

בנק לאומי לישראל בע"מ
BANK LEUMI LE- ISRAEL B.M

No. with Companies Registrar: 520018078

To: Israel Securities Authority
www.isa.gov.il

To: The Tel Aviv Stock Exchange
Ltd.
www.tase.co.il

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Immediate Report of Rating of Bonds/Rating of a Corporation, or of Withdrawal of Rating

On 06/08/2024 Maalot S&P published

A rating report/update notice: *Updated*

Notice of withdrawal of rating

1. Rating report or notice

Rating of the corporation: *Maalot S&P _____ ilAAA _____ negative*

Comments/Nature of Notice: *Reiteration of rating _____*

Rating history over the 3 years preceding the date of the rating/notice:

Date	Rating subject matter	Rating	Comments / Nature
02/05/2024	BANK LEUMI LE- ISRAEL B.M	<i>Maalot S&P _____ ilAAA _____ negative</i>	<i>Downgrading of outlook/ forecast</i>
31/10/2023	BANK LEUMI LE- ISRAEL B.M	<i>Maalot S&P _____ ilAAA _____ stable</i>	<i>Reiteration of rating</i>
02/08/2023	BANK LEUMI LE- ISRAEL B.M	<i>Maalot S&P _____ ilAAA _____ stable</i>	<i>Reiteration of rating</i>
26/07/2022	BANK LEUMI LE- ISRAEL B.M	<i>Maalot S&P _____ ilAAA _____ stable</i>	<i>Reiteration of rating</i>
23/01/2022	BANK LEUMI LE- ISRAEL B.M	<i>Maalot S&P _____ ilAAA _____ stable</i>	<i>Reiteration of rating</i>

Explanation: As part of the rating history, one should only provide the details of the rating history of the rating agency which is the subject matter of the immediate report.

Rating of the corporation's bonds:

Security name & type	Security no. with the Stock Exchange	Rating agency	Current rating	Comments / Nature of notice
Leumi Subordinated Bonds (Series 402)	6040398	Maalot S&P	<i>Maalot S&P _____ None / NOO _____ ilAAA</i>	<i>Reiteration of rating</i>
Leumi Subordinated Bonds (Series 403)	6040430	Maalot S&P	<i>Maalot S&P _____ None / NOO _____ ilAAA</i>	<i>Reiteration of rating</i>

Leumi Subordinated Bonds (Series 404)	6040471	Maalot S&P _____	Maalot S&P _____ -iIAA _____ None / NOO	Reiteration of rating _____
Leumi Subordinated Bonds (Series 405)	6040620	Maalot S&P _____	Maalot S&P _____ -iIAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 180)	6040422	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 182)	6040539	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 183)	6040547	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 184)	6040604	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 185)	1201821	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Bonds (Series 186)	1201839	Maalot S&P _____	Maalot S&P _____ iIAAA _____ None / NOO	Reiteration of rating _____
Leumi Commercial Security (Series 5)	1201847	Maalot S&P _____	Maalot S&P _____ -1+iIA _____ None / NOO	Reiteration of rating _____

Rating history over the 3 years preceding the date of the rating/notice:

Security name & type	Security no. with the Stock Exchange	Date	Type of rated security	Rating	Comments / Nature of notice
Leumi Subordinated Bonds 402	6040398	02/05/2024	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 402	6040398	31/10/2023	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 402	6040398	02/08/2023	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 402	6040398	26/07/2022	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 402	6040398	23/01/2022	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 403	6040430	02/05/2024	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 403	6040430	31/10/2023	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 403	6040430	02/08/2023	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____
Leumi Subordinated Bonds 403	6040430	26/07/2022	CoCo Bonds	Maalot S&P _____ iIAAA _____ None / NOO	Downgrading of rating _____

Leumi Subordinated Bonds 403	6040430	23/01/2022	CoCo Bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 404	6040471	02/05/2024	CoCo Bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 404	6040471	31/10/2023	CoCo Bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 404	6040471	02/08/2023	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 404	6040471	26/07/2022	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 404	6040471	23/01/2022	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 405	6040620	02/05/2024	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 405	6040620	31/10/2023	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 405	6040620	02/08/2023	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 405	6040620	26/07/2022	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Subordinated Bonds 405	6040620	09/03/2022	Coco bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	02/05/2024	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	31/10/2023	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	02/08/2023	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	26/07/2022	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	24/05/2022	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	23/01/2022	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 179)	6040372	10/01/2022	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 180)	6040422	02/05/2024	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 180)	6040422	31/10/2023	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 180)	6040422	02/08/2023	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 180)	6040422	26/07/2022	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____
Leumi Bonds (Series 180)	6040422	23/01/2022	Unsecured senior bonds	Maalot S&P _____ iAAA _____ None / NOO _____	Reiteration of rating _____

Leumi Commercial Security (Series 5)	1201847	02/05/2024	Commercial security	Maalot S&P _____ -1+ilA _____ None / NOO	Reiteration of rating _____
Leumi Commercial Security (Series 5)	1201847	14/12/2023	Commercial security	Maalot S&P _____ -1+ilA _____ None / NOO	Reiteration of rating _____

Explanation: As part of the rating history, one should only provide the details of the rating history of the rating agency which is the subject matter of the immediate report.

Attached is the rating report: FARBan20240806104744Sanitized isa.pdf

2. On _____, _____ announced the withdrawal of rating to: _____ -

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

Signatory name		Function
1	Omer Ziv	Other Head of the Capital Markets Division

Explanation: Pursuant to Regulation 5 of the Securities Regulations (Periodic and Immediate Reports), 1970, a report filed pursuant to these regulations shall be signed by the corporation's authorized signatories. A staff position of this matter may be found on the Authority's website: [click here](#) .

On 6.8.24, S&P Maalot reiterated the Bank's long-term issuer rating and senior debt rating 'iIAAA' (negative outlook), the Bank's short-term issuer rating 'iIA-1' and the rating of the Bank's bonds 'iIAA-'.
For further details in connection with the rating, see attached file.

Reference numbers of previous reports pertaining to the matter (reference does not constitute incorporation by way of reference):

The corporation's securities are listed on the Tel Aviv Stock Exchange

The form's structure was updated on: 06/08/2024

Ticker: Leumi

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Previous names of the reporting entity:

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BANK LEUMI LE-ISRAEL B.M

August 6, 2024

Rating reiteration

Reiteration of 'ilAAA' rating, negative outlook

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Rating reiteration

Reiteration of 'iAAA' rating, negative outlook

Overview

Main strengths	Main risks
<ul style="list-style-type: none"> • Leading status in the Israeli banking industry, with strong presence in all operating segments. • A broad deposit base of local customers. • Strong profitability despite the economic slowdown. 	<ul style="list-style-type: none"> • Increasing concentration in credit advanced to the local real estate market, which may put pressure on the quality of the assets in a more challenging macroeconomic environment. • Large-scale investment in securities and pension liabilities, that create certain fluctuations in the capital base. • Activity in a competitive environment.

Strong business status and large and decentralized deposit base support the credit quality of Bank Leumi le-Israel B.M. (hereinafter - “Bank Leumi” or the “Bank”). Bank Leumi is a universal bank that serves the full spectrum of customers in Israel, thus providing reasonably predictable earnings and balance-sheet metrics. The Bank benefits from large core deposit base, accounting for approx. 90% of its funding, and despite some deposit-pricing competition, its revenues remain resilient.

Higher-for-longer interest rates are a tailwind helping loss-absorption capacity and supporting the bank's capitalization. Higher-for-longer interest rates are supporting the Bank's profitability, as are cost-efficiency initiatives. We expect credit losses to remain high at 40 basis points per year on average in 2024-2026. Leumi's superior earning capacity represents a strength compared to peers and a buffer at the current rating level. We forecast that Leumi's risk-adjusted capital (RAC) ratio will improve slightly to 8.4%-8.8% in 2026, from 8.4% as of December 2023.

However, the economic slowdown and uncertain environment coupled with Leumi's stronger-than-peers growth in construction and real estate represent a risk. We forecast NPLs to increase to about 1.4% by 2026 from a low 0.9% as of March 2024 due to high interest rates and the Israel-Hamas conflict's effects on economic performance. Strong growth in the construction and real estate segment over the past few years are exacerbating tail risk, since this segment was a significant growth driver for the Bank's credit portfolio in recent years, and we believe that this sector is currently more vulnerable.

We factor into our ratings our view that Israel (A+/Negative/A-1) would provide extraordinary support to the Bank in the event of financial distress.

The rating outlook

The negative outlook on Leumi mirrors that on the sovereign and reflects our view that an escalation of the war could lead to further downgrading of Israel's sovereign rating and have negative implications for Leumi's creditworthiness over the next 12-24 months.

Downside scenario

We could lower the rating on Leumi if we lowered the rating on Israel again because we would then consider it less likely that the government would provide extraordinary support to Leumi in case of financial distress. We could also lower the rating on Leumi if we considered that security risks had escalated, with negative consequences for the banking sector and Leumi's asset quality, capitalization, or earnings.

Upside scenario

We could consider revising the outlook to stable if we revised the outlook on Israel to stable and thought that security risks and their effect on the Bank's financial ratios had lessened.

Key metrics

Leumi Israel Ltd. Key Ratios And Forecasts (%)

	2022a	2023a	2024f	2025f	2026f
Growth in customer loans	12.2	9.5	5.4-6.6	7.2-8.8	5.4-6.6
Net interest income/average earning assets (NIM)	2.8	2.9	2.4-2.6	2.1-2.4	1.9-2.1
Cost to income ratio	38.7	32.3	34.5-36.3	36.2-38.1	37.9-39.8
Return on average common equity	16.9	13.5	11.5-12.1	10.3-10.9	9.9-10.4
New loan loss provisions/average customer loans	0.1	0.6	0.5-0.5	0.4-0.4	0.3-0.3
Gross nonperforming assets/customer loans	0.8	1.1	1.5-1.6	1.6-1.7	1.3-1.4
Risk-adjusted capital ratio	9.7	8.4	8.5-9.0	8.4-8.9	8.4-8.8

a - Actual. f - Forecast. NIM - Net interest margin. All figures are S&P Global Ratings-adjusted.

Anchor: reflects the focus on activity in Israel

We use our Banking Industry Country Risk Assessment's industry risk score to determine the Bank's anchor, the starting point in assigning an issuer credit rating. Israel-based banks benefit from the wealthy and diversified domestic economy, but they display some concentration in their lending portfolios and are vulnerable to geopolitical risk. In our view, the material escalation of geopolitical and security risks that Israel faces following the onset of the Israel-Hamas war will affect Israel's economic performance in 2024. We forecast real economic growth at 0.5% in 2024, which, excluding the pandemic

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year, 2020, will be the weakest performance in decades. While we expect growth will rebound in 2025 by 5%, we believe that the war may have a long-term adverse effect on the Israeli economy. In addition, an escalation of conflict could present additional security and social risks for Israel, with a deeper impact on the domestic economy. An economic slowdown, coupled with higher debt service, will impact asset quality, in our view. Israel's real estate sector, which represents approx. 20% of banks' credit portfolio, is among the most vulnerable to current developments, in addition to consumer credit, tourism, small businesses, and the services sector. In this context, we expect credit losses to remain elevated also in 2024 after having reached about 50 bps in 2023.

Low funding risk and the proactive regulator support the banking industry The Israeli banking sector benefits from a strong funding profile and a net external creditor position, which provide a cushion in the challenging environment. Prudent regulatory oversight somewhat mitigates risks of concentration and geopolitical instability. Israel-based banks' profitability is benefiting from a recovery in business after the Covid-19 pandemic, interest rate hikes, and continuous cost-cutting initiatives. However, competition among banks and non-bank financial institutions somewhat constrains margins and fees.

Business position: leading domestic player

Leumi has a range of business lines and a significant presence in all segments of the Israeli banking industry (see charts 1 and 2).

Chart 1 - Bank Leumi enjoys a strong presence in all market segments

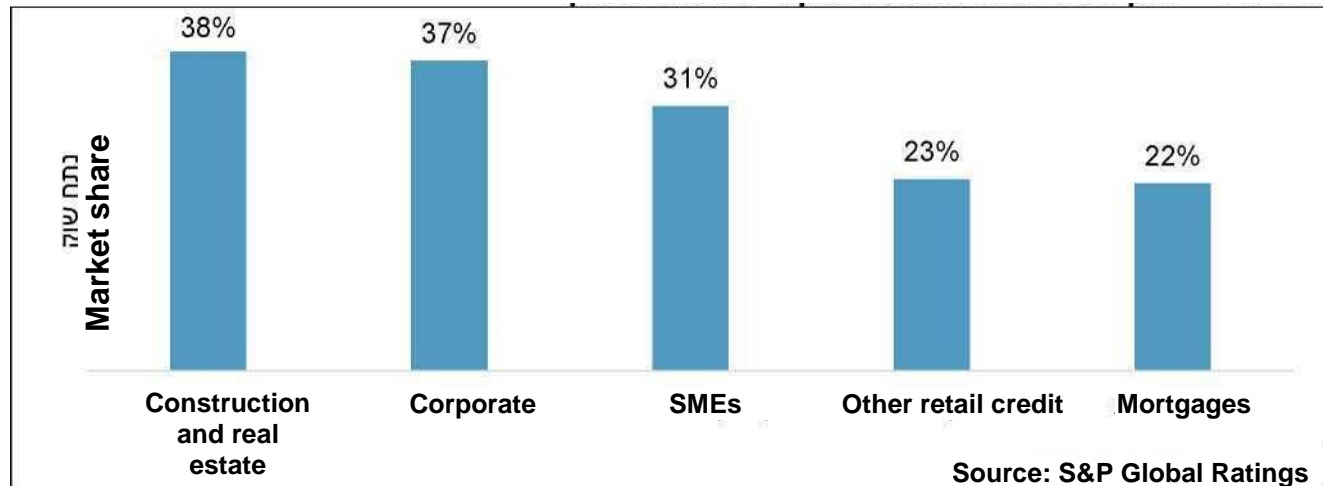
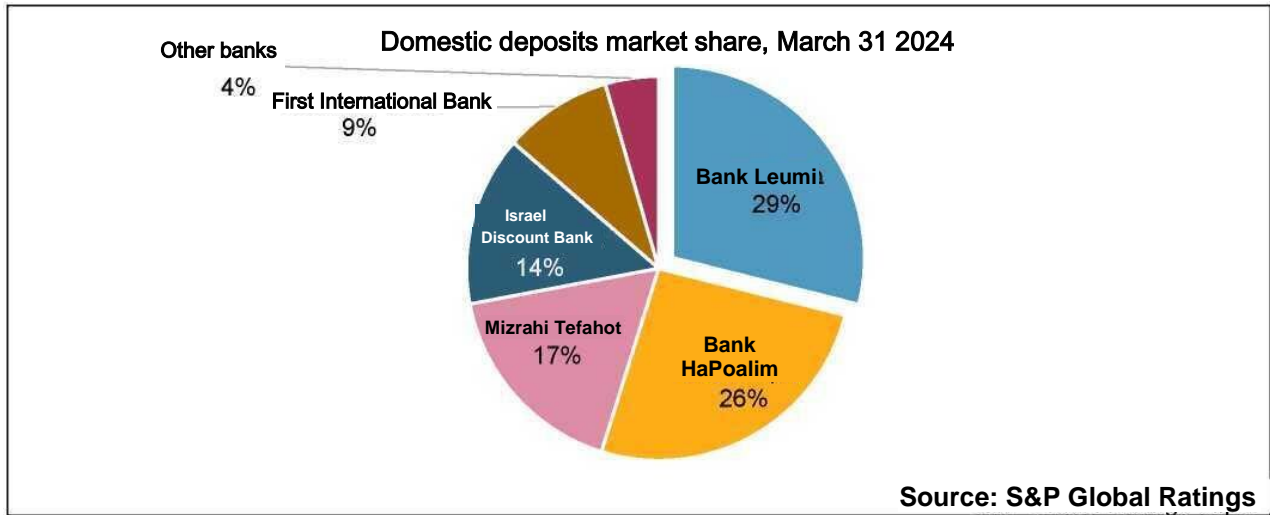


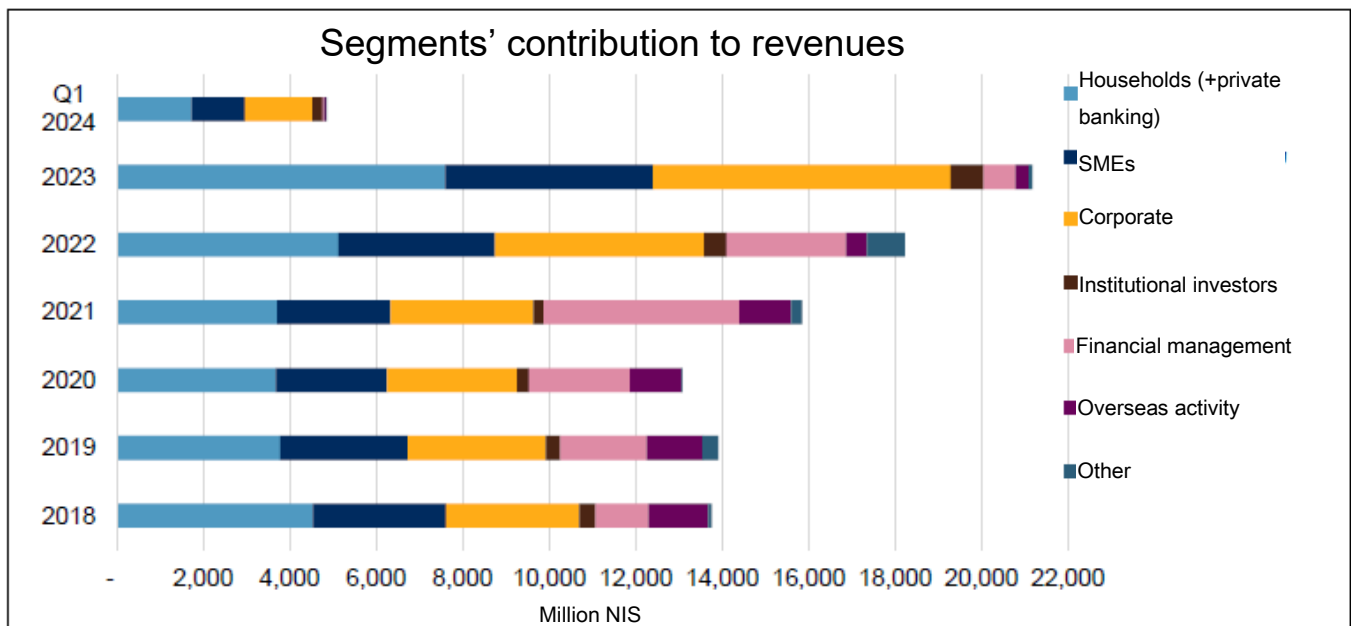
Chart 2 - Bank Leumi is one of the two largest banks in Israel



The Bank aims to maintain its current market shares in most segments while continuing to grow in the mortgages segment, amid recovered demand after negative pressure from high interest rates and the effects of the war. It also wants to grow its market share in the construction industry, but is taking a more cautious approach. At the same time, Leumi will continue to increase its digitalization and maintain tight cost controls.

Its diversified revenue base provides business stability. However, larger operations than peers in the capital markets and investment banking segments create some volatility in its revenue base (see chart 3).

Chart 3: Leumi has a diversified revenue base with a significant contribution from investments



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Bank Leumi has significantly expanded its business after the pandemic, but has mostly focused on construction and real estate segments, which we consider inherently riskier. The Bank's underwriting policies have remained conservative, but we think that rapid growth in the real estate segment might expose the Bank to increased risks amid tougher macroeconomic conditions. We expect the Bank's lending growth to slow moderately over the next two-to-three years, due to the economic slowdown, uncertainty, and tight financing conditions.

On the international front, the Bank's main exposure is its investment in Valley National Bank (hereinafter - "Valley"). Leumi cooperates with Valley to serve the US operations of large Israeli companies that are important Leumi customers. It is important for Leumi to have a presence in the USA because of the economic, political, and historical ties between the USA and Israel.

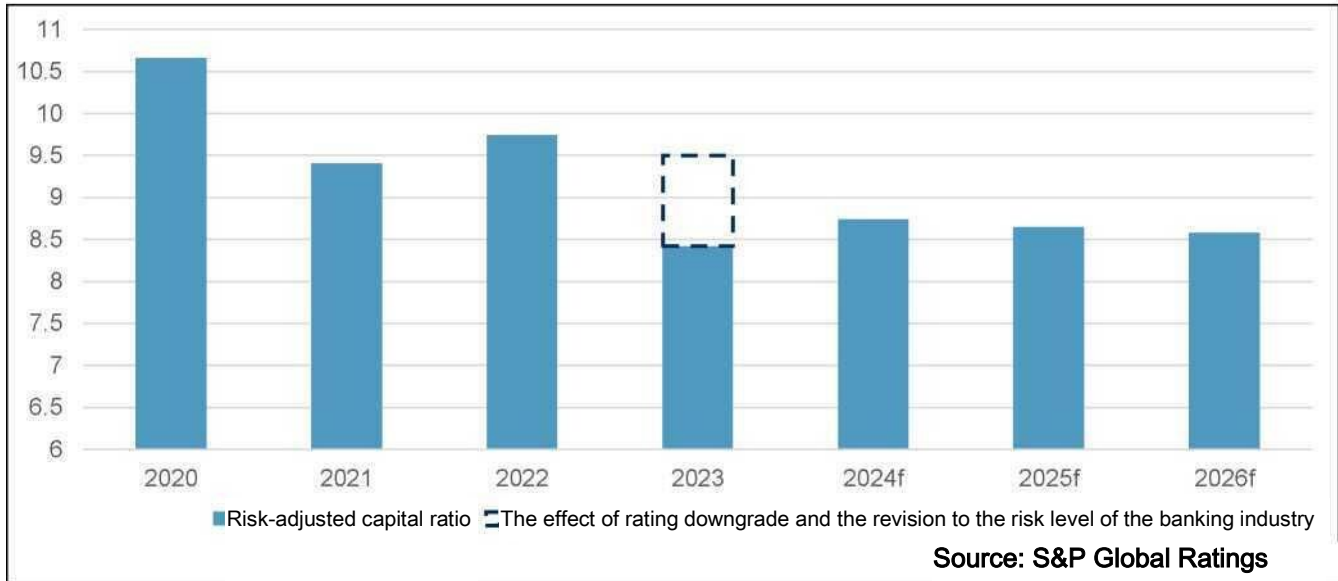
Bank Leumi's activity in the USA

Leumi sold its 85% stake in Bank Leumi USA to Valley on April 1, 2022, in exchange for cash and about 14.2% of Valley, for about USD 1.2 billion. While we think that the sale reduced Leumi's operational risk, we believe it magnified its exposure to the turmoil at US regional banks and added some volatility to the bank's performance given Valley's sizable exposure to commercial real estate of about 5x its capital (see ["Outlooks On Five US Regional Banks Revised To Negative From Stable On Commercial Real Estate Risks; Ratings Affirmed", March 26, 2024](#)). Bank Leumi's initial NIS 3.6 billion investment in Valley has been repeatedly written down to reflect Valley's weaker share price performance, in line with other US regional banks. We deduct Leumi's entire investment in Valley - currently estimated at approx. NIS 2 billion - from our calculation of capital.

Capital and profitability: higher-for-longer interest rates support profitability

We believe Bank Leumi's profitability will continue to support its capital, but we expect it to improve only marginally due to sustained credit growth and an increase in shareholder distributions. We anticipate that Leumi's RAC ratio will slightly progress to about 8.4%-8.8% in 2026, from 8.4% as of December 2023 (pro forma for new BICRA parameters; see [Bank Leumi Le-Israel B.M. - Rating Outlook Changed to Negative Due to Increased Geopolitical Risks, 'ilAAA' Rating Reiterated](#), May 2, 2024).

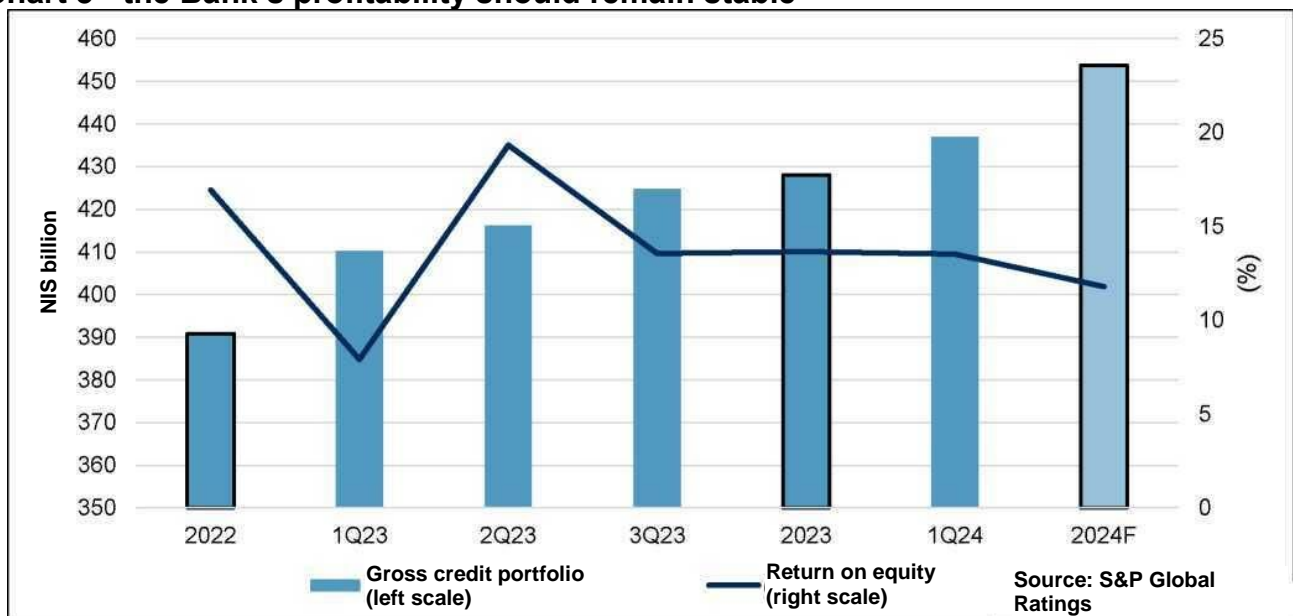
Chart 4: Development of Bank Leumi’s risk-adjusted capital ratio (RAC)



Leumi’s RAC has suffered from the ongoing conflict that led to the sovereign rating downgrade and the lowering of Israel’s economic risk in April and May 2024, respectively.

Interest rates should remain high for 2024 as a result of the Bank of Israel's cautious approach in this uncertain environment - thereby providing a tailwind to banks’ profits. Assuming geopolitical risk recedes, we expect interest rates to moderately decline from 2025. We anticipate a still-high net interest margin (NIM), lending expansion, and cost-containment measures to sustain return on equity (RoE); we forecast RoE will remain above 10% but be volatile amid provisioning efforts and extraordinary items.

Chart 5 - the Bank’s profitability should remain stable



In our forecast we factor in:

- Net interest margin gradually declining to approx. 2.0% in 2026 from 2.9% as of December 2023 balancing some of the positive effects of still-sustained lending growth, at about 6%-7%, and a high portion of interest-bearing deposits.
- Weak fee performance in 2024, and a gradual recovery thereafter due to its diversified fees-based business.
- Still-high credit losses, which will decline moderately to approx. 40 bps on average in 2024-2026.
- We also take into account the new windfall tax for the sector that will extend until end-2025.
- An increased dividend payout ratio of 40%-45% in 2024-2026.

The Bank's regulatory capital and leverage ratios are comfortably above regulatory requirements.

The Bank's CET 1 ratio stood at a historically high 11.98% as of March 2024, above the minimum target of 10.23% required by the Bank of Israel. We do not expect the Bank would maintain its current level of capitalization in a more stable geopolitical environment, as it usually works with narrower buffers. This is because Israeli banks use the standardized approach to calculating risk-weighted assets and apply the Bank of Israel's more conservative requirements to some real-estate-related exposures. We don't regard this as a risk because we understand that the Bank of Israel is comfortable with these relatively narrow margins and that Bank Leumi does not wish to approach the minimum threshold.

Bank Leumi's capitalization is more volatile than peers' due to the large securities portfolio and defined benefit pension fund, which are sensitive to interest rate changes. Interest rates have the opposite effect on mark-to-market evaluations of the Bank's securities accounted at fair value and on unrecognized losses for employee benefits. Unrealized losses associated with Bank Leumi's bonds reached approx. NIS 1.7 billion as of March 31, 2024, compared to a gain of approx. NIS 874 million as of December 2021, while unrecognized losses for employee benefits declined to NIS 743 million as of March 31, 2024, from a record amount of NIS 3.5 billion as of December 2021.

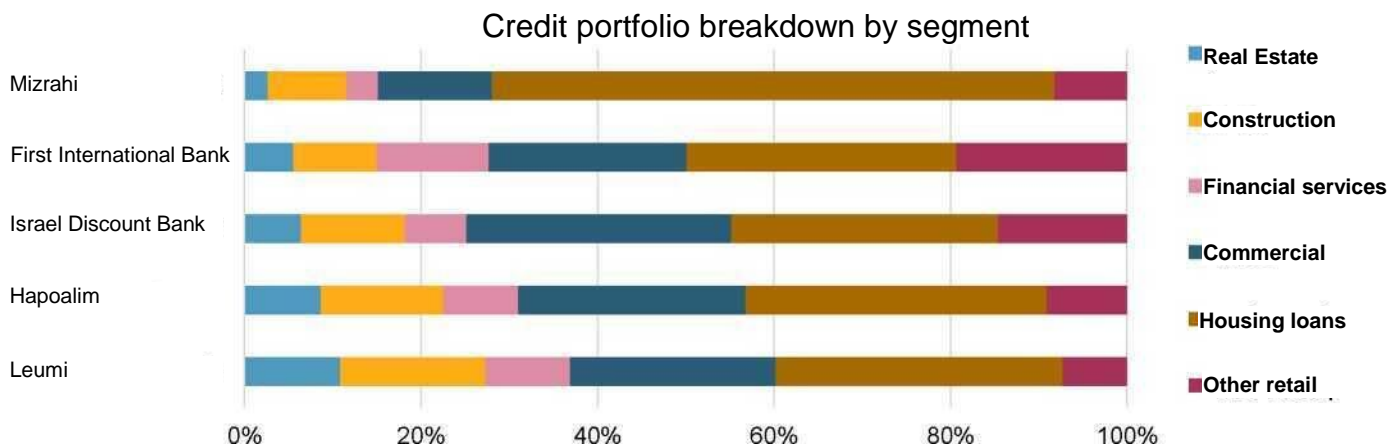
The Bank of Israel calculates its regulatory capital ratio differently to how we calculate risk-adjusted capital ratio. The Bank of Israel fully captures unrealized losses or gains on securities accounted at fair value in its regulatory capital calculation. Since July 2022, the Bank of Israel has allowed Bank Leumi to spread over four quarters the net amount of the change in the value of assets designated for hedging its employee-benefits liability derived from movement in the discount rate (the Bank does not disclose the amount).

In our risk-adjusted capital calculation, we neutralize unrealized losses or gains on securities accounted at fair value. This is because including unrealized gains and losses in total adjusted capital would create more volatility in the risk-adjusted capital ratio and could distort the true picture of the Bank's capital adequacy in cases where unrealized gains and losses are unlikely to be realized. However, while we do not include unrealized losses and gains in total adjusted capital, we consider their magnitude, their impact on liquidity, and the probability that they could result in realized losses. At the same time, we reduce banks' total adjusted capital by the full amount of unrecognized losses for employee benefits.

Risk Position: High and increasing exposure to the real estate sector

We view Bank Leumi's risk position as reflecting its higher-than-peers concentration. A key risk factor for Bank Leumi and many of its local peers is its high exposure to property-related lending (see chart 6), namely for construction (16% of portfolio as of March 2024) and real estate loans (11%). We acknowledge that the Bank's total exposure to construction and real estate is below the regulatory limit of 22%, when accounting for risk mitigation techniques.

Chart 6: Leumi's domestic property-related lending exposure is a source of risk



Source: S&P Global Ratings

Housing carries lower risk, in our view. However, we are mindful of the strong growth of both the sector and real estate prices over the past couple of years, which only temporarily slowed down in 2023 amid high interest rates and the conflict's consequences for confidence and security risk.

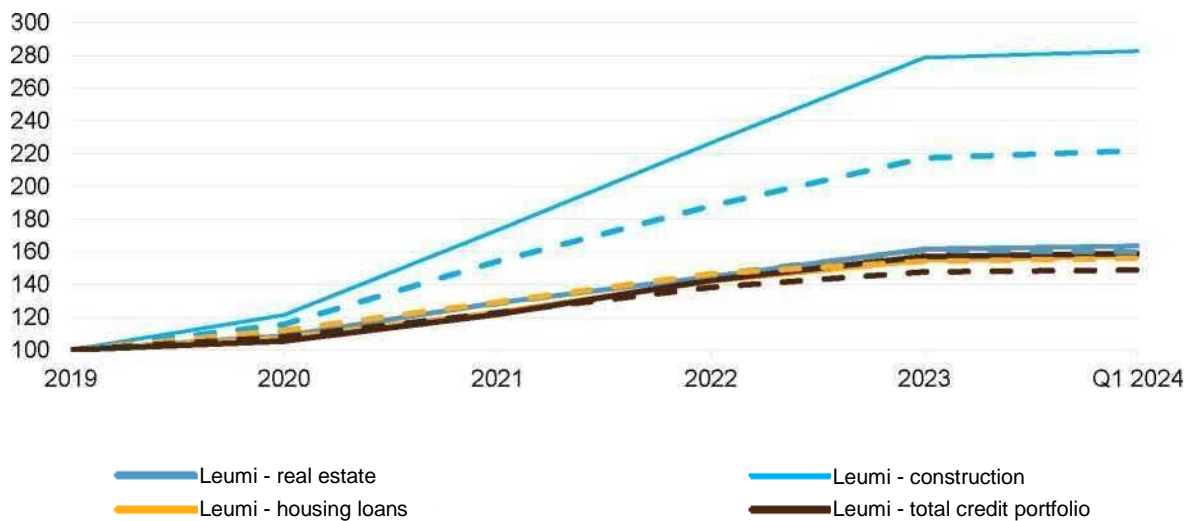
Moderate loan-to-value ratios (averaging 48.4% as of March 2024), conservative underwriting standards, and sustained housing demand due to demographic dynamics somewhat mitigate these risks.

We consider the Bank's high exposure to construction and income-producing real estate as riskier, particularly considering the Bank's strong growth in these subsegments over the past few years (see

chart 7). Approximately 60% of the Bank's exposure is concentrated in residential property projects and most of the loans have an average duration of under three years, thereby mitigating the risk. However, the new credit and the fact that recent projects might rely on pricing assumptions that could prove to be challenging amid the present macroeconomic conditions, still represent a risk, in our view.

Offices and shopping malls have been resilient during the pandemic, but we still see a risk of oversupply coming from the worsened economic conditions and reduced attractiveness of the country for foreign direct investments, particularly in the high-tech sector.

Chart 7: Bank Leumi has outgrown the sector in construction and real estate lending



Source: S&P Global Ratings

Total banking sector data is an estimate based on the financial statements of Leumi, Hapoalim, Mizrahi, Discount and First International Bank

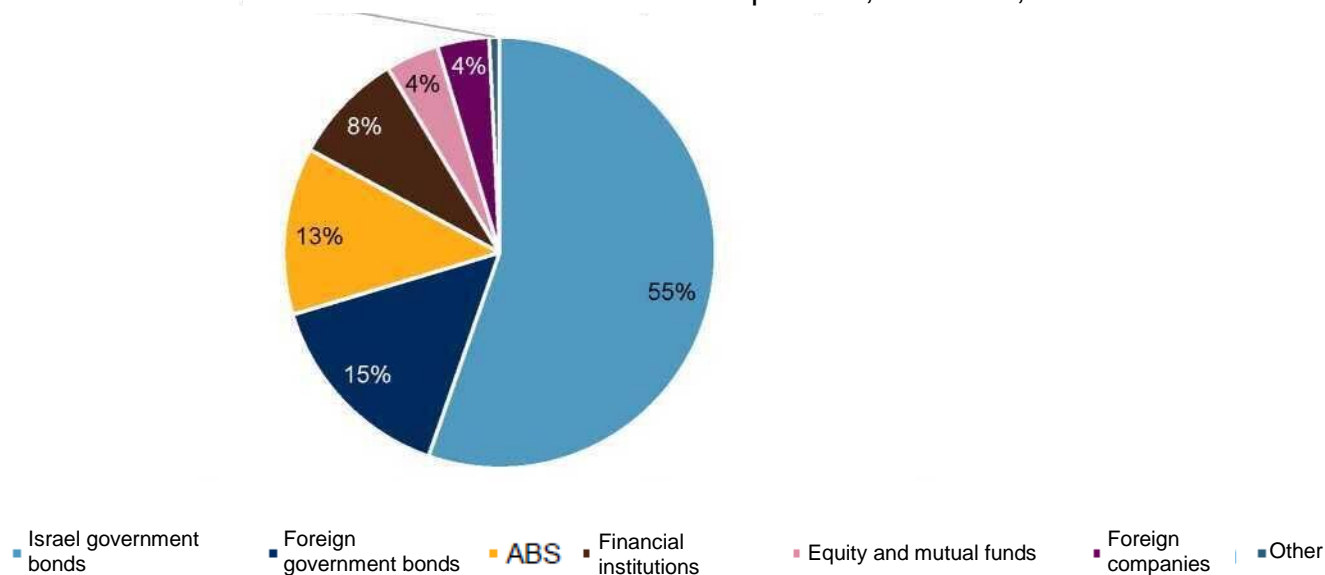
So far, the Bank's asset quality metrics have remained strong. Its nonperforming loans ratio reached 0.96% as of March 31, 2024, higher than 0.77% in 2022 but still lower than the December 2021 ratio of 1.12%. That said, because of the economic slowdown and strong growth in the Bank's exposure to construction and real estate, we still think its asset quality indicators will deteriorate. Supporting measures allowing borrowers to defer payments have impacted about 6% of Leumi's loans, and the bank has estimated a related cost of approx. NIS 440 million, although customer utilization was only approx. 42% in May 2024. We forecast non-performing loans to increase to about 1.4% by 2026 and credit losses to remain at about 50 bps in 2024, then gradually reduce to 30 bps in 2026. The Bank's high level of loan loss reserves, amounting to approx. 1.4% of total loans, mitigates the risk in our opinion. Risk could increase if

Bank Leumi continues to outgrow its exposure to construction and commercial real estate or if the risk of oversupply in the retail and office segments materializes.

Interest-rate risk is managed using the nostro portfolio, taking into account pension liabilities changes due to interest rate changes. Based on sensitivity analysis published by the Bank, as of March 31, 2024, a simultaneous decline of 1% in interest rates would lead to a positive impact on the net fair value of the financial instruments (adjusted for non-monetary items and the effect of the employee benefits liability) of approx. NIS 1.7 billion and approx. a NIS 2.5 billion decline for a 1% increase. The Bank's securities portfolio is quite diversified (see chart 8) and approx. NIS 6.5 billion is invested in equity, which carries a high 823% risk weight in our capital calculation.

Chart 8: Bank Leumi's investments portfolio is quite diversified but somewhat volatile

1% Breakdown of the Bank's securities portfolio, March 31, 2024



Source: S&P Global Ratings

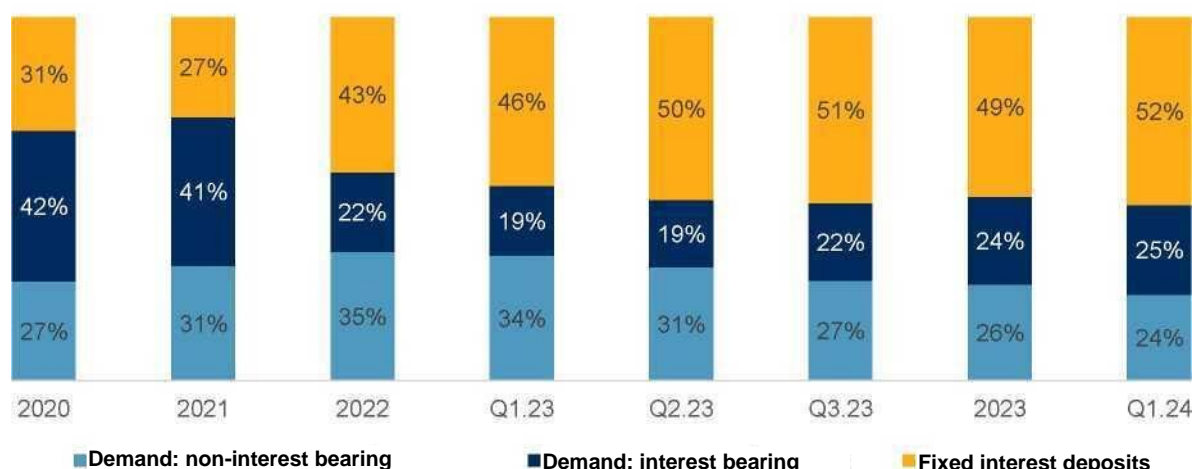
The Bank's operational risks are material, but not bank specific. They mainly relate to the geopolitical tensions in the region and potential damage to the Bank in case of tail events. These risks, including the latest developments since October 2023 are reflected in our anchor for Israeli banks. Bank Leumi has not experienced any major successful cyber-attacks but attempts have increased particularly since the last quarter of 2023. The bank continues to strengthen its cyber risk management framework and in our opinion adequately protects itself against this risk.

Funding and liquidity: sound liquidity and customer deposits support the funding base

The Bank's solid funding and liquidity metrics provide a cushion in a volatile operating environment. Bank Leumi's funding base is 90% composed of core deposits, which we see as highly diverse and stable. Corporate and institutional entities' deposits, accounting for about 53% of total domestic deposits, have a good track record of stability, but imply some deposit-pricing competition (see chart 9). Corporate and institutional entities' deposits were the main driver of deposit growth in the first quarter of 2024 and may gain weight in the future as the Bank seeks to fund its strong lending growth. Despite this, Bank Leumi has maintained strong profitability.

Chart 9: The share of non-interest bearing deposits has declined

The breakdown of deposits in Bank Leumi



Due to its large deposits base, the Bank does not rely materially on wholesale funding to finance long-term customer assets. As of March 31, 2024, total wholesale funding stood at 9.33% of Leumi's funding base. The Bank's liquid-assets cushion is material, comprising cash, deposits with the Bank of Israel and other banks, and investment in securities, which constituted approx. 38% of assets on March 31, 2024.

External support: Potential for government support

The long-term issuer rating reflects our view that the Bank has high systemic importance in Israel and that the government is supportive of the domestic banking sector. We would reconsider our assessment of government support if the regulatory authorities introduced an updated bank resolution framework, but we do not anticipate such a development in the medium term.

Environmental, social and governance factors

We think that environmental, social, and governance credit factors influence Bank Leumi's credit quality similarly to its industry and local peers. Bank Leumi has established a sustainability strategy and environmental, social, and governance factors are becoming an important consideration in its lending or investment decisions.

Over the past couple of years, some changes have occurred at the top management level, but we anticipate continuity in the Bank's strategy. We regard the management team as professional and experienced. Bank Leumi has in place a robust system of checks and balances in decision-making, with independent directors that contribute to the Bank's strategy.

Environmental and social factors do not affect Bank Leumi's credit quality differently to its industry peers. We expect that the Bank's investment in digitalization will have gradual positive environmental effects. As to company risks, Bank Leumi will continue its staff reduction as part of its strategy. We expect that it will handle early retirements carefully.

Hybrid instruments

We rate the subordinated notes with loss absorption mechanism by deducting one notch from the Bank's stand-alone credit profile for default risk, since we do not expect those instruments to benefit from state support, and one further notch for subordination from the domestic rating. The final rating of those instruments is 'iIAA-'.

Financial data and ratios

Table 1.

Leumi Israel Ltd. Key Figures (Mil. ILS)

	YTD Mar-2024	Annual 2023	Annual 2022	Annual 2021	Annual 2020
Adjusted assets	753,673	730,886	698,109	656,440	556,020
Customer loans (gross)	436,924	428,009	390,877	348,331	301,263
Adjusted common equity	54,471	51,721	45,904	38,843	34,586
Operating revenues	5,478	21,359	17,663	15,802	12,968
Noninterest expenses	1,825	6,894	6,834	7,425	6,928
Core earnings	2,228	7,708	7,068	5,968	2,128

Table 2.

Leumi Israel Ltd. Business Position (Mil. ILS)

	YTD Mar-2024	Annual 2023	Annual 2022	Annual 2021	Annual 2020
Total revenues from business line (currency in millions)	6,335	21,395	18,631	15,965	12,969
Commercial banking/total revenues from business line	44.93	57.56	48.03	42.81	50.71
Retail banking/total revenues from business line	29.31	35.53	27.75	24.03	28.57
Commercial & retail banking/total revenues from business line	74.24	93.09	75.78	66.83	79.28
Other revenues/total revenues from business line	25.76	6.91	24.22	33.17	20.72
Return on average common equity	19.96	13.52	16.93	15.21	5.75

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Table 3.

Leumi Israel Ltd. Capital and Earnings

	YTD Mar-2024	Annual 2023	Annual 2022	Annual 2021	Annual 2020
Tier 1 capital ratio	N/A	N/A	11.46	11.50	11.87
S&P Global Ratings' RAC ratio before diversification	N/A	N/A	9.74	9.41	10.66
S&P Global Ratings' RAC ratio after diversification	N/A	N/A	8.80	8.76	9.40
Adjusted common equity/total adjusted capital	100.00	100.00	100.00	100.00	100.00
Net interest income/operating revenues	68.77	74.90	74.79	65.47	67.27
Fee income/operating revenues	17.07	17.50	20.01	22.19	24.39
Market-sensitive income/operating revenues	13.40	5.99	2.95	10.85	7.91

N/A - not applicable

Table 4.

Bank Leumi le-Israel B.M. RACF [Risk-Adjusted Capital Framework] Data (Mil. ILS)

	EAD(1)	Basel III RWA(2)	Average Basel III RW(%)	S&P Global RWA	Average S&P Global RW (%)
Credit risk					
Government and central banks	222,505	5,018	2	3,695	2
Of which regional governments and local authorities	11,057	4,012	36	398	4
Institutions and CCPs	66,445	11,531	17	16,285	25
Corporate	291,005	274,931	94	328,214	113
Retail	170,328	100,275	59	67,420	40
Of which mortgage	130,126	70,021	54	37,268	29
Securitization (3)	4,012	938	23	938	23
Other assets (4)	8,979	18,280	204	23,767	265
Total Credit Risk	763,275	410,971	54	440,320	58
Total credit valuation adjustment	--	2,989	--	3,885	--
Equity in the banking book	6,477	12,439	192	53,280	823
Trading book market risk	--	5,834	--	8,750	--
Total market risk	--	18,272	--	62,030	--
Total operational risk	--	29,943	--	38,462	--
		Basel III RWA		S&P Global RWA	% of S&P Global RWA
RWA before diversification		462,176		544,697	100
Total Diversification/ Concentration Adjustments		--		62,399	11
RWA after diversification		462,176		607,095	111
	Tier 1 capital		Tier 1 ratio (%)	Total adjusted capital	S&P Global RAC ratio (%)
Capital ratio before adjustments	53,892		11.7	51,721	9.5
Capital ratio after adjustments (5)	53,892		11.7	51,721	8.5

Table 4.

Bank Leumi le-Israel B.M. RACF [Risk-Adjusted Capital Framework] Data (Mil. ILS)

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Capital ratio after adjustments (5)	53,892	11.7	51,721	8.5

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

Table 5.

Leumi Israel Ltd. Risk Position (%)

	YTD Mar-2024	Annual 2023	Annual 2022	Annual 2021	Annual 2020
Growth in customer loans	8.33	9.50	12.21	15.62	5.13
Total diversification adjustment/S&P Global Ratings' RWA before diversification	N/A	N/A	10.69	7.39	13.39

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	YTD Mar-2024	Annual 2023	Annual 2022	Annual 2021	Annual 2020
Total managed assets/adjusted common equity (x)	13.84	14.14	15.23	16.90	16.08
New loan loss provisions/average customer loans	0.21	0.58	0.13	-0.25	0.87
Net charge-offs/average customer loans	0.03	0.13	0.07	-0.03	0.18
Gross nonperforming assets/customer loans + other real estate owned	0.96	1.15	0.77	1.12	1.60
Loan loss reserves/gross nonperforming assets	165.99	137.05	165.48	115.72	109.57

N/A – not applicable

Table 6.

Leumi Israel Ltd. Funding and Liquidity

	YTD Mar-2024	Annual 2023	Annual 2022	Annual 2021	Annual 2020
Core deposits/funding base	90.67	89.40	91.07	92.45	93.13
Customer loans (net)/customer deposits	72.15	74.17	69.24	63.96	66.18
Long-term funding ratio	95.74	93.77	94.93	95.00	96.36
Stable funding ratio	134.50	129.99	137.31	145.32	140.28
Short-term wholesale funding/funding base	4.63	6.75	5.47	5.36	3.93
Regulatory net stable funding ratio	119.00	118.00	128.00	131.00	N/A
Broad liquid assets/short-term wholesale funding (x)	7.54	5.04	6.68	7.77	10.15
Broad liquid assets/total assets	30.45	29.56	31.96	36.91	34.44
Broad liquid assets/customer deposits	38.51	38.07	40.10	45.08	42.82
Net broad liquid assets/short-term customer deposits	41.75	38.14	42.62	49.09	48.26
Regulatory liquidity coverage ratio (LCR) (%)	133.00	1.24	1.31	1.24	1.37
Short-term wholesale funding/total wholesale funding	49.63	63.74	61.26	71.08	57.21

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

Methodology and related articles

- [Methodology - General Criteria: Principles of Credit Ratings, S&P, February 16, 2011](#)
- [Methodology - General Criteria: Methodology for Linking Long-Term and Short-Term Ratings, April 7, 2017](#)
- [Methodology - General Criteria: Group Rating Methodology, July 1, 2019](#)
- [Methodology - General Criteria: Credit Risks Arising from Environmental, Social, and Governance Factors, October 10, 2021](#)
- [Methodology: Methodology for Rating of Financial Institutions, December 9, 2021](#)
- [Methodology: Methodology for Banking Industry Country Risk Assessment, December 9, 2021](#)
- [Methodology - General: Hybrid Capital Rating, March 2, 2022](#)
- [Methodology - General: National Scale Credit Ratings Methodology, June 8, 2023](#)

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- [Methodology: Risk-Adjusted Capital Adequacy Assessment Methodology, April 30, 2024](#)
- [Rating Scales and Definitions: Definitions of the Rating Scales of S&P Global Ratings', June 9, 2023](#)
- [Rating Scales and Definitions: The Link Between the Global Rating Scale and the Domestic Rating Scale, February 1, 2024](#)

List of ratings

Bank Leumi Le-Israel B.M.	Rating	Publication date of initial rating	Last rating revision date
Issuer rating(s)			
Short-term	ilA-1 +	09/03/2022	02/05/2024
Long-term	ilAAA\Negative	01/05/1998	02/05/2024
Issuance rating(s)			
<u>Hybrid substandard debt</u>			
Subordinated notes with a loss absorption mechanism (Series 402)	ilAA-	31/05/2018	02/05/2024
Subordinated notes with a loss absorption mechanism (Series 403)	ilAA-	17/01/2019	02/05/2024
Subordinated notes with a loss absorption mechanism (Series 405)	ilAA-	09/03/2022	02/05/2024
Subordinated notes with a loss absorption mechanism (Series 404)	ilAA-	26/06/2019	02/05/2024
<u>Short-term debt</u>			
Series 5	ilA-1 +	14/12/2023	02/05/2024
<u>Unsecured senior debt</u>			
Bonds (Series 179)	ilAAA	31/05/2018	02/05/2024
Bonds (Series 182, 183)	ilAAA	09/11/2021	02/05/2024
Bonds (Series 184)	ilAAA	09/03/2022	02/05/2024
Bonds (Series 180)	ilAAA	17/01/2019	02/05/2024
Bonds (Series 185, 186)	ilAAA	29/11/2023	02/05/2024
Issuer rating history			
<u>Long-term</u>			
May 2, 2024	ilAAA\Negative		
October 7, 2014	ilAAA\Stable		
May 5, 2010	ilAA+\Stable		
April 30, 2009	ilAA+\Negative		
June 21, 2007	ilAAA\Stable		

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May 14, 2006	ilAAA
February 20, 2003	ilAA+
May 1, 1998	ilAAA
<u>Short-term</u>	
March 9, 2022	ilA-1 +

Additional Details

Time on which the event took place	06/08/2024 09:36
Date and time when the event first became known	06/08/2024 09:36
Rating initiated by	The rated company

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