

BANK LEUMI LE-ISRAEL B.M

October 9, 2024

Rating reiteration

Reiteration of 'ilAAA' rating, outlook remained negative

Primary credit analyst:

Pierre Hollegien, Paris, 33-14-0752513 pierre.hollegien@spglobal.com

Secondary contact:

Matan Benjamin, Ramat Gan +972-3-7539716; matan.benjamin@spglobal.com

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Rating reiteration

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Overview

- On October 1, 2024, S&P Global Ratings downgraded the State of Israel's long-term credit rating to 'A' from 'A+' due to the expectation that the key economic metrics will continue deteriorating against the backdrop of the continuation of the war and its expansion to other fronts.
- The increase in government deficit might have an indirect adverse effect on the banking sector, due to, among other things, the government's reduced ability to continue supporting the economic activity in Israel.
- Despite the uncertainty, Bank Leumi Le Israel B.M. (hereinafter - "Bank Leumi" or the "Bank") has displayed so far high resilience and its operating performance remained robust.
- We reiterate Bank Leumi Le Israel B.M.'s issuer credit rating at 'ilAAA' and its issuance ratings.
- The negative rating outlook reflects the risk of further downgrading of Israel's sovereign rating and the adverse impact on the Bank's credit profile over the next 12-18 months.

The rating action

On October 9, 2024, S&P Maalot reiterated Bank Leumi Le Israel B.M.'s issuer credit rating at 'ilAAA' and its issuance ratings. The outlook remained negative.

Key considerations

S&P Global Ratings downgraded the State of Israel's sovereign credit due to the expectation that the key economic metrics will continue deteriorating against the backdrop of the continuation of the war and its expansion to other fronts. On October 1, 2024, S&P Global Ratings downgraded the State of Israel's long-term credit rating to 'A' from 'A+' and assigned a negative rating outlook (see [Israel Long-Term Ratings Lowered To 'A' From 'A+' On Heightened Security Risk, Outlook Negative](#), October 1, 2024). Under the base scenario, we now expect that the war will continue into 2025, and that GDP growth in Israel will be lower than 1% in 2024 and approx. 2.2% in 2025. We also expect that the government deficit will be approx. 9% in 2024 and approx. 6% in 2025, mainly due to the increase in the defense budget. We expect the deposit to be approx. 5% in 2026 and 2027 too. The Bank's 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, and therefore, further changes in the sovereign rating of the State of Israel may impact the Bank's rating.

The increase in government deficit may have an indirect adverse effect on the banking sector, due to, among other things, the government's reduced ability to continue supporting the economic activity in Israel. In the past year the government took many steps to support the economic activity during the war; these steps included, among other things, supporting residents in areas that suffered directly from the war, thereby moderating the adverse effect on the banking sector. Given the continuation of the war and the increase in the government deficit, the government's ability to continue supporting the economic activity may diminish; it is also possible that the need to increase government revenues will result in the imposition of additional taxes on the banking sector.

The Bank displays robust operating performance, but uncertainty remains high. In 2023 and in the first half of 2024 the Bank presented positive results. In the first half of 2024, the Bank's net interest income increased by approx. 6% compared to the first half of 2023. On June 30, 2024, the rate of the Bank's non-performing assets stood at approx. 0.56% of the credit portfolio to the public, compared to 0.85% at the end of 2023. Return on equity stood at approx. 18% on June 30, 2024. The results were supported by the high interest environment and by increased operational efficiency. After accelerated growth of approx. 9% in the Bank's credit portfolio to the public in 2023, the growth rate slowed down to approx. 3.4% in the first half of 2024. In addition, the Bank's expense in respect of loan losses amounted to approx. 0.09% out of the total credit in the first half of 2024 compared to approx. 0.58% in the corresponding period in 2023.

Under our base scenario, we expect loan losses of 30-40 basis points in 2025-2026. We also take into account the new windfall tax for the sector that will be extended at least until the end of 2025, and a 40% dividend distribution in 2024-2026. We believe that the tourism and services sectors, as well as SMEs are more exposed to the current situation and to the deterioration in macroeconomic metrics. We will also continue to monitor the exposure to the real estate sector, which is the Bank's most prominent area of activity. The Bank's CET 1 ratio stood at 12.04% as of June 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.

The rating outlook

The negative rating outlook reflects the negative outlook of the sovereign rating of the State of Israel and the risk of adverse impact on the Bank's credit profile over the next 12-24 months.

Downside scenario

We will consider a rating downgrade if the State of Israel's rating will be downgraded again, since we would then consider it less likely that the government would provide extraordinary support in case of financial distress. We will also consider a rating downgrade if security risks will be heightened, with negative consequences for the banking sector and Bank Leumi's asset quality, capital ratios, or earnings.

Upside scenario

We will consider revising the Bank's rating outlook to stable if the State of Israel's outlook is revised to stable, and we will believe that security risks and their effect on the Bank's financial ratios had lessened.

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](#)
- [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's rating(s)			
Short-term	ilA-1 +	09/03/2022	06/08/2024
Long-term	ilAAA\Negative	01/05/1998	06/08/2024
Issuance rating(s)			
<u>Hybrid substandard debt</u>			
Subordinated notes with a contractual loss absorption mechanism (Series 402)	ilAA-	31/05/2018	06/08/2024
Subordinated notes with a contractual loss absorption mechanism (Series 403)	ilAA-	17/01/2019	06/08/2024
Subordinated notes with a contractual loss absorption mechanism (Series 405)	ilAA-	09/03/2022	06/08/2024
<u>Short-term debt</u>			
Series 5	ilA-1 +	14/12/2023	06/08/2024
Series 6	ilA-1 +	04/09/2024	04/09/2024
Unsecured senior debt			
Bonds (Series 179)	ilAAA	31/05/2018	06/08/2024
Bonds (Series 182.183)	ilAAA	09/11/2021	06/08/2024
Bonds (Series 184)	ilAAA	09/03/2022	06/08/2024
Bonds (Series 180)	ilAAA	17/01/2019	06/08/2024
Series 185.186	ilAAA	29/11/2023	06/08/2024
Issuer rating history			
<u>Long-term</u>			
May 02, 2024	ilAAA\Negative		
October 7, 2014	ilAAA\Stable		
May 05, 2010	ilAA+\Stable		
April 30, 2009	ilAA+\Negative		
June 21, 2007	ilAAA\Stable		
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	09/10/2024 14:55
Date and time when the event first became known	09/10/2024 14:55
Rating initiated by	The rated company

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