio, changes and trends in various risk indicators are examined, including in comparison to data published with regard to the banking system as a whole. The Bank tracks conditions and changes in macroeconomic indicators in general, and in the business environment of the industry in particular. Certain events have been defined as requiring a reexamination of policy, such as a sharp increase in the interest rate or in inflation, an increase in unemployment in the Israeli economy, or a material change in housing prices. The Bank continues to examine the developments in the economy and consider adjustments accordingly. The Bank uses a model to measure the probability of default and the expected loss in the portfolio. In addition, within stress scenario testing, the effect on credit for construction and real estate is also examined.

The allowance for credit losses in respect of the construction and real-estate sectors in Israel totaled approximately NIS 1,563 million as at June 30, 2023, compared with a total of approximately NIS 1,469 million as at December 31, 2022. The total allowance for credit losses as a percentage of credit to the public in the construction and real-estate sector in Israel as at June 30, 2023, is 1.90%, compared with 1.88% as at December 31, 2022.

D.3.b. Credit risk in respect of exposures to borrowers and to groups of borrowers

Table D-8: Balances of balance sheet credit risk and off-balance sheet credit risk to borrowers whose indebtedness exceeds NIS 1,200 million, by sector of the economy

	June 30, 2023			
	Number of borrowers	Balance sheet credit risk	Off-balance sheet credit risk	Total
	NIS millions			
Economic sector				
Electricity supply	1	1,727	1,093	2,820
Construction and real estate – construction	8	7,866	5,259	13,125
Construction and real estate – civil engineering	3	1,651	3,592	5,243
Hotels, hospitality, and food services	1	1,228	77	1,305
Information and communications	1	1,196	66	1,262
Financial services	12	13,903	13,625	27,528
Industry	3	1,461	4,223	5,684
Motor-vehicle trading	1	1,037	213	1,250
Total	30	30,069	28,148	58,217

	December 31, 2022			
	Number of borrowers	Balance sheet credit risk	Off-balance sheet credit risk	Total
	NIS millions			
Economic sector				
Electricity supply	1	1,310	1,360	2,670
Construction and real estate – construction	6	6,568	3,419	9,987
Construction and real estate – civil engineering	3	1,187	3,826	5,013
Hotels, hospitality, and food services	1	1,014	297	1,311
Information and communications	1	1,194	150	1,344
Financial services	10	11,662	10,557	22,219
Industry	2	1,206	3,642	4,848
Total	24	24,141	23,251	47,392

Credit risk in respect of exposure to borrower groups

As at June 30, 2023, there is no group of borrowers whose net indebtedness on a consolidated basis, in accordance with Proper Conduct of Banking Business Directive 313, "Limits on the Indebtedness of Borrowers and Groups of Borrowers" (hereinafter: "Directive 313"), exceeds 15% of the capital of the banking corporation (as defined in Directive 313).

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.

In November 2022, the Bank of Israel issued a draft update of Proper Conduct of Banking Business Directive 313, "Supervisory Framework for the Measurement and Control of Large Exposures," the essence of which is a change in the manner of calculation of indebtedness in respect of large exposures. The Bank is examining the implications of the implementation of the directive.

D.3.c. Risks in the housing loan portfolio

Table D-9: 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		Recorded debt balance in NIS millions	Rate of change during the period
	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 %		
June 30, 2023	33,690	25.9%	50,701	39.0%	14,470	11.1%	30,888	23.8%	115	0.1%	129,864	1.3%
Dec. 31, 2022	32,815	25.6%	50,886	39.7%	13,951	10.9%	30,398	23.7%	127	0.1%	128,177	11.3%
Dec. 31, 2021	27,672	24.0%	45,600	39.6%	13,610	11.8%	28,137	24.4%	147	0.1%	115,166	15.8%

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.

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 Division. The limits address LTV rates, repayment capability, distribution of credit products in the portfolio, volume of problematic debt, loan durations, geographical distribution, rate past due, 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 macroeconomic indicators in general, and in the business environment of the industry in particular. Certain events have been defined as requiring 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 a divisional 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, within stress scenario testing, the effect on the mortgage portfolio is also examined. Insurance arrangements are also in place – life insurance and building insurance.

In general, the level of credit risk in the housing credit portfolio is low, as reflected in the indicators noted above. Note that the trend of rising interest rates, and to a lesser extent the increase in the consumer price index, have caused monthly payments to grow for many borrowers. This increase has not yet been reflected in portfolio quality indicators.

Table D-10: Details of characteristics of housing credit granted by the Bank – percentage of total new loans executed

	For the three months ended				
	June 30, 2023	March 31, 2023	December 31, 2022	September 30, 2022	June 30, 2022
Characteristics					
Financing rate over 60%	42.1%	41.3%	42.6%	42.0%	41.8%
Ratio of repayment to income greater than 40% (for purchases of homes and in monthly payments)	1.0%	1.1%	0.2%	0.3%	0.2%
Percentage with floating rates	55.7%	56.2%	57.5%	60.3%	60.8%
Percentage of all-purpose loans	6.6%	5.7%	4.5%	3.0%	2.6%
Loans for investment purposes as a percentage of total purchases of homes	8.3%	9.9%	10.6%	9.8%	9.8%
Principal planned for repayment after age 67 (excluding investments)	11.3%	10.5%	9.4%	9.7%	9.2%
Average original term to maturity of loans for purchases of homes, in years (excluding bridge loans)	26.6	26.3	25.9	25.4	25.1

The balance of housing loans grew slightly, by 0.5%, in the second quarter of 2023, a lower growth rate than in the preceding quarters. The more moderate growth rate in balances was influenced by the increases in the interest rate, the increase in inflation, and the expectations of a decrease in prices, which led to a significant decrease in the quantity of transactions.

Quality indicators of new loans showed an increase (worsening) in the second quarter of 2023 in financing rates higher than 60%, the percentage of all-purpose loans, loans with principal scheduled for repayment after the age of 67, and the average term to maturity of loans for purchases of homes.

The indicator of payment-to-income ratios greater than 40% was stable in the second quarter of 2023 (a slight decrease). Decreases were recorded in the second quarter of 2023 in the percentage of loans executed at floating interest rates and in loans for investment purposes as a percentage of total purchases of homes.

The increases in the interest rate and the rise in inflation have led to higher monthly payments, which, combined with the higher uncertainty regarding economic conditions in the coming period, resulted in an increase in the risk level, and may cause a further increase in the future. The Bank has examined and will continue to examine the effects of the economic environment on borrowers' condition by analyzing the effects of forecasts and the actual effects on borrowers' condition.

The weighted average financing rate (LTV) in the housing-loan portfolio of the Bank as at June 30, 2023, is approximately 46%, similar to the financing rate as at December 31, 2022 (based on the financing rate when the loan was granted). The effective rate is even lower, due to regular repayments since the credit was granted and an increase in the value of the pledged assets. It is noted that the increase in the risk level that began in the second half of 2022 followed a period in which the risk decreased, and the overall risk level in the portfolio is low.

For further information regarding initiatives of the Bank for customers aimed at coping with the increase in the interest rate, see [the Corporate Governance Report, in the section "Housing loans."](#)

D.3.d. Credit to private individuals (excluding housing)

Table D-11: Balance of credit to private individuals in Israel

	Balance as at		Change	
	June 30, 2023	December 31, 2022		
	NIS millions			
Balance sheet				
Negative balance in current accounts	2,568	2,666	(98)	(3.7%)
Loans ⁽¹⁾	24,325	24,256	69	0.3%
Of which: bullet and balloon loans	58	48	10	20.8%
Credit for purchases of motor vehicles ⁽²⁾	2,943	3,359	(416)	(12.4%)
Debtors in respect of credit-card activity	5,181	4,849	332	6.8%
Total balance sheet credit risk	35,017	35,130	(113)	(0.3%)
Off-balance sheet				
Off-balance sheet credit risk	20,085	17,980	2,105	11.7%
Total credit risk	55,102	53,110	1,992	3.8%

(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.

The balance of loans to private individuals in Israel, including credit for the purchase of motor vehicles, decreased by approximately 1.3% in the first half of 2023 in comparison to December 31, 2022. Total balance sheet credit risk decreased by approximately 0.3% in this period, and total off-balance sheet credit risk increased by approximately 11.7%, mainly influenced by an increase in credit facilities in credit cards.

Beyond the measures taken with respect to housing credit, the Bank has taken additional measures to provide relief to borrowers in coping with the increase in the interest rate on consumer credit, such as spreading payments on existing loans and an option to extend the duration of the loan to ease monthly payments.

For details regarding problematic debts in respect of private individuals in Israel, see [Note 13 to the Condensed Financial Statements](#).

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](#).

D.3.e. Leveraged financing

The Bank provides leveraged financing to its customers from time to time. Leveraged financing is managed and defined at the Bank in accordance with the directives of the Bank of Israel, and in particular, with Proper Conduct of Banking Business Directive 311 (Credit Risk Management), Proper Conduct of Banking Business Directive 323 (Limits on Financing of Equity Transactions), and Proper Conduct of Banking Business Directive 327 (Management of Leveraged Loans).

Among other matters, leveraged financing includes equity transactions (transactions for the acquisition of an equity interest in another corporation, acquisition of all or a significant part of the assets of another corporation, buybacks of issued shareholders' equity, or capital distribution – payment of a dividend, or another transaction aimed at increasing value for shareholders, as defined in Proper Conduct of Banking Business Directive 323); financing for borrowers in various segments of specified economic sectors characterized by exceptional levels of certain parameters, relative to the accepted norms in the economic sectors, such as a high financing rate that deviates from the policy for the sector; and financing of mezzanine debt.

The Bank has set an internal limit on leveraged financing as a percentage of the Tier 1 capital of the Bank. Developments in leveraged financing and compliance with the established limit are reported each quarter to the Board of Management and the Board of Directors of the Bank, for monitoring of the risks inherent in this type of financing.

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

Table D-12: Exposures of the Bank to leveraged financing, by economic sector of the borrower*

	June 30, 2023			
	Number of borrowers	Balance sheet credit balance	Off-balance sheet credit balance	Total
	NIS millions			
Economic sector of the borrower				
Construction and real estate – real-estate activities	4	2,028	176	2,204
Hotels, hospitality, and food services	-	-	-	-
Mining and quarrying	2	330	-	330
Commerce	-	-	-	-
Financial services and insurance services	1	648	-	648
Industry	2	765	-	765
Water supply and sewage services	1	265	-	265
Total	10	4,036	176	4,212

* Net of charge-offs and allowances for credit losses calculated on an individual basis, if any.

Table D-12: Exposures of the Bank to leveraged financing, by economic sector of the borrower* (continued)

	December 31, 2022			
	Number of borrowers	Balance sheet credit balance	Off-balance sheet credit balance	Total
	NIS millions			
Economic sector of the borrower				
Construction and real estate – real-estate activities	2	1,196	216	1,412
Hotels, hospitality, and food services	1	240	-	240
Mining and quarrying	3	441	293	734
Commerce	1	350	-	350
Financial services and insurance services	1	657	51	708
Industry	1	429	-	429
Total	9	3,313	560	3,873

* Net of charge-offs and allowances for credit losses calculated on an individual basis, if any.

D.4. Credit risk mitigation: standardized approach disclosures

The Bank applies the comprehensive standardized approach in order to determine risk weightings to apply to the counterparty. The standardized approach requires the use of independent ratings prepared by international rating agencies.

Pursuant to the Basel 3 directives, under certain conditions, certain collateral, such as guarantees, credit derivatives, and financial assets held as collateral, can be deducted from risk components for the purpose of calculating the capital-adequacy ratio.

The deduction of collateral for the calculation of the capital ratio is performed after using safety margins established in the directive. These margins take into account factors including the term to maturity of the collateral, any lack of congruity between the linkage terms of the collateral and of the credit that it secures, and volatility in the value of the collateral.

The qualifying financial collateral used by the Bank to calculate capital adequacy and risk mitigation includes deposits that constitute collateral by way of liens, bonds of banking corporations and governments under permanent liens, and shares under lien traded on the primary index. In addition, the Bank uses guarantees of banking corporations, which transfer the exposure from the segment of the guaranteed party to exposure to banking corporations.

Table D-13: Credit risk mitigation

		June 30, 2023									
		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	351,744	65,417	42,422	33,409	26,124	32,008	16,298	-	-	
2	Bonds	128,207	-	-	-	-	-	-	-	-	
3	Total	479,951	65,417	42,422	33,409	26,124	32,008	16,298	-	-	
4	Of which: non-accruing or past due by 90 days or more	9,763	94	8	94	8	-	-	-	-	
		June 30, 2022									
		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	346,739	41,412	25,895	17,413	14,923	23,999	10,972	-	-	
2	Bonds	77,714	-	-	-	-	-	-	-	-	
3	Total	424,453	41,412	25,895	17,413	14,923	23,999	10,972	-	-	
4	Of which: non-accruing or past due by 90 days or more	2,985	113	3	113	3	-	-	-	-	
		December 31, 2022									
		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	345,472	62,496	39,701	32,887	23,831	29,609	15,870	-	-	
2	Bonds	103,352	-	-	-	-	-	-	-	-	
3	Total	448,824	62,496	39,701	32,887	23,831	29,609	15,870	-	-	
4	Of which: non-accruing or past due by 90 days or more	7,769	153	4	153	4	-	-	-	-	

Table D-14: Standardized approach – exposures by asset type and risk weight⁽¹⁾⁽²⁾

		June 30, 2023									Total amount of credit exposures (after CCF and after CRM)
		0%	20%	35%	50%	60%	75%	100%	150%	Other ⁽³⁾	
		NIS millions									
1	Sovereigns, central banks thereof, and national monetary authority	186,982	681	-	28	-	-	67	224	-	187,982
2	Public-sector entities (PSE) other than the central government	2,139	5,955	-	-	-	-	-	-	-	8,094
3	Banks (including multilateral development banks (MDB))	1,980	15,879	-	38	-	-	28	-	-	17,925
4	Securities companies	-	2,516	-	-	-	-	-	-	-	2,516
5	Corporations	-	14,539	-	9,999	-	-	135,298	143	-	159,979
6	Retail exposures to individuals	-	-	-	-	-	51,243	21	-	-	51,264
7	Loans to small businesses	-	-	-	-	-	9,359	-	-	-	9,359
8	Secured by a residential property	-	-	34,949	37,499	35,758	13,932	3,639	-	-	125,777
9	Secured by commercial real estate	-	-	-	-	-	-	88,633	5,876	-	94,509
10	Past-due loans	-	-	-	-	-	-	1,530	1,290	-	2,820
11	Other assets*	3,119	418	-	-	-	-	10,310	1,131	442	15,420
11A	* Of which: in respect of shares	-	-	-	-	-	-	3,368	726	-	4,094
12	Total	194,220	39,988	34,949	47,564	35,758	74,534	239,526	8,664	442	675,645

(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.

(3) In accordance with the letter of the Banking Supervision Department, the risk-adjusted assets of the subsidiary of the Bank in Turkey are weighted at a rate of 300%. The balance reflects the addition in respect of the calculation of risk-adjusted assets in accordance with this letter, relative to the calculation of risk-adjusted assets pursuant to Proper Conduct of Banking Business Directive 203.

Table D-14: Standardized approach – exposures by asset type and risk weight⁽¹⁾⁽²⁾ (continued)

		June 30, 2022									Total amount of credit exposures (after CCF and after CRM)
		0%	20%	35%	50%	60%	75%	100%	150%	Other ⁽³⁾	
		NIS millions									
1	Sovereigns, central banks thereof, and national monetary authority	220,459	355	-	9	-	-	122	34	-	220,979
2	Public-sector entities (PSE) other than the central government	1,934	4,514	-	50	-	-	-	-	-	6,498
3	Banks (including multilateral development banks (MDB))	-	14,837	-	18	-	-	45	-	-	14,900
4	Securities companies	-	2,910	-	-	-	-	-	-	-	2,910
5	Corporations	-	11,544	-	9,653	-	-	129,468	144	-	150,809
6	Retail exposures to individuals	-	-	-	-	-	51,691	24	-	-	51,715
7	Loans to small businesses	-	-	-	-	-	9,510	-	-	-	9,510
8	Secured by a residential property	-	-	33,745	37,101	31,858	18,162	3,202	-	-	124,068
9	Secured by commercial real estate	-	-	-	-	-	-	84,654	-	-	84,654
10	Past-due loans	-	-	-	-	-	-	1,496	1,076	-	2,572
11	Other assets*	3,245	-	-	-	-	-	10,960	1,101	450	15,756
11A	* Of which: in respect of shares	-	-	-	-	-	-	3,111	681	-	3,792
12	Total	225,638	34,160	33,745	46,831	31,858	79,363	229,971	2,355	450	684,371

(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.

(3) In accordance with the letter of the Banking Supervision Department, the risk-adjusted assets of the subsidiary of the Bank in Turkey are weighted at a rate of 300%. The balance reflects the addition in respect of the calculation of risk-adjusted assets in accordance with this letter, relative to the calculation of risk-adjusted assets pursuant to Proper Conduct of Banking Business Directive 203.

Table D-14: Standardized approach – exposures by asset type and risk weight⁽¹⁾⁽²⁾ (continued)

		December 31, 2022									Total amount of credit exposures (after CCF and after CRM)
		0%	20%	35%	50%	60%	75%	100%	150%	Other ⁽³⁾	
		NIS millions									
1	Sovereigns, central banks thereof, and national monetary authority	208,084	531	-	9	-	-	119	17	-	208,760
2	Public-sector entities (PSE) other than the central government	1,947	4,901	-	-	-	-	-	-	-	6,848
3	Banks (including multilateral development banks (MDB))	1,376	16,946	-	332	-	-	31	-	-	18,685
4	Securities companies	-	2,383	-	-	-	-	-	-	-	2,383
5	Corporations	-	15,003	-	10,697	-	-	133,068	124	-	158,892
6	Retail exposures to individuals	-	-	-	-	-	52,091	16	-	-	52,107
7	Loans to small businesses	-	-	-	-	-	9,661	-	-	-	9,661
8	Secured by a residential property	-	-	34,675	37,375	34,287	14,567	3,216	-	-	124,120
9	Secured by commercial real estate	-	-	-	-	-	-	85,581	4,962	-	90,543
10	Past-due loans	-	-	-	-	-	-	1,443	1,006	-	2,449
11	Other assets*	3,961	-	-	-	-	-	10,441	1,120	342	15,864
11A	* Of which: in respect of shares	-	-	-	-	-	-	3,333	715	-	4,048
12	Total	215,368	39,764	34,675	48,413	34,287	76,319	233,915	7,229	342	690,312

(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.

(3) In accordance with the letter of the Banking Supervision Department, the risk-adjusted assets of the subsidiary of the Bank in Turkey are weighted at a rate of 300%. The balance reflects the addition in respect of the calculation of risk-adjusted assets in accordance with this letter, relative to the calculation of risk-adjusted assets pursuant to Proper Conduct of Banking Business Directive 203.

E. Counterparty credit risks

Counterparty risk is defined at the Bank, according to the definition in Proper Conduct of Banking Business Directive 203A, 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.

As of July 1, 2022, data referring to counterparty credit risk are calculated according to the SA-CCR approach.

For further details, see [“Directives pertaining to capital allocation in respect of derivative financial instruments” in the section, “Capital and leverage.”](#)

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

	June 30, 2023					June 30, 2022				
	Replacement cost	Potential future exposure	Alpha used to calculate regulatory EAD	EAD after CRM	RWA	Replacement cost	Potential future exposure	EAD after CRM	RWA	
NIS millions										
1	SA-CCR approach (June 30, 2022: current exposure method)	3,332	14,654	1.4	25,180	8,691	9,342	11,020	13,981	4,448
3	Comprehensive approach to credit risk mitigation (for securities financing transactions (SFT))	-	-	-	1,801	360	-	-	*842	*168
6	Total	3,332	14,654	1.4	26,981	9,051	9,342	11,020	14,823	4,616

* Restated.

	December 31, 2022					
	Replacement cost	Potential future exposure	Alpha used to calculate regulatory EAD	EAD after CRM	RWA	
NIS millions						
1	SA-CCR approach	2,847	12,226	1.4	21,102	6,819
3	Comprehensive approach to credit risk mitigation (for securities financing transactions (SFT))	-	-	-	1,885	377
6	Total	2,847	12,226	1.4	22,987	7,196

Table E-2: Capital allocation in respect of credit value adjustment

	June 30, 2023		June 30, 2022		December 31, 2022		
	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	25,080	4,757	13,501	3,774	21,051	3,786

Table E-3: Standardized approach – exposures to counterparty credit risk based on the supervisory portfolio and risk weights

	June 30, 2023				
	0%	20%	50%	100%	Total credit exposure
	NIS millions				
Sovereigns	70	-	-	-	70
Public-sector entities (PSEs) other than the central government	-	501	-	-	501
Banks (including multilateral development banks (MDB))	-	7,423	21	-	7,444
Securities companies	-	14,369	-	-	14,369
Corporations	-	-	29	3,986	4,015
Supervisory retail portfolios	-	-	-	34	34
Loans to small businesses	-	-	-	50	50
Secured by commercial real estate	-	-	-	498	498
Other assets	-	-	-	-	-
Total	70	22,293	50	4,568	26,981

	June 30, 2022				
	0%	20%	50%	100%	Total credit exposure
	NIS millions				
Sovereigns	84	-	-	1	85
Public-sector entities (PSEs) other than the central government	-	396	-	-	396
Banks (including multilateral development banks (MDB))	-	3,118	13	2	3,133
Securities companies	-	9,076	-	-	9,076
Corporations	-	-	89	1,700	1,789
Supervisory retail portfolios	-	-	-	17	17
Loans to small businesses	-	-	-	33	33
Secured by commercial real estate	-	-	-	294	294
Other assets	-	-	-	-	-
Total	84	12,590	102	2,047	14,823

Table E-3: Standardized approach – exposures to counterparty credit risk based on the supervisory portfolio and risk weights (continued)

	December 31, 2022				Total credit exposure
	0%	20%	50%	100%	
	NIS millions				
Sovereigns	53	-	-	-	53
Public-sector entities (PSEs) other than the central government	-	582	-	-	582
Banks (including multilateral development banks (MDB))	-	6,280	17	-	6,297
Securities companies	-	12,800	-	-	12,800
Corporations	-	-	-	2,814	2,814
Supervisory retail portfolios	-	-	-	31	31
Loans to small businesses	-	-	-	47	47
Secured by commercial real estate	-	-	-	363	363
Other assets	-	-	-	-	-
Total	53	19,662	17	3,255	22,987

Table E-4: Composition of collateral in respect of exposure to counterparty credit risk

	June 30, 2023					
	Collateral used in derivatives transactions				Collateral used in securities financing transactions (SFTs)	
	Fair value of collateral received		Fair value of collateral deposited		Fair value of collateral received	Fair value of collateral deposited
	Disconnected	Not disconnected	Disconnected	Not disconnected		
NIS millions						
Cash – local currency	-	2,017	-	1,182	-	-
Cash – other currencies	-	6,676	-	3,094	12,751	-
Local sovereign debt	-	1,887	1,448	-	-	10,080
Other sovereign debt	-	2,106	139	-	-	2,488
Debt of government agency	-	-	-	-	-	-
Corporate bonds	-	177	6,501	-	-	1,984
Shares	-	-	-	-	-	-
Other collateral	-	-	-	-	-	-
Total	-	12,863	8,088	4,276	12,751	14,552

Table E-4: Composition of collateral in respect of exposure to counterparty credit risk (continued)

	June 30, 2022					
	Collateral used in derivatives transactions				Collateral used in securities financing transactions (SFTs)	
	Fair value of collateral received		Fair value of collateral deposited		Fair value of collateral received	Fair value of collateral deposited
	Disconnected	Not disconnected	Disconnected	Not disconnected		
NIS millions						
Cash – local currency	-	878	-	658	-	-
Cash – other currencies	-	4,932	-	2,516	5,808	-
Local sovereign debt	-	3	336	-	-	3,991
Other sovereign debt	-	561	60	-	-	1,422
Debt of government agency	-	-	-	-	-	1,237
Corporate bonds	-	-	780	-	-	-
Shares	-	6	-	-	-	-
Other collateral	-	-	-	-	-	-
Total	-	6,380	1,176	3,174	5,808	6,650

	December 31, 2022					
	Collateral used in derivatives transactions				Collateral used in securities financing transactions (SFTs)	
	Fair value of collateral received		Fair value of collateral deposited		Fair value of collateral received	Fair value of collateral deposited
	Disconnected	Not disconnected	Disconnected	Not disconnected		
NIS millions						
Cash – local currency	-	1,123	-	1,762	-	-
Cash – other currencies	-	5,769	-	1,805	13,296	870
Local sovereign debt	-	6	19	-	-	10,917
Other sovereign debt	-	1,605	25	-	567	3,236
Debt of government agency	-	-	-	-	-	-
Corporate bonds	-	403	2,435	-	-	725
Shares	-	-	-	-	-	-
Other collateral	-	-	-	-	-	-
Total	-	8,906	2,479	3,567	13,863	15,748

With regard to allocated capital in connection with SA-CCR, which is replacing the existing approaches to Proper Conduct of Banking Business Directive 203, see [the section “Directives pertaining to capital allocation in respect of derivative financial instruments” in the section “Capital and leverage,”](#) above.

For additional information regarding counterparty risk and the management thereof, see [the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2022.](#)

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 yield curves 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 and in actual inflation;
- **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 or decline in value 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 yield;
- **Volatility risk** – The risk of loss as a result of changes in the volatility rates quoted in the market;
- **Basis risk** – The risk of loss or decline in value as a result of changes in the spreads between different interest-rate curves or different interest bases.

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

For more extensive information regarding market, interest-rate, and investment risks and the management thereof, see [the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2022](#).

F.1. Market risk in the trading book

Market risks in the trading book arise from the Bank's activity as a market maker, trader, and manager of positions on its own behalf. The Bank's risk level is measured and controlled according to procedures that include, among other things, limits on the risk estimate in terms of VaR and on the sensitivity of economic value to changes in the primary risk factors. A risk estimate using the VaR (value at risk) method estimates the maximum potential loss to the corporation resulting from the materialization of market risks within a given period of time and at a level of statistical significance predefined by the Bank and approved by the Board of Directors.

Table F-1: Risk estimates of trading activity (VaR)

	June 30, 2023	Average in 2023 up to June 30, 2023	December 31, 2022	Average in 2022
	NIS millions			
Total trading in dealing rooms	43	52	27	41

Table F-2: Sensitivity of the Bank to changes in the exchange rates of foreign currencies with a significant volume of activity and to changes in the consumer price index

	June 30, 2023		December 31, 2022	
	NIS millions			
	10% increase	10% decrease	10% increase	10% decrease
USD	(35)	102	(82)	171
EUR	48	28	(31)	43
	3% increase	3% decrease	3% increase	3% decrease
CPI	707	(745)	555	(591)

The table above presents an analysis of the sensitivity of the economic value of the Bank to changes in exchange rates, based on revaluation of all balance sheet and off-balance sheet instruments in the risk-management system, using prevalent models for revaluation of each instrument and using representative rates as the baseline exchange rate. For the purposes of the calculation, the portfolio is revalued at an exchange rate reflecting an increase/decrease at the presented rate, with no additional assumptions. Sensitivity to the consumer price index is calculated according to the exposure of the Bank to the index, as detailed in Note 14 to the Condensed Financial Statements, plus the effect of the CPI floor on the expected accounting profit.

Table F-3: Market risk based on 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. Regulatory capital adequacy is calculated for interest-rate and share risks, as defined above, in the trading book only, and for currency risks in the banking book and in the trading book.

	June 30, 2023	June 30, 2022	December 31, 2022
	Risk-adjusted assets in NIS millions		
Direct products			
1 Interest-rate risk (general and specific)	3,537	2,625	3,537
2 Share position risk (general and specific)	-	-	-
3 Exchange-rate risk	663	888	163
4 Commodity risk	-	-	-
Options			
5 Simplified approach	-	-	-
6 Delta-plus approach	757	282	307
7 Scenario approach	-	-	-
8 Securitization	-	-	-
9 Total	4,957	3,795	4,007

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 interest income (accounting income sensitivity). This risk emerges during routine and proactive banking activity, as a result of the provision of routine services to the general public and to the business and financial sectors, and from other banking activities, including interest-rate exposure arising from the management of the Bank's investment portfolio. The risk arises from differences in the structure of assets and liabilities – durations, interest-rate bases, interest-rate reset dates, and more. Limits apply at the Bank both to the sensitivity of economic value and to the sensitivity of income and capital to scenarios of change in the shekel and CPI-linked yield curves and in yield curves in other currencies (including financial subsidiaries under the Bank's management and subsidiaries with exposure significant for the Group, if any).

The economic value sensitivity 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 the calculation in fair-value tables, where the expected cash flows are discounted by a discount rate that also reflects the risk level of the counterparty to the financial instrument. Pursuant to the Public Reporting Directives of the Bank of Israel, the Bank applies hypothetical shock and stress scenarios of changes in interest rates to the adjusted fair value of the financial instruments used by the Bank. The stress scenarios are calculated according to formulas defined in the Bank of Israel reporting requirements. The required scenarios are parallel scenarios in interest-rate curves, steepening (a decrease in the short-term interest rate and an increase in the long-term interest rate), and flattening (an increase in the short-term interest rate and a decrease in the long-term interest rate), as well as scenarios of an increase in the short-term interest rate and a decrease in the short-term interest rate. The scenarios were applied uniformly to all of the currencies included in the report to the public.

Table F-4: Adjusted* net fair value of the financial instruments of the Bank and its consolidated companies

	June 30, 2023					December 31, 2022 ⁽¹⁾				
	Unlinked NIS	CPI-linked NIS	Foreign currency – USD	Foreign currency – other	Total	Unlinked NIS	CPI-linked NIS	Foreign currency – USD	Foreign currency – other	Total
	NIS millions									
Financial assets**	453,457	61,419	85,154	15,852	615,882	458,609	57,106	84,786	14,297	614,798
Other amounts receivable in respect of derivative, hybrid, and off-balance sheet financial instruments	624,888	19,801	679,898	132,410	1,456,997	556,296	21,078	517,498	60,888	1,155,760
Financial liabilities**	391,505	28,880	142,098	16,748	579,231	402,250	30,630	136,096	15,041	584,017
Other amounts payable in respect of derivative, hybrid, and off-balance sheet financial instruments	674,840	23,862	623,353	132,030	1,454,085	599,672	25,298	466,949	60,959	1,152,878
Net fair value of financial instruments	12,000	28,478	(399)	(516)	39,563	12,983	22,256	(761)	(815)	33,663
Effect of employee benefit liabilities	-	(3,997)	-	-	(3,997)	-	(4,149)	-	-	(4,149)
Effect of spreading over periods of on-demand deposits	12,630	-	3,251	809	16,690	14,990	-	3,029	725	18,744
Adjusted net fair value*	24,630	24,481	2,852	293	52,256	27,973	18,107	2,268	(90)	48,258
Of which: banking book	25,432	25,006	2,980	204	53,622	27,953	18,598	2,224	(69)	48,706

* Net fair value of financial instruments, excluding non-monetary items, and after the effect of employee benefit liabilities and spreading over periods of on-demand deposits. For further details regarding the assumptions used to calculate the fair value of financial instruments, see [Note 15 to the Condensed Financial Statements](#).

** Excluding balance sheet balances of derivative financial instruments, fair value of off-balance sheet financial instruments, and fair value of hybrid financial instruments.

(1) Reclassified.

Table F-5: Effect of scenarios of changes in interest rates on the adjusted* net fair value of the Bank and its consolidated companies

	June 30, 2023					December 31, 2022				
	Unlinked NIS	CPI-linked NIS	Foreign currency – USD	Foreign currency – other	Total	Unlinked NIS	CPI-linked NIS	Foreign currency – USD	Foreign currency – other	Total
NIS millions										
Parallel changes										
1% parallel increase	195	(917)	(14)	2	(734)	890	(655)	27	10	272
Of which:										
banking book	153	(921)	(16)	3	(781)	844	(659)	26	9	220
1% parallel decrease	(171)	983	32	(12)	832	(843)	696	(33)	(19)	(199)
Of which:										
banking book	(128)	988	34	(13)	881	(795)	700	(32)	(18)	(145)
Non-parallel changes										
Steepening ⁽¹⁾	(522)	(166)	(53)	33	(708)	(186)	(94)	64	30	(186)
Of which:										
banking book	(511)	(167)	(52)	33	(697)	(118)	(96)	56	30	(128)
Flattening ⁽²⁾	658	(14)	36	(35)	645	454	(32)	(36)	(34)	352
Of which:										
banking book	639	(15)	35	(34)	625	375	(31)	(28)	(34)	282
Increase in short-term interest rate	672	(400)	(12)	(29)	231	751	(308)	(7)	(23)	413
Of which:										
banking book	638	(402)	(14)	(27)	195	660	(308)	1	(22)	331
Decrease in short-term interest rate	(667)	407	26	26	(208)	(746)	305	57	18	(366)
Of which:										
banking book	(632)	409	28	24	(171)	(657)	305	49	17	(286)

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

(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.

Table F-6: Sensitivity of the economic value of the Bank to parallel changes in interest-rate curves (theoretical change in economic value as a result of each scenario)

	June 30, 2023			December 31, 2022		
	Unlinked NIS	CPI-linked NIS	Foreign currency	Unlinked NIS	CPI-linked NIS	Foreign currency
	NIS millions					
Parallel changes						
1% parallel increase	(269)	(1,073)	(108)	111	(964)	(116)
1% parallel decrease	422	1,190	107	8	1,072	113

The difference between economic value sensitivity and fair value sensitivity as at June 30, 2023, mainly stems from the use of different discount curves, as described above, the effect of which is estimated at approximately NIS 0.3 billion in the unlinked segment and approximately NIS 0.2 billion in the CPI-linked segment. The continued increase in the interest rate and the level of the interest rate led to a change in depositors' behavior and a decrease in current-account balances; the current-account model was therefore updated. This update was the main cause of a change in sensitivities to the interest rate of the unlinked shekel, from sensitivity to a decrease in the interest rate to sensitivity of approximately NIS 269 million to an increase in the interest rate.

Table F-7: Effect of scenarios of changes in interest rates on net interest income and on non-interest financing income

	June 30, 2023			December 31, 2022		
	Interest income	Non-interest financing income	Total	Interest income	Non-interest financing income	Total
	NIS millions					
1% parallel increase	169	71	240	681	(243)	438
Of which: banking book	169	24	193	681	(291)	390
1% parallel decrease	(1,425)	(87)	(1,512)	(1,773)	233	(1,540)
Of which: banking book	(1,425)	(38)	(1,463)	(1,773)	284	(1,489)

Income sensitivity in the table above was calculated by shifting yield curves, using behavioral assumptions regarding changes in deposit spreads, and regarding the transfer of funds from current accounts to deposits in the case of an increase in the interest rate. The assumptions are examined and updated periodically, according to developments in the interest-rate environment. In view of the changes in the interest-rate environment, current-account balances, and customers' actual behavior, the assumptions were updated during the second quarter, and sensitivity decreased as a result. The sensitivity of the trading book was calculated using the MTM approach.

Increases in interest rates by central banks, in Israel and globally, were more moderate in the second quarter of 2023. The increase in short-term interest rates, particularly the interest rates of the central banks, has a positive effect on the income of the Bank over time, as detailed in the income sensitivity table above; part of this effect is waning with the transition from current-account deposits to other products.

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 details regarding investments of the Bank, see [Note 5 to the Condensed Financial Statements](#).

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 meet its obligations. 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 significantly impair 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 (LCR) – limited banking corporation and consolidated subsidiaries

	For the quarter ended June 30, 2023	
	Total unweighted value*	Total weighted value**
Total high-quality liquid assets		
Total high-quality liquid assets (HQLA)		175,609
Cash outflows		
Retail deposits from individuals and from small business customers, of which:	262,366	18,188
Stable deposits	76,207	3,810
Less stable deposits	107,653	12,022
Deposits for a period greater than 30 days (Section 84 of Proper Conduct of Banking Business Directive 221)	78,506	2,356
Unsecured wholesale financing, of which:	170,235	113,393
Operational deposits (all counterparties) and deposits in networks of cooperative banks	3,050	762
Non-operational deposits (all counterparties)	166,635	112,081
Unsecured debts	550	550
Secured wholesale financing	5,500	2,777
Additional liquidity requirements, of which:	132,533	22,003
Outflows related to derivative exposure and other collateral requirements	31,194	10,475
Outflows related to loss of funding on debt products	-	-
Credit and liquidity facilities	101,339	11,528
Other contractual funding obligations	11,131	11,131
Other contingent funding obligations	76,942	1,971
Total cash outflows	-	169,463
Cash inflows		
Secured lending (e.g. reverse repos)	1,591	26
Inflows from fully performing exposures	34,385	22,725
Other cash inflows	12,371	7,741
Total cash inflows	-	30,492
		Total adjusted value***
Total high-quality liquid assets (HQLA)		175,609
Total net cash outflows		138,971
Liquidity coverage ratio (%)		126%

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

** 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 58.

*** 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 (LCR) – limited banking corporation and consolidated subsidiaries (continued)

	For the quarter ended June 30, 2022	
	Total unweighted value*	Total weighted value**
Total high-quality liquid assets		
Total high-quality liquid assets (HQLA)	-	195,054
Cash outflows		
Retail deposits from individuals and from small business customers, of which:	251,017	20,753
Stable deposits	82,016	4,101
Less stable deposits	137,675	15,712
Deposits for a period greater than 30 days (Section 84 of Proper Conduct of Banking Business Directive 221)	31,326	940
Unsecured wholesale financing, of which:	203,102	131,614
Operational deposits (all counterparties) and deposits in networks of cooperative banks	2,803	701
Non-operational deposits (all counterparties)	200,045	130,659
Unsecured debts	254	254
Secured wholesale financing	3,257	210
Additional liquidity requirements, of which:	114,504	19,625
Outflows related to derivative exposure and other collateral requirements	18,015	8,914
Outflows related to loss of funding on debt products	-	-
Credit and liquidity facilities	96,489	10,711
Other contractual funding obligations	7,445	7,493
Other contingent funding obligations	75,816	2,035
Total cash outflows	-	181,730
Cash inflows		
Secured lending (e.g. reverse repos)	968	973
Inflows from fully performing exposures	32,121	18,526
Other cash inflows	12,134	7,374
Total cash inflows	-	26,873
		Total adjusted value***
Total high-quality liquid assets (HQLA)		195,054
Total net cash outflows		154,857
Liquidity coverage ratio (%)		126%

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

** 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 60.

*** 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 (LCR) – limited banking corporation and consolidated subsidiaries (continued)

	For the quarter ended December 31, 2022	
	Total unweighted value*	Total weighted value**
Total high-quality liquid assets		
Total high-quality liquid assets (HQLA)	-	179,514
Cash outflows		
Retail deposits from individuals and from small business customers, of which:	253,557	19,186
Stable deposits	79,553	3,978
Less stable deposits	122,120	13,652
Deposits for a period greater than 30 days (Section 84 of Proper Conduct of Banking Business Directive 221)	51,884	1,556
Unsecured wholesale financing, of which:	185,597	123,976
Operational deposits (all counterparties) and deposits in networks of cooperative banks	2,920	730
Non-operational deposits (all counterparties)	181,428	121,997
Unsecured debts	1,249	1,249
Secured wholesale financing	3,773	937
Additional liquidity requirements, of which:	120,669	18,850
Outflows related to derivative exposure and other collateral requirements	25,885	8,757
Outflows related to loss of funding on debt products	-	-
Credit and liquidity facilities	94,784	10,093
Other contractual funding obligations	11,227	11,227
Other contingent funding obligations	79,158	2,010
Total cash outflows	-	176,186
Cash inflows		
Secured lending (e.g. reverse repos)	1,553	-
Inflows from fully performing exposures	39,500	19,639
Other cash inflows	11,107	8,835
Total cash inflows	-	28,474
		Total adjusted value***
Total high-quality liquid assets (HQLA)		179,514
Total net cash outflows		147,712
Liquidity coverage ratio (%)		122%

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

** 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 57.

*** 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 liquidity coverage ratio during the second quarter of 2023 (the average of the daily observations in the quarter) was 126% consolidated and for the stand-alone banking corporation, while the minimum requirement is 100%. The average ratio in the second quarter of 2023 increased in comparison to the liquidity coverage ratio in the fourth quarter of 2022, due to changes in the composition of depositors and types of deposits. In view of the volatility in the markets, particularly stock markets in the United States and in Israel and the NIS-foreign currency swap market, the Bank is maintaining high liquidity levels in foreign currency. The Bank of Israel is applying a contractionary monetary policy. If this policy is maintained, the level of liquidity is expected to decrease.

The net stable financing ratio at the end of the second quarter of 2023 is 125%, consolidated, while the minimum requirement is 100%. The net stable financing ratio decreased in comparison to the ratio as at December 31, 2022, due to growth of funding needs (mainly in respect of credit) and a decrease in stable financing sources in respect of wholesale deposits.

The liquid assets of the Bank mainly consist of Israeli government bonds in NIS and in foreign currency, United States government bonds in foreign currency, and deposits with central banks (the Bank of Israel and the Federal Reserve). The Bank manages the liquidity coverage ratio, and accordingly its liquid assets, separately in 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 have 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 from private customers and from corporate clients in Israel, foreign residents, Israeli companies abroad, repo deposits, issues of CDs and other instruments secured by the FDIC in the United States, and additional resources. 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 funding source.

Table G-2: Net stable financing ratio (NSFR), limited banking corporation and consolidated subsidiaries

	June 30, 2023				Weighted value
	Unweighted value by term to maturity				
	No maturity date*	Up to 6 months	6 months to 1 year	1 year or more	
Available stable financing (ASF) items					
Capital:	-	-	-	63,621	63,621
Supervisory capital	-	-	-	63,621	63,621
Other capital instruments	-	-	-	-	-
Retail deposits from individuals and small businesses:	-	215,624	23,787	19,706	239,504
Stable deposits	-	81,799	4,766	6,430	88,667
Less stable deposits	-	133,825	19,021	13,276	150,837
Wholesale funding:	-	214,637	11,249	5,938	68,945
Operational deposits	-	-	-	-	-
Other wholesale funding	-	214,637	11,249	5,938	68,945
Liabilities with matching interdependent assets	-	-	-	-	-
Other liabilities:	-	42,918	4,954	30,154	35,311
NSFR derivative liabilities			(1,323)		
All other liabilities and equity not included in the above categories	-	44,241	4,954	30,154	35,311
Total available stable financing (ASF)	-	473,179	39,990	119,419	407,381
Required stable financing (RSF) items					
Total NSFR high-quality liquid assets (HQLA)	-	116,497	18,815	66,985	7,224
Deposits held at other financial institutions for operational purposes	-	-	-	-	-
Performing loans and securities:	-	75,458	46,890	266,067	279,162
Performing loans to financial institutions secured by Level 1 HQLA	-	-	-	-	-
Performing loans to financial institutions secured by non-Level 1 HQLA and unsecured performing loans to financial institutions	-	8,258	2,509	8,178	10,671
Performing loans to non-financial wholesale clients, loans to retail and small business customers, and loans to sovereigns, central banks, and PSEs, of which:	-	62,521	41,136	127,711	159,551
With a risk weight of less than or equal to 35% under Proper Conduct of Banking Business Directive 203	-	11,551	7,578	4,160	12,268
Performing residential mortgages, of which:	-	3,155	3,192	123,504	101,902
With a risk weight of less than or equal to 35% under Proper Conduct of Banking Business Directive 203	-	1,176	1,155	31,251	21,479
Securities that are not in default and do not qualify as HQLA, including exchange-traded equities	-	1,524	53	6,674	7,038
Assets with matching interdependent liabilities	-	-	-	-	-
Other assets:	-	24,800	107	7,892	31,544
Physical traded commodities, including gold	-				-
Assets posted as initial margin for derivative contracts and contributions to default funds of CCPs			16		13
NSFR derivative assets			8,624		9,946
NSFR derivative liabilities before deduction of variation margin posted			285		285
Others	-	15,875	107	7,892	21,300
Off-balance sheet items			189,499		8,611
Total required stable financing (RSF)					326,541
Net stable financing ratio (NSFR) (%)					125%

* Items reported in the column "no maturity date" are items with no stated maturity date. These may include, but are not limited to, items such as capital with perpetual maturity, non-maturity deposits, short positions, open maturity positions, non-HQLA equities, and physically traded commodities.

Table G-2: Net stable financing ratio (NSFR), limited banking corporation and consolidated subsidiaries (continued)

	June 30, 2022				Weighted value
	Unweighted value by term to maturity				
	No maturity date*	Up to 6 months	6 months to 1 year	1 year or more	
Available stable financing (ASF) items					
Capital:	-	-	-	49,310	49,310
Supervisory capital	-	-	-	49,310	49,310
Other capital instruments	-	-	-	-	-
Retail deposits from individuals and small businesses:	-	237,284	6,651	9,670	233,621
Stable deposits	-	86,524	1,661	3,844	87,620
Less stable deposits	-	150,760	4,990	5,826	146,001
Wholesale funding:	-	235,553	8,439	5,962	77,199
Operational deposits	-	-	-	-	-
Other wholesale funding	-	235,553	8,439	5,962	77,199
Liabilities with matching interdependent assets	-	-	-	-	-
Other liabilities:	-	32,320	3,872	38,694	43,201
NSFR derivative liabilities	-	-	1,690	-	-
All other liabilities and equity not included in the above categories	-	30,630	3,872	38,694	43,201
Total available stable financing (ASF)	-	505,157	18,962	103,636	403,331
Required stable financing (RSF) items					
Total NSFR high-quality liquid assets (HQLA)	-	163,527	6,261	51,071	6,627
Deposits held at other financial institutions for operational purposes	-	-	-	-	-
Performing loans and securities:	-	75,248	35,538	252,693	263,592
Performing loans to financial institutions secured by Level 1 HQLA	-	-	-	-	-
Performing loans to financial institutions secured by non-Level 1 HQLA and unsecured performing loans to financial institutions	-	4,242	2,168	8,911	10,631
Performing loans to non-financial wholesale clients, loans to retail and small business customers, and loans to sovereigns, central banks, and PSEs, of which:	-	66,550	30,022	120,609	149,938
With a risk weight of less than or equal to 35% under Proper Conduct of Banking Business Directive 203	-	12,166	8,268	4,332	13,033
Performing residential mortgages, of which:	-	3,351	3,348	116,920	96,848
With a risk weight of less than or equal to 35% under Proper Conduct of Banking Business Directive 203	-	1,229	1,203	29,416	20,336
Securities that are not in default and do not qualify as HQLA, including exchange-traded equities	-	1,105	-	6,253	6,175
Assets with matching interdependent liabilities	-	-	-	-	-
Other assets:	-	21,158	104	8,972	27,523
Physical traded commodities, including gold	-	-	-	-	-
Assets posted as initial margin for derivative contracts and contributions to default funds of CCPs	-	-	352	-	299
NSFR derivative assets	-	-	7,851	-	6,162
NSFR derivative liabilities before deduction of variation margin posted	-	-	258	-	258
Others	-	12,697	104	8,972	20,804
Off-balance sheet items	-	-	179,342	-	8,174
Total required stable financing (RSF)	-	-	-	-	305,916
Net stable financing ratio (NSFR) (%)	-	-	-	-	132%

* Items reported in the column "no maturity date" are items with no stated maturity date. These may include, but are not limited to, items such as capital with perpetual maturity, non-maturity deposits, short positions, open maturity positions, non-HQLA equities, and physically traded commodities.

Table G-2: Net stable financing ratio (NSFR), limited banking corporation and consolidated subsidiaries (continued)

	December 31, 2022				Weighted value
	Unweighted value by term to maturity				
	No maturity date*	Up to 6 months	6 months to 1 year	1 year or more	
Available stable financing (ASF) items					
Capital:	-	-	-	61,620	61,620
Supervisory capital	-	-	-	61,620	61,620
Other capital instruments	-	-	-	-	-
Retail deposits from individuals and small businesses:	-	223,091	12,513	17,707	234,073
Stable deposits	-	84,458	1,990	5,655	87,781
Less stable deposits	-	138,633	10,523	12,052	146,292
Wholesale funding:	-	225,342	14,709	6,303	78,343
Operational deposits	-	-	-	-	-
Other wholesale funding	-	225,342	14,709	6,303	78,343
Liabilities with matching interdependent assets	-	-	-	-	-
Other liabilities:	-	39,626	8,821	31,076	38,114
NSFR derivative liabilities	-	-	403	-	-
All other liabilities and equity not included in the above categories	-	39,223	8,821	31,076	38,114
Total available stable financing (ASF)	-	488,059	36,043	116,706	412,150
Required stable financing (RSF) items					
Total NSFR high-quality liquid assets (HQLA)	-	145,423	14,296	56,096	7,936
Deposits held at other financial institutions for operational purposes	-	-	-	-	-
Performing loans and securities:	-	78,379	41,559	260,484	272,718
Performing loans to financial institutions secured by Level 1 HQLA	-	-	-	-	-
Performing loans to financial institutions secured by non-Level 1 HQLA and unsecured performing loans to financial institutions	-	8,599	2,988	7,384	10,167
Performing loans to non-financial wholesale clients, loans to retail and small business customers, and loans to sovereigns, central banks, and PSEs, of which:	-	65,944	35,369	125,242	156,178
With a risk weight of less than or equal to 35% under Proper Conduct of Banking Business Directive 203	-	12,153	8,184	4,669	13,204
Performing residential mortgages, of which:	-	3,204	3,168	121,728	100,487
With a risk weight of less than or equal to 35% under Proper Conduct of Banking Business Directive 203	-	1,178	1,165	30,839	21,217
Securities that are not in default and do not qualify as HQLA, including exchange-traded equities	-	632	34	6,130	5,886
Assets with matching interdependent liabilities	-	-	-	-	-
Other assets:	-	24,031	103	7,445	27,377
Physical traded commodities, including gold	-	-	-	-	-
Assets posted as initial margin for derivative contracts and contributions to default funds of CCPs	-	-	135	-	115
NSFR derivative assets	-	-	6,906	-	6,503
NSFR derivative liabilities before deduction of variation margin posted	-	-	200	-	200
Others	-	16,790	103	7,445	20,559
Off-balance sheet items	-	-	183,135	-	8,290
Total required stable financing (RSF)	-	-	-	-	316,321
Net stable financing ratio (NSFR) (%)	-	-	-	-	130%

* Items reported in the column "no maturity date" are items with no stated maturity date. These may include, but are not limited to, items such as capital with perpetual maturity, non-maturity deposits, short positions, open maturity positions, non-HQLA equities, and physically traded commodities.

The Bank is in compliance with all regulatory and internal liquidity limits, including, among others, the LCR according to Proper Conduct of Banking Business Directive 221, the internal LCR model for thirty days and for shorter and longer ranges, and the NSFR (net stable financing ratio) model. In accordance with Proper Conduct of Banking Business Directive 221, as at June 30, 2023, the Bank holds consolidated liquid assets (primarily reserves at central banks, tradable government securities, and coins and bills) for times of crisis (after haircuts) in the amount of NIS 173.3 billion, in addition to liquid bonds not recognized for the purposes of the calculation of liquid assets. In light of the assumptions regarding rollover of deposits in the ordinary course of business, and other assumptions, the Bank does not foresee liquidity problems that would necessitate the use of the liquid assets; however, it is prepared for the required scenarios.

Table G-3: Details of liquid assets, by level, as required in the Basel directives

	Balance as at June 30, 2023		Average in the quarter ended June 30, 2023	
	NIS millions			
Level 1 assets	171,584		173,707	
Level 2A assets	1,599		1,768	
Level 2B assets	134		134	
Total HQLA	173,317		175,609	

	Balance as at June 30, 2022		Average in the quarter ended June 30, 2022	
	NIS millions			
Level 1 assets	190,889		193,777	
Level 2A assets	1,148		1,142	
Level 2B assets	153		135	
Total HQLA	192,190		195,054	

	Balance as at December 31, 2022		Average in the quarter ended December 31, 2022	
	NIS millions			
Level 1 assets	180,690		177,814	
Level 2A assets	1,681		1,542	
Level 2B assets	167		158	
Total HQLA	182,538		179,514	

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 and/or procedures and systems in areas related to banking activity, including units for information systems security and cyber defense, business continuity management, security, the Chief Compliance Officer, management of human resources, process controls, and more.

For additional information regarding operational risk and the management thereof, including information-technology risks, information security and cyber risks, cloud-computing risks, emergency preparedness, and insurance, see [the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2022](#).

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 legislation in Israel for implementation of the FATCA and CRS directives, and taxation aspects relevant to products or services for customers, or directives of a similar nature.

Compliance risk also includes the risk of a breach of international sanctions and lists of designated parties. Addressing this risk involves monitoring, analyzing, and applying international sanctions and lists of designated parties, monitoring international money transfers, and monitoring the opening of customer accounts and banking activity therein. The Bank applies sanctions in accordance with the established policy.

Compliance risk also includes the reputational risk that accompanies failure to comply with such directives. Compliance risk also encompasses risk related to the activity of the Bank with banks located in the Palestinian Authority, which requires the fulfillment of various regulatory requirements, in particular in connection with the prevention of money laundering and terrorism financing, and involves monitoring of fund transfers to and from residents of the Palestinian Authority.

The Bank terminated its activity with banks and branches located in the Gaza Strip at the beginning of 2009, after the government declared Gaza a hostile entity. Over the years, the Bank repeatedly notified the Bank of Israel and the Ministry of Finance that in view of the problems involved in the provision of banking services to Palestinian banks, the Bank wished to cease providing correspondent services to these banks.

In January 2018, the Bank received signed letters of immunity and indemnity from the Attorney General and the Ministry of Finance. The letter of immunity protects the Bank, its officers, and its employees from indictment in Israel for certain offenses related to money laundering and the prevention of terrorism financing in relation to services granted, or to be granted, by the Bank to Palestinian banks from March 28, 2016, to May 31, 2019 (the "Immunity and Indemnity Period"). Further to the letter of immunity, in January 2018, the Bank received a letter from the Supervisor of Banks in which she gave notice that no enforcement measures would be taken in all matters related to actions of the Bank in connection with the provision of correspondent services to which the letter of immunity applies.

In the letter of indemnity, the State of Israel made a commitment to indemnify the Bank, in an amount up to NIS 1.5 billion, for expenses (liability according to a verdict and legal expenses) borne by the Bank, within civil proceedings or criminal proceedings that do not end in a conviction, prosecuted against the Bank or an officer or employee thereof in connection with the provision of the correspondent services during the Immunity and Indemnity Period. The immunity and indemnity commitments granted to the Bank, as noted, are subject to reservations stated therein and to conditions that the Bank must fulfill.

In light of the request of the State to postpone the termination of correspondent services until the implementation of a long-term solution for the provision of correspondent services, through the establishment of a government company to provide Palestinian banks with these services, an updated letter of indemnity was issued on June 30, 2019. Pursuant to the updated letter of indemnity, the indemnity to which the State has committed towards the Bank, as detailed above, has been amended to an amount of up to NIS 1.5 billion in respect of each proceeding (not cumulatively). The letter of indemnity and the letter of immunity are extended from time to time; the most recent extension received is until March 31, 2024.

Further to the statements in Note 25F to the Financial Statements as at December 31, 2022, on May 1, 2023, with three years having elapsed from the date of the Deferred Prosecution Agreement (“DPA”) and in accordance with the provisions thereof, the United States federal court (in New York) approved, by order, the dismissal of the prosecution and the criminal proceeding against the Bank. The aforesaid order concludes the criminal proceedings against the Bank. On April 30, 2023, the Non-Prosecution Agreement (“NPA”) in respect of the FIFA investigation also ended, in accordance with the provisions thereof. For further details, see [Note 10C to the Condensed Financial Statements](#).

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, 2022](#).

J. Legal risk

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

For additional information regarding contingent liabilities and special commitments, see [Note 10 to the Condensed Financial Statements](#).

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, 2022](#).

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 loss of customers, 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, 2022](#).

L. Regulatory risk

Regulatory risk refers to regulatory directives that are not yet in effect, and is reflected in two main aspects:

- Lack of preparation for the implementation of a directive, or partial preparation for the implementation of a binding regulatory directive.
- A heavier regulatory burden that may impair the ability of the Bank to meet its obligations, realize and maximize its business objectives, or offer and deliver certain banking services, and/or may require preparation for complex and lengthy implementation and resource-intensive technological and other investments involving significant costs.

For details regarding material regulatory initiatives with an effect on the activity of the Bank during the reported period, see [the Corporate Governance Report](#).

For additional information regarding regulatory risk and the management thereof, see [the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2022](#).

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 details regarding conditions in the Israeli and global economy, see [the section "Economic and financial review" in the Report of the Board of Directors and Board of Management](#).

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, 2022](#).

N. Strategic risk

Strategic risk is the risk of material present and/or future change in profits, capital, reputation, status, and/or other material aspects as a result of a combination of one or more of the following factors: changes in the business environment; faulty business decisions; strategy and strategic goals unaligned with the organization and the environment in which it operates; improper implementation of strategy; failure to respond to changes in the industry, economy, or technology; and other factors that generate this risk.

Strategic risk is a function of the congruence (or non-congruence) of the organization's strategic goals with the environment in which it operates, the adaptation of the business plans developed to achieve these goals, resource allocation, and quality of implementation. As such, this risk constitutes forward-looking information.

O. Environmental risk

Based on the definitions of the Network for Greening the Financial System (NGFS) and the respective definitions of the Banking Supervision Department at the Bank of Israel, the term environmental risks refers to risks that derive from the exposure of a financial institution and/or the financial sector to activities that have the potential to cause environmental degradation, such as air and water pollution, ground pollution, loss of biodiversity, deforestation, and loss of ecosystems, or to be affected by such degradation.

The climate crisis is occupying an ever-growing position on the global agenda. Climate change creates harmful effects and risks referred to as climate risks. While there is some connection and overlap between climate risks and environmental risks in the classic sense referred to above, they are not identical.

According to the NGFS, and subsequently the Banking Supervision Department in Israel, climate risks for a financial institution are risks arising from its exposure to risks caused by or related to climate change:

- Physical risks – Risks resulting from acute climate events (extreme events), such as floods, storms, heat/cold waves, and wildfires, and/or chronic processes with gradual development over time, such as rising temperatures, decreasing precipitation and desertification, rising sea levels, and others.
- Transition risks – Risks that arise due to disruptions caused in the process of transforming and adapting the global economy as required, according to scientific consensus and the Paris Agreement of 2016, to fight the sources of climate change, from an economy based on carbon dioxide and other greenhouse-gas emission intensive activities to a low/zero emissions economy. Factors driving this process are changes in regulation, legislation, and government policies; technological changes; market changes and changes in consumer preferences; changes in the area of litigation; and more.

Climate risks may be reflected in the various traditional financial risks accompanying the routine operations of the Bank, such as credit risk, market risk, operational risk, liquidity risk, and other risks, through various micro- and macroeconomic transmission channels, which may have an adverse effect on the financial robustness of businesses, households, and the economy in general, as well as other risks to the Bank such as reputational risk, regulatory risk, legal risk, and more. Climate risk is considered a complex and evolving field, in that it comprises, among other matters, systemic risk on a broad, unprecedented global scale; the period in which it may materialize is far longer than the usual range of business planning for banks; and it is characterized by material uncertainty.

During the period of the report, the Bank conducted an initial trial of analysis of an acute physical climate risk scenario, concerning exposure to an extreme flooding event of collateral for the housing-loan portfolio and the portfolio of corporate credit secured by real estate, and analysis of the effects of NGFS scenarios concerning the risks of orderly transition to net-zero and disorderly transition to net-zero on losses in the corporate credit portfolio, based on assumptions, limits, and various approximations. The results of the initial analyses indicated relatively low exposure. The Bank will continue to hone its capabilities in the area of running climate scenarios, and is preparing to apply a uniform climate scenario led by the Bank of Israel. For key and strategic indicators in the area of the environment and climate, see [the section “Key environmental, social, and governance \(ESG\) indicators” in the Report of the Board of Directors and Board of Management in the Annual Financial Statements for 2022.](#)

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, 2022.](#)

P. Model risk

Model risk is the risk of adverse consequences, which may take the form of monetary loss or non-financial impacts (incorrect business and/or strategic decisions, damage to the firm’s reputation, etc.), resulting from decisions based on incorrect or inappropriate use of model outputs. The sources of this risk are possible deficiencies in input data, development methodology, technological implementation, and business use.

For additional information regarding model risk and the management thereof, see [the Report on Risks: Pillar 3 Disclosure and Additional Information Regarding Risks as at December 31, 2022.](#)