

# **BANK LEUMI LE-ISRAEL B.M. AND CONSOLIDATED COMPANIES**

## **Condensed Financial Statements as at 30 September 2009** (unaudited)

**Bank Leumi le-Israel B.M.**

**Head Office: Leumi House, 34 Yehuda Halevi Street, Tel Aviv 65546, Israel**

**Tel: (972) 3-5148111, Fax: (972) 3-5149732**

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**29 November 2009**

# Bank Leumi le-Israel B.M. and its Consolidated Companies

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### Index

|   | Page |
|---|------|
| <b>1. Directors' Report</b>   |      |
| <b>A. General Developments in the Group's Business</b>  |      |
| Description of the Leumi Group's Business Activities and their General Development  | 2    |
| Control of the Bank   | 3    |
| Capital Resources and Transactions in the Shares of the Bank  | 5    |
| Distribution of Dividends   | 6    |
| Principal Data of the Leumi Group   | 7    |
| <b>B. Other Information</b>   |      |
| Principal Developments in the Economy   | 8    |
| General Environment and Effect of External Factors on Activities  | 14   |
| Accounting Policy on Critical Subjects  | 19   |
| Procedure for the Approval of the Financial Statements  | 19   |
| <b>C. Description of the Group's Business according to Segments and Spheres of Activity</b>   |      |
| Development of Income, Expenses and Tax Provision   | 20   |
| Structure and Development of Assets and Liabilities   | 31   |
| Operational Segments in the Group   | 53   |
| Activities of Major Subsidiaries  | 82   |
| Non-Banking Activities of Companies included on the Equity Basis  | 85   |
| Exposure to Risk and Methods of Risk Management   | 85   |
| Linkage Status and Liquidity Status   | 104  |
| Preparations for Basel II   | 107  |
| Legal Proceedings   | 110  |
| <b>D. Additional Matters</b>  |      |
| Leumi for the Community   | 111  |
| Internal Auditor  | 112  |
| Controls and Procedures Regarding Disclosure in the Financial Statements  | 112  |
| <b>2. Management Review</b>   |      |
| Rates of Income and Expenses  | 115  |
| Credit to the Public – Risk by Economic Sector  | 124  |
| Exposure to Interest Rate Fluctuations  | 127  |
| Country Exposure  | 129  |
| <b>3. Certification of the President and Chief Executive Officer</b>  | 132  |
| <b>Certification of the Senior Deputy Chief Executive Officer, Chief Financial Officer, Head of Finance, Accounting and Capital Markets</b> | 133  |
| <b>4. Condensed Financial Statements</b>  |      |
| Joint Auditors' Review  | 134  |
| Condensed Balance Sheet – Consolidated  | 135  |
| Condensed Profit and Loss Statement – Consolidated  | 136  |
| Condensed Statement of Changes in Shareholders' Equity - Consolidated   | 137  |
| Condensed Statement of Cash Flows – Consolidated  | 142  |
| Notes to the Condensed Financial Statements – Consolidated  | 145  |

## A. General Developments in the Group's Business

The Directors' Report has been prepared in accordance with the public reporting directives of the Supervisor of Banks. The principles applied in preparing the interim reports are consistent with the principles used in preparing the Annual Report as at 31 December 2008. The interim reports should be read in conjunction with the Annual Report for 2008.

### Description of the Leumi Group's Business Activities and their General Development

Total assets under the management of the Group (balance sheet items and off-balance sheet items\*) amounted to some NIS 761 billion at the end of September 2009, as compared with NIS 651 billion at the end of 2008, an increase of some 16.9%, resulting primarily from the rise in the capital market and from the increase in activity.

\* Total balance sheet items as well as customers' securities portfolios, and the value of securities of mutual funds, provident funds, pension funds and supplementary training funds held in custody, in relation to which operation management and custody services are provided.

Net profit in the first nine months of 2009 totaled NIS 1,470 million, compared with NIS 1,275 million in the corresponding period in 2008, an increase of 15.3%.

Net operating profit in the first nine months of 2009 totaled NIS 1,442 million, compared with NIS 1,026 million in the corresponding period in 2008, an increase of 40.5%.

The increase in net operating profit is explained mainly as the result of an increase in operating and other income, a decrease in operating and other expenses and a low effective tax rate. On the hand, a decrease in net interest income, an increase in the provisions for doubtful debts and a reduction in the contribution to profit of companies included on the equity basis partially offset the above-mentioned increases.

Net profit per share during the first nine months of 2009 was NIS1.00, compared with NIS 0.87 in the corresponding period in 2008 and NIS 0.06 in all of 2008.

Based on data of the banking system as at 30 June 2009, as published by the Bank of Israel, the Leumi Group's share of the total banking system was as follows:

|                             | 30.6.2009 | 31.12.2008         | 31.12.2007 | 31.12.2006          | 31.12.2005 |
|-----------------------------|-----------|--------------------|------------|---------------------|------------|
| In %                        |           |                    |            |                     |            |
| Total assets                | 29.7      | 29.3               | 30.0       | 30.4                | 30.0       |
| Credit to the public        | 28.7      | 29.1               | 29.9       | 30.2                | 29.9       |
| Deposits of the public      | 30.3      | 29.8               | 30.2       | 30.5                | 30.6       |
| Operating profit before tax | 38.9      | 1.5 <sup>(1)</sup> | 38.0       | 27.5 <sup>(2)</sup> | 30.2       |
| Net operating profit        | 40.6      | - <sup>(3)</sup>   | 38.5       | 25.6 <sup>(2)</sup> | 30.5       |

<sup>(1)</sup> After neutralizing Bank Hapoalim's losses.

<sup>(2)</sup> The decrease in the Group's share arises mainly from the volume of extraordinary salary expenses, of which some half arose from the privatization.

<sup>(3)</sup> There was an after tax operating loss.

## **Control of the Bank**

The State of Israel became a shareholder of the Bank on 31 October 1993, under the Bank Shares Arrangement and the Bank Shares (Arrangement Shares) (Temporary Provision) Law, 1993 (the "Bank Shares Law"). As determined in the Bank Shares Law, the transfer of the shares in the Bank to the State and the exercise of the rights by virtue of the shares under this Law do not require a permit under the Banking (Licensing) Law, 1981.

On 30 September 2009 and on 15 November 2009, the State of Israel held 11.46% of the issued share capital of the Bank and 14.20% of the voting rights in the Bank.

On 14 June 2006, the Bank Leumi Group employees (including the Chairman of the Board of Directors) purchased 40,333,691 shares of the Bank's capital from the State. The shares are blocked until 13 June 2010. (The Chairman of the Board of Directors purchased his shares on 5 July 2006, and those shares are blocked until 4 July 2010). During the blocked period, the State has a power of attorney to vote the shares that were purchased and to use the right to appoint directors by virtue of the shares. The blocked shares constitute 2.74% of the voting rights.

The Bank Shares Law authorized the shares committee of the Bank to exercise the voting rights granted by virtue of the State's holding in the Bank in the name of the State and on its behalf.

The Bank Shares Law determines that "the use of the voting rights granted by virtue of the shares will be made by a committee functioning in the name of the State and on its behalf" (Section 3 of the Bank Shares Law).

In August 2009, the Bank received a letter from counsel for Shlomo Eliahu Holdings Ltd. ("Eliahu Holdings") according to which Eliahu Holdings is of the view that given the percentage of the State's present shareholding in the Bank, it is not possible to view the State as having control of the Bank, and under present circumstances the Bank does not in practice have a controlling shareholder as defined by law.

In light of this letter, the Bank asked M.I. Holdings Ltd. and the Bank Supervision Department for their positions on the matter. The Bank Supervision Department advised the Bank that it views the Bank as a banking corporation, in which at least one of the holders of means of control is the holder of a control permit, so long as the Board of Directors is appointed in accordance with the Bank Shares (Arrangement Shares) (Temporary Provision) Law, 1993 and the regulations promulgated thereunder.

It should be noted that to the best of the Bank's knowledge, none of the holders of means of control in the Bank has been granted a control permit.

M.I. Holdings replied to the Bank on behalf of the State of Israel as follows:

- "1. According to your above request and telephone conversations, the subject of the control of the Bank was raised during the preparation of the Bank's shelf prospectus. You have advised us that the Bank intends to state in the shelf prospectus, which it plans to publish in August 2009, that as long as over 50% of the Bank's directors are appointed in accordance with the Bank Shares (Arrangement Shares) (Temporary Provision) Law, 1993 (the "Bank Shares Law") then according to the presumption determined in the Securities Law, the State holds control of the Bank, for the purposes of the requirement of Regulation 44C of the Securities Regulations (Details, Structure and Form of Prospectus and Draft Prospectus), 1969. We have no objection to this interpretation.

2. We request you to ensure that the prospectus includes a description of the manner in which the State holds shares in the Bank, including the rules and restrictions applying to these holdings under the Bank Shares Law, including, *inter alia*, the restrictions on the State's ability to intervene in the management of the Bank's business and its decision-making process.
3. We would emphasize that nothing in the above may prevent the State from raising any claim regarding any matter concerning the State's responsibility under the securities laws or any other laws, and may not detract from or affect such claims."

All the directors serving on the Board of Directors of the Bank were appointed in accordance with the Bank Shares Law, and all the directors were proposed to the general meetings of the Bank by the Bank's shares committee, and the committee voted for them by virtue of the State's shares in the Bank. As mentioned above, under the Bank Shares Law, the committee votes at general meetings in the name of the State and on its behalf.

The Bank's current shares committee was appointed by virtue of the Bank Shares (Arrangement Shares) (Temporary Provision) Law (Appointment of Committees and Terms of Office) Directives, 2009, which were published on 12 March 2009. The committee's appointment is valid through 31 October 2011 but will end earlier if and when one of the following events takes place: (1) no other party holds a control permit pursuant to section 34(b) of the Banking (Licensing) Law, 1981 and the State's holding of shares in the Bank has fallen below a percentage which does not exceed 5%, or (2) there is another party who holds a control permit pursuant to section 34(b) of the Banking (Licensing) Law, 1981 and the percentage of the shares in the Bank held by the State has fallen below a percentage which does not exceed 10%.

### **In conclusion**

The directors holding office in the Bank at present were all proposed by the shares committee and all were elected with its support by the Bank's general meeting. The shares committee acts as mentioned above in the name of the State of Israel and votes on behalf of the State at the general meetings.

From this it may be learned that as long as over 50% of the directors of the Bank are appointed in accordance with the Bank Shares Law, then the State of Israel holds over 50% of one of the means of control of the Bank and in accordance with the presumption regarding the definition of control in the Securities Law, it holds control of the Bank, subject to the restrictions determined in the Bank Shares Law. It should be noted that there exists another interpretation, as detailed above.

### **Sale of Shares in the Bank by the State**

On 25 November 2009, M.I. Holdings notified the Bank it is preparing to sell the balance of the State's holdings in the Bank, but that it has no defined plan at this stage.

For details regarding the issue of options to employees see the Chapter on Capital Resources and Transactions in Shares of the Bank.

### **Interested Parties' Transactions**

Excellence Investments Ltd., The Phoenix Holdings Ltd., and the Delek Group Ltd. notified the Bank on 6 August 2009 they had become interested parties in the Bank due to the aggregate holdings of companies in the Excellence Group, the Phoenix Group and the Delek Group. The Bank was also notified that all the above-mentioned companies are indirectly controlled by Mr. Yitzhak Sharon (Tshuva), through companies that he controls.

Clal Insurance Enterprises Holdings Ltd., Clal Finance Ltd. and Epsilon Investment House Ltd. (the "Companies"), all three of which are members of the IDB Holding Corporation Ltd. Group, notified the Bank on 26 August 2009 that they had become interested parties in the Bank, by virtue of the aggregate holdings of the companies and/or their subsidiary and/or associated companies. On 31 August 2009, the companies informed the Bank that they had ceased to be interested parties in the Bank as of 30 August 2009.

## **Capital Resources and Transactions in the Shares of the Bank**

**Shareholders' Equity** of the Group as at 30 September 2009 amounted to NIS 21,067 million, compared with NIS 18,672 million at the end of 2008, an increase of 12.8 %. The increase in shareholders' equity derives mainly from the increase in the value of the available-for-sale securities portfolio and from the profit of the first nine months of 2009.

The securities portfolio (nostro) is mainly composed of debentures issued by governments, banks and foreign financial institutions, which generally represent the use of raised sources and the available capital. Most of the securities portfolio is classified as available-for-sale securities and is included in the balance sheet on the basis of fair value. The income is recorded in the profit and loss statement on an accrual basis, and the difference between the value on an accrual basis with regard to debentures and on a cost basis with regard to shares and the fair value is recorded directly in a separate item in shareholders' equity, after the deduction of the effect of related taxes.

A net increase in value of NIS 876 million was recorded in this item in shareholders' equity during the first nine months of 2009, compared with a net decrease in value of NIS 1,328 million in the corresponding period in 2008 (all these amounts are stated net of related taxes). Although a decline in value was recorded during the first quarter of the year, an increase in value was recorded during the second and third quarters which was larger than the the first quarter's decline in value.

The total net accrued balance of adjustments to fair value of securities held in the available-for-sale portfolio as at 30 September 2009 amounted to a positive sum of NIS 228 million (after the effect of taxes).

According to the current principles of capital adequacy computation, the balance in respect of adjusting securities to fair value does not affect the capital computation for the purpose of the minimum capital ratio, save for losses that have not yet been realized from adjustments to fair value of available-for-sale shares, after the deduction of the effect of taxes.

**Shareholders' Equity relative to Total Assets** reached 6.5% on 30 September 2009, compared with 6.0% on 31 December 2008.

**Total Capital relative to Risk Assets** reached 14.14% on 30 September 2009, compared with 11.58% on 31 December 2008. This ratio is higher than the minimum ratio of 9% set by the Supervisor of Banks. The figure as at December 2008 was reclassified in the first quarter, following a change in the allocation of Tier I and Tier II capital against exposure to market risks, following a clarification from the Bank of Israel. The ratio of Tier I capital to risk assets reached 8.39% on 30 September 2009, compared with 7.51% at the end of 2008. Regarding the report to the Bank of Israel regarding capital adequacy as at 31 December 2008 and onward according to the Basel II provisions, see page 107.

## **Issue of Subordinated Capital Notes**

During April – May 2009, the Bank raised NIS 1.0 billion through private placings of subordinated capital notes with institutional investors, which have been recognized by the Bank of Israel to as upper Tier II capital.

In May 2009, Leumi Finance Company issued subordinated capital notes (Series J) in the amount of some NIS 1.5 billion.

In August 2009, in accordance with a permit received from the Israel Securities Authority, Leumi Finance published a shelf prospectus allowing it to issue debentures, subordinated capital notes (Tier II capital) and other subordinated capital notes (upper Tier II capital). Unlisted subordinated capital notes were also issued, pursuant to the prospectus, to the shareholders of Dan Public Transportation Company Ltd., in the amount of some NIS 341 million, and listed subordinated capital notes in the amount of some NIS 2 billion were issued to the public and to institutional investors, pursuant to a shelf offering report which was published pursuant to the prospectus. The subordinated capital notes were approved by the Bank of Israel as upper Tier II capital.

On 27 August 2009, in accordance with a permit received from the Israel Securities Authority, the Bank published a shelf prospectus allowing it to issue up to 6 series of debentures (series 400 to 405), up to 11 series of subordinated capital notes (series 250 to 256 and series 300 to 303) and up to 6 series of subordinated capital notes (series 200 to 205). The maximum amount of debentures and capital notes which the Bank may issue under this shelf prospectus is NIS 4 billion par value of each of the above series. The prospectus will remain valid for two years from the date of its publication.

## **Issue of Options to Employees**

In February 2009, the exercise period of the options issued to Leumi employees in 2006 ended. The 24,062,240 options that had not been exercised by February 2009 expired.

The balance of the loans provided by Israel Discount Bank to Leumi employees in order to finance their exercise of the options was NIS 68 million as of 30 September 2009 (out of a total amount of NIS 277 million in loans that were provided in February 2008).

## **Distribution of Dividends**

### **Dividend Policy for 2009**

In light of the uncertainty prevailing in the Israeli economy regarding the scope and extent of the impact of the global financial crisis on the Israeli banking system, including on the Bank, the Board of Directors resolved on 30 March 2009 not to set a dividend policy for 2009 at that stage.

The Supervisor of Banks has announced that he expects that the banking system will not distribute dividends in light of the risks, with the purpose of building strong levels of capital in anticipation of the implementation of Basel II. Any bank wishing to distribute dividends will be required to apply to the Supervisor of Banks, give explanations and receive approval for such distribution.

**Bank Leumi le-Israel B.M. and its Subsidiaries and Affiliates**  
**Principal Data of the Leumi Group**

|   | Jan. – Sep. | Jan. – Sep. | Year      |
|---|-------------|-------------|-----------|
|   | 2009        | 2008        | 2008      |
| <b>Income, Expenses and Profits (NIS millions):</b>   |             |             |           |
| Net interest income before provision for doubtful debts   | 5,211       | 5,404       | 6,380     |
| Provision for doubtful debts  | 1,136       | 1,055       | 2,145     |
| Total operating and other income  | 3,308       | 2,255       | 2,800     |
| Total operating and other expenses  | 4,962       | 5,202       | 7,003     |
| Of which: Costs of Voluntary Retirement   | -           | -           | 3         |
| Costs of privatization, (issue of shares and options to employees)                                  | 8           | (52)        | (66)      |
| Operating profits before taxes  | 2,421       | 1,402       | 32        |
| Net operating profit (loss)   | 1,442       | 1,026       | (158)     |
| After-tax net profit from extraordinary items   | 28          | 249         | 250       |
| Net profit for the period   | 1,470       | 1,275       | 92        |
| Not operating profit (loss) per share ( in NIS)   | 0.98        | 0.7         | (0.11)    |
| Net profit per share (in NIS)   | 1.00        | 0.87        | 0.06      |
| <b>Assets and Liabilities at End of Period (NIS millions):</b>                                      |             |             |           |
| Total assets  | 323,630     | 293,811     | 310,792   |
| Credit to the public  | 203,971     | 207,489     | 213,215   |
| Securities  | 58,381      | 41,566      | 44,910    |
| Deposits of the public  | 249,433     | 225,952     | 244,783   |
| Debentures and notes  | 25,471      | 22,257      | 20,636    |
| Shareholders' equity  | 21,067      | 19,562      | 18,672    |
| <b>Major Financial Ratios in Annual Terms (%):</b>  |             |             |           |
| Credit to the public / Total assets   | 63.0        | 70.6        | 68.6      |
| Securities / Total assets   | 18.0        | 14.1        | 14.5      |
| Deposits of the public / Total assets   | 77.1        | 76.9        | 78.8      |
| Deposits of the public / Total credit   | 122.3       | 108.9       | 114.8     |
| Shareholders' equity / Risk assets (a)  | 14.14       | (e) 12.20   | (e) 11.58 |
| Tier I capital / Risk assets  | 8.39        | 7.92        | 7.51      |
| Shareholders' equity (excluding minority interest) / Total assets                                   | 6.5         | 6.7         | 6.0       |
| Net profit / Shareholders' equity average (excluding minority interest) (c)                         | 10.3        | 8.5         | 0.5       |
| Net operating profit (loss)/ Shareholders' equity average (excluding minority interest) (c)         | 10.1        | 6.8         | (0.8)     |
| Rate of tax provision from the profit   | 39.2        | 60.2        | -         |
| Provision for doubtful debts / Credit to the public (c)   | 0.74        | 0.68        | 1.01      |
| Provision for doubtful debts / Total credit risk (c)  | 0.49        | 0.45        | 0.67      |
| Net interest income before provision for doubtful debts / Total assets (c)                          | 2.15        | 2.46        | 2.05      |
| Total income / Total assets (b) (c)   | 3.53        | 3.49        | 2.95      |
| Total income / Total assets managed by the group (b) (c) (d)  | 1.48        | 1.48        | 1.41      |
| Total operating and other expenses / Total assets (c)   | 2.05        | 2.37        | 2.25      |
| Total expenses / Total assets managed by the group (c) (d)  | 0.86        | 1.00        | 1.08      |
| Net profit / Total average assets (c)   | 0.60        | 0.57        | 0.03      |
| Net operating profit (loss) / Total average assets (c)  | 0.59        | 0.46        | (0.05)    |
| Financial margin including incomes and expenses from derivative financial instruments               | 1.08        | 1.85        | 1.63      |
| Operating expenses / Total income (b)   | 58.2        | 67.9        | 76.3      |
| Operating and other income / Operating and other expenses (excluding costs of voluntary retirement) | 66.7        | 43.3        | 40.0      |
| Operating and other income / Total income (b)   | 38.8        | 29.4        | 30.5      |

- (a) Shareholders' equity - plus minority interest and less investments in the capital of companies included on the equity basis and various adjustments.  
(b) Total income - net interest income before provision for doubtful debts plus operating and other income.  
(c) On an annual basis.  
(d) Includes off-balance sheet activities.  
(e) Reclassified.



## **B. Other Information**

### **Principal Developments in the Economy\***

#### **General**

During the third quarter of 2009, economic activity accelerated in Israel and the GDP expanded at an annual rate of 2.2%, in comparison with the first quarter of the year. This was after an increase in GDP at an annual rate of some 1.0% during the second quarter of 2009. This reflects the economy's emergence from the recession experienced during the second half of 2008. The contraction of economic activity during the past year led to a sharp decline in the State's revenues from taxes, alongside a significant increase in the budgetary deficit. During the year's third quarter, this trend changed, and an increase in tax revenues was recorded in comparison with earlier quarters.

The shekel appreciated against the dollar during the first nine months of 2009 by some 1.2%, appreciating some 4.1% during the third quarter of the year. This was against the background of the weakening of the dollar globally, and the impact of local macroeconomic factors, and with the cessation of fixed purchases by the Bank of Israel in the foreign currency market furthering this trend. The shekel's exchange rate in relation to the nominal basket of currencies declined by some 2.7% during the months of January-September.

The CPI rose by 3.4% during the first nine months of the year (of which 1.3% was an increase during the third quarter, and by a total of some 2.8% in the twelve months ending September 2009 – a rate which is within the (upper) limit of the government's price stability target (of 1% to 3%). At the beginning of 2009, the Bank of Israel continued reducing the interest rate, while also using other monetary tools, with the intention of implementing an extremely expansionary monetary policy which would support economic activity. Thus, the interest rate that had reached 2.5% in December of 2008 was reduced to 0.50% and left at that level until August 2009. In the interest rate decision for September 2009, the interest rate was raised by 25 basis points to 0.75%, and it was raised by 25 basis points to 1.0% in the interest rate decision for December 2009.

On the stock market, sharp increases of 57.1% were recorded during the first nine months of 2009 in the shares and convertible securities index, with increases being recorded in each of the year's three quarters. This reflects an expression of the optimism of investors in Israel and throughout the world regarding an imminent end to the recession – optimism which is supported by positive data and an expansionary monetary policy. Prices for both government and corporate debentures rose as well.

#### **The Global Crisis**

During the second and third quarter of the year, the global economy showed signs of improvement in economic activity, although the Bank of Israel and international institutions estimate that the recovery is expected to be slow and ongoing. The International Monetary Fund (IMF) estimated that the global economy is emerging from the recession. Against this background, in October 2009 the IMF adjusted its global growth forecast for the year 2009 upward, as compared with the previous forecasts published during the course of the year. It now estimates that growth in the United States and in the euro zone will be negative in 2009, at a rate of -2.7% and -4.2%, respectively, as compared with positive growth rates of 0.4%

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\* Data sources: publications of the Central Bureau of Statistics, the Bank of Israel, the Ministry of Finance and the Tel Aviv Stock Exchange

and 0.7%, respectively, in 2008. The IMF's forecasts for 2010 were adjusted upward at a more significant rate.

## **Business Product and Economic Sectors**

Business sector product expanded during the third quarter of the year at a real annual rate of some 1.6%, relative to the second quarter of the year. This is in comparison with an annual growth rate of some 1.1% during the second quarter of 2009. This acceleration of the growth rate reflects a positive change in the economic activity trend within the business sector.

The Bank of Israel's survey of Israeli companies for the third quarter of 2009 also indicated the continued recovery of economic activity in the business sector. The net balance (the difference between the number of companies and businesses reporting increases in activity, and those reporting decreases in activity) indicates a slight increase, primarily influenced by the moderate increase in local activity. This trend is also evident in an examination of the commercial and construction sectors and in the various industrial sectors. Regarding the last quarter of the year, the industrial sector (except for export industries), commercial, business service and construction companies are expecting increases in economic activity.

## **The State Budget and its Financing**

The state budget deficit (excluding net credit granted) amounted to some NIS 21.9 billion during the first nine months of the year, compared with a planned budget deficit of NIS 44.4 billion (6% of GDP) for all of 2009. The quarterly development of the State's revenues from taxes indicates an increase in revenues during the year's third quarter, as compared to previous quarters. This increase during the third quarter resulted partly from an exceptional increase in revenues during the month of July and partly from the recovery in economic activity.

There was also a significant increase in revenues during the months of January to September, beyond that which was forecasted in the budget, in the amount of some NIS 2.5 billion. Against this background, and given that growth this year is expected to be more rapid than had been forecasted (the Ministry of Finance having based its forecast for the State's revenues on negative growth of some 1% while the Central Bureau of Statistics is currently predicting a rate of 0% growth), and taking into consideration the implementation rate for expenditures until the current time, the Bank of Israel estimates that the deficit in 2009 is expected to amount to less than 6% of the GDP, which is the government target deficit rate.

In July 2009, the Knesset approved the State budget for 2009-2010, which was based on the expansion of the biannual State budget for those years by 3.05% annually (1.7% pursuant to the Budget Law and an additional and temporary amount of 1.35% for each of the years), and established a maximum budget deficit target of 6% of GDP for 2009 and of 5.5% of GDP for 2010.

## **Foreign Trade and Capital Flows**

During the first nine months of the year, Israel's trade deficit – the gap between imports and exports – contracted by some US\$ 5.8 billion as compared with the corresponding period in 2008. When the impact of fluctuating components (shipping, airplanes, diamonds and energy resources) are neutralized, there was a surplus of exports over imports during this period, which was measured in each one of the year's three quarters. Imports of goods into Israel – excluding shipping, airplanes, fuel and diamonds accelerated significantly during the third quarter. Moreover, the expansion of imports, at the rate of some 11.8% compared with the second quarter of the year, on the basis of net-of-seasonality data, was reflected in all of the key areas (imports of raw materials, investment goods and consumer goods). The increase in imports of raw materials was particularly remarkable, which reflects increasing needs of the

industrial sectors for the purpose of increasing their production. Exports of goods, excluding shipping, airplanes and diamonds, expanded during the third quarter of this year, according to net-of-seasonality data, at the rate of some 6.6% in comparison with the second quarter. This follows stability in the rate of such exports during the second quarter of the year. Although a significant part of the increase in exports during the quarter arose in the electronic components sector (Intel's new factory may have had a substantial impact), other industrial exports also contributed to the increase.

Capital flows into and from Israel from the beginning of the year through the month of September indicate a significant trend towards an increase in financial investments by Israeli residents abroad (primarily by institutional investors), both in shares and in debentures, which increases diversification in investment portfolios and thus perhaps allows for making the most of opportunities created during the period of the financial crisis. In total, these are investments of some US\$ 5.8 billion dollars (some US\$ 7.3 billion, in annual terms), which constitute the most significant component among the capital flows. An additional significant component is presented by the direct capital flows of foreign investors into Israel, which continue to expand but at a slightly slower rate than in the past (some US\$ 4.1 billion dollars, in annual terms). The combination of the outgoing and incoming flows indicates outgoing foreign currency capital flows were higher than the incoming flows. At the same time, the recent strengthening of the shekel has been affected by additional factors which appear to carry significant weight, such as the global weakening of the dollar, and the improvement of the current balance of payments. The cessation of the Bank of Israel's continual intervention in foreign currency trading also served to strengthen the shekel.

### **Exchange Rate and Foreign Currency Reserves**

An appreciation of some 1.2% in the exchange rate of shekel against the dollar was recorded in the first nine months of 2009, with an appreciation of some 4.1% during the third quarter. The shekel depreciated against the euro at a rate of some 4.0% during the months of January-September. The shekel's exchange rate against the currency basket, calculated by the Bank of Israel and composed of 38 currencies of Israel's trading partners, declined by some 2.7% during this period.

The shekel's appreciation against the dollar beginning in the second quarter of the year is a result of the combination of the depreciation of the dollar globally, and the impact of local macroeconomic factors, while the cessation of fixed purchases by the Bank of Israel in the foreign currency market also furthered this trend.

On 25 March 2009, the Bank of Israel announced that in light of the global economic situation and as part of its overall policy, it would continue to purchase US\$ 100 million on a daily average in the Israeli foreign currency market, and during July the Bank announced that it would continue to follow this policy. On 3 August 2009, the central bank announced that "it would operate in the foreign currency market in the event of unusual movements in the exchange rate which do not conform with basic economic conditions or when the foreign currency market is not functioning as usual" and that it was continuing its daily purchases of US\$ 100 million in the foreign currency market. On 11 August 2009, the Bank of Israel discontinued its program of fixed daily purchases of US\$ 100 million.

The Bank of Israel's foreign currency reserves amounted to some US\$ 60.0 billion at the end of September 2009, as compared with some US\$ 42.5 billion at the end of December 2008. During the third quarter of 2009, the reserves grew by some US\$ 9.7 billion.

### **Inflation and Monetary Policy**

The CPI increased by 3.4% during the first nine months of 2009 and during the twelve month period ending on September 2009, rose by 2.8%. This increase is within the price stability target range (1%-3%). The increase in the CPI during January-September 2009 resulted from

an increase in most of the CPI components. Noticeable factors were increases in the housing sector component (a contribution of some one third of the entire increase in the CPI) and an increase in taxes on the various goods and services (VAT, the water shortage charge, etc.) In October, the CPI rose by 0.2%.

At the beginning of 2009, the Bank of Israel continued to lower interest rates, with the intention of supporting economic activity in light of the global economic crisis. As such, the Bank of Israel acted in a similar manner to other central banks throughout the world that lowered interest rates, and used other monetary tools as well with the intention of implementing an extremely expansionary monetary policy. In this way, the Bank of Israel interest rate, which had stood at 2.5% at the end of 2008, was reduced to 0.50% by the April and remained at that level through August 2009. In the interest rate decision for September 2009, the interest rate was raised by 25 basis points to 0.75%, and it was raised by 25 basis points to 1.0% in the interest rate decision for December 2009. Between December 2008 and February 2009, the Bank of Israel announced a series of monetary tool measures available to it. Details in this regard can be found in the Directors Report in the 2008 Annual Report, on pages 30-31.

On 25 March 2009, the Bank of Israel announced an expansion of its activity in the debentures market, through the purchase of government debentures on an average daily basis of some NIS 200 million. On 5 August 2009, the Bank of Israel discontinued the above-mentioned purchasing activity and announced that it did not intend to sell the securities that it had purchased.

## **The Capital Market**

During the first nine months of 2009, the share and convertible securities index rose by some 57.1%, following a sharp decline of 46.4% in 2008, and the Tel Aviv 100 Index rose by some 64.5% during the months of January-September. These increases, which appeared in each of the year's three quarters, are explained primarily by the reduction in the interest rate to a record low of 0.5%, while the publication of positive economic data during the second quarter of the year also contributed to a positive trend in the stock market. The trading turnovers were also an expression of this trend: the trading turnovers for shares and convertible securities, which had been low during the first quarter of the year (some NIS 1,208 million on a daily average), rose to some NIS 1,781 million on a daily average during the second quarter and amounted to some NIS 1,953 million during the third quarter – similar to the average level for the entire year of 2008 (some NIS 1,964 million). The positive trend in the stock market continued during October and the shares and convertible securities index rose by some 3.1%.

The debenture market was characterized during the first nine months of 2009 by increases in the prices of both (CPI-linked and non-CPI linked) government and corporate debentures. The prices of CPI-linked government debentures rose by some 10.1%, with especially noticeable increases in the prices of medium term debentures (5-7 years), which rose by some 12.0%. Prices of unlinked government debentures rose at a moderate rate of 2.5%. The increase in the prices of debentures was influenced by both the Bank of Israel's intervention in trading, and also possibly by the transition to investments in debentures with longer maturities, against the background of the low short-term interest rate.

Prices for CPI-linked non-government debentures (corporate debentures) rose sharply during the months of January-September at a rate of some 35.9%. This followed sharp declines in 2008, and particularly during the final quarter of the year. Prices increased during each one of the year's three quarters. It appears that there has been a combination of excessive concern towards the end of the past year regarding the condition of many companies in the economy, together with under-pricing, which was expressed in the debentures' yields. (In this context, it should be noted that in its inflation report for the second quarter of the year, the Bank of Israel noted that the margin between the government debenture yields and those of the

corporate debentures had been too low before the crisis and had not accurately reflected debentures' risk levels.)

## **Financial Assets of the Public**

The portfolio of financial assets held by the public grew by some 16.5% during the first nine months of 2009 and amounted to some NIS 2,202 billion at the end of September 2009, after it had contracted at the rate of 8.2% in 2008. The main reason for the increase in the portfolio's value since the beginning of the year has been the increases in the balances of shares in Israel and overseas, which contributed some 61% to the total increase in the asset portfolio, primarily as a result of the increase in share prices. At the same time, the other portfolio components (non-CPI linked, CPI linked and foreign currency linked) showed nominal increases.

Total financial assets of the public managed by the **Group** (deposits of the public, debentures and capital notes, securities portfolios, including securities of mutual funds, provident funds, pension funds and supplementary training funds held in custody, in relation to which operation management and custody services are provided) amounted at the end of September 2009 to some NIS 713 billion, compared with some NIS 606 billion at the end of December 2008, an increase of 17.6%.

## **Bank Credit**

During the first eight months of 2009, bank credit in the economy (before provisions for doubtful debts, including credit for housing and excluding directed credit) remained unchanged. This was following an increase of some 9.0% during 2008. This was the result of a contraction in credit granted to the business sector, which took place, *inter alia*, against the background of a decline in demand, while credit provided to households increased— primarily with respect to housing credit (an increase of some 8%), in light of the increased demand for mortgages as a result of the low interest rate in the economy. There was a certain increase in bank credit and non-bank during the third quarter of 2009. In particular, non-financial business sector debenture (traded and non-traded) issues increased significantly, which according to Bank of Israel data, amounted to some NIS 9.4 billion. This followed issues of some NIS 10.4 billion during the first half of the year. It should be recalled that in 2009, as in the coming years, significant amounts of debenture redemptions are expected.

At the end of September 2009, credit to the public at the Bank amounted to some NIS 134 billion, a decrease of 7.6 % compared with the end of 2008.

## **Credit Rating of the State of Israel and of Bank Leumi**

The Moody's credit rating agency announced on 12 March 2009 that it was lowering certain ratings for a number of Israeli banks, including Leumi, in light of the concerns regarding the banks' financial stability as a result of the worsening of Israel's economic situation, which could lead to a higher level of provisions for doubtful debts than in the past. The rating change for Leumi included, *inter alia*, a reduction of the rating for local currency deposits to 'A1'.

On 30 April 2009, the S&P Ma'alot rating agency announced that it was reducing the issuer rating of the Leumi Group to 'ilAA+' from 'ilAAA'. The Bank's rating outlook was changed to "negative" from "stable". At the same time, the global long-term rating had been reduced from 'A-' to 'BBB+' and the short-term rating remained unchanged at a level of 'A-2'. The global ratings outlook is "negative". The lowering of the ratings reflects the agency's view regarding the negative impact of the global and local recession on the profitability of the Leumi Group and on the quality of its credit portfolio. The "negative" ratings outlook reflect their expectation that, notwithstanding the Bank's satisfactory financial and business profile, it could be adversely affected from negative developments in the environment in which it

operates, primarily from the weakening of both local and global economic activity and capital markets.

### Foreign and local ratings agencies' credit ratings

|   | Rating agency | Short-term rating | Long-term rating | Long-term ratings outlook | Date of adjustment |
|---|---------------|-------------------|------------------|---------------------------|--------------------|
| State's rating in foreign currency  | Moody's       | P-1               | A1               | stable                    | August 2009        |
|   | S&P           | A-1               | A                | stable                    | July 2009          |
|   | Fitch         | F1                | A                | stable                    | November 2009      |
| Leumi's rating in foreign currency  | Moody's       | P-1               | A1               | negative                  | August 2009        |
|   | S&P           | A-2               | BBB+             | negative                  | April 2009         |
|   | Fitch         | F2                | A-               | stable                    | August 2009        |
| Leumi's rating in local currency  | Moody's       | P-1               | A1               | negative                  | August 2009        |
| Leumi's rating in local currency for debentures and standard deposits           | Ma'a lot      | A-1+              | AA+              | negative                  | May 2009           |
|   | Midrug        | P-1               | Aaa              | stable                    | August 2009        |
| Leumi's rating in local currency for subordinated capital notes                 | Ma'alot       | - *               | AA               | negative                  | May 2009           |
|   | Midrug        | - *               | Aa1              | stable                    | August 2009        |
| Leumi's rating in local currency for subordinated capital notes (Upper Tier II) | Ma'alot       | - *               | (A+,A)**         | negative                  | August 2009        |
|   | Midrug        | - *               | Aa2              | stable                    | August 2009        |

\* Not relevant

\*\* A: Upper Tier II capital with compulsory conversion of principal into shares (updated rating in April 2009).

A+: "New" Upper Tier II capital, not convertible into shares (rating given in August 2009).

### Developments regarding Leumi Shares

From the beginning of the year through 30 September 2009, the price of Leumi shares has risen from 790 points to 1,445 points, a change of 82.9%. During this period, the Bank's market value has increased from NIS 11.6 billion to NIS 21.3 billion.

Since the end of September and until 24 November, the share price has continued to rise, reaching 1,565 points, and the Bank's market value has reached NIS 23.1 billion.

**The following table sets out details of changes in the CPI and in exchange rates:**

|   | For the three months<br>ended 30 September |        | For the nine months<br>ended 30<br>September |         | For the<br>year |
|---|--|--------|--|---------|-----------------|
|   | 2009                                       | 2008   | 2009   | 2008    | 2008            |
|   | (in percentages)                           |        |  |         |                 |
| Rate of increase of the "known" CPI                           | <b>2.44</b>                                | 2.10   | <b>3.62</b>                                  | 5.00    | 4.5             |
| Rate of increase (decrease) in the rate of the US dollar      | <b>(4.11)</b>                              | 2.06   | <b>(1.16)</b>                                | (11.05) | (1.1)           |
| Rate of increase (decrease) in the rate of the euro           | <b>(0.45)</b>                              | (5.39) | <b>4.02</b>                                  | (11.65) | (6.4)           |
| Rate of increase (decrease) in the rate of the pound sterling | <b>(7.10)</b>                              | (5.77) | <b>9.00</b>                                  | (18.44) | (28.0)          |
| Rate of increase (decrease) in the rate of the Swiss franc    | <b>0.69</b>                                | (4.35) | <b>2.44</b>                                  | (8.01)  | 4.2             |

**The following table sets out the principal representative exchange rates:**

|                | 30 September |       | 31 December |       |
|----------------|--------------|-------|-------------|-------|
|                | 2009         | 2008  | 2008        | 2007  |
|                | In NIS       |       |             |       |
| US dollar      | <b>3.758</b> | 3.421 | 3.802       | 3.846 |
| Euro           | <b>5.510</b> | 4.999 | 5.297       | 5.659 |
| Pound sterling | <b>6.047</b> | 6.288 | 5.548       | 7.710 |
| Swiss franc    | <b>3.652</b> | 3.146 | 3.565       | 3.420 |

## **General Environment and the Effect of External Factors on Activities**

### **Description of the Banking Corporation's Business and Forward-Looking Information in the Directors' Report**

The Directors' Report includes, in addition to data relating to the past, information that relates to the future, which is defined in the Securities Law, 1968 as "forward-looking information." Forward-looking information relates to a future event or matter, the realization of which is not certain and is not within the exclusive control of the Bank.

**Forward-looking information** is generally drafted using words or phrases such as "the Bank believes", "the Bank foresees", "the Bank expects", "the Bank intends", "the Bank plans", "the Bank estimates", "the Bank's policy", "the Bank's plans", "the Bank's forecast", "strategy", "aims", "likely to affect" and additional phrases testifying to the fact that the matter in question is a forecast of the future and not past facts.

Forward-looking information included in the Directors' Report is based, *inter alia*, on forecasts of the future regarding various matters related to economic developments in Israel and abroad, and especially to the foreign exchange and capital markets, legislation, directives of regulatory bodies, the behavior of competitors, technological developments and personnel issues.

As a result of the inability to foresee with certainty that these forecasts will be realized, and the fact that in reality events may turn out differently from those forecasted, readers of the Report should relate to information defined as "forward-looking" with caution, since reliance on such information involves risks and uncertainty and the future financial and business results of the Leumi Group are likely to be materially different.

The Bank does not undertake to publish updates of the forward-looking information included in this Report. This does not detract from the Bank's reporting obligations pursuant to any relevant law.

## **Property of Holocaust Victims**

In January 2005, the Parliamentary Committee of Inquiry Regarding the Tracing and Restitution of Property of Holocaust Victims published its concluding report. The report indicates that assets of Holocaust victims that had been deposited with the Anglo-Palestine Bank were transferred, pursuant to provisions that were in force at the time, to the British government's Custodian of Enemy Property, to the Israeli Custodian of Enemy Property, to the Administrator General, or were returned to those entitled to them. Nevertheless, the report recommended that the funds be revalued, together with retroactive linkage differentials, for the period in the past during which they were held by the Bank.

On 3 January 2006, the Assets of Holocaust Victims (Restitution to Heirs and Endowment for the purpose of Assistance and Commemoration) Law, 2006 (the "Law") came into effect. The Law provides that a party who holds, in Israel, assets of Holocaust victims (as such terms are defined in the Law) must transfer them to the Tracing and Restitution of Property of Holocaust Victims Company Ltd. (the "Company"), which was established pursuant to the provisions of the Law, together with linkage differentials and interest in amounts determined by a special revaluating committee. The revaluating committee's report was delivered to the Bank, and appropriate provisions were made, as estimated by the Bank.

Out of sensitivity to public sentiment and to demonstrate its goodwill, the Bank transferred the sum of NIS 20 million to the Company, to be used for making payments to the heirs of victims and to survivors during their lifetime, in accordance with the provisions of the Law and pursuant to appropriate criteria to be established by the Company, as required by the Law.

The Bank has notified the Company that if it is determined that the Bank is not obligated to make any payments whatsoever (which is the Bank's position), or that it is required to make a payment which is lower than that which has been paid, any balance of the amount will be considered to be a donation to be used for the above purposes. If it is determined that the Bank is required to pay amounts to Holocaust survivors or to the heirs of Holocaust victims which are higher than the amount that has been paid, then the Bank will set off the payment made (linked to the CPI and bearing interest) against the amount of the liability.

On 4 March and on 18 September 2008, the Bank received two requests from the Company for the payment of amounts which the Company claimed that the Bank was required to transfer to it according to the Law. The total of the two requests, after having been reduced by the Company and revalued to 31 December 2008, is some NIS 186 million. The Bank responded to these two requests while rejecting the claim that it has any financial liability with respect to the majority of the assets included in the requests.

On 11 February 2009, the Bank received a third request from the Company, for the payment of a revalued amount of some NIS 120 million, which the Company claimed that the Bank was required to transfer to it according to the Law. On 7 April 2009, the Bank responded to this request, while rejecting the claim that it has any financial liability with respect to the assets included in the request.



The Bank appointed the Honorable Supreme Court Justice (ret'd) Theodore Orr as an external examiner to carry out an independent and impartial investigation of the Bank's obligations pursuant to the Law, if any, and of the Bank's conduct regarding the assets of Holocaust victims, as such are defined in the Law. In the report that he delivered to the Bank, the examiner reinforced the Bank's position with regard to the main points of disagreement between the Bank and the Company. The examiner referred to the dormant accounts, details of which were published by the Bank in 2000 on its website, in coordination with the Administrator General, as "unclaimed accounts". The examiner stated that the legal burden of proof as to whether these funds belong to Holocaust victims is borne by the Company, and that it will be difficult to prove this. The examiner recommended that the Bank grant the Company a certain amount, as a gesture of goodwill, such to be estimated by the Bank in the future, following the submission of all the Company's requests. The examiner mentioned the amount already transferred by the Bank, as referred to above, and that such amount may constitute all or part of this grant.

On 24 June 2009, the Company filed a claim in the Jerusalem District Court (File No. 8262/09), whereby it requested that the Court make various declarations regarding "assets of Holocaust victims." (See details in Note 6.C.2.D.)

The parties are holding discussions regarding the transfer of the case to arbitration, for the sake of efficiency, and to advance its resolution. At this early stage, it is not possible to estimate whether, in light of what is stated in the claim, it is necessary to make an additional provision beyond that which was already made in respect of the requests or in respect of the contents of the examiner's report.

### **Pension Counseling**

In August 2008, the Bank received a pension counseling license, which included certain restrictions.

Details regarding this subject are provided in the 2008 Annual Report, from page 36.

During the first half of 2009, the deployment of the pension counseling service, which began in pilot branches during the last quarter of 2008, was expanded to reach all the branches throughout the country. The counseling is provided subject to the terms of the license, by licensed pension counselors, most of whom also have investment counseling licenses.

Pursuant to the terms of the license from the Ministry of Finance, as of 1 April 2009, the restrictive terms in the pension counseling license were removed, and the Bank may provide comprehensive pension counseling regarding pension products, including insurance products, to the entire population throughout the country.

The provision of comprehensive pension counseling regarding all pension products to the entire population requires complex operational and business preparations, in which the Bank has invested and continues to invest considerable resources.

As a rule, the absence of computerized interfaces between the Bank and the institutional bodies (clearing houses) complicates the monitoring of the implementation of the recommendations and makes such monitoring difficult. This issue becomes especially significant with regard to counseling provided to salaried employees, and to counseling with respect to insurance products.

Regarding counseling to salaried employees – the absence of the interfaces between the Bank and the institutional bodies, and the absence of interfaces between the Bank and the employers and their salary departments, both regarding information and regarding the clearing of funds for the employees after the provision of counseling, seriously damages the implementation of the counseling process for salaried employees.

Regarding insurance counseling – the absence of computerized interfaces between institutional bodies and the distributors of insurance products, and the fact that the Ministry of Finance has not dealt on its website (“BituachNet”) with standardized values which would allow for the products to be examined and identified, makes it difficult to construct a model to support decisions and therefore prevents the provision of insurance counseling. Similarly, in the absence of standardized values, as stated, and in the absence of interfaces with the institutional bodies, it is not possible to monitor the implementation of the counseling recommendations *vis-à-vis* the institutional bodies.

Leumi is in the process of creating computerized interfaces with the institutional bodies that manage provident funds in order to simplify the process of transferring information, and executing transactions carried out pursuant to pension counseling and pursuant to counseling on supplementary training funds, in the framework of investment counseling. A Ministry of Finance circular dealing with an abridged uniform structure for the transfer of information from the institutional bodies to the licensees was published in August of 2009. This circular, which will come into effect at the beginning of February of 2010, determines which data an institutional body must transfer to a licensee and the rules for such a transfer of information. The Bank is preparing for the implementation of this circular.

In parallel, the Ministry of Finance has begun promoting the establishment of a clearing house in the pension savings field, whose main functions will be the transfer of information between the various parties active in the pension savings market (including pension counselors, pension agents, institutional bodies and employers), and the clearing of pension savings payments. In July 2009, the Ministry of Finance published a memorandum of understanding on cooperation in promoting such a clearinghouse. The model planned for the operation of the clearing house involves the establishment of a company to be owned jointly by the various entities in the market (institutional bodies, distributors and salary departments). A steering committee, led by the Ministry of Finance, has been established to promote the creation of the clearing house. The Bank is represented on this steering committee. Additionally, no regulations have yet been enacted to regulate payment of distribution commissions for counseling regarding insurance products. In September 2008, a draft amendment of the Financial Services (Control) (Provident Funds) (Distribution Commissions) Regulations was submitted to the Knesset Finance Committee for approval. In September 2009, a draft of the regulations was re-submitted to the Knesset Finance Committee. Pursuant to the draft, no distribution commissions will be paid for some of the insurance products in respect of which counseling will be provided, and for those in respect of which distribution commissions may be paid, the maximum rate of commission will be an annual rate of 0.25% of the accumulated amount saved in regard to the insurance product on which counseling has been given.

In April 2009, a number of private members' bills were tabled before the Knesset for the amendment of the Financial Services (Control) (Engagement in Pension Counseling and Pension Marketing) Law, 2005. Pursuant to the proposed laws, the banks will be defined as distributor counselors, and not as objective counselors. It is proposed that the distribution commission which is currently paid by the institutional bodies in respect of the counseling will not be paid under certain circumstances. It is also proposed that the banks be responsible for the products that they distribute, in addition to their existing responsibility for the counseling, and to delay for a period of 60 days the coming into effect of customers' instructions to transfer funds to a different pension product, unless the instructions regarding the change are given through the counselor through whom the product was purchased.

A preliminary analysis of the proposed laws indicates that they do not protect those who receive the counseling and may even have the opposite effect, and if they are enacted the Bank's ability to provide pension counseling will be materially adversely affected.

In July 2009, draft regulations and a draft circular were published concerning the adaptation of savings tracks to the characteristics of the saver (the "Chilean model"). According to these

drafts, the institutional bodies will be required to establish investment tracks for the management of provident fund members' savings which will serve as default options for fund members when they join the provident funds managed by such institutions. This will be in accordance with the model for the classification of fund members – a plan to be established by the institutional bodies based on relevant characteristics determined by them, including the age of the fund member. In the absence of other instructions from fund members, the institutional body will transfer the members who invest via the general investment tracks (as opposed to members who invest via the specialized tracks) to the default tracks established for them. As far as the Bank is aware, the Ministry of Finance will be issuing a new circular on this subject.

In August 2009, regulations to enable the operation of personally managed provident funds were approved. According to the regulations, the model will be implemented at this stage only with regard to funds held in supplementary training funds, and to funds of self-employed fund members that are not accompanied by employer contributions. The regulations prohibit the payment of a distribution commission in respect of a personally managed provident fund. This means that the banks are not entitled to a distribution fee in respect of counseling in connection with such a fund.

### **Changes in Value Added Tax Rates**

On 1 July 2009, the Value Added Tax Order (Tax Rate for Non-profit Organizations and Financial Institutions) 2009 was published in the Israel Government Gazette. The Order raised the rates for salary tax and profit tax that are applicable to financial institutions, as from 1 July 2009 and continuing through 31 December 2010, from 15.5% to 16.5%.

As the Bank is a “financial institution” for the purpose of the Value Added Tax Law, the increase in the profit tax will increase the overall tax rate to which the Bank is subject, such that in 2009 it will be subject to an overall tax rate of 36.21% instead of 35.93% (an increase of 0.28 percentage points) and in 2010, it will be subject to an overall tax rate 35.62% instead of 35.06% (an increase of 0.56 percentage points).

During the first nine months of the year, the total impact of the change in the rate of value added tax on the provision for taxes was not material.

### **Changes in Companies Tax Rates**

In July 2009, the Knesset approved the Improved Economic Efficiency Law (Statutory Amendments for Implementation of the Economic Plan for 2009-2010), 2009, which gradually reduces the companies tax rates from 25% in 2010 to 18% for the year 2016 and thereafter. The tax rate to which the banks will be subject, including the profit tax, will drop from 35.62% in 2010 to 29.0% for the year 2016 and thereafter. The change in the tax rates increased the tax expense for the third quarter of 2009 in the amount of NIS 146 million, taking into account the balance of deferred taxes as at 30 June 2009.

### **The Reform of Bank Commissions**

In July 2008, a material reform regarding commissions came into effect, which is anchored in an amendment to the Banking (Service to Customers) Law, 1981.

Details regarding the reform are provided in the 2008 Annual Report on pages 39-40.

Upon the convening of the 18<sup>th</sup> Knesset in April 2009, a private member's bill, the purpose of which is to impose additional restrictions on the collection of commissions, has been re-introduced.

## **Accounting Policy on Critical Subjects**

The Financial Statements have been prepared in accordance with generally accepted accounting principles and the directives of the Supervisor of Banks and his guidelines relating to the preparation of the annual and quarterly financial statements of a banking corporation, as detailed in Note 1 to the Annual Financial Statements as at 31 December 2008.

The preparation of the Consolidated Financial Statements in accordance with generally accepted accounting principles and the directives of the Supervisor of Banks, requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the amounts of income and expenses.

The actual results relating to these estimates may differ from the estimates and/or the assumptions.

The estimates and assumptions are generally based on economic forecasts, assumptions regarding the various markets and past experience, following due consideration, and which Management believes to be reasonable at the time of signature of the Financial Statements.

The principal critical accounting subjects referred to in the Annual Report as at 31 December 2008 were as follows: provisions for doubtful debts, derivatives, securities, obligations regarding employee rights, obligations in respect of legal claims, buildings and equipment and taxation on income.

During the period January - September 2009, there were no changes in the accounting policy on critical subjects compared with that described in the 2008 Annual Report.

For further details, see pages 48-53 of the Annual Report for 2008.

## **Procedure for the Approval of the Financial Statements**

The Bank's Board of Directors is the entity ultimately responsible for supervision within the Bank and for the approval of the Bank's Financial Statements. All the members of the Board of Directors possess accounting and financial expertise, and possess the qualifications of external directors (as required by the Bank Shares (Arrangement Shares) (Temporary Provisions) Law, 1993).

In September 2008, the Board of Directors established a Financial Statements Review Committee, composed of members of the Board, the function of which is to discuss the Financial Statements and recommend their approval to the Board of Directors.

Before the Financial Statements are submitted to the Financial Statements Review Committee for discussion, the Bank's Financial Statements are discussed by the Disclosure Committee. The Disclosure Committee is a Management committee comprised of all the members of the Bank's Management, as well as the Acting Head of the Commercial Banking Division, the Chief Legal Adviser, the Group Secretary, and the Head of the Risk Management Control Department. The Chief Internal Auditor and additional senior managers of the Bank participate in the discussions of the Committee.

Prior to the discussion of the Financial Statements by the full Board of Directors, the Financial Statements Review Committee discusses them, with the participation of the President and Chief Executive Officer, the Senior Deputy Chief Executive Officer, the Chief Accounting Officer, the Chief Internal Auditor and others.

Following the discussions by the Committee, there is discussion by the full Board of Directors of the final draft of the Financial Statements, with the participation of the President and Chief Executive Officer, the Senior Deputy Chief Executive Officer, the Chief

Accounting Officer, the Chief Internal Auditor, and when the discussion concerns the approval of annual Financial Statements, the members of the Bank's Management.

All the discussions of the Board of Directors, the Financial Statements Review Committee and the Disclosure Committee regarding the Financial Statements are held with the participation of representatives of the Bank's joint auditors, who are available to the participants to answer questions and provide clarifications. The Financial Statements are approved by the Board of Directors following presentation by the joint auditors to the Board of Directors of any material weaknesses that may have arisen during the audit processes that they carried out, and after the Board is presented with the certifications of the President and Chief Executive Officer and of the Senior Deputy Chief Executive Officer, regarding the evaluation of the Bank's disclosure controls and procedures for the Financial Statements.

## **C. Description of the Group's Business According to Segments and Spheres of Activity**

### **Development of Income, Expenses and Tax Provisions**

The Group's **net profit** for the first nine months of 2009 was NIS 1,470 million, compared with NIS 1,275 million in the corresponding period in 2008, an increase of 15.3%.

The net profit of the Leumi Group for the third quarter of 2009 amounted to NIS 534 million, as compared with a loss of NIS 84 million during the corresponding quarter in 2008.

The increase in the Group's net profit for the first nine months of 2009, as compared with the corresponding period in 2008, is explained primarily by the following factors:\*

1. An increase in operating and other income in the amount of NIS 1,053 million, an increase of 46.7%, before the effect of taxes.
2. A decrease in operating and other expenses (including salaries) in the amount of NIS 240 million, a decrease of 4.6%, before the effect of taxes.
3. A decrease in the effective tax rate of 21.0 basis points, being some NIS 508 million, as explained on page 27 in the provision for taxes item.

On the other hand, the following factors partially offset the above-mentioned increase:

1. A decline in the Group's share of the profits of companies included on the equity basis in the amount of NIS 471 million, net.
2. A decrease in net interest income, before provisions for doubtful debts in the amount of NIS 193 million, a decrease of 3.6% before the effect of taxes.
3. An increase in provisions for doubtful debts in the amount of NIS 81 million, before the effect of taxes, an increase of 7.7%.
4. A decline in profit from extraordinary items in the amount of NIS 221 million, net.

\* Before minority interests in consolidated companies.

As explained above, the net profit for the year's third quarter of 2009 amounted to NIS 534 million as compared with a loss of NIS 84 million in the corresponding quarter in 2008, an increase of NIS 618 million. The following are the main factors leading to the increase in profitability.\*

1. An increase in the profit from operating and other income in the amount of NIS 752 million, an increase of 139.3%, before the effect of taxes.
2. An increase in net interest income before the provision for doubtful debts in the amount of NIS 432 million, an increase of 29.0% before the effect of taxes.
3. A decrease in the provisions for doubtful debts in the amount of NIS 52 million, a decrease of 10.5% before the effect of taxes.

On the other hand, the following factors partially offset the above-mentioned increase:

1. A decline in the Group's share of the profits of companies included on the equity basis in the amount of NIS 161 million, net.
2. An increase in operating and other expenses (including salaries) in the amount of NIS 12 million, an increase of 0.7%, before the effect of taxes.
3. An increase in the provision for taxes, as explained on page 27 in the provision for taxes item.

\* Before minority interests in consolidated companies.

**Net interest income before provision for doubtful debts** of the Leumi Group amounted to NIS 5,211million for the first nine months of 2009, compared with NIS 5,404 million in the corresponding period in 2008 – a reduction of NIS 193 million, which constitutes a decrease of 3.6%.

Net interest income before provision for doubtful debts amounted to NIS 1,923 million for the third quarter of 2009, compared with NIS 1,491 million for the corresponding period in 2008, an increase of 29.0%.

The decrease in the Group's net interest income before provision for doubtful debts for the first nine months of 2009 as compared with the corresponding period in 2008 stems mainly from:

|   | For the nine months ending |                         |          |
|---|----------------------------|-------------------------|----------|
|   | 30<br>September<br>2009    | 30<br>September<br>2008 | % Change |
|   | NIS millions               |                         |          |
| Current activities  | <b>4,806</b>               | 4,884                   | (1.6)    |
| Collection and reduction of interest in respect of problem loans  | <b>274</b>                 | 416                     | (34.1)   |
| Exchange rate differentials in respect of financing shares recorded in operating income or the capital fund | <b>(61)</b>                | 228                     | -        |
| Profit (losses) from sale of available-for-sale, net  | <b>295</b>                 | (508)                   | +        |
| Profit (losses) realized or not yet realized from adjustments to market value of debentures for trading     | <b>221</b>                 | (65)                    | +        |
| Financing costs in connection with hedging of overseas investments*   | <b>(7)</b>                 | 36                      | -        |
| Adjustments to fair value of derivatives  | <b>(368)</b>               | 59                      | -        |
| Effect of the known CPI   | <b>51</b>                  | 354                     | (85.6)   |
| Total   | <b>5,211</b>               | 5,404                   | (3.6)    |

\* The cost of hedging the asymmetry in the tax liabilities in respect of the exchange rate differentials relating to overseas investments, as compared with the exchange rate differentials relating to financing sources. The compensation for this cost is recorded in the tax item. See also the impact on the tax.

As indicated in the above table, net interest income from current activities declined by 1.6%, while the decrease in the margin was partly compensated by the increase in the scope of activities.

The following table sets out the development of net interest income according to the principal operational segments:

|  | For the nine months ending |                      |          |
|--|----------------------------|----------------------|----------|
|  | 30 September<br>2009       | 30 September<br>2008 | % Change |
|  | NIS millions               |                      |          |
| Households                             | <b>1,569</b>               | 1,978                | (20.7)   |
| Small businesses                       | <b>628</b>                 | 678                  | (7.4)    |
| Corporate banking                      | <b>1,430</b>               | 1,476                | (3.1)    |
| Commercial banking                     | <b>1,022</b>               | 1,127                | (9.3)    |
| Private banking                        | <b>440</b>                 | 243                  | 81.1     |
| Financial management – capital markets | <b>128</b>                 | (63)                 | +        |
| Other                                  | <b>(6)</b>                 | (35)                 | +        |
| Total                                  | <b>5,211</b>               | 5,404                | (3.6)    |

**Total Interest Margin** (excluding transactions in financial derivatives) in the first nine months of 2009 was 2.19%, compared with 2.84% in the corresponding period in 2008. The interest margin including financial derivative transactions was 1.08% in the first nine months

of 2009, compared with 1.85% during the corresponding period in 2008, and 1.63% for the whole of 2008.

The financial spread during the first nine months of 2009 was impacted negatively by, *inter alia*, the following causes:

- a. The low interest rate at the Bank of Israel as well as the low interest rates throughout the world caused an erosion of the interest margin as a result of current account balances which do not bear interest, the interest received in respect of which has declined substantially.
- b. The low interest rates caused a contraction in the interest margin primarily in the unlinked shekel sector because of fixed time deposits in small amounts, the interest rates of which were not reduced at the same rate as the reduction in the Bank of Israel interest.
- c. Competitive factors within the system also contributed to the decline of the interest margin.
- d. The decrease in the overall interest margin arises also from timing differences in measuring profitability from activities in financial derivatives, from exchange rate differentials in respect of hedging overseas investments and the investments in shares, and from differences between the known CPI between the two periods.
- e. On the other hand these decreases were partially offset by the raising of the credit risk margins.

The ratio of net interest income before provision for doubtful debts to the average balance of the financial assets was 2.32%, compared with 2.60% (in annual terms) during the corresponding period in 2008.

**Financing commissions** amounted to NIS 256 million during the first nine months of 2009, compared with NIS 252 million during the corresponding period in 2008, an increase of 1.6%. These commissions include mainly the income from off-balance sheet activity, such as guarantees for granting credit, guarantees for apartment purchasers and other guarantees, as well as commissions from foreign trade activity.

**Other Financing Income and Expenses** include mainly profits/losses from the sale of debentures and the adjustment of debentures for trading to fair value or market value, income from early credit repayment commissions, interest collection in respect of doubtful debts from previous years and the reduction of provisions for uncollected interest. Net income from these operations amounted to NIS 921 million during the first nine months of 2009, compared with NIS 20 million in the corresponding period in 2008.



The following are the main changes in other financing income and expenses:

|  | For the nine months ending |                         |        |
|--|----------------------------|-------------------------|--------|
|  | 30<br>September<br>2009    | 30<br>September<br>2008 | Change |
|  | NIS millions               |                         | %      |
| Net profit (loss) from sales of available-for-sale debentures                    | 446                        | 10                      | +      |
| Decline in value of available-for-sale debentures                                | (151)                      | (518)                   | +      |
| Profit (loss) from sales and adjustments to fair value of debentures for trading | 221                        | (65)                    | +      |
| Collection/reduction of interest in respect of doubtful debts                    | 274                        | 416                     | (34.2) |
| Early credit repayment commissions   | 85                         | 111                     | (23.8) |
| Other  | 46                         | 66                      | (30.3) |
| Total  | 921                        | 20                      | +      |

**The Provision for Doubtful Debts** in the Leumi Group for the first nine months of 2009 amounted to NIS 1,136 million, compared with NIS 1,055 million in the corresponding period of 2008, an increase of NIS 81million, 7.7%.

The provision for doubtful debts amounted to NIS 443 million for the third quarter of 2009, compared with NIS 495 million during the corresponding period in 2008, a decrease of NIS 52 million, 10.5%.

The additional and general provision for doubtful debts, in respect of unidentified risks in the loan portfolio - which are based upon the risk characteristics of the loan portfolio - and in respect of sectoral credit excess, were reduced by NIS 44 million during the first nine months of 2009, compared with a reduction of NIS 25 million during the corresponding period in 2008, and an increase of NIS 73 million for the whole of 2008.

The overall rate of the provision for doubtful debts for the first nine months of 2009 was 0.74% of total credit to the public (in annual terms), compared with a rate of 0.68% in the corresponding period in 2008, and compared with 1.01% for the whole of 2008. The rate of the overall provision for doubtful debts in relation to overall credit risk (balance sheet and off-balance sheet) was 0.49%, 0.45% and 0.67%, respectively.

The aggregate balance of the general provision and the additional provision for doubtful debts (according to the risk characteristics defined by the Supervisor of Banks) at the Bank and its consolidated companies amounted to NIS 904 million (constituting 0.44% of total credit to the public) on 30 September 2009, compared with NIS 948 million at the end of 2008.

The following table sets out the development of the provisions for doubtful debts according to principal operational segments:

| Segment            | First nine months of 2009 |     | First nine months of 2008 |     |
|--------------------|---------------------------|-----|---------------------------|-----|
|                    | (NIS millions)            | % * | (NIS millions)            | %*  |
| Households         | 207                       | 0.4 | 227                       | 0.5 |
| Small businesses   | 150                       | 1.2 | 76                        | 0.6 |
| Corporate banking  | 511                       | 1.0 | 532                       | 1.0 |
| Commercial banking | 256                       | 0.8 | 207                       | 0.6 |

\* Percentage of total credit at the end of the period on an annual basis.  
See pages 30 and 37 for further details.

**Profit from Net Interest Income after Provision for Doubtful Debts** of the Leumi Group for the first nine months of 2009 amounted to NIS 4,075 million, compared with NIS 4,349 million for the corresponding period in 2008, a decrease of 6.3%.

The profit from net interest income after provision for doubtful debts amounted to NIS 1,480 million in the third quarter of 2009, compared with NIS 996 million for the corresponding period in 2008, an increase of 48.6%.

**Total Operating and Other Income** of the Leumi Group for the first nine months of 2009 amounted to NIS 3,308 million, compared with NIS 2,255 million in the corresponding period in 2008, an increase of 46.7%.

Operating and other income totaled NIS 1,292 million during the third quarter of the year, compared with NIS 540 million for the corresponding period in 2008, an increase of 139.3%

The following are the main changes in operating and other income:

|   | For the nine months ending   |                      |                 |       |
|---|------------------------------|----------------------|-----------------|-------|
|   | <b>30 September<br/>2009</b> | 30 September<br>2008 | Change          |       |
|   | NIS<br>millions              |                      | NIS<br>millions | %     |
| Operating commissions <sup>(1)</sup>                          | <b>2,586</b>                 | 2,671                | (85)            | (3.2) |
| Profits (losses) from<br>investments in shares <sup>(2)</sup> | <b>471</b>                   | (478)                | 949             | +     |
| Other income <sup>(3)</sup>                                   | <b>251</b>                   | 62                   | 189             | 304.8 |
| Total operating and other<br>Income                           | <b>3,308</b>                 | 2,255                | 1,053           | 46.7  |

The following are the main additional details regarding each of the above-mentioned items:

1. Operating commissions (NIS (85) million):
  - a. A decrease in income from credit handling and preparation of legal documents in the amount of NIS 90 million, (32.6%).
  - b. A decrease in commissions from conversion differentials in the amount of NIS 12 million (5.3%).
  - c. A decrease in distribution commissions of financial products in the amount of NIS 14 million (9.8%).
  - d. An increase in income from securities transactions in the amount of NIS 33 million, (5.6%).
  - e. An increase in income from account management in the amount of NIS 17 million (2.8%).
2. Profits (losses) from investments in shares (NIS 949 million).
  - a. Net profits from the sale of available-for-sale securities in the amount of NIS 390 million, compared with net losses and reductions in the amount of NIS 119 million in the corresponding period in 2008. See page 49 below.

- b. Profits from the realization and adjustment to fair value of securities for trading in the amount of NIS 6 million, compared with losses of NIS 444 million during the corresponding period in 2008.

3. Other income (NIS 189 million)

The main increase was in the profits of the severance pay provident fund, in the amount of NIS 187 million, compared with the corresponding period in 2008.

The ratio of operating and other income to total income (i.e. net interest income before provision for doubtful debts and operating and other income) was 38.8%, compared with 29.4% in the corresponding period in 2008 and 30.5% for the whole of 2008.

Operating and other income covers 66.7% of operating and other expenses, compared with cover of 43.3% in the corresponding period in 2008, and compared with 40.0% for the whole of 2008.

**Total Operating and Other Expenses** of the Leumi Group in the first nine months of 2009 amounted to NIS 4,962 million, compared with NIS 5,202 million in the corresponding period in 2008, a decrease of 4.6%.

Operating and other expenses amounted to NIS 1,758 million in the third quarter of 2009, compared with NIS 1,746 million in the corresponding period in 2008, an increase of 0.7%.

Salary expenses decreased by NIS 285 million in the first nine months of 2009, and at the rate of 9.1%, compared with the corresponding period in 2008. The decrease in salary expenses derives primarily from the positive yield in the severance pay fund and pension fund, which also serve as a reserve for covering employee pension obligations, compared with a negative yield during the corresponding period in 2008. In the first nine months of 2009, the salary expenses were reduced due to the funds' profits of some NIS 271 million; in addition, income in the amount of NIS 187 million was recorded with respect to operating and other income (of which NIS 72 million was recorded during the third quarter), compared with the first nine months of 2008 in which salary expenses increased due to the funds' negative yields by some NIS 98 million.

Operating and other expenses (maintenance of buildings and equipment, depreciation and others) increased by the amount of NIS 45 million in the first nine months of 2009, an increase of 2.2%, compared with the corresponding period in 2008, mainly as a result of an increase in depreciation expenses at the rate of 20.1%.

Operating expenses constitute 58.2% of total income, compared with 67.9% in the corresponding period in 2008, and compared with 76.3% for the whole of 2008.

Total operating and other expenses (in annual terms) constitute 2.05% of total assets, compared with 2.37% in the corresponding period in 2008, and compared with 2.25% for the whole of 2008.

**Operating Profit before Taxes** of the Leumi Group for the first nine months of 2009 amounted to NIS 2,421million, compared with NIS 1,402 million in the corresponding period in 2008, an increase of 72.7%.

Operating profit before taxes amounted to NIS 1,014 million for the third quarter of 2009, compared with an operating loss before taxes of NIS 210 million in the corresponding period in 2008.

**Provision for Taxes on Operating Profit** of the Leumi Group in the first nine months of 2009 amounted to NIS 950 million, compared with NIS 844 million in the corresponding period in 2008. The rate of provision in the said period was some 39.2% of the pre-tax profit, compared with 60.2% in the corresponding period in 2008, a decrease of some 21.0 percentage points, being some NIS 508 million.

The changes in the rate of the provision for taxes were principally affected by:

1. Exchange rate differentials in respect of overseas investments that are not included in the tax basis calculation and which were positive in the relevant period, compared with negative exchange rate differentials in the corresponding period in 2008, as detailed on page 83 of the Report, reduced the rate of the tax provision by 0.5 percentage points, compared with an increase of 15.4 percentage points in the corresponding period in 2008.
2. The program for the reduction of the companies tax rate, as described below, and which took effect in July of 2009, had the effect of increasing the tax expenses by NIS 146 million due to an adjustment of deferred taxes in accordance with the reduction of the future companies tax rates to 25% in 2010 and to 18% in 2016.
3. During the first nine months of 2009 (primarily during the year's third quarter), the provisions for taxes for previous years were reduced by a net amount of NIS 75 million, following the conclusion of an agreement between the tax authorities and the Bank and a number of its subsidiaries, the updating of the tax shield regarding the value of the benefit to employees relating to the issue of shares in 2006 and other adjustments, including the settlement of assessments.

On 1 July 2009, the Value Added Tax Order (Tax Rate for Non-profit Organizations and Financial Institutions) 2009 was published in the Israeli Government Gazette). The Order raised the rates for salary tax and profit tax that are applicable to financial institutions, commencing 1 July 2009 and continuing through 31 December 2010, from 15.5% to 16.5%.

As the Bank is a "financial institution" for the purpose of the Value Added Tax Law, the increase in the profit tax will increase the overall tax rate to which the Bank is subject, such that in 2009 it will be subject to an overall tax rate of 36.21% instead of 35.93% (an increase of 0.28 percentage points) and in 2010, it will be subject to an overall tax rate 35.62% instead of 35.06% (an increase of 0.56 percentage points).

The total impact of the change in the Value Added Tax rate on the provision for taxes during the first nine months of 2009 was not material.

**Operating Profit after Taxes** for the first nine months of 2009, amounted to NIS 1,471 million, compared with NIS 558 million in the corresponding period in 2008, an increase of 163.6%. In the third quarter of the year, the operating profit after taxes amounted to NIS 515 million, compared with a loss of NIS 271 million in the corresponding period in 2008.

**The Group's Share in Operating Profit (Loss) after Taxes of Companies Included on the Equity Basis** amounted to "0" in the first nine months of 2009, compared with NIS 471 million in the corresponding period in 2008, i.e., there was a decline of some NIS 471 million in this contribution, of which NIS 161 million was in the third quarter of the year. For details, see page 72 below.

**Minority Interests in the Profits of the Group** amounted to a profit of NIS 29 million in the first nine months of 2009, compared with a profit of NIS 3 million in the corresponding period in 2008.

**Net Operating Profit** of the Group for the first nine months of 2009 amounted to NIS 1,442 million, compared with a profit of NIS 1,026 million in the corresponding period in 2008, an increase of 40.5%. During the third quarter of 2009, the net operating profit amounted to NIS 534 million, compared with a loss of NIS 85 million in the corresponding period in 2008.

**Net Profit from Extraordinary Items after Taxes** amounted to NIS 28 million in the first nine months of 2009, compared with a profit of NIS 249 million in the corresponding period in 2008. In the corresponding period in 2008, the profit resulted primarily from the allocation of 20% of the issued and paid-up share capital of Leumi Card to Canit – Investment and Finance Management Ltd.

**Net Basic Operating Profit per share** reached NIS 0.98 in the first nine months of 2009, compared with NIS 0.70 in the corresponding period in 2008.

**Net Basic Profit per share** reached NIS 1.00 during the first nine months of 2009, compared with NIS 0.87 in the corresponding period in 2008.

**Return on Shareholders' Equity – Average for the Period (excluding minority interests) in Annual Terms of:**

|                      | For the first nine months ending on 30 September |      |
|----------------------|--|------|
|                      | 2009   | 2008 |
|                      | %  |      |
| Net profit           | 10.3   | 8.5  |
| Net operating profit | 10.1   | 6.8  |

**Return on Shareholders' Equity – Average for the Period (excluding minority interests) in Annual Terms:**

|                             | 2009        |             |             | 2008        |             |             |             |
|-----------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
|                             | 3rd Quarter | 2nd Quarter | 1st Quarter | 4th Quarter | 3rd Quarter | 2nd Quarter | 1st Quarter |
|                             | %           |             |             |             |             |             |             |
| Net profit (loss)           | 11.0        | 11.1        | 9.7         | (22.2)      | (1.6)       | 19.1        | 9.8         |
| Net operating profit (loss) | 11.0        | 10.4        | 9.6         | (22.2)      | (1.6)       | 13.4        | 9.8         |

## Development of Profit during the Last Seven Quarters

- A. The following table is a condensed statement of operating profit and loss after taxes for the last seven quarters (excluding the Group's share in the profits of companies included on the equity basis):

|                                      | 2009             |                   | 2008             |                   |                  |                   |                  |
|--------------------------------------|------------------|-------------------|------------------|-------------------|------------------|-------------------|------------------|
|                                      | Third<br>Quarter | Second<br>Quarter | First<br>Quarter | Fourth<br>Quarter | Third<br>Quarter | Second<br>Quarter | First<br>Quarter |
|                                      | (NIS millions)   |                   |                  |                   |                  |                   |                  |
| Net interest income                  | <b>1,923</b>     | 1,926             | 1,362            | 976               | 1,491            | 1,953             | 1,960            |
| Provision for doubtful debts         | <b>(443)</b>     | (339)             | (354)            | (1,090)           | (495)            | (316)             | (244)            |
| Operating and other income           | <b>1,292</b>     | 1,013             | 1,003            | 545               | 540              | 864               | 851              |
| Operating and other expenses         | <b>(1,758)</b>   | (1,640)           | (1,564)          | (1,801)           | (1,746)          | (1,662)           | (1,794)          |
| Operating profit (loss) before taxes | <b>1,014</b>     | 960               | 447              | (1,370)           | (210)            | 839               | 773              |
| Provision for taxes                  | <b>(499)</b>     | (409)             | (42)             | 423               | (61)             | (400)             | (383)            |
| Operating profit (loss) after taxes  | <b>515</b>       | 551               | 405              | (947)             | (271)            | 439               | 390              |

- B. The following table shows the development of the principal items in net interest income, before provision for doubtful debts:

|   | 2009             |                   | 2008             |                   |                  |                   |                  |
|---|------------------|-------------------|------------------|-------------------|------------------|-------------------|------------------|
|   | Third<br>Quarter | Second<br>Quarter | First<br>Quarter | Fourth<br>Quarter | Third<br>Quarter | Second<br>Quarter | First<br>Quarter |
|   | (NIS millions)   |                   |                  |                   |                  |                   |                  |
| Current activity  | <b>1,492</b>     | 1,683             | 1,631            | 1,794             | 1,584            | 1,671             | 1,629            |
| Collection and reduction of interest on problem loans   | <b>97</b>        | 88                | 89               | 91                | 80               | 87                | 249              |
| Exchange rate differentials in respect of shares recorded in operating income or the capital fund | <b>17</b>        | 31                | (109)            | (30)              | 2                | 129               | 97               |
| Profits (losses) from the sale of available-for-sale debentures, net                              | <b>120</b>       | 32                | 143              | (829)             | (456)            | (80)              | (28)             |
| Realized and unrealized profits (losses) from adjustments to fair value of debentures for trading | <b>60</b>        | 48                | 113              | 147               | (135)            | (4)               | 74               |
| Financing costs in connection with hedging of overseas investments                                | <b>87</b>        | 50                | (144)            | (134)             | 9                | -                 | 27               |
| Adjustments to fair value of derivative instruments   | <b>19</b>        | (59)              | (328)            | (25)              | 250              | (22)              | (169)            |
| Effect of the known CPI   | <b>31</b>        | 53                | (33)             | (38)              | 157              | 172               | 25               |
| Total   | <b>1,923</b>     | 1,926             | 1,362            | 976               | 1,491            | 1,953             | 1,960            |

C. The following table shows the quarterly development of the provisions for doubtful debts:

|  | <b>2009</b>      |                   | <b>2008</b>      |                   |                  |                   |                  |
|--|------------------|-------------------|------------------|-------------------|------------------|-------------------|------------------|
|  | Third<br>Quarter | Second<br>Quarter | First<br>Quarter | Fourth<br>Quarter | Third<br>Quarter | Second<br>Quarter | First<br>Quarter |
|  | (NIS millions)   |                   |                  |                   |                  |                   |                  |
| Specific provision   | <b>461</b>       | 396               | 323              | 992               | 500              | 311               | 269              |
| Additional provision   | <b>(18)</b>      | (57)              | 31               | 98                | (5)              | 5                 | (25)             |
| Total  | <b>443</b>       | 339               | 354              | 1,090             | 495              | 316               | 244              |
| Rate of provision out of<br>total credit to the public<br>(on an annual basis) | <b>0.87%</b>     | 0.66%             | 0.67%            | 2.05%             | 0.96%            | 0.63%             | 0.49%            |

D. The following table shows the quarterly development of operating and other income:

|  | <b>2009</b>      |                   | <b>2008</b>      |                   |                  |                   |                  |
|--|------------------|-------------------|------------------|-------------------|------------------|-------------------|------------------|
|  | Third<br>Quarter | Second<br>Quarter | First<br>Quarter | Fourth<br>Quarter | Third<br>Quarter | Second<br>Quarter | First<br>Quarter |
|  | (NIS millions)   |                   |                  |                   |                  |                   |                  |
| Operating commissions                          | <b>915</b>       | 840               | 831              | 867               | 887              | 882               | 902              |
| Profits (losses) from<br>investments in shares | <b>286</b>       | 90                | 95               | (434)             | (363)            | (44)              | (71)             |
| Other income                                   | <b>91</b>        | 83                | 77               | 112               | 16               | 26                | 20               |
| Total operating and other<br>income            | <b>1,292</b>     | 1,013             | 1,003            | 545               | 540              | 864               | 851              |

E. The following table shows the quarterly development of salary expenses:

|  | <b>2009</b>      |                   | <b>2008</b>      |                   |                  |                  |                  |
|--|------------------|-------------------|------------------|-------------------|------------------|------------------|------------------|
|  | Third<br>Quarter | Second<br>Quarter | First<br>Quarter | Fourth<br>Quarter | Third<br>Quarter | Third<br>quarter | First<br>Quarter |
|  | (NIS millions)   |                   |                  |                   |                  |                  |                  |
| Salary expenses,<br>excluding special salary<br>expenses         | <b>961</b>       | 948               | 1,003            | 982               | 861              | 956              | 953              |
| Special salary expenses  | <b>91</b>        | (19)              | (120)            | (13)              | 182              | 19               | 178              |
| Of which: Expenses for<br>issue of options to<br>employees       | -                | -                 | -                | (14)              | (37)             | 6                | 29               |
| Recording of benefit<br>regarding sale of shares<br>to employees | <b>15</b>        | -                 | -                | -                 | (39)             | 11               | (22)             |
| Provision for severance<br>pay and pensions                      | <b>76</b>        | (20)              | (120)            | 108               | 258              | 2                | 163              |
| Salary tax refunds   | -                | -                 | -                | (154)             | -                | -                | -                |
| Actuarial changes in<br>respect of jubilee bonus                 | -                | -                 | -                | 47                | -                | -                | -                |
| Miscellaneous  | -                | 1                 | -                | -                 | -                | -                | 8                |
| Total salary expenses  | <b>1,052</b>     | 929               | 883              | 969               | 1,043            | 975              | 1,131            |

## Structure and Development of Assets and Liabilities<sup>(1)</sup>

**Total Assets** of the Leumi Group as at 30 September 2009 amounted to NIS 323.6 billion, compared with NIS 310.8 billion at the end of 2008, an increase of 4.1%, and an increase of 10.1% compared with 30 September 2008.

The value of the assets in the balance sheet denominated in and or linked to foreign currency was some NIS 96.5 billion, some 29.8% of total assets. During the first nine months of 2009, the shekel appreciated against the US dollar by 1.16% and depreciated against the euro by 4.02%. The changes in the rates of exchange in the first nine months of the year led to an increase of 0.2% in total assets.

The total assets under the Group's management - total balance sheet as well as customers' securities portfolios, and provident funds and supplementary training funds in respect of which operating management and custody services are provided - amount to some NIS 761 billion, compared with NIS 651 billion at the end of 2008 (some US\$ 203 billion and US\$ 173 billion, respectively), as detailed below.

The following table sets out the development of the main balance sheet items:

|  | <b>30<br/>September<br/>2009</b> | 31<br>December<br>2008 | Rate of change            |                            |
|--|----------------------------------|------------------------|---------------------------|----------------------------|
|  |                                  |                        | Since<br>December<br>2008 | Since<br>September<br>2008 |
|  | NIS millions                     |                        | %                         |                            |
| Total assets   | <b>323,630</b>                   | 310,792                | 4.1                       | 10.1                       |
| Deposits of the public                                   | <b>249,433</b>                   | 244,783                | 1.9                       | 10.4                       |
| Debentures, capital notes and subordinated capital notes | <b>25,471</b>                    | 20,636                 | 23.4                      | 14.4                       |
| Deposits from banks                                      | <b>5,395</b>                     | 3,742                  | 44.2                      | (16.4)                     |
| Cash and deposits with banks                             | <b>43,934</b>                    | 33,130                 | 32.6                      | 51.4                       |
| Securities   | <b>58,381</b>                    | 44,910                 | 30.0                      | 40.5                       |
| Credit to the public                                     | <b>203,971</b>                   | 213,215                | (4.3)                     | (1.7)                      |
| Buildings and equipment                                  | <b>3,544</b>                     | 3,445                  | 2.9                       | 5.2                        |

**Deposits of the public** amounted to NIS 249.4 billion as at 30 September 2009, compared with NIS 244.8 billion as at 31 December 2008, an increase of 1.9%, and an increase of 10.4% compared with 30 September 2008.

The depreciation of the shekel in relation to most foreign currencies in the first nine months of 2009 contributed to a 0.2% increase in total deposits of the public.

The following table sets out the development of deposits of the public according to principal operational segments:

| Segment  | <b>30 September 2009</b> | 31 December 2008 | % Change |
|--|--------------------------|------------------|----------|
|  | NIS millions             |                  |          |
| Households                                     | <b>119,084</b>           | 120,846          | (1.5)    |
| Small businesses                               | <b>14,396</b>            | 14,475           | (0.5)    |
| Corporate banking                              | <b>27,131</b>            | 23,111           | 17.4     |
| Commercial banking                             | <b>31,442</b>            | 29,659           | 6.0      |
| Private banking                                | <b>40,348</b>            | 38,057           | 6.0      |
| Financial management, capital market and other | <b>17,032</b>            | 18,635           | (8.6)    |
| Total  | <b>249,433</b>           | 244,783          | 1.9      |

(1) The changes in percentages were calculated according to the balances in NIS millions.



**Debentures, Capital Notes and Subordinated Capital Notes** totaled NIS 25.5 billion on 30 September 2009, compared with NIS 20.6 billion on 31 December 2008, an increase of 23.4%, and compared with 30 September 2008, an increase of 14.4%.

### Off-balance sheet activity

The following table sets out the development of balances of the customers' (off-balance sheet) financial assets<sup>(1)</sup> managed by the Leumi Group:

|   | <b>30 September<br/>2009</b> | 31 December<br>2008 | <b>Change</b>  |      |
|---|------------------------------|---------------------|----------------|------|
|   | (NIS millions)               |                     | (NIS millions) | %    |
| Securities portfolios                                   | <b>381,287</b>               | 295,853             | 85,434         | 28.9 |
| of which: managed by<br>mutual funds <sup>(2) (3)</sup> | <b>45,391</b>                | 36,572              | 8,819          | 24.1 |
| Provident and pension<br>funds <sup>(2) (3)</sup>       | <b>39,369</b>                | 31,794              | 7,575          | 23.8 |
| Supplementary training<br>funds <sup>(2) (3)</sup>      | <b>16,618</b>                | 12,769              | 3,849          | 30.1 |
| <b>Total</b>  | <b>437,274</b>               | 340,416             | 96,858         | 28.3 |

(1) Including an increase in the market value of securities and in value of securities of mutual and provident funds held in custody, regarding which operating management and custody services are provided.

(2) The Group in Israel does not manage any mutual funds, provident funds or supplementary training funds.

(3) Assets of customers in respect of which the Group provides operating management services, including the fund balances of customers who are counseled by Leumi.

**Credit to the public** totaled NIS 204.0 billion on 30 September 2009, compared with NIS 213.2 billion on 31 December 2008, a decrease of 4.3%, and a decrease of 1.7% compared with 30 September 2008.

The depreciation of the shekel in relation to most foreign currencies in the first nine months of 2009 led to an increase of 0.1% in total credit to the public.

In addition to credit to the public, the Group also invests in corporate debentures which amounted to NIS 8,020 million on 30 September 2009, in comparison with NIS 8,204 million on 31 December 2008, a decrease of 2.2%.

The following table sets out the development of the overall credit risk\* to the public according to principal sectors of the economy:

| Economy Sectors                         | <b>30 September 2009</b>             |               | 31 December 2008                            |               | Change |
|---|--------------------------------------|---------------|---|---------------|--------|
|   | Overall credit                       | Percentage    | Overall                                     | Percentage    |        |
|   | risk to the public<br>(NIS millions) | of total<br>% | credit risk to the public<br>(NIS millions) | of total<br>% |        |
| Agriculture                             | <b>2,235</b>                         | <b>0.7</b>    | 2,501                                       | 0.8           | (10.6) |
| Industry                                | <b>44,767</b>                        | <b>14.6</b>   | 52,212                                      | 16.3          | (14.3) |
| Construction and real estate            | <b>62,273</b>                        | <b>20.2</b>   | 60,681                                      | 18.9          | 2.6    |
| Electricity and water                   | <b>1,973</b>                         | <b>0.6</b>    | 1,851                                       | 0.6           | 6.6    |
| Trade                                   | <b>29,288</b>                        | <b>9.5</b>    | 31,009                                      | 9.7           | (5.6)  |
| Hotels, accommodation and food services | <b>4,889</b>                         | <b>1.6</b>    | 5,275                                       | 1.6           | (7.3)  |
| Transportation and storage              | <b>6,213</b>                         | <b>2.0</b>    | 6,673                                       | 2.1           | (6.9)  |
| Communications and computer services    | <b>6,017</b>                         | <b>2.0</b>    | 7,084                                       | 2.2           | (15.1) |
| Financial services                      | <b>35,953</b>                        | <b>11.7</b>   | 42,565                                      | 13.3          | (15.5) |
| Other business services                 | <b>8,601</b>                         | <b>2.8</b>    | 9,279                                       | 2.9           | (7.3)  |
| Public and community services           | <b>8,237</b>                         | <b>2.7</b>    | 8,564                                       | 2.7           | (3.8)  |
| Private persons - housing loans         | <b>46,624</b>                        | <b>15.2</b>   | 43,603                                      | 13.5          | 6.9    |
| Private persons – other                 | <b>50,331</b>                        | <b>16.4</b>   | 49,197                                      | 15.4          | 2.3    |
| <b>Total</b>                            | <b>307,401</b>                       | <b>100.0</b>  | 320,494                                     | 100.0         | (4.1)  |

\* Including off-balance sheet credit risk, investments of the public in debentures and other assets in respect of derivatives.

The following table sets out the development of credit to the public according to principal operational segments:

| Segment            | <b>30 September 2009</b> | 31 December 2008 | Change |
|--------------------|--------------------------|------------------|--------|
|                    | (NIS millions)           |                  | %      |
| Households*        | <b>65,401</b>            | 62,145           | 5.2    |
| Small businesses   | <b>17,283</b>            | 18,161           | (4.8)  |
| Commercial banking | <b>43,747</b>            | 48,506           | (9.8)  |
| Corporate banking  | <b>70,016</b>            | 76,563           | (8.6)  |
| Private banking    | <b>6,286</b>             | 6,438            | (2.4)  |

\* Credit to households also includes housing loans (mortgages).

### **Pledge in favor of the Bank of Israel**

On 21 May 2008, the Bank signed a debenture pursuant to which it granted a first degree floating charge in favor of the Bank of Israel, on its rights to receive amounts and monetary shekel payments that are due and that will become due to the Bank from time to time, from customers which are corporations (established according to the laws of the State of Israel), which are not in arrears with their repayments to the Bank of credits received from it, and where the average duration of the credit does not exceed three years, and which was granted and that will be granted to these customers by the Bank. The charge is in an amount equal to the level of the amounts secured by the debenture, from time to time, up to an amount of NIS 1.1 billion.

This charge is to secure monies that will be required for the Bank's activities for the purpose of its activities with the CLS clearing house.

**Following is further data on total credit:**

The following table sets out the spread of total credit to the public\* and off-balance sheet credit risk according to the size of the credit to a single borrower:

| <b>30 September 2009</b>        |         |   |  |  |
|---------------------------------|---------|---|--|--|
| Credit ceiling in NIS thousands |         | Percentage of<br>total number of<br>borrowers | Percentage of<br>total balance<br>sheet credit | Percentage of<br>total off-balance<br>sheet credit |
| From                            | To      | %   |  |  |
| 0                               | 80      | <b>84.1</b>                                   | <b>6.2</b>                                     | <b>17.6</b>  |
| 80                              | 600     | <b>14.0</b>                                   | <b>19.7</b>                                    | <b>12.7</b>  |
| 600                             | 1,200   | <b>1.1</b>                                    | <b>7.4</b>                                     | <b>2.8</b>   |
| 1,200                           | 2,000   | <b>0.3</b>                                    | <b>3.5</b>                                     | <b>1.5</b>   |
| 2,000                           | 8,000   | <b>0.3</b>                                    | <b>9.1</b>                                     | <b>5.8</b>   |
| 8,000                           | 20,000  | <b>0.1</b>                                    | <b>8.1</b>                                     | <b>6.4</b>   |
| 20,000                          | 40,000  | <b>0.05</b>                                   | <b>7.9</b>                                     | <b>6.6</b>   |
| 40,000                          | 200,000 | <b>0.04</b>                                   | <b>17.7</b>                                    | <b>19.0</b>  |
| 200,000                         | 800,000 | <b>0.01**</b>                                 | <b>13.8</b>                                    | <b>16.9</b>  |
| Above 800,000                   |         | <b>0.001***</b>                               | <b>6.6</b>                                     | <b>10.7</b>  |
| Total                           |         | <b>100.0</b>                                  | <b>100.0</b>                                   | <b>100.0</b>                                       |

| <b>31 December 2008</b>         |         |   |  |  |
|---------------------------------|---------|---|--|--|
| Credit ceiling in NIS thousands |         | Percentage of<br>total number of<br>borrowers | Percentage of<br>total balance<br>sheet credit | Percentage of<br>total off-balance<br>sheet credit |
| From                            | To      | %   |  |  |
| 0                               | 80      | 83.4  | 5.8  | 16.5   |
| 80                              | 600     | 14.6  | 18.8   | 12.0   |
| 600                             | 1,200   | 1.1   | 6.4  | 2.6  |
| 1,200                           | 2,000   | 0.3   | 3.1  | 1.5  |
| 2,000                           | 8,000   | 0.4   | 9.0  | 5.7  |
| 8,000                           | 20,000  | 0.1   | 8.3  | 6.4  |
| 20,000                          | 40,000  | 0.05  | 8.1  | 4.8  |
| 40,000                          | 200,000 | 0.04  | 17.1   | 22.7   |
| 200,000                         | 800,000 | 0.01**  | 15.3   | 15.7   |
| Above 800,000                   |         | 0.001***                                      | 8.1  | 12.1   |
| Total                           |         | 100.0   | 100.0  | 100.0  |

\* After deducting the specific provisions for doubtful debts.

\*\* On 30 September 2009 – 122 borrowers and on 31 December 2008 - 131 borrowers

\*\*\* On 30 September 2009 - 19 borrowers and on 31 December 2008 - 20 borrowers.

The following are details of the balances of credit to the public and of the off-balance sheet credit risk which exceed NIS 800 million per individual borrower based on a more detailed breakdown of credit areas and based on a breakdown of economic sectors:

1. Credit risk according to size of credit to the borrower

| <b>30 September 2009</b>       |       |                     |                          |                      |                          |                          |                          |
|--------------------------------|-------|---------------------|--------------------------|----------------------|--------------------------|--------------------------|--------------------------|
|                                |       | Number of borrowers |                          | Balance sheet credit |                          | Off-balance sheet credit |                          |
| Credit ceiling in NIS millions |       | Total               | Of this, related parties | Total                | Of this, related parties | Total                    | Of this, related parties |
| From                           | To    | In NIS millions     |                          |                      |                          |                          |                          |
| 800                            | 1,200 | 12                  | 1                        | 8,651                | 267                      | 2,450                    | 547                      |
| 1,200                          | 1,600 | 3                   | -                        | 2,205                | -                        | 2,346                    | -                        |
| 1,600                          | 2,000 | 3                   | 1                        | 2,785                | 1,312                    | 2,724                    | 596                      |
| 2,000                          | 2,400 | 1                   | -                        | 19                   | -                        | 2,354                    | -                        |
| 2,400                          | 2,800 | -                   | -                        | -                    | -                        | -                        | -                        |
| 2,800                          | 3,200 | -                   | -                        | -                    | -                        | -                        | -                        |
| Total                          |       | 19                  | 2                        | 13,660               | 1,579                    | 9,874                    | 1,143                    |

All the related parties are corporations in which the Bank holds up to 20% and they are not controlling shareholders of the Bank. The credits specified in the above table do not include any debts for which provisions were made for doubtful debts.

| <b>31 December 2008</b>        |       |                     |                          |                      |                          |                          |                          |
|--------------------------------|-------|---------------------|--------------------------|----------------------|--------------------------|--------------------------|--------------------------|
|                                |       | Number of Borrowers |                          | Balance sheet credit |                          | Off-balance sheet credit |                          |
| Credit ceiling in NIS millions |       | Total               | Of this, related parties | Total                | Of this, related parties | Total                    | Of this, related parties |
| From                           | To    | In NIS millions     |                          |                      |                          |                          |                          |
| 800                            | 1,200 | 8                   | 1                        | 5,051                | 657                      | 2,666                    | 266                      |
| 1,200                          | 1,600 | 5                   | -                        | 4,096                | -                        | 2,246                    | -                        |
| 1,600                          | 2,000 | 4                   | 1                        | 3,789                | 1,340                    | 3,271                    | 341                      |
| 2,000                          | 2,400 | 1                   | 1                        | 1,876                | 1,876                    | 436                      | 436                      |
| 2,400                          | 2,800 | 1                   | -                        | 1                    | -                        | 2,677                    | -                        |
| 2,800                          | 3,200 | 1                   | -                        | 2,857                | -                        | -                        | -                        |
| Total                          |       | 20                  | 3                        | 17,670               | 3,873                    | 11,296                   | 1,043                    |

## 2. Credit risk according to economic sectors

| <b>30 September 2009</b>                |                        |                         |                             |
|---|------------------------|-------------------------|-----------------------------|
|   | Number of<br>borrowers | Balance<br>sheet credit | Off-balance<br>sheet credit |
|   | Total                  | Total                   | Total                       |
| In NIS millions                         |                        |                         |                             |
| Industry                                | 7                      | 4,173                   | 6,786                       |
| Construction and real estate            | 6                      | 4,225                   | 1,288                       |
| Communications and<br>computer services | 2                      | 2,088                   | 312                         |
| Financial services                      | 3                      | 2,272                   | 1,480                       |
| Public and community<br>services        | 1                      | 902                     | 8                           |
| <b>Total</b>                            | <b>19</b>              | <b>13,660</b>           | <b>9,874</b>                |

  

| <b>31 December 2008</b>                 |                        |                         |                             |
|---|------------------------|-------------------------|-----------------------------|
|   | Number of<br>borrowers | Balance<br>sheet credit | Off-balance<br>sheet credit |
|   | Total                  | Total                   | Total                       |
| In NIS millions                         |                        |                         |                             |
| Industry                                | 7                      | 5,723                   | 6,265                       |
| Construction and real estate            | 4                      | 2,883                   | 995                         |
| Trade                                   | 1                      | 1,876                   | 436                         |
| Communications and<br>computer services | 2                      | 2,645                   | 341                         |
| Financial services                      | 5                      | 4,503                   | 2,371                       |
| Public and community<br>services        | 1                      | 40                      | 888                         |
| <b>Total</b>                            | <b>20</b>              | <b>17,670</b>           | <b>11,296</b>               |

The indebtedness of the six largest groups of borrowers represented 8.8% of total credit risk of 30 September 2009 and 77.5% of the capital calculated for the limitation on the six largest groups of borrowers.

**Problem Loans** – the following table sets out the development of the problem loans <sup>(1) (6)</sup> according to the classifications determined in the directives of the Supervisor of Banks:

|  | <b>30 September<br/>2009</b> | 30 September<br>2008 | 31 December<br>2008 |
|--|------------------------------|----------------------|---------------------|
|  | (NIS millions)               |                      |                     |
| <b>Problem loans<sup>(1)</sup></b>   |                              |                      |                     |
| Non-performing   | <b>2,053</b>                 | 1,660                | 2,012               |
| Restructured <sup>(2)</sup>  | <b>565</b>                   | 421                  | 405                 |
| To be restructured <sup>(3)</sup>  | <b>464</b>                   | 36                   | 558                 |
| In temporary arrears   | <b>589</b>                   | 614                  | 562                 |
| Under special supervision*   | <b>13,464</b>                | 12,223               | 14,545              |
| Total balance sheet credit to problem borrowers <sup>(1)</sup>   | <b>17,135</b>                | 14,954               | 18,082              |
| Off-balance sheet credit risk to problem borrowers <sup>(1) (5)</sup>  | <b>3,172</b>                 | 3,500                | 3,482               |
| Debentures of problem borrowers (public)   | <b>588</b>                   | 104                  | 506                 |
| The banks' overall credit risk (debentures + deposits in banks)  | <b>197</b>                   | -                    | 108                 |
| Other assets in respect of derivatives of problem borrowers  | <b>337</b>                   | 210                  | 612                 |
| Total credit risk in respect of problem borrowers <sup>(1)</sup>   | <b>21,429</b>                | 18,768               | 22,790              |
| Assets received in respect of repaid credit  | <b>84</b>                    | 488                  | 302                 |
| * of which: debts in respect of which there is a specific provision <sup>(4)</sup>                             | <b>6,603</b>                 | 5,490                | 7,373               |
| * of which: credit for housing in respect of which there is a provision according to the extent of the arrears | <b>454</b>                   | 505                  | 505                 |

- (1) Not including problem loans that are covered by collateral that is deductible for the purpose of restrictions on the obligations of a borrower and a group of borrowers (Proper Banking Management Directive No. 313).
- (2) Credit that was restructured during the course of the current year and also credit that was restructured in previous years with a waiver of income.
- (3) Credit to borrowers in respect whereof a decision has been made by the banking corporation's management to restructure, but restructuring has yet to be implemented.
- (4) Except for credit for housing, in respect of which there is a provision in accordance with the extent of the arrears.
- (5) As calculated for the purpose of restrictions on the obligations of a borrower and a group of borrowers, except in respect of guarantees given by a borrower to secure an obligation of a third party.
- (6) Credit to problem borrowers as detailed in the disclosure format.
- (7) Problem loans include classifications of credit from the implementation of Proper Banking Management Directive No. 325 "Management of Current Account Credit Lines." Pursuant to the above Directive and to clarifications of the Supervisor of Banks, the Bank is required to classify deviations from approved credit lines (where the deviation is over NIS 1,000), if it charges the customer excess interest. In such a case, the deviation is to be classified as a non-performing loan, and the credit within the credit line and the balance of the customer's obligations are to be classified as a loan under special supervision. As a result, non-performing loans in the amount of NIS 86 million and loans under special supervision in the amount of NIS 1,641million were classified, and at the end of 2008 NIS 100 million and NIS 1,948 million, respectively, were classified.

**Credit to Governments** amounted to NIS 430 million on 30 September 2009, compared with NIS 520 million on 31 December 2008, a decrease of 17.3%, and a decrease of 16.0% compared with 30 September 2008.

## Securities

The Group's investments in securities amounted to NIS 58,381million on 30 September 2009, compared with NIS 44,910 million on 31 December 2008, an increase of 30.0%, primarily as a result of investments in government debentures as explained below.

Securities are classified in three categories: securities for trading, available-for-sale securities and debentures held to maturity.

Securities for trading are presented in the balance sheet at fair value and the difference between the fair value and the adjusted cost is charged to the profit and loss statement. Available-for-sale securities are presented at fair value, where the difference between fair value and adjusted cost is presented as a separate item in shareholders' equity in "other overall profit" called "adjustments for presentation of available-for-sale securities at fair value" ("shareholders equity" or "capital fund") less the related tax. Whenever the decrease in value is of a non-temporary nature, the difference is charged to the profit and loss statement. Debentures held to maturity are presented at adjusted cost (par value together with accrued interest and linkage differentials, less/plus a disaggio or aggio).

For details of accounting policy and the manner of valuing the securities portfolio and the difference between a temporary decline in value and that of a non-temporary nature, see the Section "Accounting Policy on Critical Subjects" on pages 50-51 and Note 1 to the 2008 Annual Financial Statements.

The following table sets out the classification of the securities item in the consolidated balance sheet in accordance with the above-mentioned rules:

| 30 September 2009       |                  |  |   |               |                           |
|-------------------------|------------------|--|---|---------------|---------------------------|
|                         | Adjusted<br>cost | Unrealized<br>gains from<br>adjustments to<br>fair value | Unrealized<br>losses from<br>adjustments to<br>fair value | Fair<br>Value | Balance<br>sheet<br>value |
|                         | NIS millions     |  |   |               |                           |
| <b>Debentures</b>       |                  |  |   |               |                           |
| Held to maturity        | 890              | 9  | (3)   | 896           | 890                       |
| Available-for-sale      | 44,341           | 525  | (842)   | 44,024        | 44,024                    |
| For trading             | 10,883           | 169  | (50)  | 11,002        | 11,002                    |
| Total                   | 56,114           | 703  | (895)   | 55,922        | 55,916                    |
| <b>Shares and Funds</b> |                  |  |   |               |                           |
| Available-for-sale      | 1,687            | 687  | (1)   | 2,373         | 2,373                     |
| For trading             | 442              | -  | (350)   | 92            | 92                        |
| Total                   | 2,129            | 687  | (351)   | 2,465         | 2,465                     |
| <b>Total Securities</b> | <b>58,243</b>    | <b>1,390</b>   | <b>(1,246)</b>  | <b>58,387</b> | <b>58,381</b>             |

| 31 December 2008        |               |   |  |            |                     |
|-------------------------|---------------|---|--|------------|---------------------|
|                         | Adjusted cost | Unrealized gains from adjustments to fair value | Unrealized losses from adjustments to fair value | Fair Value | Balance sheet value |
| NIS millions            |               |   |  |            |                     |
| <b>Debentures</b>       |               |   |  |            |                     |
| Held to maturity        | 1,509         | 30  | (1)  | 1,538      | 1,509               |
| Available-for-sale      | 30,748        | 502   | (1,923)  | 29,327     | 29,327              |
| For trading             | 10,778        | 168   | (196)  | 10,750     | 10,750              |
|                         | 43,035        | 700   | (2,120)  | 41,615     | 41,586              |
| <b>Shares and funds</b> |               |   |  |            |                     |
| Available-for-sale      | 2,790         | 430   | (1)  | 3,219      | 3,219               |
| For trading             | 457           | -   | (352)  | 105        | 105                 |
|                         | 3,247         | 430   | (353)  | 3,324      | 3,324               |
| <b>Total securities</b> | 46,282        | 1,130   | (2,473)  | 44,939     | 44,910              |

As of 30 September 2009, some 79.5% of the Group's nostro portfolio was classified as available-for-sale securities and some 19.0% as securities for trading. This classification allows for flexibility in the management of the securities portfolio. Some 4.2% of the value of the securities represents investments in shares of companies that are not presented on the equity basis, but according to cost or to the market value of the shares traded on a stock exchange.

The following table sets out details of the Group's activity in debentures:

|   | 30 September 2009 | 31 December 2008 |
|---|-------------------|------------------|
| NIS millions  |                   |                  |
| Debentures redeemed and/or sold (held to redemption and available-for-sale)                         | 16,751            | 46,987           |
| Purchases of debentures held to redemption and available-for-sale                                   | 29,582            | 45,615           |
| Net profit from investments in debentures:  |                   |                  |
| • financing income on accrual basis   | 1,333             | 914              |
| • profit (loss) from sale and from decrease in value of available-for-sale debentures               | 295               | (1,337)          |
| • profit (loss) realized and/or unrealized from adjustments to fair value of debentures for trading | 221               | 82               |

The following table sets out details of the composition of investments in debentures according to linkage basis:

|  | 30 September 2009  |                   |                    | 31 December 2008   |                   |                    |
|--|--------------------|-------------------|--------------------|--------------------|-------------------|--------------------|
|  | Govt. of<br>Israel | Foreign<br>govts. | Other<br>companies | Govt. of<br>Israel | Foreign<br>govts. | Other<br>Companies |
|  | NIS millions       |                   |                    | NIS millions       |                   |                    |
| Israeli currency:  |                    |                   |                    |                    |                   |                    |
| Unlinked   | 19,728             | -                 | 93                 | 9,422              | -                 | 42                 |
| CPI-linked   | 8,389              | -                 | 905                | 4,948              | -                 | 1,046              |
| Foreign currency<br>including foreign<br>currency-linked |                    |                   |                    |                    |                   |                    |
|  | 1,964              | 3,172             | 21,665             | 2,127              | 4,601             | 19,400             |
| Total debentures*  | 30.081             | 3.172             | 22.663             | 16.497             | 4.601             | 20.488             |

\* of which NIS 3,136 million in subordinated debentures.



There was an increase of some NIS 2.2 billion during the first nine months of 2009, some 10.6%, in the Group's investments in corporate debentures (including of banks), mainly in foreign currency debentures abroad, partially as a result of the depreciation of the shekel in relation to the Euro. Some 59.5% of the amount invested in debentures is invested in government debentures, mainly of the Israeli government.

See Note 2 to the Financial Statements for further details.

The following table sets out the value of securities according to the method of calculation in NIS millions:

|  | <b>30 September 2009</b> | 31 December 2008 |
|--|--------------------------|------------------|
| Securities traded on an active market*                                   | <b>48,710</b>            | 38,594           |
| Securities according to prices determined according to external models** | <b>7,921</b>             | 3,540            |
| Securities according to quotation from counterparty or to cost           | <b>1,750</b>             | 2,776            |
| <b>Total</b>   | <b>58,381</b>            | 44,910           |

\* Including fair value calculated according to models based on current market data.

\*\* Including securities in the amount of NIS 407 million which were valued according to the model of a subsidiary.

The following table shows details of investments in corporate debentures only (excluding banks), issued in Israel and overseas, according to sectors of the economy (in the available-for-sale and trading portfolios):

|                                      | <b>30 September 2009</b> |                 |
|--------------------------------------|--------------------------|-----------------|
|                                      | Issued in Israel         | Issued overseas |
| Economy sector                       | NIS millions             |                 |
| Industry                             | <b>148</b>               | <b>67</b>       |
| Construction and real estate         | <b>74</b>                | <b>121</b>      |
| Electricity and water                | <b>133</b>               | <b>148</b>      |
| Trade                                | <b>161</b>               | -               |
| Transport and storage                | <b>20</b>                | <b>14</b>       |
| Communications and computer services | <b>75</b>                | <b>53</b>       |
| Financial services                   | <b>305</b>               | <b>6,564</b>    |
| Business services and others         | -                        | <b>65</b>       |
| Public and community services        | <b>27</b>                | <b>45</b>       |
| <b>Total</b>                         | <b>943</b>               | <b>7,077</b>    |

### **The available-for-sale portfolio**

The following table shows the available-for-sale portfolio as at 30 September 2009:

|                  | <b>30 September 2009</b> |               | 31 December 2008 |           | Change |           |
|------------------|--------------------------|---------------|------------------|-----------|--------|-----------|
|                  | NIS millions             |               |                  |           |        |           |
|                  | Abroad                   | In Israel     | Abroad           | In Israel | Abroad | In Israel |
| Debentures       | <b>21,398</b>            | <b>22,626</b> | 20,246           | 9,144     | 1,152  | 13,482    |
| Shares and funds | <b>579</b>               | <b>1,794</b>  | 1,260            | 1,959     | (681)  | (165)     |
| <b>Total</b>     | <b>21,977</b>            | <b>24,420</b> | 21,506           | 11,103    | 471    | 13,317    |

- a. In the first nine months of 2009, NIS 1,365 million was credited to shareholders' equity in respect of the available-for-sale portfolio, due to an increase in value and exchange rate

differentials in respect of debentures denominated in foreign currency, compared with a decline in value of NIS 2,062 million in the corresponding period of 2008. Most of the increase in value was in subordinated debentures issued by foreign banks, during the second quarter of the year.

- b. In addition, NIS 295 million was credited to profit and loss in respect of profits from the sale of debentures after offsetting provisions defined as decreases in value of securities of a non-temporary nature, compared with losses of NIS 508 million in the corresponding period of 2008.
- c. The following table shows a summary of the above results in respect of the available-for-sale portfolio (including financing income):

|  | <b>For the period ending on</b>  |                         |                        |
|--|----------------------------------|-------------------------|------------------------|
|  | <b>30<br/>September<br/>2009</b> | 30<br>September<br>2008 | 31<br>December<br>2008 |
|  | NIS millions                     |                         |                        |
| Profits (losses) in respect of securities which were charged to profit and loss*   | <b>1,478</b>                     | (2,285)                 | (772)                  |
| Adjustments for increase (decrease) in value of securities in shareholders' equity | <b>1,365</b>                     | (2,062)                 | (1,784)                |

\* Of this, NIS 332 is due to positive exchange rate differentials during the first nine months of 2009, compared with negative exchange rate differentials in the amount of NIS 3,073 million during the corresponding period of 2008, and of NIS 1,330 million for all of 2008.

- d. The following table shows net balances in shareholders' equity (net adjustments in respect of available-for-sale securities before tax):

|                               | <b>30<br/>September<br/>2009</b> | 30<br>June<br>2009 | 31<br>March<br>2009 | 31<br>December<br>2008 | Quarterly movement         |                            |                            |
|-------------------------------|----------------------------------|--------------------|---------------------|------------------------|----------------------------|----------------------------|----------------------------|
|                               |                                  |                    |                     |                        | 1 <sup>st</sup><br>quarter | 2 <sup>nd</sup><br>quarter | 3 <sup>rd</sup><br>quarter |
| Shares                        | <b>686</b>                       | 883                | 510                 | 429                    | 81                         | 373                        | (197)                      |
| Israel government debentures  | <b>183</b>                       | 323                | 516                 | 434                    | 82                         | (193)                      | (140)                      |
| Foreign government debentures | <b>5</b>                         | 5                  | 6                   | 9                      | (3)                        | (1)                        | -                          |
| Other debentures              | <b>(505)*</b>                    | (1,322)            | (2,721)             | (1,864)                | (857)                      | 1,399                      | 817                        |
| Other credit instruments      | <b>(23)</b>                      | (22)               | (16)                | (27)                   | 11                         | (6)                        | (1)                        |
| Total                         | <b>346</b>                       | (133)              | (1,705)             | (1,019)                | (686)                      | 1,572                      | 479                        |
| Related tax                   | <b>(118)</b>                     | 63                 | 627                 | 371                    | 256                        | (564)                      | (181)                      |
| Net total                     | <b>228</b>                       | (70)               | (1,078)             | (648)                  | (430)                      | 1,008                      | 298                        |

\* of which as of 30 September 2009, NIS 334 million in subordinated debentures issued by foreign banks.

The value of the available-for-sale portfolio has continued to improve since the end of September 2009, and the capital fund totaled NIS 426 million at the end of October 2009, compared with NIS 346 million.

The accumulated net balance of adjustments to fair value of securities held in the available-for-sale portfolio as at 30 September 2009 totaled the positive amount of NIS 228 million (after the effect of taxes) and this was for the first time after a number of consecutive quarters in which the balance was negative and amounted to NIS 70 million at the end of June 2009 and NIS 1,078 million at the end of March 2009 and NIS 648 million at the end of 2008. These amounts represent losses/profits which had not been realized at the dates of the financial statements.

According to the (Basel I) rules for calculating capital adequacy, the balance in respect of adjustment of securities to fair value does not affect the calculation of the capital for the purpose of the minimum capital ratio, except for net unrealized losses from adjustments to fair value of available-for-sale shares, less the effect of taxes.

The accumulated balance of the decline in value in the debentures item, in the amount of NIS 317 million, relates mainly to the decrease in value of subordinated capital notes issued by foreign banks.

- e. The following are the declines in value of available-for-sale securities which were charged to shareholders' equity (accumulated as at 30 September 2009):

|                 |                         | Duration of decline in value since commencement of the decline* |            |             |                     |              |
|-----------------|-------------------------|---|------------|-------------|---------------------|--------------|
|                 |                         | Up to 6 months  | 6-9 months | 9-12 months | More than 12 months | Total amount |
| NIS millions    |                         |   |            |             |                     |              |
| Rate of decline |                         |   |            |             |                     |              |
| Up to 10%       | Shares                  | -   | -          | -           | -                   | -            |
|                 | Asset-backed debentures | 2   | -          | -           | 39                  | 41           |
|                 | Other debentures        | 46  | 10         | 6           | 219                 | 281          |
|                 | Total                   | 48  | 10         | 6           | 258                 | 322          |
| 10%- 20%        | Shares                  | -   | -          | -           | -                   | -            |
|                 | Asset-backed debentures | -   | 1          | -           | 49                  | 50           |
|                 | Other debentures        | -   | -          | 24          | 289                 | 313          |
|                 | Total                   | -   | 1          | 24          | 338                 | 363          |
| 20%-30%         | Shares                  | -   | -          | -           | -                   | -            |
|                 | Asset-backed debentures | -   | -          | -           | 1                   | 1            |
|                 | Other debentures        | -   | -          | -           | 114                 | 114          |
|                 | Total                   | -   | -          | -           | 115                 | 115          |
| 30%-35%         | Shares                  | -   | -          | -           | -                   | -            |
|                 | Asset-backed debentures | -   | -          | -           | 1                   | 1            |
|                 | Other debentures        | -   | -          | -           | -                   | -            |
|                 | Total                   | -   | -          | -           | 1                   | 1            |
| 35%-40%         | Shares                  | -   | -          | -           | -                   | -            |
|                 | Asset-backed debentures | -   | -          | -           | 1                   | 1            |
|                 | Other debentures        | -   | -          | -           | -                   | -            |
|                 | Total                   | -   | -          | -           | 1                   | 1            |
| Above 40%       | Shares                  | -   | -          | -           | 1                   | 1            |
|                 | Asset-backed debentures | -   | 27         | -           | 5                   | 32           |
|                 | Other debentures        | -   | -          | -           | 8                   | 8            |
|                 | Total                   | -   | 27         | -           | 14                  | 41           |
| Total amount    | Shares                  | -   | -          | -           | 1                   | 1            |
|                 | Asset-backed debentures | 2   | 28         | -           | 96                  | 126          |
|                 | Other debentures        | 46  | 10         | 30          | 630                 | 716          |
| Overall total   |                         | 48  | 38         | 30          | 727                 | 843          |

\* The duration of the decline in value since the beginning of the decline means the duration since the beginning of any decline in the value of the security.

For the treatment of the valuation of securities and the distinction between a decline in value of a temporary nature and that of a non-temporary nature, see pages 50 and 51 in the 2008 Annual Report.

### The trading portfolio

The following table shows the composition of the trading portfolio as at 30 September 2009:

|                  | <b>30 September 2009</b> |              | 31 December 2008 |           | Change |           |
|------------------|--------------------------|--------------|------------------|-----------|--------|-----------|
|                  | NIS millions             |              |                  |           |        |           |
|                  | Abroad                   | In Israel    | Abroad           | In Israel | Abroad | In Israel |
| Debentures       | <b>4,539</b>             | <b>6,463</b> | 4,869            | 5,881     | (330)  | 582       |
| Shares and funds | <b>91</b>                | <b>1</b>     | 105              | -         | (14)   | 1         |
| Total            | <b>4,630</b>             | <b>6,464</b> | 4,974            | 5,881     | (344)  | 583       |

In respect of debentures for trading, realized and unrealized profits in the amount of NIS 221 million were recorded in the profit and loss statement, compared with losses of NIS 65 million in the corresponding period in 2008, and in respect of shares and funds, realized and unrealized profits were recorded in the amount of NIS 6 million, compared with realized and unrealized losses of NIS 444 million in the corresponding period in 2008.

### Investments in Securities Issued Abroad

The Group's securities portfolio includes some NIS 27.2 billion (some US\$ 7.2 billion) of securities issued abroad, all of which (but for some 3.5%) are investment grade securities, of which some 95% are rated 'A-' and above, of which some 32% are rated 'AAA'; the portfolio includes subordinated debentures issued by foreign banks having a fair value of NIS 3,136 million, some 11.5% of the total investment in securities issued abroad. Of the said portfolio, some NIS 22.0 billion (some US\$ 5.8 billion) is classified in the available-for-sale portfolio, some NIS 4.6 billion (some US\$ 1.2 billion) is classified in the securities for trading portfolio and the balance in the portfolio held to redemption.

The following table shows the composition of investments in securities issued abroad:

|  | <b>30 September 2009</b>     |                   | 31 December 2008             |                   |
|--|------------------------------|-------------------|------------------------------|-------------------|
|  | Available-for-sale portfolio | Trading portfolio | Available-for-sale portfolio | Trading portfolio |
| Balance sheet value                            |                              |                   |                              |                   |
|  | NIS millions                 |                   |                              |                   |
| Government debentures                          | <b>2,023</b>                 | <b>2,327</b>      | 2,175                        | 3,707             |
| Debentures of banks and financial institutions | <b>13,267</b>                | <b>1,898</b>      | 11,240                       | 472               |
| Asset-backed debentures                        | <b>5,656</b>                 | <b>121</b>        | 4,211                        | 207               |
| Other debentures                               | <b>452</b>                   | <b>193</b>        | 2,620                        | 483               |
| Shares and funds                               | <b>579</b>                   | <b>91</b>         | 1,260                        | 105               |
| Total  | <b>21,977</b>                | <b>4,630</b>      | 21,506                       | 4,974             |

The fair value is based on prices received from external sources. The value of most of the portfolio is calculated each month by a recognized international institution which carries on the business of calculating the fair value of financial assets for the purpose of disclosure in financial statements. This institution is independent of both the issuing entities and the marketing entities. The calculation is mainly based on the prices of transactions on active markets and on the valuation of similar transactions. The calculation reflects the price that a willing buyer in the market would pay for the securities on the basis of observable market inputs. Since only a small part of the securities are traded globally on a daily basis, the institution uses two valuation methods:

- a. Valuation at the asset group level: most of the securities are valued through yield rates (capitalization) relating to groups of assets with similar characteristics (according to country, sector, type of asset, rating, etc.); in most cases, by considering the information available in the market, generally by reference to the relevant index.
- b. Valuation and quotations for specific securities: the other securities are valued in a specific manner (valuation of the issuer and of the individual security) on the basis of direct price quotations regarding the security's spread or regarding the specific issuer. A small part of the assets in this group are valued only on the basis of price quotations from very active markets (primarily government debentures, which have active market makers).

The CLO portfolio, which constitutes a relatively small part of the securities portfolio, is valued by a professional external entity, whose business is the valuation of this type of instrument. Since there is no active market in these instruments, the valuation is based on a model. The Bank validated the model and ensured, to a reasonable degree of certainty, the accuracy of the fair value. The validation includes, *inter alia*, an examination of the systemic-logical connection between the data and the valuation, reference to factors material to the valuation and the validity of the data and the parameters on which the valuation was based. Internal models were not used for the purpose of valuing securities.

According to generally accepted accounting principles, a temporary decline in value in the available-for-sale securities portfolio is charged to shareholders' equity, while a decline in value which is of a non-temporary nature is charged to the profit and loss statement.

See also section 2 below on page 47.

The Management of the Bank estimates that the decline in the value of the available-for-sale portfolio is mostly temporary in nature and the results as of the end of the quarter support this approach. From the time the investments were made, the Bank's intention was to hold them until maturity. The Bank intends, and is able, to continue to hold the investments until the expected return of the full cost of the assets or until maturity. Therefore, this decline in value is charged to shareholders' equity. The total decline charged to shareholders' equity in respect of securities issued abroad, from the date of purchase until 30 September 2009, amounts to some NIS 454 million (some NIS 290 million after taxes). During the first nine months of 2009, the negative capital fund was reduced by NIS 887 million (an increase in the negative capital fund of NIS 1,298 million in the first quarter, a decrease in the negative capital fund of NIS 1,314 million in the second quarter, and a decrease in the negative capital fund of NIS 871 million in the third quarter). Most of the movement relates to an increase in value of subordinated debentures issued by overseas banks, as explained below.

In addition to the temporary increase in value which was recorded in shareholders' equity, a decline in value in the amount of some NIS 151 million was charged to the profit and loss account during the first nine months of 2009, all in the first half of the year.

The following table shows the fair value as at 30 September 2009 of debentures of banks and financial institutions abroad (excluding asset-backed securities):

|                                  | AAA to<br>AA- | A+    | A     | A-    | BBB+<br>to BBB- | BB+ to<br>B- | Unrated | Total  |
|----------------------------------|---------------|-------|-------|-------|-----------------|--------------|---------|--------|
| In NIS millions                  |               |       |       |       |                 |              |         |        |
| United Kingdom                   | 269           | 395   | 607   | -     | -               | -            | -       | 1,271  |
| Austria                          | -             | -     | 454   | -     | -               | -            | -       | 454    |
| Italy                            | -             | -     | 262   | 6     | -               | -            | 39      | 307    |
| Ireland                          | 23            | -     | 239   | -     | 89              | -            | -       | 351    |
| Belgium                          | -             | -     | 378   | -     | -               | -            | -       | 378    |
| Germany                          | 188           | 646   | -     | 4     | 94              | -            | -       | 932    |
| Netherlands                      | 586           | -     | 617   | 273   | 28              | -            | -       | 1,504  |
| Luxembourg                       | -             | 376   | 144   | -     | -               | -            | -       | 520    |
| Spain                            | 11            | 104   | 70    | 141   | -               | -            | -       | 326    |
| Portugal                         | -             | -     | -     | 17    | -               | -            | -       | 17     |
| Finland                          | -             | 56    | -     | -     | -               | -            | -       | 56     |
| France                           | 252           | 93    | 91    | -     | -               | -            | -       | 436    |
| Switzerland                      | 7             | 20    | 155   | -     | -               | -            | -       | 182    |
| Australia                        | 433           | -     | 119   | -     | -               | -            | -       | 552    |
| Sweden                           | 121           | -     | 366   | -     | -               | -            | -       | 487    |
| New Zealand                      | 456           | -     | -     | -     | -               | -            | -       | 456    |
| Other (1)                        | 70            | 225   | 169   | 91    | -               | 26           | 193     | 774    |
| United States                    |               |       |       |       |                 |              |         |        |
| – by bank                        |               |       |       |       |                 |              |         |        |
| Citigroup Inc. NY                | -             | 356   | -     | 625   | -               | -            | -       | 981    |
| Chase Manhattan Bank N.A.        | -             | 897   | -     | -     | -               | -            | -       | 897    |
| Merrill Lynch International B.A. | -             | -     | 498   | -     | -               | -            | -       | 498    |
| Bank of America                  | -             | 176   | 642   | -     | -               | -            | -       | 818    |
| Goldman, Sachs and Co.           | -             | -     | 290   | -     | -               | -            | -       | 290    |
| Wachovia International Banking   | 508           | -     | -     | -     | -               | -            | -       | 508    |
| Wells Fargo Bank N.A.            | 388           | -     | -     | -     | -               | -            | -       | 388    |
| Morgan Stanley                   | -             | -     | 351   | -     | -               | -            | -       | 351    |
| United States                    |               |       |       |       |                 |              |         |        |
| – other (2)                      | 318           | 197   | 707   | -     | 195             | 19           | 58      | 1,494  |
| Total                            | 3,630         | 3,541 | 6,159 | 1,157 | 406             | 45           | 290     | 15,228 |

(1) This amount includes investments in 5 countries

(2) This amount includes investments in 24 banks in the United States.

(3) Including subordinated debentures the fair value of which as at 30 September 2009 was NIS 3,136 million (including the available-for-sale and trading portfolios).

## 1. Investments in foreign asset-backed securities

The Group's securities portfolio includes some NIS 5.8 billion (some US\$ 1.5 billion) of asset-backed securities (both mortgage-backed and non-mortgage-backed), all of which (save for 5%) are rated 'A-' and above, of which some 83% are rated 'AAA'. Of the said portfolio, some NIS 5.7 billion (some US\$ 1.5 billion) is classified in the available-for-sale portfolio, and the balance in the securities for trading and the holding to redemption portfolios.

The following table shows a summary of investments in asset-backed securities in the available-for-sale portfolio as at 30 September 2009:

|  | Adjusted Cost | Unrealized profits | Unrealized losses | Balance sheet value (fair value) |
|--|---------------|--------------------|-------------------|----------------------------------|
|  | NIS millions  |                    |                   |                                  |
| MBS - mortgage-backed securities                         | 4,599         | 53                 | (61)              | 4,591                            |
| ABS-asset-backed securities (other than mortgage-backed) | 944           | 186                | (65)              | 1,065                            |
| Of which: CLO  | 761           | 153                | (57)              | 857                              |
| SCDO   | 99            | 26                 | (4)               | 121                              |
| other  | 84            | 7                  | (4)               | 87                               |
| Total  | 5,543         | 239                | (126)             | 5,656                            |

The Group's portfolio of available-for-sale investments in foreign asset-backed securities as of 30 September 2009 includes investments in mortgage-backed securities in the total amount of some NIS 4.6 billion. 99% of the mortgage-backed securities in the available-for-sale portfolio are guaranteed or directly issued by United States federal agencies (FNMA, FHLMC, GNMA). FNMA and FHLMC have come under governmental protection under the U.S. administration's rescue plan and the GNMA debentures have government guarantees.

As of 30 September 2009, the accumulated net decrease in value charged to shareholders' equity resulting from the mortgage-backed securities portfolio was some NIS 8 million.

The total of the mortgage-backed securities that are not (U.S.) government guaranteed and are not backed by American federal entities in both the available-for-sale and trading portfolios, amounts to some NIS 94 million.

The projected term to maturity for all the mortgage-backed securities portfolio is some 2.6 years, on average.

In addition to the mortgage-backed securities, the Group's available-for-sale portfolio also includes other securities that are backed by assets other than mortgages (car financing credit and other types of credit), in the amount of some NIS 1,065 million. All these securities, save for 8.9%, are rated 'A-' and above, of which 27% are rated 'AAA'. This portfolio includes, *inter alia*, SCDOs in the amount of some NIS 121 million, and CLOs in the amount of some NIS 857 million. The projected term to maturity of the portfolio of securities that are backed by assets other than mortgages is some 4.9 years on average.

The Management of the Bank estimates, and on the basis of examination according to the criteria detailed on pages 50 to 51 of the Annual Report for 2008, that the decline in the value of the portfolio of securities that are backed by assets other than mortgages is partly of a temporary nature. This part was recorded in shareholders' equity. As of 30 September 2009, the increase in value recorded in shareholders' equity attributed to the portfolio of securities backed by assets other than mortgages totalled some NIS 121 million (some NIS 77 million after tax).

The total portfolio of asset-backed securities of the SDCO type amounted to NIS 121 million. A decrease in value of NIS 29 million was recorded in the profit and loss statement in respect of this portfolio in the first nine months of 2009.

The total portfolio of asset-backed securities of the CLO type amounted to NIS 857 million. An increase in value of NIS 196 million was recorded in shareholders' equity in respect of these securities in the first nine months of 2009, and a decrease in value in the amount of NIS 17 million was charged to the profit and loss statement.

The charge to profit and loss in respect of these two portfolios was made on the basis of the policy detailed in the critical accounting policies section on pages 50 to 51 of the Annual Report for 2008, although as at the date of publication of this Report, there has been only one credit failure in the SCDO-type asset-backed securities which was written down to 0 in the books, and there have been no credit failures in the CLO-type asset-backed securities.

The securities for trading portfolio includes investments in asset-backed securities in the amount of some NIS 121 million (US\$ 32 million), of which some NIS 105 million is invested in mortgage-backed securities and some NIS 16 million is invested in other asset-backed securities. This portfolio includes securities that are backed by sub-prime mortgages in the amount of NIS 3 million (US\$ 0.8 million), 38% of which are rated 'AAA' and the balance 'BBB'. Any difference which may arise between fair value and the adjusted cost is charged to the profit and loss statement.

For the definition of asset-backed securities see Note 3 to the Financial Statements for 2008.

## **2. Investments in other (non asset-backed) foreign securities**

The Group's securities portfolio as of 30 September 2009 includes some NIS 21.4 billion (some US\$ 5.7 billion) of non-asset-backed securities, which include mainly securities issued by banks and financial institutions, including subordinated debentures, the balance being securities issued by the governments of the USA, France and Israel, and securities of Israeli companies that were issued abroad. Of these securities, NIS 16.3 billion (US\$ 4.3 billion) are classified in the available-for-sale portfolio, and some NIS 4.5 billion in the securities for trading portfolio. Of these securities, 97.5% are rated 'A-' or above, of which 21.6% are rated 'AAA'.

For further details regarding exposure to overseas banks and financial institutions see page 101.

The Bank estimates that the decline in the prices of these securities is mostly of a temporary nature, and most of the decline in value was therefore charged to shareholders' equity. This was based on the criteria described under critical accounting policies at pages 50 and 51 of the 2008 Annual Report, and took into consideration additional parameters such as the involvement and backing – including direct capital investment – of governments for insuring the strength of these and other banks in their countries, and market expectations regarding the risk of bank failures, as expressed in the prices of the credit derivatives (CDS), as well as the increase in value after the date of the Financial Statements, a high credit rating (A and higher) and stress test survival analyses.

As of 30 September 2009, the accumulated decrease in value charged to shareholders' equity in respect of non-asset-backed securities issued abroad in the available-for-sale portfolio amounted to NIS 543 million (NIS 346 million after tax), after a reduction of NIS 729 million during the first nine months of 2009.

The vast majority of the debentures which are not asset-backed securities and which were issued abroad are debentures issued by banks.



The bank debentures portfolio is invested in Western European countries (45%) and in the United States (46%), in large and well-known banks. Of this, slightly under US\$ 900 million is invested in subordinated debentures. The debentures of this type that are held by the Group do not include a component that is convertible into shares and their final maturity dates are in less than ten years. The issuer of this type of debenture generally holds an early call option with respect to the debentures. If the issuer does not exercise the early call option, the debentures' duration is extended by a number of years (generally three to five) and the interest rate rises (the "step-up" mechanism). Due to the low level of liquidity in the world markets, it is not yet clear whether the banks will behave as they have in the past by exercising the call options or whether the debentures' redemption periods will be extended and the interest rates will rise.

Most of the decline in the value of securities issued abroad has been with respect to subordinated debentures. As of 30 September 2009, the fair value of the available-for-sale subordinated debenture portfolio of some NIS 2.9 billion as at the date of the Report is some NIS 2.7 billion. Since a material component of the decline in value results from the increased probability that the issuer will utilize its right not to exercise the early call option and thus extend the average duration of the debentures, and since the Bank has carried out individual examinations of the repayment ability of each of the banks in this group, and considering the significant improvement since the date of the balance sheet, the Bank has decided that this decline in value is a temporary one. The first three quarters of the year were materially different from each other with regard to the fair value of these investments. While the first quarter was characterized by a significant decline in the fair value and a resulting increase in the negative capital fund, there was a change in direction in the second and third quarters and the entire decline in value of the first quarter was eradicated and the final result for the first nine months of 2009 was an increase in value of NIS 260 million. The contraction, from the beginning of October through the middle of November, of the spreads in the debentures, as well as the even more significant contraction in the spreads of the relevant credit derivatives (CDS) of those banks in the group for which there are CDS, supports the view that this decline in value is temporary.

The Bank intends, and is able, to continue to hold these debentures until maturity or at least until the return of their value.

|  | Fair value              |                    |                     |                        | Difference in<br>fair value<br>during the first<br>nine months |
|--|-------------------------|--------------------|---------------------|------------------------|--|
|  | 30<br>September<br>2009 | 30<br>June<br>2009 | 31<br>March<br>2009 | 31<br>December<br>2008 |  |
| NIS millions   |                         |                    |                     |                        |  |
| Total subordinated bank<br>debentures issued<br>abroad   | 2,650                   | 2,542              | 2,261               | 2,614                  | 36   |
| Of this, subordinated<br>debentures that<br>declined in value by<br>more than 35% as of<br>30 September 2009 | 24                      | 34                 | 1,073               | 24                     | -  |

In addition, the Bank holds long-term senior debentures in the amount of some NIS 324 million of an American bank (Citi). As of 30 September 2009, these debentures, because of their long maturity period, declined in value by 14.0%. The involvement of the administration in the management of Citi and in ensuring its stability, as well as an individual examination of its capabilities (in addition to the examination of its value by the US authorities) indicate that the decline in value is not permanent. From the balance-sheet date through the middle of November, these debentures too recovered to some extent.

In addition to the temporary decline in value which was charged to shareholders' equity, NIS 106 million (NIS 69 million after tax) was charged to the profit and loss statement with respect to such securities in the available-for-sale portfolio during the first nine months of 2009, all in the first half of the year.

In addition to those in the available-for-sale portfolio, there are also non-asset backed securities in the trading portfolio. The trading portfolio includes mainly securities of banks and financial institutions, and securities portfolios that are managed by external investment managers, and securities funds. All the securities in the trading portfolio are investment grade securities, and some 99% of them are rated 'A' and above. The value of the trading portfolio which is non-asset backed as at 30 September 2009 amounted to some NIS 4.5 billion (US\$ 1.2 billion). The difference between the fair value and the adjusted cost, to the extent there is such, is charged to the profit and loss statement.

### **Investments in corporate debentures issued in Israel**

Investments in debentures issued in Israel amounted to NIS 29.3 billion on 30 September 2009, of which NIS 28.3 billion was in debentures issued by the government of Israel, and the balance of NIS 1.0 billion was in corporate debentures. Of the corporate debentures 94.2% are rated 'A-' and above, of which 76.2% are rated 'AA-' and above. The corporate debenture portfolio is spread among various branches of the economy. The investment of some 18.0% of the portfolio in the real estate sector is the largest. As of 30 September 2009, investments in corporate debentures amounted to NIS 0.8 billion in the available-for-sale portfolio, and the balance was in the trading portfolio.

All the corporate debentures in the trading portfolio and part of those in the available-for-sale portfolio are listed and traded on the Stock Exchange. Some 64.7% of the corporate debentures in the available-for-sale portfolio are not listed. The valuation of the listed corporate debentures is based on market prices on the stock exchange, and the non-listed corporate debentures are valued by a professional entity which carries on business as a valuer and which is a subsidiary of the Bank. Since there is no active market in these debentures, the valuation is based on a model. The Bank validated the model and ensured, to a reasonable degree of certainty, the accuracy of the fair value. The validation includes, *inter alia*, an examination of the systemic-logical connection between the data and the valuation, reference to factors material to the valuation and the validity of the data and the parameters on which the valuation was based, including specific reference to the results of the model of the "Sha'arei Ribit" company, which values these assets for use in the financial statements of financial institutions.

The test for determining whether a decline in value of a debenture in the available-for-sale portfolio is of a non-temporary nature is based primarily on the criteria set out in accounting policy at pages 50 to 51 of the 2008 Annual Report.

Out of the total amount of NIS 0.8 billion in the corporate debenture portfolio in the available-for-sale portfolio, the positive capital fund amounts to NIS 28 million, and the negative fund amounts to NIS 17 million, with the highest decline in value being 16.0%. The Bank estimates that the decline in the value of the corporate debentures portfolio is mainly of a temporary nature, on the basis of an individual examination of each debenture. The Bank intends, and is able, to continue to hold the debentures until the restoration of their adjusted cost value and even until maturity.

### **3. Investments in shares and funds**

Total investments in shares and funds amounted to some NIS 2,465 million as at 30 September 2009, of which NIS 1,458 million was in listed shares and NIS 1,007 million was

in non-listed shares. Of the total investment, NIS 2,373 million is classified as available-for-sale and NIS 92 million is classified in the trading portfolio.

The following table sets out the principal investments in shares and funds recorded in the securities item (available-for-sale portfolio)<sup>(1)</sup>:

|   | The Bank's share on a consolidated basis in the paid up capital giving the right to receive profits |                  | Value of the investment in the consolidated balance sheet |                  |
|---|---|------------------|---|------------------|
|   | <b>30 September 2009</b>  | 31 December 2008 | <b>30 September 2009</b>                                  | 31 December 2008 |
|   | %   |                  | NIS millions  |                  |
| Migdal Insurance and Financial Holdings Ltd. <sup>(2)</sup> | <b>9.85</b>   | 9.85             | <b>621</b>  | 411              |
| Africa Israel Properties Ltd.                               | <b>4.3</b>  | 4.3              | <b>35</b>   | 15               |
| Super-Pharm (Israel) Ltd. *                                 | <b>18.0</b>   | 18.0             | <b>182</b>  | 182              |
| Hot – Cable Communications Systems Ltd. <sup>(3)</sup>      | -   | 14.96            | -   | 239              |
| Otzar Hityashvuth Hayehudim B.M.                            | <b>8.62</b>   | 8.62             | <b>72</b>   | 29               |
| Bezeq – Israel Communications Company Ltd. <sup>(4)</sup>   | <b>2.75</b>   | 4.23             | <b>507</b>  | 683              |
| Union Bank of Israel Ltd. <sup>(5)</sup>                    | -   | 6.46             | -   | 101              |
| Tower Semiconductor capital notes                           | -   | -                | <b>49</b>   | 49               |
| Visa International  | -   | -                | <b>35</b>   | 27               |
| CLS Bank  | -   | -                | <b>21</b>   | 21               |
| Funds   | -   | -                | <b>285</b>  | 991              |
| Apax  | -   | -                | <b>43</b>   | 56               |
| Other   | -   | -                | <b>615</b>  | 520              |
| <b>Total</b>  | -   | -                | <b>2,465</b>  | 3,324            |

\* not listed

(1) See page 72 for details of non-banking investments presented on the equity basis.

The following table shows investments (positions) in shares and funds in the securities item (available-for-sale portfolio and trading portfolio) (in NIS millions):

|  | Balance sheet amount     |                  |
|--|--------------------------|------------------|
|  | <b>30 September 2009</b> | 31 December 2008 |
| Listed shares                            | <b>1,383</b>             | 1,718            |
| Funds according to quote by counterparty | <b>360</b>               | 988              |
| Unlisted shares                          | <b>722</b>               | 618              |
| <b>Total</b>                             | <b>2,465</b>             | 3,324            |

(2) For additional details see page 73.

(3) On 3 August 2009, the Bank sold 11,376,902 ordinary shares of Hot-Cable Communications Systems Ltd., which had been held by the Bank to Cool Holding Ltd. for a total amount of NIS 381,126,210. An after-tax profit from the sale of the shares of some NIS 115 million was recorded.

- (4) In accordance with the Supervisor of Banks' July 2003 instructions, the classification of credit granted to a certain customer for the financing of the purchase of shares in Bezeq was changed from the credit to the public item to the securities item. On 10 August 2009, the customer's receiver announced that he had completed a transaction for the sale of 155,000,000 ordinary shares of NIS 1 par value each in the company, constituting 5.849% of Bezeq's share capital, and that the consideration, some NIS 1,137 million after deducting commissions and expenses, would be used to reduce the customer's debts to the banks, in accordance with each bank's share in the financing of the purchase of the Bezeq shares in 1999. The Bank's share in this consideration, after deducting commissions and expenses, amounted to some NIS 273 million and the net profit amounted to some NIS 55 million.

On 19 October 2009, the customer's receiver announced that he had completed a transaction for the sale of 120,000,000 ordinary shares in the company of NIS 1 par value each, constituting 4.52% of Bezeq's share capital, and that the consideration, some NIS 977 million after deducting commissions and expenses, would be used to reduce the customer's debts to the banks, in accordance with each bank's share in the financing of the purchase of the Bezeq shares in 1999. The Bank's share in this consideration, after deducting commissions and expenses, amounted to some NIS 233 million and the net profit totaled some NIS 60 million.

On 9 November 2009, the customer's receiver announced that he had completed a transaction for the sale of all the Bezeq shares owned by the customer. The total number of shares sold amounted to some 184,331,617 ordinary shares of NIS 1 par value each, constituting 6.94% of Bezeq's share capital, and the consideration would amount to some NIS 1.5 billion. The Bank's share in this consideration will amount to some NIS 242 million and the net profit to some NIS 27 million.

For details regarding a claim for declaratory judgments filed by the customer against 7 banks, including the Bank, see note 6.C.1.Q

#### **(5) Union Bank**

On 17 November 2003, an agreement was signed between the Bank, Sherodar Assets Ltd. ("Sherodar") and Yeshayu Landau Holdings (1993) Ltd. ("Landau") for the extension of the put option and of the call option that were granted in an agreement dated 18 November 1999, in respect of the balance of the shares in Union Bank held by the Bank, for a period ending on 17 November 2010.

On 11 May 2009, the Bank gave Sherodar and Landau notice regarding the exercise of the put option.

The transaction was completed on 28 June 2009 and the Bank sold the said shares, constituting all of the Bank's holdings in Union Bank, to Landau and Sherodar, in consideration of a total amount of some NIS 108 million. The Bank's profit from the sale of the said shares is some NIS 17 million, net.

- (6) On 21 August 2009, the Bank signed an agreement with the Scailex Corporation Ltd. ("Scailex") for the acquisition of 7,677,037 ordinary shares constituting 4.99% of the issued and paid-up share capital of Partner Communications Ltd. (on an undiluted basis and after neutralizing dormant shares), for a consideration of NIS 514,553,405. The agreement includes standard minority protection rights and an option to purchase debentures convertible into Scailex shares in the amount of some NIS 103 million.

Leumi Partners Ltd. (a wholly owned subsidiary of the Bank) acted as an investment house in all aspects related to this transaction, including vis-à-vis additional potential investors and therefore Scailex agreed to pay Leumi Partners a finders fee in the amount of US\$ 3 million to be paid upon the completion of the transaction.

On 18 October 2009, in exercise of the option, Leumi Partners was allocated NIS 102,705,270 par value convertible debentures (Series 1) of Scailex at a price of NIS 1.002 for every NIS 1 par value, for a total consideration of NIS 102,910,681 (the "Debentures"). The Debentures were allocated through the expansion of the debenture series (Series 1), all in accordance with the provisions of the law, and the shelf prospectus published by Scailex on 21 August 2009. The banks and Scailex agreed that notwithstanding the provisions of the agreement, the exercise of the option and the allocation of the Debentures would not be conditional on the completion and execution of the transaction which is the subject of the agreement, and should the transaction not

be completed, the provisions detailed in the Debentures' trust deed regarding such an event would apply.

The transaction between the Bank and Scailex was completed on 28 October 2009, and thereunder Leumi Partners Ltd. acquired 7,667,037 ordinary shares from Scailex, constituting 4.99% of the issued and paid-up capital of Partner Communications Ltd. (on an undiluted basis and after neutralizing dormant shares), for a consideration of NIS 514,887,507.

- (7) On 13 September 2009, Leumi Partners Ltd. (a wholly owned subsidiary of the Bank) signed an agreement with GN Communication Industries Ltd. (a company wholly owned by Ms. Gal Naor) (the "Purchaser") for the sale of 4,124 ordinary shares of Keshet Broadcasting Ltd. ("Keshet") and 20 deferred shares of Keshet, constituting 20% of Keshet's issued and paid-up capital, and for the sale of rights deriving from the owner's loans of NIS 6.5 million that it had extended to Keshet (the "Sold Shares and Rights" and the "Purchase Agreement".) The Purchaser will pay US\$ 6 million for the Sold Shares and Rights. The Purchase Agreement is subject to conditions precedent which include receipt of approvals from the Council of the Second Authority for Television and Radio, Bank Hapoalim Ltd. and the Board of Directors of Keshet.

### **Other assets**

On 30 September 2009, other assets amounted to NIS 9.6 billion, compared with NIS 13.5 billion at the end of 2008, a decrease of 28.8%. The decrease in this item resulted primarily from payments received from customers in respect of transactions and from a decrease in the balance of the fair value of derivative instruments, the transactions in which had been carried out with or for customers, of some NIS 3.2 billion.

## Operational Segments in the Group

The Group operates in various operational segments through the Bank and its subsidiaries, in all fields of banking and financial services. Furthermore, the Group invests in non-banking corporations that operate in various fields, including insurance, real estate, shipping, energy, industry and others.

The operational segments are defined in accordance with the characteristics determined by the Bank of Israel. A detailed description of the operational segments and the manner of their measurement is provided in the Annual Report for 2008.

The following table sets out the net operating profit according to operational segments:

| Segments  | For the three months ending |                         |        | For the nine months ending |                         |        |
|---|-----------------------------|-------------------------|--------|----------------------------|-------------------------|--------|
|   | 30<br>September<br>2009     | 30<br>September<br>2008 | Change | 30<br>September<br>2009    | 30<br>September<br>2008 | Change |
|   | NIS millions                |                         | %      | NIS millions               |                         | %      |
| Households  | <b>97</b>                   | 181                     | (46.4) | <b>205</b>                 | 692                     | (70.4) |
| Small businesses                                    | <b>37</b>                   | 74                      | (50.0) | <b>155</b>                 | 276                     | (43.8) |
| Corporate banking                                   | <b>314</b>                  | 60                      | 423.3  | <b>667</b>                 | 445                     | 49.9   |
| Commercial banking                                  | <b>54</b>                   | 102                     | (47.1) | <b>246</b>                 | 374                     | (34.2) |
| Private banking                                     | <b>54</b>                   | (21)                    | +      | <b>161</b>                 | 53                      | 203.8  |
| Financial management –<br>capital markets and other | <b>(22)</b>                 | (480)                   | +      | <b>36</b>                  | (565)                   |        |
| Total   | <b>534</b>                  | (84)                    | +      | <b>1,470</b>               | 1,275                   | 15.3   |

The following table sets out the net operating profit according to operational segments, after neutralizing special salary expenses:

| Segments  | For the nine months ending on |                      |        | Contribution to<br>profit |
|---|-------------------------------|----------------------|--------|---------------------------|
|   | 30 September<br>2009          | 30 September<br>2008 | Change |                           |
|   | (NIS millions)                |                      | %      |                           |
| Households  | <b>193</b>                    | 517                  | (62.7) | 13.9                      |
| Small businesses                                    | <b>153</b>                    | 265                  | (42.3) | 11.1                      |
| Corporate banking                                   | <b>666</b>                    | 447                  | 49.0   | 48.1                      |
| Commercial banking                                  | <b>244</b>                    | 354                  | (31.1) | 17.6                      |
| Private banking                                     | <b>160</b>                    | 52                   | 207.7  | 11.6                      |
| Financial management –<br>capital markets and other | <b>(32)</b>                   | (288)                | +      | (2.3)                     |
| Total   | <b>1,384</b>                  | 1,347                | 2.7    | 100.0                     |

Explanations for the changes in profitability are provided below.

## 1. Households

The following tables set out a summary of the profit and loss of the households segment:

|   | Banking<br>and<br>finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Overseas<br>Activities | Total     |
|---|---------------------------|-----------------|-------------------|----------------|------------------------|-----------|
| <b>For the three months ending 30 September 2009</b>    |                           |                 |                   |                |                        |           |
| NIS millions  |                           |                 |                   |                |                        |           |
| <b>Profit (loss) from net interest income:</b>          |                           |                 |                   |                |                        |           |
| From external sources                                   | (450)                     | 40              | 1                 | 637            | (1)                    | 227       |
| Inter-segmental   | 847                       | (3)             | 1                 | (552)          | (3)                    | 290       |
| <b>Operating and other income:</b>                      |                           |                 |                   |                |                        |           |
| From external sources                                   | 151                       | 115             | 139               | 30             | 2                      | 437       |
| Inter-segmental   | -                         | 57              | -                 | 5              | -                      | 62        |
| Total income  | 548                       | 209             | 141               | 120            | (2)                    | 1,016     |
| Provisions for doubtful debts                           | 69                        | 5               | -                 | 1              | -                      | 75        |
| <b>Operating and other expenses:</b>                    |                           |                 |                   |                |                        |           |
| External  | 528                       | 136             | 77                | 51             | 6                      | 798       |
| Inter-segmental   | 1                         | (2)             | -                 | 6              | -                      | 5         |
| Operating profit (loss) before taxes                    | (50)                      | 70              | 64                | 62             | (8)                    | 138       |
| Tax provision (benefit) on operating profit             | (32)                      | 21              | 24                | 25             | (4)                    | 34        |
| Operating profit (loss) after taxes                     | (18)                      | 49              | 40                | 37             | (4)                    | 104       |
| Minority interests in profits of consolidated companies | -                         | (7)             | -                 | -              | -                      | (7)       |
| <b>Net (loss) profit</b>                                | <b>(18)</b>               | <b>42</b>       | <b>40</b>         | <b>37</b>      | <b>(4)</b>             | <b>97</b> |

  

|   | Banking<br>and<br>finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Overseas<br>Activities | Total      |
|---|---------------------------|-----------------|-------------------|----------------|------------------------|------------|
| <b>For the three months ending 30 September 2008</b>    |                           |                 |                   |                |                        |            |
| NIS millions  |                           |                 |                   |                |                        |            |
| <b>Profit from net interest income:</b>                 |                           |                 |                   |                |                        |            |
| From external sources                                   | (686)                     | 50              | 1                 | 740            | (5)                    | 100        |
| Inter-segmental   | 1,207                     | (23)            | (1)               | (599)          | 9                      | 593        |
| <b>Operating and other income:</b>                      |                           |                 |                   |                |                        |            |
| From external sources                                   | 163                       | 111             | 115               | 32             | 2                      | 423        |
| Inter-segmental   | 10                        | 64              | -                 | 3              | -                      | 77         |
| Total income  | 694                       | 202             | 115               | 176            | 6                      | 1,193      |
| Provisions for doubtful debts                           | 69                        | 5               | -                 | 24             | (1)                    | 97         |
| <b>Operating and other expenses:</b>                    |                           |                 |                   |                |                        |            |
| External  | 491                       | 97              | 46                | 57             | 6                      | 697        |
| Inter-segmental   | 12                        | 7               | -                 | 4              | -                      | 23         |
| Operating profit before taxes                           | 122                       | 93              | 69                | 91             | 1                      | 376        |
| Tax provision on operating profit                       | 97                        | 30              | 26                | 35             | -                      | 188        |
| Profit from extraordinary items after taxes             | 25                        | 63              | 43                | 56             | 1                      | 188        |
| Minority interests in profits of consolidated companies | -                         | (7)             | -                 | -              | -                      | (7)        |
| <b>Net profit</b>                                       | <b>25</b>                 | <b>56</b>       | <b>43</b>         | <b>56</b>      | <b>1</b>               | <b>181</b> |

## Households (cont.)

|  | Banking<br>and<br>finance | Credit<br>cards | Capital<br>market | Mortgages  | Overseas<br>Activities | Total       |
|--|---------------------------|-----------------|-------------------|------------|------------------------|-------------|
| <b>For the nine months ending 30 September 2009</b>              |                           |                 |                   |            |                        |             |
| NIS millions   |                           |                 |                   |            |                        |             |
| <b>Profit from net interest income:</b>                          |                           |                 |                   |            |                        |             |
| From external sources  | (816)                     | 120             | 2                 | 1,423      | (6)                    | 723         |
| Inter-segmental  | 2,021                     | (16)            | -                 | (1,172)    | 13                     | 846         |
| <b>Operating and other income:</b>                               |                           |                 |                   |            |                        |             |
| From external sources  | 457                       | 332             | 380               | 90         | 6                      | 1,265       |
| Inter-segmental  | -                         | 162             | -                 | 11         | -                      | 173         |
| Total income   | 1,662                     | 598             | 382               | 352        | 13                     | 3,007       |
| Provisions for doubtful debts                                    | 182                       | 17              | -                 | (1)        | 9                      | 207         |
| <b>Operating and other expenses:</b>                             |                           |                 |                   |            |                        |             |
| External   | 1,681                     | 389             | 222               | 151        | 20                     | 2,463       |
| Inter-segmental  | 3                         | (3)             | -                 | 13         | 0                      | 13          |
| Operating profit (loss) before taxes                             | (204)                     | 195             | 160               | 189        | (16)                   | 324         |
| Tax provision (benefit) on operating profit                      | (89)                      | 60              | 58                | 73         | (4)                    | 98          |
| Operating profit (loss) after taxes                              | (115)                     | 135             | 102               | 116        | (12)                   | 226         |
| Minority interests in profits of consolidated companies          | -                         | (21)            | -                 | -          | -                      | (21)        |
| <b>Net (loss) profit</b>   | <b>(115)</b>              | <b>114</b>      | <b>102</b>        | <b>116</b> | <b>(12)</b>            | <b>205</b>  |
| <b>% Return on equity</b>  |                           |                 |                   |            |                        | <b>6.4%</b> |
| Average balance of assets  | 15,335                    | 6,327           | 90                | 41,794     | 333                    | 63,879      |
| Of which: investments in companies included on the equity basis  | -                         | 8               | -                 | -          | -                      | 8           |
| Average balance of liabilities                                   | 113,236                   | 599             | -                 | 11,176     | 1,046                  | 126,057     |
| Average balance of risk assets                                   | 14,212                    | 6,187           | 90                | 35,859     | 355                    | 56,703      |
| Average balance of mutual funds and supplementary training funds | -                         | -               | 35,954            | -          | -                      | 35,954      |
| Average balance of securities                                    | -                         | -               | 44,134            | -          | 155                    | 44,289      |
| Average balance of other assets under management                 | 166                       | -               | -                 | 7,365      | -                      | 7,531       |
| Balance of credit to the public                                  | 15,376                    | 6,461           | 91                | 43,156     | 317                    | 65,401      |
| Balance of deposits of the public                                | 111,652                   | 26              | -                 | 6,406      | 1,000                  | 119,084     |



## Households (cont.)

|  | Banking and<br>finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Overseas<br>Activities | Total      |
|--|------------------------|-----------------|-------------------|----------------|------------------------|------------|
| For the nine months ending 30 September 2008                     |                        |                 |                   |                |                        |            |
| NIS millions   |                        |                 |                   |                |                        |            |
| <b>Profit from net interest income:</b>                          |                        |                 |                   |                |                        |            |
| From external sources  | (1,711)                | 117             | 3                 | 1,742          | (13)                   | 138        |
| Inter-segmental  | 3,221                  | (41)            | (2)               | (1,366)        | 28                     | 1,840      |
| <b>Operating and other income:</b>                               |                        |                 |                   |                |                        |            |
| From external sources  | 501                    | 331             | 342               | 92             | 6                      | 1,272      |
| Inter-segmental  | 13                     | 177             | -                 | 10             | -                      | 200        |
| Total income   | 2,024                  | 584             | 343               | 478            | 21                     | 3,450      |
| Provisions for doubtful debts                                    | 120                    | 12              | -                 | 89             | 6                      | 227        |
| <b>Operating and other expenses:</b>                             |                        |                 |                   |                |                        |            |
| External   | 1,652                  | 321             | 188               | 165            | 20                     | 2,346      |
| Inter-segmental  | 12                     | 9               | -                 | 12             | -                      | 33         |
| Operating profit (loss) before taxes                             | 240                    | 242             | 155               | 212            | (5)                    | 844        |
| Tax provision on operating profit                                | 132                    | 78              | 57                | 80             | -                      | 347        |
| Operating profit (loss) after taxes                              | 108                    | 164             | 98                | 132            | (5)                    | 497        |
| Minority interests in profits of consolidated companies          | -                      | (7)             | -                 | -              | -                      | (7)        |
| Net operating profit (loss)                                      | 108                    | 157             | 98                | 132            | (5)                    | 490        |
| Profit from extraordinary items after taxes                      | -                      | 202             | -                 | -              | -                      | 202        |
| <b>Net profit (loss)</b>   | <b>108</b>             | <b>359</b>      | <b>98</b>         | <b>132</b>     | <b>(5)</b>             | <b>692</b> |
| <b>% Return on equity</b>  | <b>22.9%</b>           |                 |                   |                |                        |            |
| Average balance of assets  | 15,453                 | 5,931           | 78                | 38,089         | 294                    | 59,845     |
| Of which: investments in companies included on the equity basis  | -                      | 8               | -                 | -              | -                      | 8          |
| Average balance of liabilities                                   | 107,256                | 421             | -                 | 12,065         | 1,022                  | 120,764    |
| Average balance of risk assets                                   | 13,361                 | 5,758           | 75                | 31,835         | 301                    | 51,330     |
| Average balance of mutual funds and supplementary training funds | -                      | -               | 33,497            | -              | -                      | 33,497     |
| Average balance of securities                                    | -                      | -               | 43,342            | -              | 142                    | 43,484     |
| Average balance of other assets under management                 | 213                    | -               | -                 | 7,925          | -                      | 8,138      |
| Balance of credit to the public as at 31 December 2008           | 15,064                 | 6,050           | 92                | 40,603         | 336                    | 62,145     |
| Balance of deposits of the public as at 31 December 2008         | 112,883                | 18              | -                 | 6,917          | 1,028                  | 120,846    |

**The following table presents data concerning new loans granted and loans refinanced for the purchase of residential apartments, while pledging residential apartments:**

|                                | <b>First nine months<br/>of 2009</b> | First nine months<br>of 2008 | <b>Change</b> |
|--------------------------------|--------------------------------------|------------------------------|---------------|
|                                | <b>NIS millions</b>                  |                              | <b>%</b>      |
| From Bank funds                | <b>6,826</b>                         | 6,936                        | (1.6)         |
| From Ministry of Finance funds |                                      |                              |               |
| Loans                          | <b>46</b>                            | 183                          | (74.9)        |
| Standing loans                 | <b>3</b>                             | 5                            | (40.0)        |
| Total new loans                | <b>6,875</b>                         | 7,124                        | (3.5)         |
| Refinanced loans               | <b>1,595</b>                         | 933                          | 71.0          |
| Total                          | <b>8,470</b>                         | 8,057                        | 5.1           |

### **Main Changes in the Scope of Operations**

Total credit to the public in the households segment increased by NIS 3,256 million, 5.2% compared with the end of 2008. Housing loans increased by 6.3%, and credit after neutralizing housing loans increased by 3.3%. Deposits of the public decreased by NIS 1,762 million, a decrease of 1.5% compared with the end of 2008.

### **Main Changes in Net Profit**

In the first nine months of 2009, net profit in the households segment totaled NIS 205 million, compared with NIS 692 million in the corresponding period in 2008, a decrease of 70.4%. The decrease in profit stems primarily from the decrease of NIS 202 million in profit from extraordinary items (from the allocation of 20% of the share capital of Leumi Card to Canit in 2008). Operating profit amounted to NIS 205 million compared with NIS 490 million in the corresponding period in 2008, a decrease of 58.2%. The decrease in profit stems mainly from a decrease in net interest income in the amount of NIS 409 million, a decrease in operating income of NIS 34 million and an increase in expenses of NIS 97 million.

Return on equity of the net profit was 6.4%.

## 2. Small Businesses

The following tables set out a summary of the profit and loss of the small businesses segment:

|  | Banking<br>and finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Real<br>estate | Overseas activities<br>Banking<br>and Finance | Real<br>estate | Total     |
|--|------------------------|-----------------|-------------------|----------------|----------------|---|----------------|-----------|
| <b>For the three months ending 30 September 2009</b> |                        |                 |                   |                |                |   |                |           |
| NIS millions   |                        |                 |                   |                |                |   |                |           |
| <b>Profit from net interest income:</b>              |                        |                 |                   |                |                |   |                |           |
| From external sources                                | 189                    | 7               | 0                 | 2              | 70             | 11  | 1              | 280       |
| Inter-segmental                                      | (34)                   | 0               | 0                 | (2)            | (23)           | (17)  | -              | (76)      |
| <b>Operating and other income:</b>                   |                        |                 |                   |                |                |   |                |           |
| From external sources                                | 68                     | 41              | 7                 | -              | 11             | 3   | 1              | 131       |
| Inter-segmental                                      | -                      | (27)            | -                 | -              | -              | -   | -              | (27)      |
| Total income   | 223                    | 21              | 7                 | -              | 58             | (3)   | 2              | 308       |
| Provisions for doubtful debts                        | 34                     | 1               | -                 | -              | 22             | 6   | -              | 63        |
| <b>Operating and other expenses:</b>                 |                        |                 |                   |                |                |   |                |           |
| External   | 140                    | 17              | 2                 | -              | 21             | 8   | 1              | 189       |
| Inter-segmental                                      | (1)                    | 1               | -                 | -              | -              | -   | -              | -         |
| Operating profit (loss) before taxes                 | 50                     | 2               | 5                 | -              | 15             | (17)  | 1              | 56        |
| Tax provision (benefit) on operating profit          | 14                     | 1               | 2                 | -              | 6              | (5)   | 1              | 19        |
| <b>Net profit (loss)</b>                             | <b>36</b>              | <b>1</b>        | <b>3</b>          | <b>-</b>       | <b>9</b>       | <b>(12)</b>                                   | <b>-</b>       | <b>37</b> |

|  | Banking<br>and finance | Credit<br>cards | Capital<br>market | Mortgages | Real<br>estate | Overseas<br>activities | Total     |
|--|------------------------|-----------------|-------------------|-----------|----------------|------------------------|-----------|
| <b>For the three months ending 30 September 2008</b> |                        |                 |                   |           |                |                        |           |
| NIS millions   |                        |                 |                   |           |                |                        |           |
| <b>Profit from net interest income:</b>              |                        |                 |                   |           |                |                        |           |
| From external sources                                | 215                    | 3               | 1                 | 1         | 87             | 17                     | 324       |
| Inter-segmental                                      | (41)                   | (1)             | (1)               | (1)       | (41)           | (11)                   | (96)      |
| <b>Operating and other income:</b>                   |                        |                 |                   |           |                |                        |           |
| From external sources                                | 69                     | 13              | 5                 | -         | 12             | 4                      | 103       |
| Inter-segmental                                      | 1                      | (6)             | -                 | -         | -              | -                      | (5)       |
| Total income   | 244                    | 9               | 5                 | -         | 58             | 10                     | 326       |
| Provisions for doubtful debts                        | 34                     | -               | -                 | -         | 5              | 4                      | 43        |
| <b>Operating and other expenses:</b>                 |                        |                 |                   |           |                |                        |           |
| External   | 117                    | 3               | 1                 | -         | 17             | 8                      | 146       |
| Inter-segmental                                      | 3                      | (1)             | -                 | -         | -              | -                      | 2         |
| Operating profit (loss) before taxes                 | 90                     | 7               | 4                 | -         | 36             | (2)                    | 135       |
| Tax provision (benefit) on operating profit          | 45                     | 2               | 2                 | -         | 13             | (1)                    | 61        |
| <b>Net profit (loss)</b>                             | <b>45</b>              | <b>5</b>        | <b>2</b>          | <b>-</b>  | <b>23</b>      | <b>(1)</b>             | <b>74</b> |

## Small businesses (cont.)

|  | Banking and<br>finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Real<br>estate | Overseas activities    |                | Total        |
|--|------------------------|-----------------|-------------------|----------------|----------------|------------------------|----------------|--------------|
|  | Banking and<br>finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Real<br>estate | Banking<br>and finance | Real<br>estate | Total        |
| <b>For the nine months ending 30 September 2009</b>              |                        |                 |                   |                |                |                        |                |              |
| NIS millions   |                        |                 |                   |                |                |                        |                |              |
| <b>Profit from net interest income:</b>                          |                        |                 |                   |                |                |                        |                |              |
| From external sources  | 525                    | 14              | 1                 | 5              | 191            | 42                     | 2              | 780          |
| Inter-segmental  | (63)                   | (2)             | -                 | (4)            | (53)           | (30)                   | -              | (152)        |
| <b>Operating and other income:</b>                               |                        |                 |                   |                |                |                        |                |              |
| From external sources  | 205                    | 72              | 17                | 0              | 33             | 11                     | 1              | 339          |
| Inter-segmental  | -                      | (44)            | -                 | -              | -              | -                      | -              | (44)         |
| Total income   | 667                    | 40              | 18                | 1              | 171            | 23                     | 3              | 923          |
| Provision for doubtful debts                                     | 103                    | 1               | -                 | -              | 36             | 7                      | 3              | 150          |
| <b>Operating and other expenses:</b>                             |                        |                 |                   |                |                |                        |                |              |
| External   | 402                    | 31              | 7                 | -              | 63             | 27                     | 2              | 532          |
| Inter-segmental  | -                      | 2               | -                 | -              | -              | -                      | -              | 2            |
| Operating profit (loss) before taxes                             | 162                    | 6               | 11                | 1              | 72             | (11)                   | (2)            | 239          |
| Tax provision (benefit) on operating profit                      | 57                     | 2               | 4                 | -              | 26             | (5)                    | -              | 84           |
| <b>Net profit (loss)</b>   | <b>105</b>             | <b>4</b>        | <b>7</b>          | <b>1</b>       | <b>46</b>      | <b>(6)</b>             | <b>(2)</b>     | <b>155</b>   |
| <b>% Return on equity</b>  |                        |                 |                   |                |                |                        |                | <b>19.0%</b> |
| Average balance of assets  | 11,196                 | 654             | 24                | 151            | 4,755          | 720                    | 93             | 17,593       |
| Average balance of liabilities                                   | 11,834                 | 980             | -                 | -              | 1,993          | 570                    | 100            | 15,477       |
| Average balance of risk assets                                   | 8,300                  | 635             | 27                | 153            | 4,783          | 762                    | 87             | 14,747       |
| Average balance of mutual funds and supplementary training funds | -                      | -               | 1,483             | -              | -              | -                      | -              | 1,483        |
| Average balance of securities                                    | -                      | -               | 3,136             | -              | -              | 2                      | -              | 3,138        |
| Average balance of other assets under management                 | 392                    | -               | -                 | -              | -              | -                      | -              | 392          |
| Balance of credit to the public                                  | 10,973                 | 722             | 14                | 148            | 4,662          | 674                    | 90             | 17,283       |
| Balance of deposits of the public                                | 11,798                 | -               | -                 | -              | 1,933          | 566                    | 99             | 14,396       |

## Small businesses (cont.)

|  | Banking<br>and finance<br>in Israel | Credit<br>cards | Capital<br>market | Mortgages | Real<br>estate | Overseas<br>activities | Total      |
|--|-------------------------------------|-----------------|-------------------|-----------|----------------|------------------------|------------|
| For the nine months ending 30 September 2008                     |                                     |                 |                   |           |                |                        |            |
| NIS millions   |                                     |                 |                   |           |                |                        |            |
| <b>Profit from net interest income:</b>                          |                                     |                 |                   |           |                |                        |            |
| From external sources  | 619                                 | 11              | 4                 | 7         | 253            | 48                     | 942        |
| Inter-segmental  | (107)                               | (4)             | (3)               | (5)       | (117)          | (28)                   | (264)      |
| <b>Operating and other income:</b>                               |                                     |                 |                   |           |                |                        |            |
| From external sources  | 227                                 | 43              | 15                | -         | 36             | 12                     | 333        |
| Inter-segmental  | 2                                   | (25)            | -                 | -         | -              | -                      | (23)       |
| Total income   | 741                                 | 25              | 16                | 2         | 172            | 32                     | 988        |
| Provisions for doubtful debts                                    | 55                                  | -               | -                 | -         | 9              | 12                     | 76         |
| <b>Operating and other expenses:</b>                             |                                     |                 |                   |           |                |                        |            |
| External   | 383                                 | 14              | 5                 | -         | 57             | 28                     | 487        |
| Inter-segmental  | 3                                   | (1)             | -                 | -         | -              | -                      | 2          |
| Operating profit (loss) before taxes                             | 300                                 | 12              | 11                | 2         | 106            | (8)                    | 423        |
| Tax provision (benefit) on operating profit                      | 121                                 | 4               | 4                 | 1         | 39             | (4)                    | 165        |
| Operating profit (loss) after taxes                              | 179                                 | 8               | 7                 | 1         | 67             | (4)                    | 258        |
| Profit from extraordinary items after taxes                      | -                                   | 18              | -                 | -         | -              | -                      | 18         |
| <b>Net profit (loss)</b>   | <b>179</b>                          | <b>26</b>       | <b>7</b>          | <b>1</b>  | <b>67</b>      | <b>(4)</b>             | <b>276</b> |
| <b>% Return on equity</b>  | <b>31.1%</b>                        |                 |                   |           |                |                        |            |
| Average balance of assets  | 11,555                              | 575             | 106               | 144       | 4,735          | 733                    | 17,848     |
| Average balance of liabilities                                   | 10,995                              | 826             | -                 | -         | 1,763          | 560                    | 14,144     |
| Average balance of risk assets                                   | 8,951                               | 557             | 125               | 141       | 4,721          | 724                    | 15,219     |
| Average balance of mutual funds and supplementary training funds | -                                   | -               | 1,376             | -         | -              | -                      | 1,376      |
| Average balance of securities                                    | -                                   | -               | 3,554             | -         | -              | 22                     | 3,576      |
| Average balance of other assets under management                 | 474                                 | -               | -                 | -         | -              | -                      | 474        |
| Balance of credit to the public as at 31 December 2008           | 11,665                              | 594             | 35                | 149       | 4,852          | 866                    | 18,161     |
| Balance of deposits of the public as at 31 December 2008         | 11,923                              | -               | -                 | -         | 1,928          | 624                    | 14,475     |

## Main Changes in the Scope of Operations

Total credit to the public in the segment decreased by NIS 878 million compared with the end of 2008, a decrease of 4.8%, and total deposits of the public declined by 0.5%.

## Main Changes in the Net Profit

In the first nine months of 2009, net profit in the small businesses segment totaled NIS 155 million, compared with NIS 276 million in the corresponding period in 2008, a decrease of 43.8%. The decrease in profit stems mainly from a decrease in income of NIS 65 million, from an increase in the provisions for doubtful debts in the amount of NIS 74 million, from an increase in operating expenses in the amount of NIS 45 million, and from a net decrease of NIS 18 million in profit from

extraordinary items.

Return on equity of the net profit was 19.0%.

### 3. Corporate Banking

The following tables set out a summary of the profit and loss of the corporate banking segment:

|  | Banking<br>and<br>finance<br>in Israel | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas activities       |                | Total      |
|--|--|-----------------|-------------------|----------------|---------------------------|----------------|------------|
|  | Banking<br>and<br>finance<br>in Israel | Credit<br>cards | Capital<br>market | Real<br>estate | Banking<br>and<br>finance | Real<br>estate | Total      |
| <b>For the three months ending 30 September 2009</b> |  |                 |                   |                |                           |                |            |
| NIS millions   |  |                 |                   |                |                           |                |            |
| <b>Profit from net interest income:</b>              |  |                 |                   |                |                           |                |            |
| From external sources                                | 688                                    | 3               | 9                 | 408            | 2                         | 1              | 1,111      |
| Inter-segmental                                      | (367)                                  | (1)             | (9)               | (248)          | -                         | 1              | (624)      |
| <b>Operating and other income:</b>                   |  |                 |                   |                |                           |                |            |
| From external sources                                | 318                                    | 21              | 7                 | 12             | 3                         | -              | 361        |
| Inter-segmental                                      | (2)                                    | (14)            | -                 | -              | -                         | -              | (16)       |
| Total income   | 637                                    | 9               | 7                 | 172            | 5                         | 2              | 832        |
| Provisions for doubtful debts                        | (1)                                    | 1               | -                 | 198            | -                         | -              | 198        |
| <b>Operating and other expenses:</b>                 |  |                 |                   |                |                           |                |            |
| External   | 105                                    | 5               | 2                 | 37             | 4                         | 1              | 154        |
| Inter-segmental                                      | -                                      | -               | -                 | -              | -                         | -              | -          |
| Operating profit (loss) before taxes                 | 533                                    | 3               | 5                 | (63)           | 1                         | 1              | 480        |
| Tax provision (benefit) on operating profit          | 186                                    | -               | 2                 | (23)           | -                         | 1              | 166        |
| <b>Net profit (loss)</b>                             | <b>347</b>                             | <b>3</b>        | <b>3</b>          | <b>(40)</b>    | <b>1</b>                  | <b>-</b>       | <b>314</b> |

|   | Banking<br>and<br>finance<br>in Israel | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas<br>Activities | Total     |
|---|--|-----------------|-------------------|----------------|------------------------|-----------|
|   | Banking<br>and<br>finance<br>in Israel | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas<br>Activities | Total     |
| <b>For the three months ending 30 September 2008</b>    |  |                 |                   |                |                        |           |
| NIS millions  |  |                 |                   |                |                        |           |
| <b>Profit from net interest income:</b>                 |  |                 |                   |                |                        |           |
| From external sources                                   | 945                                    | 10              | -                 | 150            | (1)                    | 1,104     |
| Inter-segmental   | (667)                                  | (5)             | -                 | 2              | 7                      | (663)     |
| <b>Operating and other income:</b>                      |  |                 |                   |                |                        |           |
| From external sources                                   | 18                                     | 63              | 5                 | 14             | 1                      | 101       |
| Inter-segmental   | 1                                      | (45)            | -                 | -              | -                      | (44)      |
| Total income  | 297                                    | 23              | 5                 | 166            | 7                      | 498       |
| Provisions for doubtful debts                           | 256                                    | 1               | -                 | 1              | -                      | 258       |
| <b>Operating and other expenses:</b>                    |  |                 |                   |                |                        |           |
| External  | 81                                     | 20              | 3                 | 29             | 5                      | 138       |
| Inter-segmental   | 1                                      | (1)             | -                 | -              | -                      | -         |
| Operating profit (loss) before taxes                    | (41)                                   | 3               | 2                 | 136            | 2                      | 102       |
| Tax provision (benefit) on operating profit             | (10)                                   | -               | 1                 | 50             | -                      | 41        |
| Operating profit (loss) after taxes                     | (31)                                   | 3               | 1                 | 86             | 2                      | 61        |
| Minority interests in profits of consolidated companies | -                                      | (1)             | -                 | -              | -                      | (1)       |
| <b>Net profit (loss)</b>                                | <b>(31)</b>                            | <b>2</b>        | <b>1</b>          | <b>86</b>      | <b>2</b>               | <b>60</b> |

## Corporate Banking (cont.)

|  | Banking<br>and finance<br>in Israel | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas activities    |                | Total      |
|--|-------------------------------------|-----------------|-------------------|----------------|------------------------|----------------|------------|
|  | Banking<br>and finance              |                 |                   |                | Banking<br>and finance | Real<br>estate |            |
| For the nine months ending 30 September 2009                     |                                     |                 |                   |                |                        |                |            |
| NIS millions   |                                     |                 |                   |                |                        |                |            |
| <b>Profit from net interest income:</b>                          |                                     |                 |                   |                |                        |                |            |
| From external sources  | 1,287                               | 19              | 9                 | 1,136          | 9                      | 1              | 2,461      |
| Inter-segmental  | (401)                               | (5)             | (9)               | (624)          | 4                      | 4              | (1,031)    |
| <b>Operating and other income:</b>                               |                                     |                 |                   |                |                        |                |            |
| From external sources  | 418                                 | 122             | 20                | 43             | 5                      | 1              | 609        |
| Inter-segmental  | (1)                                 | (88)            | -                 | -              | -                      | -              | (89)       |
| Total income   | 1,303                               | 48              | 20                | 555            | 18                     | 6              | 1,950      |
| Provisions for doubtful debts                                    | 257                                 | 2               | -                 | 252            | -                      | -              | 511        |
| <b>Operating and other expenses:</b>                             |                                     |                 |                   |                |                        |                |            |
| External   | 249                                 | 46              | 9                 | 93             | 11                     | 3              | 411        |
| Inter-segmental  | -                                   | -               | -                 | -              | -                      | -              | -          |
| Operating profit before taxes                                    | 797                                 | -               | 11                | 210            | 7                      | 3              | 1,028      |
| Tax provision on operating profit                                | 279                                 | -               | 4                 | 75             | 2                      | 1              | 361        |
| <b>Net profit</b>  | <b>518</b>                          | <b>-</b>        | <b>7</b>          | <b>135</b>     | <b>5</b>               | <b>2</b>       | <b>667</b> |
| <b>% Return on equity</b>  | <b>13.1%</b>                        |                 |                   |                |                        |                |            |
| Average balance of assets  | 50,830                              | 481             | 40                | 27,228         | 559                    | 81             | 79,219     |
| Average balance of liabilities                                   | 25,689                              | 2,876           | -                 | 5,054          | 652                    | 272            | 34,543     |
| Average balance of risk assets                                   | 62,884                              | 559             | 1                 | 27,305         | 758                    | 65             | 91,572     |
| Average balance of mutual funds and supplementary training funds | -                                   | -               | 734               | -              | -                      | -              | 734        |
| Average balance of securities                                    | -                                   | -               | 62,745            | -              | 167                    | -              | 62,912     |
| Average balance of other assets under management                 | 263                                 | -               | -                 | -              | -                      | -              | 263        |
| Balance of credit to the public                                  | 42,053                              | 415             | 156               | 26,675         | 609                    | 108            | 70,016     |
| Balance of deposits of the public                                | 22,137                              | -               | -                 | 4,194          | 509                    | 291            | 27,131     |

## Corporate Banking (cont.)

|  | Banking<br>and<br>finance | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas<br>activities | Total   |
|--|---------------------------|-----------------|-------------------|----------------|------------------------|---------|
| For the nine months ending 30 September 2008                     |                           |                 |                   |                |                        |         |
| NIS millions   |                           |                 |                   |                |                        |         |
| <b>Profit from net interest income:</b>                          |                           |                 |                   |                |                        |         |
| From external sources  | 2,111                     | 25              | -                 | 863            | (12)                   | 2,987   |
| Inter-segmental  | (1,090)                   | (12)            | -                 | (440)          | 31                     | (1,511) |
| <b>Operating and other income:</b>                               |                           |                 |                   |                |                        |         |
| From external sources  | 31                        | 160             | 16                | 38             | 4                      | 249     |
| Inter-segmental  | 2                         | (123)           | -                 | -              | -                      | (121)   |
| Total income   | 1,054                     | 50              | 16                | 461            | 23                     | 1,604   |
| Provisions for doubtful debts                                    | 495                       | 2               | -                 | 35             | -                      | 532     |
| <b>Operating and other expenses:</b>                             |                           |                 |                   |                |                        |         |
| External   | 221                       | 51              | 9                 | 76             | 15                     | 372     |
| Inter-segmental  | 1                         | (1)             | -                 | -              | -                      | -       |
| Operating profit (loss) before taxes                             | 337                       | (2)             | 7                 | 350            | 8                      | 700     |
| Tax provision (benefit) on operating profit                      | 123                       | (1)             | 3                 | 129            | 2                      | 256     |
| Operating profit (loss) after taxes                              | 214                       | (1)             | 4                 | 221            | 6                      | 444     |
| Minority interests in profits of consolidated companies          | -                         | (1)             | -                 | -              | -                      | (1)     |
| Net operating profit (loss)                                      | 214                       | (2)             | 4                 | 221            | 6                      | 443     |
| Profit from extraordinary items after taxes                      | -                         | 2               | -                 | -              | -                      | 2       |
| <b>Net profit (loss)</b>   | 214                       | -               | 4                 | 221            | 6                      | 445     |
| <b>% Return on Equity</b>  |                           |                 |                   |                |                        | 9.2%    |
|  |                           |                 |                   |                |                        |         |
| Average balance of assets  | 46,719                    | 385             | -                 | 22,547         | 759                    | 70,410  |
| Average balance of liabilities                                   | 20,381                    | 3,030           | -                 | 4,156          | 1,631                  | 29,198  |
| Average balance of risk assets                                   | 58,825                    | 356             | 1                 | 21,490         | 761                    | 81,433  |
| Average balance of mutual funds and supplementary training funds | -                         | -               | 753               | -              | -                      | 753     |
| Average balance of securities                                    | -                         | -               | 75,192            | -              | 217                    | 75,409  |
| Average balance of other assets under management                 | 291                       | -               | -                 | -              | -                      | 291     |
| Balance of credit to the public as at 31 December 2008           | 48,632                    | 495             | 4                 | 26,832         | 600                    | 76,563  |
| Balance of deposits of the public as at 31 December 2008         | 17,596                    | -               | -                 | 4,730          | 785                    | 23,111  |

## Main Changes in the Scope of Operations

Total credit to the public in the segment decreased by NIS 6,547 million compared with the end of 2008, a decrease of 8.6%, and total deposits of the public increased by NIS 4,020 million, some 17.4%.

## Main Changes in Net Profit

In the first nine months of 2009, net profit in the corporate banking segment totaled NIS 667



million, compared with NIS 445 million during the corresponding period in 2008, an increase of 49.9%. The increase in profit stems mainly from an increase in operating income in the amount of NIS 392 million, a decrease in provisions for doubtful debts in the amount of NIS 21 million, which was partially offset by a decrease in net interest income in the amount of NIS 46 million, and by an increase in expenses in the amount of NIS 39 million.

Return on equity of net profit was 13.1%.

#### 4. Commercial Banking

The following tables set out a summary of the profit and loss of the commercial banking segment:

|   |   |                 |                   |                |                | Overseas activity         |                   |                |       |
|---|---|-----------------|-------------------|----------------|----------------|---------------------------|-------------------|----------------|-------|
|   | Banking<br>and<br>finance<br>in<br>Israel | Credit<br>cards | Capital<br>market | Mort-<br>gages | Real<br>estate | Banking<br>and<br>finance | Capital<br>Market | Real<br>Estate | Total |
| For the three months ending 30 September 2009 |   |                 |                   |                |                |                           |                   |                |       |
| NIS millions                                  |   |                 |                   |                |                |                           |                   |                |       |
| Profit from net interest income:              |   |                 |                   |                |                |                           |                   |                |       |
| From external sources                         | 244                                       | 3               | 1                 | 6              | 99             | 112                       | -                 | 30             | 495   |
| Inter-segmental                               | (55)                                      | -               | (1)               | (6)            | (49)           | (26)                      | -                 | (17)           | (154) |
| Operating and other income:                   |   |                 |                   |                |                |                           |                   |                |       |
| From external sources                         | 52  | 22              | 12                | -              | 8              | 11                        | 2                 | 5              | 112   |
| Inter-segmental                               | -   | (14)            | -                 | -              | -              | -                         | -                 | -              | (14)  |
| Total income                                  | 241                                       | 11              | 12                | -              | 58             | 97                        | 2                 | 18             | 439   |
| Provisions for doubtful debts                 | 63  | 1               | -                 | (5)            | 10             | 45                        | -                 | 3              | 117   |
| Operating and other expenses:                 |   |                 |                   |                |                |                           |                   |                |       |
| External                                      | 129                                       | 8               | 7                 | 1              | 14             | 67                        | -                 | 11             | 237   |
| Inter-segmental                               | 1   | -               | -                 | -              | -              | -                         | -                 | -              | 1     |
| Operating profit (loss) before taxes          | 48  | 2               | 5                 | 4              | 34             | (15)                      | 2                 | 4              | 84    |
| Tax provision (benefit) on operating profit   | 15  | -               | 2                 | 2              | 12             | (2)                       | -                 | 1              | 30    |
| Net profit (loss)                             | 33  | 2               | 3                 | 2              | 22             | (13)                      | 2                 | 3              | 54    |

|   | Overseas activity         |                 |                   |                |                |                           |                   |                |            |
|---|---------------------------|-----------------|-------------------|----------------|----------------|---------------------------|-------------------|----------------|------------|
|   | Banking<br>and<br>finance | Credit<br>cards | Capital<br>market | Mort-<br>gages | Real<br>estate | Banking<br>and<br>finance | Capital<br>Market | Real<br>Estate | Total      |
| For the three months ending 30 September 2008 |                           |                 |                   |                |                |                           |                   |                |            |
| NIS millions                                  |                           |                 |                   |                |                |                           |                   |                |            |
| <b>Profit from net interest income:</b>       |                           |                 |                   |                |                |                           |                   |                |            |
| From external sources                         | 134                       | 2               | 1                 | 7              | 91             | 143                       | -                 | 42             | 420        |
| Inter-segmental                               | 79                        | (1)             | 1                 | (6)            | (44)           | (68)                      | -                 | (25)           | (64)       |
| <b>Operating and other income:</b>            |                           |                 |                   |                |                |                           |                   |                |            |
| From external sources                         | 49                        | 13              | 11                | -              | 7              | 9                         | 4                 | 3              | 96         |
| Inter-segmental                               | 3                         | (11)            | -                 | -              | -              | -                         | -                 | -              | (8)        |
| Total income                                  | 265                       | 3               | 13                | 1              | 54             | 84                        | 4                 | 20             | 444        |
| Provisions for doubtful debts                 | 38                        | -               | -                 | 1              | 4              | 5                         | -                 | 1              | 49         |
| <b>Operating and other expenses:</b>          |                           |                 |                   |                |                |                           |                   |                |            |
| External                                      | 118                       | 4               | 9                 | 1              | 13             | 55                        | 2                 | 10             | 212        |
| Inter-segmental                               | 3                         | (2)             | -                 | -              | -              | -                         | -                 | -              | 1          |
| Operating profit (loss) before taxes          | 106                       | 1               | 4                 | (1)            | 37             | 24                        | 2                 | 9              | 182        |
| Tax provision on operating profit             | 49                        | 1               | -                 | -              | 14             | 13                        | -                 | 3              | 80         |
| <b>Net profit (loss)</b>                      | <b>57</b>                 | <b>-</b>        | <b>4</b>          | <b>(1)</b>     | <b>23</b>      | <b>11</b>                 | <b>2</b>          | <b>6</b>       | <b>102</b> |

## Commercial Banking (cont.)

|  | Banking<br>and<br>finance | Credit<br>cards   | Capital<br>market | Mort-<br>gages      | Real<br>estate | Overseas activities |          |           | Total       |
|--|---------------------------|-------------------|-------------------|---------------------|----------------|---------------------|----------|-----------|-------------|
|  | Banking<br>and<br>finance | Capital<br>market | Real<br>estate    | Overseas activities |                |                     |          |           |             |
| <b>For the nine months ending 30 September 2009</b>              |                           |                   |                   |                     |                |                     |          |           |             |
| NIS millions   |                           |                   |                   |                     |                |                     |          |           |             |
| <b>Profit from net interest income:</b>                          |                           |                   |                   |                     |                |                     |          |           |             |
| From external sources  | 611                       | 8                 | 1                 | 20                  | 238            | 370                 | -        | 107       | 1,355       |
| Inter-segmental  | (53)                      | (1)               | (1)               | (17)                | (97)           | (103)               | -        | (61)      | (333)       |
| <b>Operating and other income:</b>                               |                           |                   |                   |                     |                |                     |          |           |             |
| From external sources  | 159                       | 45                | 37                | 1                   | 23             | 32                  | 4        | 8         | 309         |
| Inter-segmental  | -                         | (30)              | -                 | -                   | -              | -                   | -        | -         | (30)        |
| Total income   | 717                       | 22                | 37                | 4                   | 164            | 299                 | 4        | 54        | 1,301       |
| Provisions for doubtful debts                                    | 146                       | 1                 | -                 | (2)                 | 20             | 85                  | -        | 6         | 256         |
| <b>Operating and other expenses:</b>                             |                           |                   |                   |                     |                |                     |          |           |             |
| External   | 335                       | 17                | 24                | 2                   | 43             | 208                 | 2        | 33        | 664         |
| Inter-segmental  | 1                         | -                 | -                 | -                   | -              | -                   | -        | -         | 1           |
| Operating profit before taxes                                    | 235                       | 4                 | 13                | 4                   | 101            | 6                   | 2        | 15        | 380         |
| Tax provision on operating profit                                | 82                        | 1                 | 5                 | 2                   | 36             | 4                   | -        | 4         | 134         |
| <b>Net profit</b>  | <b>153</b>                | <b>3</b>          | <b>8</b>          | <b>2</b>            | <b>65</b>      | <b>2</b>            | <b>2</b> | <b>11</b> | <b>246</b>  |
| <b>% Return on equity</b>  |                           |                   |                   |                     |                |                     |          |           | <b>9.8%</b> |
| Average balance of assets  | 23,521                    | 294               | 55                | 474                 | 5,936          | 13,457              | -        | 3,463     | 47,200      |
| Average balance of liabilities                                   | 20,804                    | 726               | -                 | 129                 | 2,009          | 8,643               | -        | 509       | 32,820      |
| Average balance of risk assets                                   | 22,445                    | 302               | 7                 | 469                 | 6,034          | 12,680              | -        | 3,053     | 44,990      |
| Average balance of mutual funds and supplementary training funds | -                         | -                 | 2,749             | -                   | -              | -                   | 105      | -         | 2,854       |
| Average balance of securities                                    | -                         | -                 | 30,178            | -                   | -              | -                   | 2,016    | -         | 32,194      |
| Average balance of other assets under management                 | 638                       | -                 | -                 | -                   | -              | -                   | -        | -         | 638         |
| Balance of credit to the public                                  | 21,356                    | 304               | 199               | 489                 | 5,774          | 12,158              | -        | 3,467     | 43,747      |
| Balance of deposits of the public                                | 20,713                    | -                 | -                 | 75                  | 2,004          | 8,289               | -        | 361       | 31,442      |

## Commercial Banking (cont.)

|  | Banking<br>and<br>finance in<br>Israel       | Credit<br>cards   | Capital<br>market | Mortgages | Real<br>estate | Overseas activities |          |           | Total        |
|--|--|-------------------|-------------------|-----------|----------------|---------------------|----------|-----------|--------------|
|  | Banking<br>and<br>finance                    | Capital<br>market | Real<br>estate    |           |                |                     |          |           |              |
|  | For the nine months ending 30 September 2008 |                   |                   |           |                |                     |          |           |              |
|  | NIS millions                                 |                   |                   |           |                |                     |          |           |              |
| <b>Profit from net interest income:</b>  |  |                   |                   |           |                |                     |          |           |              |
| From external sources  | 748  | 6                 | 2                 | 17        | 289            | 429                 | -        | 120       | 1,611        |
| Inter-segmental  | (80)   | (3)               | (2)               | (14)      | (145)          | (170)               | -        | (70)      | (484)        |
| <b>Operating and other income:</b>   |  |                   |                   |           |                |                     |          |           |              |
| From external sources  | 173  | 37                | 36                | -         | 19             | 27                  | 10       | 10        | 312          |
| Inter-segmental  | 3  | (27)              | -                 | -         | -              | -                   | -        | -         | (24)         |
| Total income   | 844  | 13                | 36                | 3         | 163            | 286                 | 10       | 60        | 1,415        |
| Provisions for doubtful debts  | 131  | -                 | -                 | (1)       | 46             | 31                  | -        | -         | 207          |
| <b>Operating and other expenses:</b>   |  |                   |                   |           |                |                     |          |           |              |
| External   | 345  | 11                | 24                | 2         | 41             | 183                 | 6        | 33        | 645          |
| Inter-segmental  | 3  | (2)               | -                 | -         | -              | -                   | -        | -         | 1            |
| Operating profit before taxes  | 365  | 4                 | 12                | 2         | 76             | 72                  | 4        | 27        | 562          |
| Tax provision on operating profit  | 143  | 2                 | 4                 | 1         | 28             | 28                  | 1        | 8         | 215          |
| Operating profit after taxes   | 222  | 2                 | 8                 | 1         | 48             | 44                  | 3        | 19        | 347          |
| Group's share in profits of companies included on the equity basis after taxes | -  | 1                 | -                 | -         | -              | -                   | -        | -         | 1            |
| Net operating profit   | 222  | 3                 | 8                 | 1         | 48             | 44                  | 3        | 19        | 348          |
| Profit from extraordinary items after taxes                                    | -  | 26                | -                 | -         | -              | -                   | -        | -         | 26           |
| <b>Net profit</b>  | <b>222</b>                                   | <b>29</b>         | <b>8</b>          | <b>1</b>  | <b>48</b>      | <b>44</b>           | <b>3</b> | <b>19</b> | <b>374</b>   |
| <b>% Return on equity</b>  |  |                   |                   |           |                |                     |          |           | <b>12.9%</b> |
|  |  |                   |                   |           |                |                     |          |           |              |
| Average balance of assets  | 27,424                                       | 284               | 29                | 352       | 5,966          | 14,699              | -        | 1,569     | 50,323       |
| Of which: investments in companies included on the equity basis                | -  | 5                 | -                 | -         | -              | -                   | -        | -         | 5            |
| Average balance of liabilities   | 18,722                                       | 717               | -                 | 104       | 2,180          | 8,411               | -        | 767       | 30,901       |
| Average balance of risk assets   | 25,749                                       | 299               | 31                | 325       | 6,025          | 13,653              | -        | 2,710     | 48,792       |
| Average balance of mutual funds and supplementary training funds               | -  | -                 | 2,851             | -         | -              | -                   | 27       | -         | 2,878        |
| Average balance of securities  | -  | -                 | 38,375            | -         | -              | -                   | 3,066    | -         | 41,441       |
| Average balance of other assets under management                               | 1,017  | -                 | -                 | -         | -              | -                   | -        | -         | 1,017        |
| Balance of credit to the public as at 31 December 2008                         | 25,057                                       | 297               | 10                | 460       | 5,778          | 13,665              | -        | 3,239     | 48,506       |
| Balance of deposits of the public as at 31 December 2008                       | 18,480                                       | -                 | -                 | 75        | 1,908          | 8,537               | -        | 659       | 29,659       |

## Main Changes in the Scope of Operations

Total credit to the public in the segment decreased by NIS 4,759 million, 9.8% as compared with the end of 2008, and total deposits of the public increased by NIS 1,783 million, 6.0%.

**Main Changes in Net Profit**

In the first nine months of 2009, net profit in the commercial banking segment totaled NIS 246 million, compared with NIS 374 million during the corresponding period in 2008, a decrease of 34.2%. The decrease in profit stems from a decrease in income of NIS 114 million, an increase in provisions for doubtful debts of NIS 49 million, and from a net decrease in profit from extraordinary items of NIS 26 million. Of the decrease of NIS 128 million in net profit, some NIS 51 million arises from activities in the segment abroad.

Return on equity of net profit was 9.8%.

## 5. Private banking

The following tables set out a summary of the profit and loss of the private banking segment:

|   | Banking<br>and<br>finance | Credit<br>cards   | Capital<br>market | Real<br>estate | Overseas activities       |                   |                | Total |
|---|---------------------------|-------------------|-------------------|----------------|---------------------------|-------------------|----------------|-------|
|   | Banking<br>and<br>finance | Capital<br>market | Real<br>estate    |                | Banking<br>and<br>finance | Capital<br>market | Real<br>estate |       |
| For the three months ending 30 September 2009           |                           |                   |                   |                |                           |                   |                |       |
| NIS millions  |                           |                   |                   |                |                           |                   |                |       |
| Profit from net interest income:                        |                           |                   |                   |                |                           |                   |                |       |
| From external sources                                   | (82)                      | -                 | -                 | 1              | 30                        | -                 | 1              | (50)  |
| Inter-segmental   | 115                       | -                 | 0                 | 2              | 65                        | -                 | 1              | 183   |
| Operating and other income:                             |                           |                   |                   |                |                           |                   |                |       |
| From external sources                                   | 9                         | -                 | 34                | 1              | 36                        | 29                | -              | 109   |
| Inter-segmental   | -                         | 1                 | -                 | -              | 5                         | -                 | -              | 6     |
| Total income  | 42                        | 1                 | 34                | 4              | 136                       | 29                | 2              | 248   |
| Provisions for doubtful debts                           | -                         | -                 | -                 | -              | 1                         | -                 | -              | 1     |
| Operating and other expenses:                           |                           |                   |                   |                |                           |                   |                |       |
| External  | 31                        | -                 | 16                | 1              | 97                        | 18                | 1              | 164   |
| Inter-segmental   | -                         | -                 | -                 | -              | -                         | -                 | -              | -     |
| Operating profit before taxes                           | 11                        | 1                 | 18                | 3              | 38                        | 11                | 1              | 83    |
| Tax provision on operating profit                       | 6                         | -                 | 6                 | 1              | 10                        | 3                 | 1              | 27    |
| Operating profit after taxes                            | 5                         | 1                 | 12                | 2              | 28                        | 8                 | -              | 56    |
| Minority interests in profits of consolidated companies | -                         | -                 | -                 | -              | (2)                       | -                 | -              | (2)   |
| Net profit  | 5                         | 1                 | 12                | 2              | 26                        | 8                 | -              | 54    |

|   | Banking<br>and finance | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas activities    |                   | Total |
|---|------------------------|-----------------|-------------------|----------------|------------------------|-------------------|-------|
|   | Banking<br>and finance |                 |                   |                | Banking<br>and finance | Capital<br>Market |       |
| For the three months ending 30 September 2008 |                        |                 |                   |                |                        |                   |       |
| NIS millions                                  |                        |                 |                   |                |                        |                   |       |
| <b>Profit from net interest income:</b>       |                        |                 |                   |                |                        |                   |       |
| From external sources                         | (138)                  | -               | -                 | 1              | (55)                   | -                 | (192) |
| Inter-segmental                               | 171                    | -               | -                 | 3              | 48                     | -                 | 222   |
| <b>Operating and other income:</b>            |                        |                 |                   |                |                        |                   |       |
| From external sources                         | 10                     | -               | 29                | 1              | 23                     | 31                | 94    |
| Inter-segmental                               | -                      | 1               | -                 | -              | 2                      | -                 | 3     |
| Total income                                  | 43                     | 1               | 29                | 5              | 18                     | 31                | 127   |
| Provisions for doubtful debts                 | -                      | -               | -                 | -              | -                      | -                 | -     |
| <b>Operating and other expenses:</b>          |                        |                 |                   |                |                        |                   |       |
| External                                      | 32                     | -               | 7                 | 1              | 46                     | 37                | 123   |
| Inter-segmental                               | -                      | -               | -                 | -              | 1                      | -                 | 1     |
| Operating profit (loss) before taxes          | 11                     | 1               | 22                | 4              | (29)                   | (6)               | 3     |
| Tax provision on operating profit             | 8                      | -               | 8                 | 2              | 6                      | -                 | 24    |
| Net profit (loss)                             | 3                      | 1               | 14                | 2              | (35)                   | (6)               | (21)  |

Private banking (cont'd.)

|  | Banking<br>and finance<br>in Israel | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas activities                          |                   |                | Total  |
|--|-------------------------------------|-----------------|-------------------|----------------|--|-------------------|----------------|--------|
|  |                                     |                 |                   |                | Banking<br>and<br>finance                    | Capital<br>market | Real<br>estate |        |
|  |                                     |                 |                   |                | For the nine months ending 30 September 2009 |                   |                |        |
| NIS millions   |                                     |                 |                   |                |  |                   |                |        |
| <b>Profit from net interest income:</b>                          |                                     |                 |                   |                |  |                   |                |        |
| From external sources  | (253)                               | -               | -                 | 3              | 82   | -                 | (1)            | (169)  |
| Inter-segmental  | 372                                 | -               | -                 | 5              | 227  | -                 | 5              | 609    |
| <b>Operating and other income:</b>                               |                                     |                 |                   |                |  |                   |                |        |
| From external sources  | 23                                  | -               | 102               | 3              | 96   | 85                | 1              | 310    |
| Inter-segmental  | 1                                   | 1               | -                 | -              | 11   | -                 | -              | 13     |
| Total income   | 143                                 | 1               | 102               | 11             | 416  | 85                | 5              | 763    |
| Provisions for doubtful debts                                    | 1                                   | -               | -                 | -              | -  | -                 | -              | 1      |
| <b>Operating and other expenses:</b>                             |                                     |                 |                   |                |  |                   |                |        |
| External   | 104                                 | 1               | 44                | 5              | 296  | 61                | 3              | 514    |
| Inter-segmental  | -                                   | -               | -                 | -              | 1  | -                 | -              | 1      |
| Operating profit before taxes                                    | 38                                  | -               | 58                | 6              | 119  | 24                | 2              | 247    |
| Tax provision on operating profit                                | 15                                  | -               | 19                | 2              | 38   | 7                 | 1              | 82     |
| Operating profit after taxes                                     | 23                                  | -               | 39                | 4              | 81   | 17                | 1              | 165    |
| Minority interests in profits of consolidated companies          | -                                   | -               | -                 | -              | (4)  | -                 | -              | (4)    |
| <b>Net profit</b>  | 23                                  | -               | 39                | 4              | 77   | 17                | 1              | 161    |
| <b>% Return on equity</b>  |                                     |                 |                   |                |  |                   |                | 37.5%  |
|  |                                     |                 |                   |                |  |                   |                |        |
| Average balance of assets  | 1,337                               | 50              | -                 | 381            | 9,225  | -                 | 51             | 11,044 |
| Average balance of liabilities                                   | 24,318                              | -               | -                 | 707            | 16,324                                       | -                 | 294            | 41,643 |
| Average balance of risk assets                                   | 1,469                               | 51              | -                 | 366            | 5,977  | -                 | 49             | 7,912  |
| Average balance of mutual funds and supplementary training funds | -                                   | -               | 2,608             | -              | -  | 1,325             | -              | 3,933  |
| Average balance of securities                                    | -                                   | -               | 30,044            | -              | -  | 28,165            | -              | 58,209 |
| Average balance of other assets under management                 | 297                                 | -               | -                 | -              | -  | -                 | -              | 297    |
| Balance of credit to the public                                  | 939                                 | 49              | -                 | 422            | 4,829  | -                 | 47             | 6,286  |
| Balance of deposits of the public                                | 23,260                              | -               | -                 | 693            | 16,137                                       | -                 | 258            | 40,348 |

## Private banking (cont'd.)

|  | Banking and<br>finance | Credit<br>cards | Capital<br>market | Real<br>estate | Overseas activities    |                   | Total        |
|--|------------------------|-----------------|-------------------|----------------|------------------------|-------------------|--------------|
|  | Banking and<br>finance | Credit<br>cards | Capital<br>market | Real<br>estate | Banking and<br>finance | Capital<br>market | Total        |
| For the nine months ending 30 September 2008                     |                        |                 |                   |                |                        |                   |              |
| NIS millions   |                        |                 |                   |                |                        |                   |              |
| <b>Profit from net interest income:</b>                          |                        |                 |                   |                |                        |                   |              |
| From external sources  | (424)                  | -               | -                 | (2)            | (75)                   | -                 | (501)        |
| Inter-segmental  | 529                    | -               | -                 | 8              | 207                    | -                 | 744          |
| <b>Operating and other income:</b>                               |                        |                 |                   |                |                        |                   |              |
| From external sources  | 26                     | 1               | 88                | 3              | 72                     | 101               | 291          |
| Inter-segmental  | 1                      | 1               | -                 | -              | 9                      | -                 | 11           |
| Total income   | 132                    | 2               | 88                | 9              | 213                    | 101               | 545          |
| Provisions for doubtful debts                                    | -                      | -               | -                 | -              | (1)                    | -                 | (1)          |
| <b>Operating and other expenses:</b>                             |                        |                 |                   |                |                        |                   |              |
| External   | 118                    | 1               | 29                | 4              | 186                    | 92                | 430          |
| Inter-segmental  | -                      | -               | -                 | -              | 3                      | 1                 | 4            |
| Operating profit before taxes                                    | 14                     | 1               | 59                | 5              | 25                     | 8                 | 112          |
| Tax provision on operating profit                                | 8                      | -               | 22                | 2              | 23                     | 6                 | 61           |
| Operating profit after taxes                                     | 6                      | 1               | 37                | 3              | 2                      | 2                 | 51           |
| Minority interests in profits of consolidated companies          | -                      | -               | -                 | -              | (1)                    | -                 | (1)          |
| Net operating profit   | 6                      | 1               | 37                | 3              | 1                      | 2                 | 50           |
| Profit from extraordinary items after taxes                      | -                      | 3               | -                 | -              | -                      | -                 | 3            |
| <b>Net profit</b>  | <b>6</b>               | <b>4</b>        | <b>37</b>         | <b>3</b>       | <b>1</b>               | <b>2</b>          | <b>53</b>    |
| <b>% Return on equity</b>  |                        |                 |                   |                |                        |                   | <b>12.3%</b> |
| Average balance of assets  | 1,449                  | 49              | -                 | 217            | 8,179                  | -                 | 9,894        |
| Average balance of liabilities                                   | 22,753                 | -               | -                 | 567            | 14,420                 | -                 | 37,740       |
| Average balance of risk assets                                   | 839                    | 49              | -                 | 194            | 6,146                  | -                 | 7,228        |
| Average balance of mutual funds and supplementary training funds | -                      | -               | 3,106             | -              | -                      | 1,786             | 4,892        |
| Average balance of securities                                    | -                      | -               | 29,035            | -              | -                      | 33,588            | 62,623       |
| Average balance of other assets under management                 | 295                    | -               | -                 | -              | -                      | -                 | 295          |
| Balance of credit to the public as at 31 December 2008           | 1,292                  | 50              | -                 | 291            | 4,805                  | -                 | 6,438        |
| Balance of deposits of the public as at 31 December 2008         | 23,098                 | -               | -                 | 719            | 14,240                 | -                 | 38,057       |

## Main Changes in the Scope of Operations

Total credit to the public in the segment decreased by NIS 152 million compared with the end of 2008, and total deposits of the public increased by NIS 2,291 million, 6.0%.

## Main Changes in Net Profit

In the first nine months of 2009, net profit in the private banking segment totaled NIS 161 million, compared with NIS 53 million in the corresponding period in 2008, an increase of 203.9%. The increase in profit arises from an increase in income of NIS 218 million, 40%, which was partially offset by an increase in operating expenses in the amount of NIS 81 million, 18.7%. The increase of the net profit in private banking arises primarily from activity overseas.



Return on equity of net profit was 37.5%.

## 6. Financial Management – Capital Markets

In the first nine months of 2009, the net profit in the financial management segment totaled NIS 123 million, compared with a loss of NIS 541 million in the corresponding period in 2008, an increase of NIS 664 million. The improvement in the profit stems from:

- An increase in operating income in the amount of NIS 737 million, as a result of provisions for decreases in value of mutual funds in the corresponding period in 2008.
- A decrease in operating and other expenses in the amount of NIS 547 million, mainly in respect of salary expenses that are not attributable to other segments.
- An increase in net interest income in the amount of NIS 191 million.
- On the other hand, there was a decrease in the Group's portion of profits of companies included on the equity basis in the amount of NIS 460 million, which partially offset these effects.

Positive exchange rate differentials arising from the overseas investments and attributable to this segment and which are not included in the tax calculation, led to a decline in the rate of the tax provision.

**Companies Included on the Equity Basis (Non-Banking)** – (presented in the Financial Management Sector)

This includes the results of the Group's investment in non-banking (real) investments.

The Leumi Group's total investments in companies included on the equity basis amounted to NIS 1,908 million on 30 September 2009, compared with NIS 1,842 million on 31 December 2008.

| Name of the Company         | Book value (in NIS millions) |                  |            | Market value (in NIS millions) |                  |                  |
|-----------------------------|------------------------------|------------------|------------|--------------------------------|------------------|------------------|
|                             | 30 September 2009            | 31 December 2008 | % change   | 30 September 2009              | 31 December 2008 | 24 November 2009 |
| The Israel Corporation Ltd. | 1,144                        | 1,186            | (3.5)      | 3,139                          | 1,184            | 4,280            |
| Paz Oil Company Ltd.        | 559                          | 485              | 15.3       | 881                            | 570              | 925              |
| Others                      | 205                          | 171              | 19.9       | -                              | -                | -                |
| <b>Total</b>                | <b>1,908</b>                 | <b>1,842</b>     | <b>3.6</b> | <b>4,020</b>                   | <b>1,754</b>     | <b>5,205</b>     |

The contribution to Group profit of the companies included on the equity basis in the first nine months of 2009 amounted to zero, compared with a profit of NIS 471 million in the corresponding period in 2008.

The following table shows the companies' contribution to the Group's net profit (in NIS millions):

|                             | For the nine months ending 30 September |      |          |
|-----------------------------|---|------|----------|
|                             | 2009                                    | 2008 | % change |
| The Israel Corporation Ltd. | (73)                                    | 354  | (120.6)  |
| Paz Oil Company Ltd.        | 66                                      | 99   | (33.3)   |
| Others                      | 7                                       | 18   | (61.1)   |
|                             | (-)                                     | 471  | (-)      |

#### **The Israel Corporation Ltd. – Restrictions in the Permit for Control of Oil Refineries Ltd. (ORL)**

The control permit for ORL, which was granted to the Israel Corporation Ltd. (the "Israel Corporation"), contains certain restrictions on the Bank with respect to directors serving on behalf of the Bank in the Israel Corporation. The purpose of the restrictions is the maintenance of "Chinese walls" between ORL and the Ashdod Oil Refinery Ltd. ("AOR"), for so long as: the Israel Corporation controls ORL, and Paz Oil Company Ltd. ("Paz") controls AOR; and the Bank has the right or the ability to appoint, to recommend or to otherwise influence the appointment of a director of the Israel Corporation and of Paz.

#### **Holdings in Non-banking Holding Corporations (Conglomerates)**

The Bank's holdings in non-banking corporations are subject to restrictions determined in the Banking (Licensing) Law, 1981 (the "Banking Law"). The Banking Law determines, *inter alia*, in section 24A that a banking corporation is entitled to hold means of control in only one conglomerate (a corporation whose capital exceeds some NIS 1,901 million and operates in more than three branches of the economy). With regard to the proposed law for the amendment to section 24A of the Banking Law, see below. The Bank has holdings in one conglomerate - the Israel Corporation Ltd.

The financial statements of Paz for the first quarter of 2007, in which new accounting standards were implemented, indicate that the shareholders' equity of Paz exceeds the minimal amount of capital in the definition of a conglomerate.

Prior to the publication of the said financial statements, discussions had already been held between the Bank and the Bank of Israel with regard to the interpretation of the Banking Law relating to the definition of Paz as a conglomerate. Further to these discussions, the Bank of Israel notified the Bank, in its letter of 3 July 2007, that it does not accept the Bank's interpretation that the energy sector constitutes one branch of the economy. Therefore, according to the Bank of Israel's position, Paz is a conglomerate under the Banking Law.

At the Bank's request, the Bank of Israel agreed that the sale of the Bank's holdings in Paz take place by 30 December 2010, subject to the Bank's holdings in Paz being transferred to a trustee. To this end, the Bank transferred its holdings to a trustee at the end of June 2009.

#### **Migdal Insurance and Financial Holdings Ltd.**

The Bank holds 9.85% of the issued and fully paid share capital of Migdal Insurance and Financial Holdings Ltd. ("Migdal Holdings") (9.74%, fully diluted), the controlling shareholder of Migdal Insurance Company Ltd.

According to the Bank of Israel's interpretation of the Banking (Licensing) Law, with which the Bank disagrees, the Bank is also required to sell the holdings in Migdal Holdings, which, pursuant to the said law, is considered to be a conglomerate.

It should be noted that pursuant to legislation enacted following the capital market reform, a bank may hold 5% of the share capital of an insurance company, and 10% of the share capital of a corporation that controls an insurance company.

On 27 July 2009, the Knesset approved, in its first reading, a proposed law for the amendment of Section 24A of the Banking (Licensing) Law, pursuant to which, *inter alia*, a corporation which is an insurer operates in the insurance industry only, and is therefore not considered to be a conglomerate.

At the Bank's request, the Bank of Israel extended the permit issued to the Bank for the holding of the shares in Migdal, provided that the shares be transferred to a trustee. The shares were transferred to a trustee on 4 January 2009. Pursuant to the Bank of Israel directives, if the shares held by the trustee are not sold by 31 August 2010, the trustee will sell the shares to a third party by no later than 31 December 2010. The trustee was vested with all the rights that the shares confer (excluding the right to receive dividends and the rights vested with the Bank – the right to sell the shares to a third party or the right to distribute them as a dividend *in specie* up until 31 August 2010).

## **7. Others** - This segment includes activities not allocated to the other segments.

This segment includes the other activities of the Group, none of which amounts to a profit segment according to the directives of the Bank of Israel.

This activity includes primarily: part of the operations of companies that are not allocated to the other segments.

During the first nine months of 2009, the loss in the "Others" segment amounted to NIS 87 million, compared with a loss of NIS 24 million in the corresponding period in 2008.

The following table sets out details of the main changes, in NIS millions:

|  | For the nine months ending 30 September |      |                  |
|--|---|------|------------------|
|  | 2009                                    | 2008 | Change in amount |
| Profit (loss) from extraordinary items | <b>28</b>                               | (1)  | 29               |
| From operating activity at the Bank    | <b>13</b>                               | 12   | 1                |
| Leumi Partners                         | <b>9</b>                                | 40   | (31)             |
| Other companies in Israel              | <b>(3)</b>                              | (5)  | 2                |
| Overseas companies                     | <b>(4)</b>                              | (13) | 9                |
| Tax adjustments <sup>(1)</sup>         | <b>(130)</b>                            | (57) | (73)             |
| Total                                  | <b>(87)</b>                             | (24) | (63)             |

(1) Tax differentials between tax calculations in the segments and the effective tax in the Consolidated Report.

## Activities in Products

**A. Capital market activities** - The Group's activities in the capital market include investment counselling activity, including counseling in relation to supplementary training funds, brokerage in the securities and financial instruments market, including activity carried out through the foreign currency and Israeli and foreign securities dealing rooms, brokerage and custody services, and banking and financial services for entities active in the capital market. A subsidiary company of Leumi Partners Ltd. engages in underwriting and distribution of public and private offerings.

The following tables set out details of the capital market operations as presented in the various operational segments:

|  | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Financial management and others | Overseas activities | Total |
|--|-------------|------------------|-------------------|--------------------|-----------------|---------------------------------|---------------------|-------|
| <b>For the three months ending 30 September 2009</b> |             |                  |                   |                    |                 |                                 |                     |       |
| NIS millions   |             |                  |                   |                    |                 |                                 |                     |       |
| Profit from net interest income                      | 2           | -                | -                 | -                  | -               | -                               | -                   | 2     |
| Operating and other income                           | 139         | 7                | 7                 | 12                 | 34              | 22                              | 36                  | 257   |
| Total income   | 141         | 7                | 7                 | 12                 | 34              | 22                              | 36                  | 259   |
| Operating and other expenses                         | 77          | 2                | 2                 | 7                  | 16              | 7                               | 21                  | 132   |
| Operating profit before taxes                        | 64          | 5                | 5                 | 5                  | 18              | 15                              | 15                  | 127   |
| Net profit (loss)                                    | 40          | 3                | 3                 | 3                  | 12              | 11                              | 15                  | 87    |

  

|  | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Financial management and others | Overseas activities | Total |
|--|-------------|------------------|-------------------|--------------------|-----------------|---------------------------------|---------------------|-------|
| <b>For the three months ending 30 September 2008</b> |             |                  |                   |                    |                 |                                 |                     |       |
| NIS millions   |             |                  |                   |                    |                 |                                 |                     |       |
| Profit from net interest income                      | -           | -                | -                 | 2                  | -               | -                               | -                   | 2     |
| Operating and other income                           | 115         | 5                | 5                 | 11                 | 29              | 26                              | 67                  | 258   |
| Total income   | 115         | 5                | 5                 | 13                 | 29              | 26                              | 67                  | 260   |
| Operating and other expenses                         | 46          | 1                | 3                 | 9                  | 7               | 16                              | 61                  | 143   |
| Operating profit before taxes                        | 69          | 4                | 2                 | 4                  | 22              | 10                              | 6                   | 117   |
| Net profit   | 43          | 2                | 1                 | 4                  | 14              | 5                               | 1                   | 70    |

|   | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Financial management and others | Overseas activities | Total |
|---|-------------|------------------|-------------------|--------------------|-----------------|---------------------------------|---------------------|-------|
| <b>For the nine months ending 30 September 2009</b> |             |                  |                   |                    |                 |                                 |                     |       |
| NIS millions  |             |                  |                   |                    |                 |                                 |                     |       |
| Profit from net interest income                     | 2           | 1                | -                 | -                  | -               | -                               | -                   | 3     |
| Operating and other income                          | 380         | 17               | 20                | 37                 | 102             | 59                              | 98                  | 713   |
| Total income  | 382         | 18               | 20                | 37                 | 102             | 59                              | 98                  | 716   |
| Operating and other expenses                        | 222         | 7                | 9                 | 24                 | 44              | 28                              | 75                  | 409   |
| Operating profit before taxes                       | 160         | 11               | 11                | 13                 | 58              | 31                              | 23                  | 303   |
| Net profit  | 102         | 7                | 7                 | 8                  | 39              | 20                              | 18                  | 201   |

  

|   | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Financial Management and others | Overseas activities | Total |
|---|-------------|------------------|-------------------|--------------------|-----------------|---------------------------------|---------------------|-------|
| <b>For the nine months ending 30 September 2008</b> |             |                  |                   |                    |                 |                                 |                     |       |
| NIS millions  |             |                  |                   |                    |                 |                                 |                     |       |
| Profit from net interest income                     | 1           | 1                | -                 | -                  | -               | -                               | -                   | 2     |
| Operating and other income                          | 342         | 15               | 16                | 36                 | 88              | 79                              | 149                 | 725   |
| Total income  | 343         | 16               | 16                | 36                 | 88              | 79                              | 149                 | 727   |
| Operating and other expenses                        | 188         | 5                | 9                 | 24                 | 29              | 35                              | 122                 | 412   |
| Operating profit before taxes                       | 155         | 11               | 7                 | 12                 | 59              | 44                              | 27                  | 315   |
| Net profit  | 98          | 7                | 4                 | 8                  | 37              | 28                              | 15                  | 197   |

In the first nine months of 2009, net operating profit after taxes from capital market operations amounted to NIS 201 million, compared with NIS 197 million in the corresponding period in 2008.

## **B. Credit Cards - Leumi Card**

This activity includes mainly the issue of credit cards to private customers and providing acquiring services for businesses.

The principal credit card activities are carried out by the subsidiary, Leumi Card, which engages in the issue of credit cards, the provision of acquiring services and the development of payment solutions.

Leumi Card ended the first nine months of 2009 with a net profit of NIS 108 million, compared with NIS 124 million in the corresponding period in 2008. The decline in the net profit results from the profit from extraordinary items in the amount of NIS 17 million during the first nine months of 2008 from the sale of the company's share in Gamma Management and Clearing Ltd.

During the first nine months of 2009, the volume of activity of Leumi Card card holders increased by 3.3 %, compared with the activity in the corresponding period in 2008. The number of valid cards increased by some 5.4 % in the first nine months of 2009, as compared with the corresponding period in 2008.

The following tables set out details of the credit card activity as presented in the various operational segments:

|  | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Total |
|--|-------------|------------------|-------------------|--------------------|-----------------|-------|
| <b>For the three months ending 30 September 2009</b> |             |                  |                   |                    |                 |       |
| NIS millions   |             |                  |                   |                    |                 |       |
| Profit from net interest income                      | 37          | 7                | 2                 | 3                  | -               | 49    |
| Operating and other income                           | 172         | 14               | 7                 | 8                  | 1               | 202   |
| Total income   | 209         | 21               | 9                 | 11                 | 1               | 251   |
| Provision for doubtful debts                         | 5           | 1                | 1                 | 1                  | -               | 8     |
| Operating and other expenses                         | 134         | 18               | 5                 | 8                  | -               | 165   |
| Operating profit before taxes                        | 70          | 2                | 3                 | 2                  | 1               | 78    |
| Minority Interests                                   | (7)         | -                | -                 | -                  | -               | (7)   |
| Net profit   | 42          | 1                | 3                 | 2                  | 1               | 49    |

|  | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Total |
|--|-------------|------------------|-------------------|--------------------|-----------------|-------|
| <b>For the three months ending 30 September 2008</b> |             |                  |                   |                    |                 |       |
| NIS millions   |             |                  |                   |                    |                 |       |
| Profit from net interest income                      | 27          | 2                | 5                 | 1                  | -               | 35    |
| Operating and other income                           | 175         | 7                | 18                | 2                  | 1               | 203   |
| Total income   | 202         | 9                | 23                | 3                  | 1               | 238   |
| Provisions for doubtful debts                        | 5           | -                | 1                 | -                  | -               | 6     |
| Operating and other expenses                         | 104         | 2                | 19                | 2                  | -               | 127   |
| Operating profit before taxes                        | 93          | 7                | 3                 | 1                  | 1               | 105   |
| Operating profit after taxes                         | 63          | 5                | 3                 | -                  | 1               | 72    |
| Profit from extraordinary items after taxes          | (7)         | -                | (1)               | -                  | -               | (8)   |
| Net profit   | 56          | 5                | 2                 | -                  | 1               | 64    |

|   | House-holds | Small businesses | Corporate banking | Commercial banking | Private banking | Total |
|---|-------------|------------------|-------------------|--------------------|-----------------|-------|
| <b>For the nine months ending 30 September 2009</b> |             |                  |                   |                    |                 |       |
| NIS millions  |             |                  |                   |                    |                 |       |
| Profit from net interest income                     | 104         | 12               | 14                | 7                  | -               | 137   |
| Operating and other income                          | 494         | 28               | 34                | 15                 | 1               | 572   |
| Total income  | 598         | 40               | 48                | 22                 | 1               | 709   |
| Provisions for doubtful debts                       | 17          | 1                | 2                 | 1                  | -               | 21    |
| Operating and other expenses                        | 386         | 33               | 46                | 17                 | 1               | 483   |
| Operating profit before taxes                       | 195         | 6                | -                 | 4                  | -               | 205   |
| Operating profit after taxes                        | 135         | 4                | -                 | 3                  | -               | 142   |
| Minority interests                                  | (21)        | -                | -                 | -                  | -               | (21)  |
| Net profit  | 114         | 4                | -                 | 3                  | -               | 121   |

|   | House-holds | Small businesses | Commercial banking | Corporate banking | Private banking | Total |
|---|-------------|------------------|--------------------|-------------------|-----------------|-------|
| <b>For the nine months ending 30 September 2008</b>                     |             |                  |                    |                   |                 |       |
| NIS millions  |             |                  |                    |                   |                 |       |
| Profit from net interest income   | 76          | 7                | 13                 | 3                 | -               | 99    |
| Operating and other income  | 508         | 18               | 37                 | 10                | 2               | 575   |
| Total income  | 584         | 25               | 50                 | 13                | 2               | 674   |
| Provisions for doubtful debts   | 12          | -                | 2                  | -                 | -               | 14    |
| Operating and other expenses  | 330         | 13               | 50                 | 9                 | 1               | 403   |
| Operating profit (loss) before taxes                                    | 242         | 12               | (2)                | 4                 | 1               | 257   |
| Operating profit (loss) after taxes                                     | 164         | 8                | (1)                | 2                 | 1               | 174   |
| Leumi's share in profits of companies included on the equity basis, net | -           | -                | -                  | 1                 | -               | 1     |
| Minority interests in profits of consolidated companies                 | (7)         | -                | (1)                | -                 | -               | (8)   |
| Profit from extraordinary items after taxes                             | 202         | 18               | 2                  | 26                | 3               | 251   |
| Net Profit  | 359         | 26               | -                  | 29                | 4               | 418   |

In the first nine months of 2009, net operating profit from credit card activity amounted to NIS 121 million, compared with NIS 167 million in the corresponding period in 2008, a decrease of 27.5%, resulting primarily from an increase in expenses in the amount of NIS 80 million and

from an increase in provisions for doubtful debts in the amount of NIS 7 million, which were partially offset by an increase in income in the amount of NIS 35 million. There was also a net decrease of NIS 13 million, primarily as a result of the reduction of the Bank's holdings in Leumi Card following the allocation of 20% of the Leumi Card shares to Canit – Investment and Finance Management Ltd.

### C. Real estate

|  | Small<br>businesses | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Overseas<br>activities | Total |
|--|---------------------|----------------------|-----------------------|--------------------|------------------------|-------|
| <b>For the three months ending 30 September 2009</b> |                     |                      |                       |                    |                        |       |
| NIS millions   |                     |                      |                       |                    |                        |       |
| Profit from net interest income                      | 47                  | 160                  | 50                    | 3                  | 15                     | 275   |
| Operating and other income                           | 11                  | 12                   | 8                     | 1                  | 7                      | 39    |
| Total income   | 58                  | 172                  | 58                    | 4                  | 22                     | 314   |
| Provision for doubtful debts                         | 22                  | 198                  | 10                    | -                  | 3                      | 233   |
| Operating and other expenses                         | 21                  | 37                   | 14                    | 1                  | 14                     | 87    |
| Operating profit (loss) before taxes                 | 15                  | (63)                 | 34                    | 3                  | 5                      | (6)   |
| Net profit (loss)                                    | 9                   | (40)                 | 22                    | 2                  | 1                      | (6)   |

  

|  | Small<br>businesses | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Overseas<br>activities | Total |
|--|---------------------|----------------------|-----------------------|--------------------|------------------------|-------|
| <b>For the three months ending 30 September 2008</b> |                     |                      |                       |                    |                        |       |
| NIS millions   |                     |                      |                       |                    |                        |       |
| Profit from net interest income                      | 46                  | 152                  | 47                    | 4                  | 23                     | 272   |
| Operating and other income                           | 12                  | 14                   | 7                     | 1                  | 4                      | 38    |
| Total income   | 58                  | 166                  | 54                    | 5                  | 27                     | 310   |
| Provision for doubtful debts                         | 5                   | 1                    | 4                     | -                  | 1                      | 11    |
| Operating and other expenses                         | 17                  | 29                   | 13                    | 1                  | 10                     | 70    |
| Operating profit before taxes                        | 36                  | 136                  | 37                    | 4                  | 16                     | 229   |
| Net profit   | 23                  | 86                   | 23                    | 2                  | 11                     | 145   |



|   | Small<br>businesses | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Overseas<br>activities | Total      |
|---|---------------------|----------------------|-----------------------|--------------------|------------------------|------------|
| <b>For the nine months ending 30 September 2009</b> |                     |                      |                       |                    |                        |            |
| NIS millions  |                     |                      |                       |                    |                        |            |
| Profit from net interest income                     | <b>138</b>          | <b>512</b>           | <b>141</b>            | <b>8</b>           | <b>42</b>              | <b>841</b> |
| Operating and other income                          | <b>33</b>           | <b>43</b>            | <b>23</b>             | <b>3</b>           | <b>14</b>              | <b>116</b> |
| Total income  | <b>171</b>          | <b>555</b>           | <b>164</b>            | <b>11</b>          | <b>56</b>              | <b>957</b> |
| Provision for doubtful debts                        | <b>36</b>           | <b>252</b>           | <b>20</b>             | <b>-</b>           | <b>9</b>               | <b>317</b> |
| Operating and other expenses                        | <b>63</b>           | <b>93</b>            | <b>43</b>             | <b>5</b>           | <b>41</b>              | <b>245</b> |
| Operating profit before taxes                       | <b>72</b>           | <b>210</b>           | <b>101</b>            | <b>6</b>           | <b>6</b>               | <b>395</b> |
| Net profit  | <b>46</b>           | <b>135</b>           | <b>65</b>             | <b>4</b>           | <b>4</b>               | <b>254</b> |

  

|  | Small<br>businesses | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Overseas<br>activities | Total |
|--|---------------------|----------------------|-----------------------|--------------------|------------------------|-------|
| <b>For the nine months ending on 30 September 2008</b> |                     |                      |                       |                    |                        |       |
| NIS millions   |                     |                      |                       |                    |                        |       |
| Profit from net interest income                        | 136                 | 423                  | 144                   | 6                  | 51                     | 760   |
| Operating and other income                             | 36                  | 38                   | 19                    | 3                  | 13                     | 109   |
| Total income   | 172                 | 461                  | 163                   | 9                  | 64                     | 869   |
| Provision for doubtful debts                           | 9                   | 35                   | 46                    | -                  | -                      | 90    |
| Operating and other expenses                           | 57                  | 76                   | 41                    | 4                  | 33                     | 211   |
| Operating profit before taxes                          | 106                 | 350                  | 76                    | 5                  | 31                     | 568   |
| Net profit   | 67                  | 221                  | 48                    | 3                  | 22                     | 361   |

## Profit Centers in the Group

The following table sets out details of the contribution of the Group's major profit centers to net operating profit:

|  | For the first nine months of |                     |        | For the first nine months of |                     |        |
|--|------------------------------|---------------------|--------|------------------------------|---------------------|--------|
|  | 2009 <sup>(1)</sup>          | 2008 <sup>(1)</sup> | Change | 2009 <sup>(2)</sup>          | 2008 <sup>(2)</sup> | Change |
|  | NIS millions                 |                     | %      | NIS millions                 |                     | %      |
| The Bank   | <b>1,047</b>                 | 277                 | 278.0  | <b>1,020</b>                 | 612                 | 66.7   |
| Consolidated companies in Israel <sup>(3)</sup>                                | <b>373</b>                   | 488                 | (23.6) | <b>373</b>                   | 488                 | (23.6) |
| Overseas consolidated companies <sup>(4)</sup>                                 | <b>87</b>                    | (99)                | +      | <b>114</b>                   | (434)               | +      |
| Companies included on the equity basis <sup>(3)</sup>                          | <b>(65)</b>                  | 360                 | -      | <b>(65)</b>                  | 360                 | -      |
| Net operating profit   | <b>1,442</b>                 | 1,026               | 40.5   | <b>1,442</b>                 | 1,026               | 40.5   |
| Overseas subsidiaries' profit, in nominal terms (US\$ millions) <sup>(5)</sup> | <b>23.9</b>                  | 24.7                | (3.2)  | <b>23.9</b>                  | 24.7                | (3.2)  |

- (1) Translation adjustments in respect of overseas investments were offset against translation adjustments of the financing sources at the Bank after the effect of taxes.
- (2) According to the financial statements (not including translation adjustments of the financing sources at the Bank).
- (3) The companies included on the equity basis of the Israeli companies were included in the data of the consolidated companies in Israel.
- (4) After certain adjustments to Israeli accounting principles.
- (5) As reported by the overseas subsidiaries, including overseas branches and minority interests.

### The following are the main changes in the contribution of the profit centers (after translation adjustments):

- The increase in net operating profit at the Bank arises mainly from an increase in operating and other income, from a reduction in salary expenses and from a decrease in provisions for taxes, which were partially offset by a decrease in net interest income and by an increase in provisions for doubtful debts.
- The decrease in net operating profit of consolidated companies in Israel derives mainly from a decrease in the profits of Leumi Real Holdings' due to a decrease in the contribution of Paz, and from a decrease in the Group's share of the profits of Leumi Card due to the sale of 20% of the company and from a decrease in the profits of Leumi Mortgage Bank, Leumi Leasing and Leumi Partners.
- The increase in the profit of overseas subsidiaries derives mainly from positive exchange rate differentials in respect of overseas investments, compared with negative exchange rate differentials in the corresponding period in 2008, which were partially offset by a decrease in current profitability of the overseas subsidiaries.

The overseas subsidiaries' operating profits in nominal terms as published by them (including the Bank's overseas branches and minority interests) totaled some US\$ 23.9 million, a decrease of US\$ 0.8 million compared with the corresponding period in 2008. The contribution of the overseas subsidiaries in shekels, after certain adjustments to Israeli accounting principles,

amounted to a profit of NIS 114 million, compared with a loss of NIS 434 million in the corresponding period in 2008. Excluding the effect of exchange rate differentials in respect of the cost of financing sources, net, the profit of the overseas subsidiaries amounted to NIS 86 million, as compared with a loss of NIS 99 million in the corresponding period in 2008, an increase of NIS 185 million, deriving mainly from positive exchange rate differentials in respect of the overseas investments, due to the weakening of the shekel in relation to the foreign currencies.

## Activities of Major Subsidiaries and Affiliates

### General

The Bank Leumi Group operates in Israel and abroad through overseas subsidiaries which are banks, a mortgage bank, finance companies and financial service companies. The Group also invests in non-banking companies operating in the fields of insurance, infrastructure and real estate.

### Consolidated Subsidiaries in Israel

The Bank's investments in consolidated subsidiaries in Israel amounted to NIS 6,253 million on 30 September 2009, compared with NIS 5,561 million on 31 December 2008. The contribution to net profit in the first nine months of 2009 was NIS 373 million, compared with NIS 505 million in the corresponding period in 2008, a decrease of 26.2%.

The following table sets out the contribution of the major consolidated companies in Israel to the net profit of the Group:

|  | Return on Group's investment       |             | Contribution to Group's profit <sup>(1)</sup> |              |               |
|--|------------------------------------|-------------|---|--------------|---------------|
|  | For the period ending 30 September |             |   |              |               |
|  | 2009                               | 2008        | 2009  | 2008         | Change        |
|  | %                                  |             | NIS millions                                  |              | %             |
| Leumi Mortgage Bank                              | 5.7                                | 7.0         | 93.0  | 105.8        | (12.1)        |
| Arab Israel Bank                                 | 25.3                               | 25.2        | 65.5  | 64.3         | 1.9           |
| Leumi Card                                       | 20.2                               | 53.3        | 86.5  | 115.3        | (25.0)        |
| Leumi Partners <sup>(2)</sup>                    | 5.7                                | 15.6        | 12.3  | 47.4         | (74.1)        |
| Leumi Securities (previously Psagot – Ofek)      | 2.3                                | 4.7         | 0.8   | 1.5          | (46.7)        |
| Leumi Real Holdings                              | 16.1                               | 27.6        | 66.6  | 100.6        | (33.8)        |
| Leumi Leasing and Investments                    | 5.0                                | 8.0         | 31.4  | 48.4         | (35.1)        |
| Others   | 2.5                                | 3.4         | 16.6  | 22.0         | (24.5)        |
| <b>Total consolidated subsidiaries in Israel</b> | <b>8.7</b>                         | <b>12.8</b> | <b>372.7</b>                                  | <b>505.3</b> | <b>(26.2)</b> |

(1) The profit (loss) presented is according to the Group's share in the results.

(2) Including the profit and/or loss of companies included on the equity basis of Leumi Partners.

### Leumi Mortgage Bank Ltd.

On 30 June 2009, Leumi Mortgage Bank issued 44,220 shares of NIS 1 par value each to the Bank, for a consideration of some NIS 100 million, and on 29 September 2009, Leumi Mortgage Bank issued 43,046 shares of NIS 1 par value each to the Bank for a consideration of some NIS 100 million.

**The following table presents data on new loans granted and loans refinanced for the purchase of residential apartments, while pledging residential apartments:**

|                                 | 2009         | 2008        |        |
|---------------------------------|--------------|-------------|--------|
|                                 | Nine months  | Nine months | Change |
|                                 | NIS millions |             | %      |
| From Leumi Mortgage Bank funds  | <b>6,100</b> | 6,049       | 0.8    |
| From Ministry of Finance funds: |              |             |        |
| Loans                           | <b>46</b>    | 183         | (74.9) |
| Standing loans                  | <b>3</b>     | 5           | (40.0) |
| Total new loans                 | <b>6,149</b> | 6,237       | (1.4)  |
| Refinanced loans                | <b>1,595</b> | 933         | 71.0   |
| Total                           | <b>7,744</b> | 7,170       | 8.0    |

### Overseas Consolidated Subsidiaries

The Bank's investments in overseas consolidated subsidiaries amounted to NIS 4,309 million on 30 September 2009, compared with NIS 4,057 million on 31 December 2008.

In the first nine months of 2009, the contribution of the overseas consolidated subsidiaries to the net operating profit of the Group, as reported in shekels and after offsetting translation adjustments, amounted to a profit of NIS 87 million, compared with a loss of NIS 100 million in the corresponding period in 2008, as detailed below.

|  | For the nine months ending<br>30 September |       |
|--|--|-------|
|  | 2009                                       | 2008  |
|  | NIS millions                               |       |
| Operating profit of the subsidiaries in shekels (the Group's share)                      | <b>85</b>                                  | 72    |
| Exchange rate differentials in respect of the investment                                 | <b>29</b>                                  | (507) |
| Total  | <b>114</b>                                 | (435) |
| Exchange rate differentials in respect of the net cost of financing sources, after taxes | <b>(27)</b>                                | 335   |
| Total contribution of the subsidiaries (after offsetting net financing sources)          | <b>87</b>                                  | (100) |

The following table sets out the contribution of the principal overseas consolidated companies to the net profit of the Group:

|   | Return on the Group's investment   |          | Contribution to the Group's profit <sup>(*)</sup> |                |          |
|---|------------------------------------|----------|---|----------------|----------|
|   | For the period ending 30 September |          |   |                | Change   |
|   | 2009                               | 2008     | 2009  | 2008           |          |
|   | %                                  |          | NIS millions                                      |                | %        |
| Leumi USA (BLC)                                 | 1.0                                | -        | 17.8  | (19.1)         | +        |
| Leumi UK  | 7.7                                | -        | 35.1  | (12.8)         | +        |
| Leumi Switzerland                               | 4.2                                | -        | 17.5  | (10.0)         | +        |
| Leumi Luxembourg                                | 75.9                               | -        | 11.2  | (53.6)         | +        |
| Leumi Re  | -                                  | 14.7     | (2.6)   | 11.0           | -        |
| Leumi Romania                                   | 1.8                                | -        | 5.8   | (12.8)         | +        |
| Others  | 1.1                                | -        | 2.1   | (3.1)          | +        |
| <b>Total overseas consolidated subsidiaries</b> | <b>2.7</b>                         | <b>-</b> | <b>86.9</b>                                       | <b>(100.4)</b> | <b>+</b> |

(\*) Translation adjustments in respect of the overseas investments were offset against translation adjustments in respect of the Bank's financing sources after the effect of taxes, in the amount of NIS (27) million (NIS 335 million in 2008). The following are some of the sums that were offset:

Leumi USA - NIS 18 million in 2009, compared with NIS 163 million in 2008.  
Leumi UK - NIS (33) million in 2009, compared with NIS 88 million in 2008.  
Leumi Switzerland - NIS (13) million in 2009, compared with NIS 24 million in 2008.  
Leumi Romania - NIS 3 million in 2009, compared with NIS 35 million in 2008.

The increase in the contribution to profit derives mainly from the effect of the depreciation of the shekel in relation to most currencies. The effect of the exchange rate differentials was to increase pre-tax profit by NIS 29 million during the first nine months of 2009, compared with a reduction of pre-tax profit by NIS 507 million in the corresponding period in 2008. Net financing expenses recorded at the Bank, and which offset part of these exchange rate differentials, totaled some NIS 27 million during the first nine months of 2009, compared with income of NIS 335 million in the corresponding period in 2008.

The following table sets out details of the net profit (loss) of the overseas subsidiaries as reported by them:

|                         | For the nine months ending 30 September |       |         |
|-------------------------|---|-------|---------|
|                         | 2009                                    | 2008  | Change  |
|                         | NIS millions                            |       | %       |
| Leumi USA (BLC) (US\$)  | 5.3                                     | 21.6  | (75.5)  |
| Leumi (UK) (£)          | 4.0                                     | 7.8   | (48.7)  |
| Leumi Switzerland (CHF) | 6.8                                     | 2.8   | 142.9   |
| Leumi Luxembourg (€)    | 2.1                                     | (8.2) | (125.6) |
| Leumi Re (US\$)         | (0.5)                                   | 4.4   | (111.4) |
| Leumi Romania – Ron     | 11.7                                    | 7.3   | 60.3    |

The nominal profit of the overseas consolidated subsidiaries as reported by them totaled US\$ 24.8 million in the first nine months of 2009, compared with US\$ 35.8 million in the corresponding period in 2008, a decrease of 11.8%.

### **Bank Leumi Switzerland**

In October 2009, Bank Leumi Switzerland was reprimanded by the Swiss bank regulatory authority (FINMA), in respect of a one-time incident that occurred at the bank's Geneva branch at the end of 2007.

This was an incident which was examined by FINMA which determined that the branch transmitted incorrect information to FINMA about a specific customer. It also found that the branch had used the services of an attorney, who had worked with the bank for many years, but who in this case had also been involved with the customer's account as an authorized signatory, which led to a conflict of interests.

FINMA appointed an international accounting firm to examine the manner in which the examination's findings were implemented by Bank Leumi Switzerland.

### **Bank Leumi (Luxembourg)**

In April 2009, Bank Leumi (Luxembourg) increased its capital by € 6 million, through the issue of shares to the Bank.

See Note 6 to the Financial Statements regarding legal proceedings and other matters relating to the consolidated companies.

## **Non-Banking Activities of Companies Included on the Equity Basis**

Total investments of the Group in companies included on the equity basis amounted to NIS 1,908 million on 30 September 2009, compared with NIS 1,842 million on 31 December 2008.

During the first nine months of 2009, the contribution to net profit was "0", compared with a profit of some NIS 471 million in the corresponding period in 2008.

## **Exposure to Risk and Methods of Risk Management**

### **Exposure and Management of Market Risk**

The business results, the fair value of the assets and the liabilities, the shareholders' equity, the cash-flows and the value of the Bank are exposed to market risks arising from volatility in the interest rates, the exchange rates, the CPI, the prices of securities in Israel and abroad and other economic indices.

The ongoing market risk management is intended to assist in achieving the business goals while estimating the anticipated profit from managing the risks, together with the damage that may result from exposure to the said risks. Such management is based on ongoing forecasts and evaluations

of developments in the capital and financial markets in Israel and throughout the world. The Bank manages the exposures to market risk in a dynamic fashion.

The market risk management policy includes the establishment of limits on the financial exposures. The limits are intended to reduce the damage that could occur as a result of unexpected market changes. The system of limits defines the effect of exposure on the economic value, the accounting profit and the liquidity situation to unexpected changes in the various risk factors, such as interest rates, the CPI, exchange rates, etc.

The limits set at Group level include all of the subsidiaries in Israel and abroad. The subsidiaries abroad set market risk management policy in coordination with the Bank in Israel. The frameworks for market risk exposures are determined according to a uniform format prescribed by the Bank and are approved by the Bank's Manager of Market Risks. Leumi Mortgage Bank and Leumi Partners manage market risks independently, but in coordination with the Bank's Manager of Market Risks, due to the dissimilar nature of their activities from those of the Bank. Information regarding the position of the exposures according to the prescribed frameworks is received from the subsidiaries once a month or upon request, and is taken into account in the overall management of the Group's exposures.

The following table shows the capital requirements in respect of market risks, in accordance with the directives of the Bank Supervision Department:

|  | <b>30 September<br/>2009</b> | 31 December<br>2008 |
|--|------------------------------|---------------------|
|  | NIS millions                 |                     |
| <b>Capital requirement in respect of</b>             |                              |                     |
| Interest risks                                       | <b>432</b>                   | 333                 |
| Share price risk                                     | <b>19</b>                    | 4                   |
| Exchange rate risk                                   | <b>89</b>                    | 78                  |
| Inflation risk                                       | <b>241</b>                   | 17                  |
| Options  | <b>64</b>                    | 61                  |
| Total capital requirement in respect of market risks | <b>845</b>                   | 493                 |

### **Basis Exposure**

The exposure to basis risk is expressed as the loss that may occur in consequence of the effect of changes in the CPI and exchange rates on the difference between the values of the assets and the liabilities. Basis exposure includes the effect of futures transactions, in each of the linkage sectors, and the exposure to share indices.

The Bank uses an economic approach in managing basis exposure. Accordingly, there is no strict adherence to the accounting classification as presented in the Note on assets and liabilities according to linkage basis, but adjustments are made taking into account the economic reality. In its ongoing management of the exposure, the Bank takes into consideration the inconsistency that is sometimes created, with the objective of limiting the impact on the reported accounting profit.

According to accounting principles, the capital is defined as an unlinked shekel source, such that an investment of the capital in a sector other than the unlinked shekel sector is defined as a basis

exposure. All the exposure to basis risks is measured as a percentage of the Bank's exposed capital.

The exposed capital at Bank level, includes the shareholders' equity and certain reserves, less fixed assets and investments in subsidiaries and associated companies, excluding the investments in subsidiaries abroad that are financed from sources in foreign currency, and are not therefore deducted from the capital. At Group level, the exposed capital includes the shareholders' equity and certain reserves, less fixed assets and investments in companies included on the equity basis.

The following table sets out the actual exposure at Group level compared with the limits fixed by the Board of Directors. The data is presented in terms of percentages of the exposed capital:

|                                | Approved limits<br>maximum surplus<br>(or deficit) | Actual exposure (%) <sup>*</sup> |                         |                        |
|--------------------------------|--|----------------------------------|-------------------------|------------------------|
|                                |  | <b>30<br/>September<br/>2009</b> | 30<br>September<br>2008 | 31<br>December<br>2008 |
| Unlinked                       | 50% - (100%)                                       | <b>10.5</b>                      | (48.8)                  | (25.0)                 |
| CPI-linked                     | 100% - (50%)                                       | <b>(8.2)</b>                     | 48.3                    | 26.1                   |
| Foreign currency <sup>**</sup> | 25% - (10%)  | <b>(2.3)</b>                     | 0.6                     | (1.1)                  |

\* Excluding CPI/shekel options embedded in financial instruments. Taking into account the delta exposure for these options, the CPI-linked deficit for 30 September 2009 would be increased by 17%, and the CPI-linked surplus for 30 September 2008 and 31 December 2008 would be reduced by 14% and by 15% respectively.

\*\* In addition, the Bank and the subsidiaries have limits on the maximum position that can be invested in each currency.

During the first nine months of 2009, the percentage of the exposed capital that was invested in the CPI-linked sector fluctuated between a surplus of 24% to a deficit of some 12%, with an average surplus of some 3.7%. A relatively low volume of capital was channeled to the foreign currency and foreign-currency-linked sector, and therefore the effect of the change in exchange rates did not materially affect profits.

Changes in the exchange rate affect the effective tax rate, since the exchange rate differentials in respect of the overseas investments are not taken into account in the income basis for calculating the provision for taxes. Subject to the rates of change in the exchange rates of the various currencies relative to the shekel, and considering the volume of the overseas investments, this may have a material effect on the provision for taxes. The tax exposure in respect of the overseas investments is covered by forward transactions.

The actual effect of the exchange rate differentials during the first nine months of 2009 is presented on page 83, in the context of the contribution of the overseas consolidated subsidiaries to Group profit.

During the first nine months of 2009, the Group complied with all the basis exposure limits approved by the Board of Directors.



The following table shows the sensitivity to changes in the exchange rates of the major currencies as at 30 September 2009. The measurement relates to the effect of such changes on the capital of the Bank and includes the activity in balance sheet and off-balance sheet instruments:

|                                  | US\$ | €    | £    | CHF | Yen |
|----------------------------------|------|------|------|-----|-----|
| NIS millions                     |      |      |      |     |     |
| Increase of 5% in exchange rate  | (7)  | 17   | 8    | (2) | 2   |
| Increase of 10% in exchange rate | (5)  | 36   | 15   | (3) | 4   |
| Decrease of 5% in exchange rate  | 27   | (11) | (7)  | 0   | 0   |
| Decrease of 10% in exchange rate | 62   | (20) | (14) | (3) | 2   |

These data do not take into account the effect of changes in the exchange rates on the income and expense cash flows in foreign currency. According to the assessment of the Bank's Management, a 1% decline in the exchange rate of the shekel against the foreign currencies would reduce the net after tax annual profit by some NIS 10 million, and a similar increase in the exchange rate would raise the profit by a similar amount.

## Interest Exposure

The exposure to risk from changes in interest arises from the gaps between the interest payment dates and the interest adjustment dates of the assets and liabilities in each of the sectors. For the purpose of managing interest risk, the gaps between the assets and liabilities in future periods are examined, and the average durations of the assets, liabilities and capital in each sector are monitored and analyzed. In addition, in each sector, a measurement is made of the exposure to changes in interest relating to the potential erosion of the economic value<sup>1</sup> and the annual accounting profit in consequence of a shift of the yield curves in each of the sectors. During the first nine months of 2009, the Group complied with all the interest exposure limits set by the Board of Directors.

The following table presents the exposure to interest changes at the Group level, calculated according to accounting principles, and in accordance with the presentation in Exhibit C of the Management Review – i.e., the presentation of the current value of future cash flows that extend until the maturity date or the interest adjustment date, whichever is earlier. These cash flows are capitalized at the internal rate of return.

<sup>1</sup> The economic value of the capital is defined as the difference between the current values of the assets and of the liabilities. In calculating the current value, the cash flows are deducted from the credit risk free yields curve - i.e., from the yields of government debentures.

For detailed data on interest exposure, see Exhibit C to the Management Review below.

|   | 30 September 2009 |               |  | 31 December 2008 |            |  |
|---|-------------------|---------------|--|------------------|------------|--|
|   | Unlinked          | CPI-linked    | Foreign currency and foreign currency linked | Unlinked         | CPI-linked | Foreign currency and foreign currency linked |
| <b>Average duration (in years):</b>           |                   |               |  |                  |            |  |
| of assets <sup>(1)</sup>                      | <b>0.36</b>       | <b>3.42</b>   | <b>0.65</b>                                  | 0.45             | 3.33       | 0.55   |
| of liabilities <sup>(1)</sup>                 | <b>0.36</b>       | <b>4.37</b>   | <b>0.38</b>                                  | 0.37             | 4.18       | 0.39   |
| The gap in duration in years                  | -                 | <b>(0.95)</b> | <b>0.27</b>                                  | 0.08             | (0.85)     | 0.16   |
| Difference in the internal rate of return (%) | <b>0.1</b>        | <b>0.22</b>   | <b>0.98</b>                                  | 1.53             | 0.97       | 1.67   |

(1) Excluding forward transactions and options.

The average duration of liabilities in the CPI-linked sector is calculated after taking into account estimates of early repayments of savings plans and withdrawals at exit points, on the basis of a model that estimates the anticipated early repayments on the basis of the behavior of the savers. The average duration of liabilities, according to the original cash-flow of the savings schemes, is longer, and reaches 4.38 years, while the gap in the internal rate of return (IRR) amounts to 0.24%.

The data presented above take into account early repayments of CPI-linked mortgages, pursuant to a statistical model that estimates expected repayments on the basis of the borrowers' behavior and the development of market variables. The average duration of assets as at 30 September 2009, according to the original cash flow, without taking into account early repayments, is longer, and reaches 3.72 years, and the IRR gap amounts to 0.24%.

Current account balances are presented in Exhibit C to the Management Review pursuant to directives of the Bank of Israel as demand deposits for up to one month. However, for the purposes of interest exposure, a certain percentage of the current account balances in shekels and in foreign currency is spread over a repayment period of up to ten years, in accordance with a behavioral model whose basic assumptions are updated on a periodic basis. Taking into account the above assumptions, the average duration of liabilities is longer and reaches 0.57 years in unlinked shekels and 0.53 years in foreign currency, with the IRR gap reaching 1.38% and 1.43% respectively.

Interest exposure risk is managed on the basis of economic exposures and is based on various behavioral assumptions regarding the original payment dates of the assets and liabilities. With the aim of limiting interest risks, the Board of Directors of the Bank and the boards of directors of the Israel and overseas subsidiaries have approved limits on the maximum potential erosion of the economic value and the accounting profit as a result of parallel changes in the interest curves.

The following table presents a summary of the exposures to unforeseen fluctuations of interest rates at the Group level (in NIS millions):\*

| Effect of a parallel change of 1% in the interest curve: | Potential erosion of economic value <sup>1</sup> |                   |                  | Potential erosion of annual profit** |                   |                  |
|--|--|-------------------|------------------|--------------------------------------|-------------------|------------------|
|  | <b>30 September 2009</b>                         | 30 September 2008 | 31 December 2008 | <b>30 September 2009</b>             | 30 September 2008 | 31 December 2008 |
| Actual   | <b>744</b>                                       | 122               | 321              | <b>391</b>                           | 257               | 320              |
| Limit  | <b>1,000</b>                                     | 1,000             | 1,000            | <b>600</b>                           | 700               | 600              |

\* In a direction that causes harm to the Bank.

\*\* The maximum erosion of the annual profit based on an examination of the next three years.

During the first nine months of 2009, the potential erosion of the economic value and annual profit ranged between NIS 321 million in December 2008 to NIS 744 million in September 2009, and between NIS 255 million in April 2009 and NIS 428 million in August 2009, respectively.

The potential erosion of the economic value of the capital resulting from a 1% change in interest rates increased in the first nine months of 2009 by some NIS 423 million, and totalled NIS 744 million at the end of September 2009.

The potential erosion of the accounting profit resulting from a 1% change in interest rates increased from the beginning of the year by some NIS 71 million and totalled NIS 391 million at the end of September 2009.

During the first nine months of 2009, the Group complied with all interest exposure limits prescribed by the Board of Directors.

The following table illustrates the impact of hypothetical changes in the interest rates on the economic value of the financial instruments of the Bank and consolidated companies, excluding non-financial items:

| Change in economic value <sup>1</sup> after the impact of changes in interest rates, as at 30 September 2009, in NIS millions: |                  |            |   |       |                |             |       |        |
|--|------------------|------------|---|-------|----------------|-------------|-------|--------|
|  | Israeli currency |            | Foreign currency, including Israeli currency linked to foreign currency |       |                |             |       |        |
|  | Un-linked        | CPI-linked | Dollar  | Euro  | Pound Sterling | Swiss Franc | Yen   | Others |
| Immediate parallel increase of 1%  | 96.7             | 508.9      | 139.0   | 7.3   | 4.4            | (13.8)      | (1.7) | 10.1   |
| Immediate parallel increase of 0.1%  | 9.7              | 50.9       | 13.9  | 0.7   | 0.4            | (1.4)       | (0.2) | 1.0    |
| Immediate parallel decrease of 1%  | (90.1)           | (483.2)    | (133.7)   | (7.7) | (2.6)          | 15.6        | 1.7   | (9.1)  |

<sup>1</sup> The economic value of the capital is defined as the difference between the current values of the assets and of the liabilities. In calculating the current value, the cash flows are deducted from the credit risk free yields curve - i.e., from the yields of government debentures.

The economic value is, as stated, defined as the difference between the current values of the assets and of the liabilities. In calculating the current value, the cash flows are deducted from the credit risk free yield curve.

### Value at Risk (VaR)

The Bank manages the exposure to market risks by various means, as mentioned above, as well as by means of a statistical model – the VaR model. According to Bank of Israel directives, the risk measured by the VaR relates to the potential loss from holding all the balance-sheet and off-balance-sheet positions exposed to market risks, including the positions in the trading portfolios.

The VaR measures the expected potential loss resulting from possible changes in market prices. In practice, it measures the expected decrease in the present value of the assets less the liabilities in the given mix in the portfolio's structure, at a given confidence level, over a given future period, according to a given statistical distribution. The VaR is calculated monthly at Group level, and more frequently at the Bank level and for the trading portfolios.

The VaR and the limits in VaR terms are calculated according to the parametric model, at a confidence level of 99%, and for a two-week position-holding period. The VaR model has a number of weaknesses. The model assumes that the statistical structure of the changes in prices foreseen in the capital market gives an indication of the future behaviour of these prices. The parametric VaR model also assumes a multivariate normal distribution of the changes in the risk factors. This measurement, by definition, ignores losses that are liable to occur over and above the given significance level (the distribution tail). Examination of stress scenarios provides the lacking perspective.

In order to test the validity of the VaR model, the Bank performs daily backtesting, by comparing the actual change in the economic value of the Bank with the estimated change as derived from the VaR model. The tests performed thus far confirm the validity of the model. As stated above, the Bank's VaR is calculated every two weeks and with a probability of 99%. After two weeks, the backtesting process examines the theoretical change in the Bank's value, assuming that the positions do not change and that the only changes are those in the market prices.

The Bank also periodically calculates the VaR using an historical simulation, and examines the gap between the two measurement methods. Historical simulation enables risk to be measured without reliance on a particular probability structure. The VaR of the option book in the trading portfolio is examined using both the parametric and the Monte Carlo simulation method (in order to test the non-linear risk components).

The following table presents the estimated VaR at Group level in NIS millions:

|           | VaR at Group level               |                         |                        | VaR in mark-to-market portfolios |                         |                        |
|-----------|----------------------------------|-------------------------|------------------------|----------------------------------|-------------------------|------------------------|
|           | <b>30<br/>September<br/>2009</b> | 30<br>September<br>2008 | 31<br>December<br>2008 | <b>30<br/>September<br/>2009</b> | 30<br>September<br>2008 | 31<br>December<br>2008 |
| Actual    | <b>364</b>                       | 242                     | 243                    | <b>82</b>                        | 265                     | 204                    |
| The limit | <b>600</b>                       | 700                     | 600                    | <b>500</b>                       | 500                     | 500                    |

The VaR of the economic value ranged between NIS 389 million in May of 2009 and NIS 236 million in January 2009. The VaR on the Group's mark-to-market portfolios ranged between NIS 228 million in February 2009 and NIS 82 million in September 2009.

During the first nine months of 2009, the Group complied with all the VaR limits set by the Board of Directors.

## **Liquidity Risk**

Liquidity is defined as the corporation's ability to finance increases in assets and to comply with its payment liabilities. The ability to withstand liquidity risk involves the uncertainty relating to the possibility of raising sources and/or realizing assets unexpectedly within a short period, without causing a material loss.

In accordance with Bank of Israel directives, the Bank implements an overall liquidity risk management policy in Israeli currency and in foreign currency. The purpose of this policy is to support the achievement of business goals while evaluating and limiting losses that may arise from exposure to liquidity risks. The principles of the Bank's liquidity management policies have been adopted by the subsidiaries abroad.

The Bank maintains ongoing monitoring of the liquidity position and liquidity risk indices. Liquidity risk is measured and managed through an internal model, Liquidity at Risk (LAR), whose purpose is to evaluate and monitor the liquid means at the Bank's disposal, under various scenarios, which are examined and updated in line with market developments. These scenarios are:

1. A normal scenario that assumes the ordinary course of business, which ensures that the Bank will be able to finance an increase in assets and that it has sufficient sources to pay all its obligations, without having to incur expenses or losses in the process.
2. A statistical scenario relating to an exceptional situation under normal operating conditions, which estimates, at the desired confidence level, the maximum possible decline in the liquidity level during a given period on the basis of some 300 historical observations in Israeli currency and some 250 in foreign currency.
3. Two stress scenarios, assuring the continuation of the Bank's activities at reasonable cost during a bridging period of about a month when stress conditions prevail, as follows:
  - 3.1 A systemic stress scenario, deriving from a negative external event, such as a failure in the capital market or in the entire banking system, which will affect Leumi.
  - 3.2 A stress scenario at Leumi, deriving from a negative internal event occurring solely at Leumi, such as a strike by Leumi employees, the lowering of the Bank's credit rating, embezzlement or fraud on a major scale, and so on.

The liquidity position is examined in each of the scenarios by means of two quantitative indices: the liquidity gap and the liquidity ratio. The liquidity gap is the difference between total liquid assets and total liquid liabilities according to payment periods. The liquidity gap is examined for each of the periods: one day, up to one week, up to one month, up to three months, up to six months and up to one year. The liquidity ratio is the ratio between total liquid assets and total liquid liabilities, and it is also examined according to each of the said payment periods.

The principles at the basis of the model propose that in so far as there are more liquid assets (such as cash, deposits at the Bank of Israel, a realizable debenture portfolio and credit, the repayment of which is expected) than there are liabilities that are expected to be realized pursuant to the model, so does the Bank secure its ability to meet all its liquidity needs. For this purpose, the assets are classified according to their level of liquidity, while liabilities are classified according to the probability of their realization.

The rate of the change in the balance of deposits and credit for all payment periods, under different scenarios, is established according to different parameters in accordance with the level of the scenario's severity. The behavioral functions are defined on the basis of the judgment of the business elements, exercised with the assistance of historical data; these take into consideration parameters such as the size and substance of the deposit according to which the expected cash flows are calculated.

It should be noted that the stress scenarios are more severe than anything that the Bank has experienced in the past and the assumptions of these scenarios are therefore necessarily based more on the judgement of the senior professional elements at the Bank than on any historical data.

The liquidity management policy at Group level is based on the two following principles:

- each subsidiary in Israel and abroad is responsible for the formulation and maintenance of an independent liquidity management policy, while maintaining strict compliance with obligatory directives of the relevant regulatory authorities.
- the subsidiaries may rely, amongst other sources, on the use of credit lines from the Bank, subject to prior arrangement, and subject to regulatory limits.

Leumi has prepared a contingency plan as part of its preparations for an extreme scenario, which includes the strategy for managing a liquidity crisis, including the appointment of a management team to be responsible for dealing with the crisis and defining the procedures and steps required for contending therewith.

In addition to the model described above, Leumi operates an additional measurement system for early warning of exceptional and unexpected developments in liquidity risk.

In September 2008, the Basel Committee issued an updated document addressing liquidity risk management. The document was written as an outcome of the lessons learned from the current financial crisis, and it details a list of new rules pertaining to liquidity management, including: control procedures for the Management and the Board of Directors, the need to determine margins and risk "warning signs," costing of the risk, the need to maintain a "safety cushion", a list of risk-measurement principles, including the use of stress scenarios, management of the intraday liquidity, contingency plans, and more.

The Bank is examining these rules with the objective of implementing them as part of its implementation of the Basel II directives.

As required by the Bank of Israel's Directive No. 342, the Board of Directors has approved the policy for managing liquidity risks and prescribed limits, as follows: the liquidity ratio must be higher than 1 and the liquidity gap must be higher than zero in each of the scenarios during the planned periods of one day, one week and one month.

During the first nine months of 2009, the Group complied with all limits prescribed by the Board of Directors.

For additional details regarding the management of market risks, see pages 173-184 of the 2008 Annual Report.

## **Credit Risk**

For details regarding the exposure to and management of credit risks, see pages 189-202 of the Annual Report for 2008.

The Bank's credit policy is based on the spreading of risks and their supervised management. This is effected through the spread of the Bank's credit portfolio among the various sectors of the economy and among a large number of borrowers. The credit policy serves as a guideline for the Bank's specialized subsidiaries in Israel and abroad, but these subsidiaries delineate the policy in the market segments under their management, except in relation to certain fields, for which there is Group-wide policy. Since it fulfils a central role in financing the Israeli economy, the Bank implements a strategy of involvement in the principal activity sectors of the economy and provides credit to the various types of manufacturing and trading sectors, to infrastructure projects, to the diverse public sector, to individuals and to households.

Within the context of the credit policy of the Bank in Israel, principles and rules have been prescribed according to which the Bank's credit portfolio is to be granted, managed and supervised, with the object of improving the quality of the portfolio and reducing the risk inherent in its management. These principles and rules relate both to the individual customer and to the sectors of the economy.

The Bank's Board of Directors approves the Bank's credit policy, and the sectoral and other limits.

The credit authorities existing in the Bank are valid only if the credit under discussion complies with the Bank's credit policy, or, in the event of a deviation from that policy, if approval was obtained from the entity authorized for such purpose. The authorities to establish credit lines at the various levels were established in light of the borrower's risk rating, the size of the credit line and the nature of the credit, while observing the principle that the worse the borrower's risk rating and the more complex the nature of the credit, the more senior the entity that will make the decision.

As described in the 2008 Annual Report, in order to improve credit risk management, and also to adjust to regulatory requirements, the Bank has established independent units to manage credit risks. These units carry out an independent examination of the credit risks and the risk aspects.

### **The “periodic credit monitoring” process –**

The Bank carries out, in addition to the daily monitoring and examinations which the business elements carry out on an ongoing basis, a quarterly, systematic monitoring process with regard to a broad selection of borrowers, in accordance with the borrowers' risk ratings.

The purpose of the process is to locate and identify potential weaknesses among a broad cross-section of customers. The scope of the examination is determined on a differential basis, in accordance with the risk ratings of the various borrowers. In the context of the process, decisions are made regarding the need to increase supervision of and to intensify of the monitoring of a part of the customer population.

The business elements identify borrowers by using a number of tools and means at the same time, which include both reference to the risk characteristics of the borrower itself and the economic/market/regulatory conditions which could affect the borrower's position. During discussions that are held on a quarterly basis, a decision is made regarding the actions and steps to be taken in order to reduce the borrower's risk and if necessary, classification as a problem loan or recording a provision in respect of the loan is considered.

## **Dealing with the risks resulting from developments in the money and capital markets**

The slowdown in global economic activity in general, and in the local market in particular, and the significant worsening in the ratings of the economic sectors, both in absolute terms and in comparison with previous quarters, necessitate a cautious credit policy with regard to those branches of the economy and credit sectors that are characterized by a high level of risk.

The impact of the lows in the money and capital markets, the crisis in the residential real estate market and in the mortgage markets in the United States and in the United Kingdom, along with the significant write-downs by large banking groups, together obligate the Bank to take measures to identify borrowers whose levels of exposure and risk have risen, borrowers who are likely to encounter difficulties and sectors and populations that are likely to be adversely affected by developments and are in need of intensive attention and support.

The Bank has been monitoring debts that are based on shares constituting a significant portion of their asset value and/or the collateral upon which the Bank is relying.

Borrowers that had designated funds that they had raised as shareholders' equity for the leveraging of investments abroad are also being examined.

As is known, during the years 2006-2007, there was a sharp increase in the amounts raised through debenture offerings by Israeli real estate companies. A part of the funds raised through these offerings was used for making investments abroad, *inter alia*, for purchasing land for the construction of projects abroad – in the United States, Canada, Western Europe as well as in Central and Eastern Europe. The payments to be made under the debentures were to be based on the completion of projects, the sale of assets and on further rounds of capital raising. In light of the decline in the value of the assets in most of the above countries, the impact of macro-economic factors abroad and the prevailing uncertainty, some of the companies are encountering difficulties in raising the resources they need in order to pay the debenture-holders.

Taking note of the difficulty of raising sources of cash flows as stated, and in light of the payment obligations due in the near future, some of the companies have initiated contacts with debenture holders for the purpose of reaching debt arrangements. These companies are negotiating with their creditors in order to formulate a framework for the payment of their debts on the one hand and for their continued operation, on the other hand. The re-scheduling of these companies' obligations will include compensation to the debt-holders in the form of increased interest rates and/or the conversion of part of the debt into equity.

For some of the companies, it will be necessary to obtain the financing bank's/banks' consent to participate in the arrangement.

Regarding Israeli entrepreneurs who are Bank customers and who are active in the real estate sector overseas, including subsidiaries of holding companies based in Israel, the Bank is examining the possibility that the value of their assets has been eroded as a result of the global financial crisis, and that the profitability and cash flows that were expected to be generated by such activity, may be adversely affected.

The Bank continues to review its credit portfolio on an ongoing basis, as well as the implications of the declines on global stock markets for the ability of weak companies to raise funds.

The Bank is aware of the adverse effect of the exposure to changes in the exchange rates, especially on the financial/economic position of exporters and/or those highly dependent upon



foreign currency proceeds. Volatility in the currency rates and in the prices of raw materials necessitates the execution of hedging transactions.

Emphasis is also placed on customers who are exposed to the effect of the continued deterioration in the payment ethic and the credit shortage, to declines in demand for consumer products and to changes in activity in the real estate sectors, to the condition of other economic sectors in Israel and throughout the world, including connection with geographical regions that have been particularly affected, etc. The credit ratings of borrowers are regularly updated, in accordance with the circumstances.

The Bank's Management regularly discusses exposures that might arise from the crisis, including in-depth discussions of customers that have been defined as sensitive.

For the purpose of managing the Bank's credit portfolio as a whole, there exists a unit whose functions include, *inter alia*, the following matters: evaluation of the credit portfolio's performance in terms of yield versus risk, formulation of recommendations regarding voluntary limits in different segments (such as economic sectors, concentrations), formulation of recommendations regarding the credit portfolio's optimal structure and for limits on the credit portfolio and the creation of transparency in the credit portfolio in accordance with its risk levels and factors. In addition, the unit examines the impact of new transactions on the credit portfolio's structure and risks, and it makes recommendations regarding the carrying-out of transactions/measures in order to improve the portfolio's structure and risks. All this is in order to optimize the credit portfolio and to improve the order of priorities with regard to the allocation of capital, while increasing profitability in conformity with the risk presented by the transactions. The unit is engaged in the development of advanced methodological and computerized tools which will enable the optimal carrying-out of the above-mentioned functions.

The following are certain data relating to credit exposures and risks:

# 1. Exposure and Management of Credit Risks in Credit to the Public

Following are the weighted balances of the credit risk in the balance sheet:

| 30 September 2009  |                           |                 |        |        |         |                          |                             |                  |
|--|---------------------------|-----------------|--------|--------|---------|--------------------------|-----------------------------|------------------|
|  | Balance-sheet<br>balances | Weighting rates |        |        |         |                          | Deduction<br>from<br>equity | Risk<br>balances |
|  |                           | 0 %             | 20%    | 50 %   | 100%    | 200 %                    |                             |                  |
| In NIS millions  |                           |                 |        |        |         |                          |                             |                  |
| Assets   |                           |                 |        |        |         |                          |                             |                  |
| Cash and deposits in banks   | 43,934                    | 31,893          | 12,041 | -      | -       | -                        | -                           | 2,408            |
| Securities   | 58,381                    | 34,530          | 18,447 | -      | 4,889   | 146                      | 369                         | 8,869            |
| Securities borrowed or purchased under buy-back agreements           | 1,823                     | 1,823           | -      | -      | -       | -                        | -                           | -                |
| Credit to the public   | 204,304                   | 13,731          | 967    | 14,891 | 174,715 | -                        | -                           | 182,354          |
| Credit to the government   | 430                       | 418             | -      | -      | 12      | -                        | -                           | 12               |
| Investments in companies included on the equity basis <sup>(a)</sup> | 1,908                     | -               | -      | -      | 1,828   | -                        | 80                          | 1,828            |
| Buildings and equipment  | 3,544                     | -               | -      | -      | 3,544   | -                        | -                           | 3,544            |
| Other assets   | 9,639                     | 1,061           | 3,982  | -      | 4,490   | -                        | 106                         | 5,286            |
| Total assets   | 323,963                   | 83,456          | 35,437 | 14,891 | 189,478 | 146                      | 555                         | 204,301          |
|  |                           |                 |        |        |         |                          |                             |                  |
| 31 December 2008   |                           |                 |        |        |         |                          |                             |                  |
|  | Balance-sheet<br>balances | Weighting rates |        |        |         | Deduction<br>from equity | Risk balances               |                  |
|  |                           | 0%              | 20%    | 50%    | 100%    |                          |                             |                  |
| NIS millions   |                           |                 |        |        |         |                          |                             |                  |
| Assets   |                           |                 |        |        |         |                          |                             |                  |
| Cash and deposits in banks   | 33,130                    | 19,304          | 13,808 | -      | 18      | -                        | -                           | 2,779            |
| Securities   | 44,910                    | 20,719          | 16,117 | -      | 8,074   | -                        | -                           | 11,298           |
| Securities borrowed or purchased under buy-back agreements           | 201                       | 125             | -      | -      | 76      | -                        | -                           | 76               |
| Credit to the public   | 213,548                   | 14,644          | 900    | 14,761 | 183,243 | -                        | -                           | 190,803          |
| Credit to the government   | 520                       | 481             | -      | -      | 39      | -                        | -                           | 39               |
| Investments in companies included on the equity basis (a)            | 1,842                     | -               | -      | -      | 1,772   | 70                       | -                           | 1,772            |
| Buildings and equipment  | 3,445                     | -               | -      | -      | 3,445   | -                        | -                           | 3,445            |
| Other assets   | 13,529                    | 1,361           | 5,473  | -      | 6,440   | 255                      | -                           | 7,535            |
| Total assets   | 311,125                   | 56,634          | 36,298 | 14,761 | 203,107 | 325                      | -                           | 217,747          |

(a) Balances of investments in shares and subordinated capital notes of financial companies are deducted from the capital, and therefore, also from the balance of securities and from investments in companies included on the equity basis.

2. The following table presents data on reductions in credit risk in the Group as at 30 September 2009, in NIS millions:

|   | Secured by government securities | Secured by bank securities | Secured by deposits | Covered by bank guarantees | Covered by foreign trade risk insurance |
|---|----------------------------------|----------------------------|---------------------|----------------------------|---|
| Cash and deposits with banks  | -                                | -                          | -                   | -                          | <b>190</b>                              |
| Credit to the public  | <b>1,548</b>                     | <b>17</b>                  | <b>12,229</b>       | <b>772</b>                 | <b>9</b>                                |
| Other assets  | <b>125</b>                       | -                          | <b>211</b>          | -                          | -                                       |
| Book value of transactions in which the balance represents a credit risk. | <b>244</b>                       | -                          | <b>2,170</b>        | <b>433</b>                 | -                                       |
| Book value of derivatives   | <b>493</b>                       | -                          | <b>504</b>          | -                          | -                                       |

The following table presents data on reductions in credit risk in the Group as at 31 December 2008, in NIS millions:

|   | Secured by government securities | Secured by bank securities | Secured by deposits | Covered by bank guarantees | Covered by foreign trade risk insurance |
|---|----------------------------------|----------------------------|---------------------|----------------------------|---|
| Cash and deposits with banks  | -                                | -                          | -                   | -                          | 69                                      |
| Credit to the public  | 1,547                            | 3                          | 13,125              | 775                        | 19                                      |
| Other assets  | 60                               | -                          | 140                 | -                          | -                                       |
| Book value of transactions in which the balance represents a credit risk. | 205                              | -                          | 2,638               | 521                        | 1                                       |
| Book value of derivatives   | 198                              | -                          | 248                 | -                          | -                                       |

The above data are for the purpose of reducing the risk assets for the capital adequacy calculation, as required in Bank of Israel directives.

### 3. Credit risk in derivatives activity

The following table presents the weighted balances of off-balance-sheet credit risk:

| <b>30 September 2009</b>                            |                       |               |                 |               |     |               |                  |
|---|-----------------------|---------------|-----------------|---------------|-----|---------------|------------------|
|   | Par value<br>balances | Book<br>value | Weighting rates |               |     |               | Risk<br>balances |
|   |                       |               | 0%              | 20%           | 50% | 100%          |                  |
| NIS millions  |                       |               |                 |               |     |               |                  |
| <b>Off-balance-sheet instruments</b>                |                       |               |                 |               |     |               |                  |
| Transactions whose balance represents a credit risk | <b>90,097</b>         | <b>25,866</b> | <b>2,418</b>    | <b>1,698</b>  | -   | <b>21,750</b> | <b>22,089</b>    |
| Derivatives   | <b>272,433</b>        | <b>27,712</b> | <b>997</b>      | <b>17,319</b> | -   | <b>9,396</b>  | <b>12,860</b>    |
| Others  | <b>1,209</b>          | <b>121</b>    | -               | -             | -   | <b>121</b>    | <b>121</b>       |
| Total off-balance-sheet instruments                 | <b>363,739</b>        | <b>53,699</b> | <b>3,415</b>    | <b>19,017</b> | -   | <b>31,267</b> | <b>35,070</b>    |
| <b>31 December 2008</b>                             |                       |               |                 |               |     |               |                  |
|   | Par value<br>balances | Book<br>value | Weighting rates |               |     |               | Risk<br>balances |
|   |                       |               | 0%              | 20%           | 50% | 100%          |                  |
| NIS millions  |                       |               |                 |               |     |               |                  |
| <b>Off-balance-sheet instruments</b>                |                       |               |                 |               |     |               |                  |
| Transactions whose balance represents credit risk   | 96,273                | 25,252        | 2,870           | 1,290         | -   | 21,092        | 21,350           |
| Derivatives   | 250,939               | 25,472        | 448             | 15,987        | -   | 9,037         | 12,234           |
| Others  | 1,595                 | 159           | -               | -             | -   | 159           | 159              |
| Total off-balance-sheet instruments                 | 348,807               | 50,883        | 3,318           | 17,277        | -   | 30,288        | 33,743           |

4. The following table presents the credit exposure with respect to the fair value of derivatives, according to counterparties to the contract (presented in other assets as at 30 September 2009):

|   | AAA to<br>AA-   | A+    | A   | A-  | BBB<br>to<br>BBB- | Below<br>B- | Unrated | Total |
|---|-----------------|-------|-----|-----|-------------------|-------------|---------|-------|
| Overseas Banks  | In NIS millions |       |     |     |                   |             |         |       |
| Euro zone <sup>(1)</sup>  | 213             | 528   | 165 | 203 | 3                 | -           | 11      | 1,123 |
| United Kingdom <sup>(2)</sup>                                   | 322             | 546   | 344 | 50  | 10                | -           | -       | 1,272 |
| United States   | 26              | 143   | 115 | 3   | -                 | -           | -       | 287   |
| Other   | 42              | 128   | 5   | -   | -                 | -           | -       | 175   |
| Total overseas<br>banks   | 603             | 1,345 | 629 | 256 | 13                | -           | 11      | 2,857 |
| Israeli banks <sup>(3)</sup>                                    | 171             | 301   | -   | -   | 483               | -           | 31      | 986   |
| <b>Corporate customers according to branches of the economy</b> |                 |       |     |     |                   |             |         |       |
| Financial services <sup>(4)</sup>                               |                 |       |     |     |                   |             |         | 1,027 |
| Industry <sup>(5)</sup>   |                 |       |     |     |                   |             |         | 774   |
| Construction and real estate                                    |                 |       |     |     |                   |             |         | 295   |
| Transportation and storage                                      |                 |       |     |     |                   |             |         | 153   |
| Trade   |                 |       |     |     |                   |             |         | 105   |
| Electricity and water   |                 |       |     |     |                   |             |         | 208   |
| Business services   |                 |       |     |     |                   |             |         | 31    |
| Private individuals   |                 |       |     |     |                   |             |         | 25    |
| Communications and computer<br>services                         |                 |       |     |     |                   |             |         | 50    |
| Others  |                 |       |     |     |                   |             |         | 11    |
| Total corporate customers                                       |                 |       |     |     |                   |             |         | 2,679 |
| Others*   |                 |       |     |     |                   |             |         | 323   |
| Total exposure  |                 |       |     |     |                   |             |         | 6,845 |

- Reverse transactions carried out by the customers and offset for the purpose of risk according to the branches of the economy.

(1) This amount includes transactions in 7 countries.

(2) This amount includes transactions with 23 banks.

(3) This amount includes transactions with 11 banks.

(4) This amount includes transactions with 289 customers, where the highest amount for a single customer is NIS 213 million.

(5) This amount includes transactions with 259 customers, where the highest amount for a single customer is NIS 629 million.

## Credit exposure to overseas financial institutions

The following table sets out the credit exposure to overseas financial institutions <sup>(1)</sup>:

| <b>As at 30 September 2009</b>  |  |                           |   |                     |
|---|--|---------------------------|---|---------------------|
|   | Balance<br>Sheet Credit<br>risk <sup>(2)</sup> | Securities <sup>(3)</sup> | Current off-balance sheet<br>credit risk <sup>(4)</sup> | Current credit risk |
|   | NIS millions                                   |                           |   |                     |
| <b>External credit<br/>rating <sup>(5)</sup></b>                          |  |                           |   |                     |
| AAA to AA-  | 3,277  | 3,631                     | 144   | 7,052               |
| A+ to A-  | 9,749  | 10,854                    | 337   | 20,940              |
| BBB+ to BBB-  | 452  | 406                       | 9   | 867                 |
| BB+ to B-   | 195  | 44                        | 11  | 250                 |
| Below B   | 12   | -                         | -   | 12                  |
| Unrated   | 688  | 293                       | 27  | 1,008               |
| Total current<br>credit exposure to<br>overseas financial<br>institutions | 14,373   | 15,228                    | 528   | 30,129              |
| Problem loan<br>balances  | 4  | -                         | 193   | 197                 |

  

| <b>As at 31 December 2008</b>   |  |                           |   |                            |
|---|--|---------------------------|---|----------------------------|
|   | Balance<br>sheet credit<br>risk <sup>(2)</sup> | Securities <sup>(3)</sup> | Current off-<br>balance sheet<br>credit risk <sup>(4)</sup> | Current credit<br>exposure |
|   | NIS millions                                   |                           |   |                            |
| <b>External credit<br/>rating <sup>(5)</sup></b>                            |  |                           |   |                            |
| AAA to AA-  | 6,195  | 3,921                     | 2,084   | 12,200                     |
| A+ to A-  | 9,353  | 8,999                     | 3,755   | 22,107                     |
| BBB+ to BBB-  | 221  | 225                       | 39  | 485                        |
| BB+ to B-   | 402  | -                         | 15  | 417                        |
| Below B   | 8  | 111                       | 3   | 122                        |
| Unrated   | 679  | 9                         | 105   | 793                        |
| Total current<br>credit exposure<br>to foreign<br>financial<br>institutions | 16,858   | 13,265                    | 6,001   | 36,124                     |
| Problem loan<br>balances  | -  | 135                       | -   | 135                        |

See footnotes on next page.

- (1) Overseas financial institutions include banks, investment banks, insurance companies and institutional bodies.
- (2) Deposits in banks, credit to the public, securities that were borrowed or purchased in the context of buy-back agreements and other assets in respect of derivatives (fair value of derivatives).
- (3) Including subordinated bank debentures, whose fair value, as at 30 September 2009, was NIS 3,136 million, and as at 31 December 2008, was NIS 3,083 million.
- (4) Mainly guarantees and undertakings for the provision of credit (excluding off-balance sheet derivatives.)
- (5) In general, the overseas banks in respect of which there exists credit exposure are rated by two or three of the leading international rating agencies. (S&P, Moody's, Fitch)

**Notes:**

- a. Credit exposures are presented after deducting the specific provisions for doubtful debts.
- b. Credit exposures do not include investments in asset-backed securities (see the details in the Note on securities).
- c. Some of the banks have received government support of various types, including direct investments in the bank's capital, government guarantees of certain asset portfolios of the banks, guarantees enabling the banks to raise sources of financing, etc.
- d. For further information regarding the composition of the credit exposure in respect of derivatives vis-à-vis banks and broker/dealers (local and overseas), see Note 7 to the Financial Statements.

Credit exposure to overseas financial institutions refers to commercial banks, bank holding companies, investment banks, insurance companies and institutional bodies.

The exposure by country is divided as follows: United States 39.0%; Europe (Germany, France, Switzerland, Spain and the Benelux countries) 23.6%; United Kingdom 23.3%; and other countries 13.0%.

The exposure includes mainly deposits in overseas banks, some 90% of which are short-term deposits of up to one week, and debentures, usually for a period of up to five years. Against the backdrop of the crisis in the financial markets, and the weakening of banks' financial strength, the Bank is closely monitoring the condition of banks throughout the world. During 2008 and the first quarter of 2009, the Bank significantly reduced the list of banks with which the Bank and its overseas subsidiaries make deposits, and reduced the extent of their exposure.

Against the backdrop of the global financial crisis, the Bank is acting and taking steps to reduce the exposures and risks as far as possible.

Additional details regarding investments in securities, mainly debentures of overseas banks, are presented on pages 45.

Management of the exposure to and credit lines of overseas financial institutions takes into consideration, *inter alia*:

- Their size, as reflected *inter alia* in the size of their shareholders' equity after write-offs due to losses and capital increases during the past year.
- Their strength, as reflected in capital adequacy ratios (especially Tier I capital).
- The market's valuation, as reflected in the market value of their shares and their risk, as estimated with the help of their credit derivatives (CDS).
- The ratings assigned to them by the international rating agencies.

- The financial strength of the country where the bank's center of activity is located.
- Additional considerations, such as the level of support, including direct investment in the banks' capital by their governments, for the purpose of insuring the stability of these banks and of other banks in their countries.
- The policy for managing the exposure to overseas financial institutions includes, *inter alia*, limits on the amounts of exposure at bank and country level.

### Exposure to country risk

The exposure to country risk according to final risk is distributed among geographical regions and countries, the main exposure being to countries in Western Europe and in North America. The exposure to country risk is the exposure to customers who operate in these countries.

The following table presents the exposure to countries according to the credit rating of the countries as rated by the World Bank, in NIS millions as at 30 September 2009:

| Rating                         | Balance sheet exposure | Off-balance-sheet exposure | Total exposure | Percentage of exposure in relation to total | Of which, problematic |
|--------------------------------|------------------------|----------------------------|----------------|---|-----------------------|
| OECD countries                 | 57,145                 | 25,212                     | 82,357         | 94.5  | 1,818                 |
| High-income countries          | 1,531                  | 112                        | 1,643          | 1.9   | -                     |
| Countries with mid-high income | 2,208                  | 376                        | 2,584          | 3.0   | 31                    |
| Countries with mid-low income  | 376                    | 49                         | 425            | 0.5   | 3                     |
| Countries with low income      | 22                     | 24                         | 46             | 0.1   | -                     |
| Total                          | 61,282                 | 25,773                     | 87,055         | 100   | 1,852                 |

The amount of exposure to countries with liquidity problems, as defined by the Bank of Israel (countries which receive financial aid from the IMF or whose obligations are rated with a credit rating of CCC or below) totals NIS 445 millions and relates to 13 countries.

The countries are rated according to national income per capita as follows:

High income - exceeding US\$ 11,455 per capita.

Mid-high income - from US\$ 3,706 to US\$ 11,455 per capita.

Mid-low income - from US\$ 936 to US\$ 3,706 per capita.

Low income – up to US\$ 935 per capita.

Following are the names of the principal countries in each of the categories:

a. OECD countries:

USA, Italy, Australia, Austria, Ireland, Belgium, Canada, Czech Republic, Denmark, Finland, Hungary, France, United Kingdom, Japan, Spain, Switzerland, Luxembourg, the Netherlands, Sweden.

b. Countries with high income:

Israel, Cyprus, Hong Kong, Monaco, Singapore, Slovenia, Cayman Islands.



- c. Countries with mid-high income:  
Argentina, Brazil, Bulgaria, Chile, Mexico, Panama, Poland, Romania, Russia, South Africa, Turkey, Venezuela, Uruguay.
- d. Countries with mid-low income:  
China, Colombia, Ecuador, Egypt, India, Jordan, Peru, Paraguay, the Philippines, Thailand, the Ukraine.
- e. Countries with low income:  
A large number of the African countries, Haiti, Nepal.

## Operating and Legal Risks

See pages 184-188 of the Annual Report of 2008 for details of operating and legal risks.

## Linkage Status and Liquidity Status

### Linkage Status

During the first nine months of 2009, the Group's exposure in the CPI-linked sector fell from a surplus of some NIS 2.5 billion to a deficit of some NIS 1.1 billion. The deficit is mainly due to the raising of funds through issues of subordinated capital notes and to the surplus of repayments over grants of CPI-linked credit.

The following table sets out the status of assets and liabilities classified according to linkage basis:

|                                  | As at 30 September 2009 |                |                                 | As at 31 December 2008 |            |                                 |
|----------------------------------|-------------------------|----------------|---------------------------------|------------------------|------------|---------------------------------|
|                                  | Unlinked                | CPI-linked     | Foreign Currency <sup>(2)</sup> | Unlinked               | CPI-linked | Foreign Currency <sup>(2)</sup> |
|                                  | NIS millions            |                |                                 |                        |            |                                 |
| Total assets <sup>(1)</sup>      | <b>158,467</b>          | <b>60,004</b>  | <b>116,978</b>                  | 139,574                | 60,377     | 117,153                         |
| Total liabilities <sup>(1)</sup> | <b>140,266</b>          | <b>61,087</b>  | <b>120,631</b>                  | 125,563                | 57,920     | 123,266                         |
| Total exposure in sector         | <b>18,201</b>           | <b>(1,083)</b> | <b>(3,653)<sup>(3)</sup></b>    | 14,011                 | 2,457      | (6,113)                         |

(1) Including forward transactions and options.

(2) Including foreign-currency-linked.

(3) The short position arises mainly from a hedging transaction in respect of the investments in overseas subsidiaries and from the negative capital fund in respect of foreign debentures.

## **Funding and Liquidity Status**

### **Liquidity Status**

#### **The Banking System -**

From the beginning of the year through the end of the third quarter of 2009, the Bank of Israel increased the net balances of *Makam* tenders by some NIS 8.5 billion, to a level of some NIS 79 billion.

The volume of the banking system's balances with the Bank of Israel (current account balances and monetary deposits) at the end of September 2009 stood at some NIS 97 billion, compared with some NIS 78 billion and some NIS 44 billion at the end of the year's second quarter and at the end of 2008, respectively.

The volume of these balances during the third quarter of 2009 stood at an average of some NIS 93 billion, compared with an average of some NIS 66 billion during the second quarter of the year.

The volume of Leumi's balances with the Bank of Israel at the end of September 2009 stood at some NIS 26 billion, compared with NIS 19 billion and some NIS 13 billion at the end the second quarter of 2009 and at the end of 2008, respectively.

The average volume of Leumi's balances in the third quarter of 2009 stood at some NIS 22 billion, as compared with an average of some NIS 15 billion in the second quarter of the year.

The significant increase in the banking system's and in Leumi's balances during the first three quarters of 2009 result from, *inter alia*, the following actions taken by the Bank of Israel:

As of March 2008, the Bank of Israel carried out a program to increase the levels of the foreign currency balances through purchases of US dollars. On 3 August 2009, the Bank of Israel announced that it would in the future operate in the foreign currency market in the event of unusual movements in the exchange rate which do not conform to the basic economic conditions or when the foreign currency market is not functioning properly, or when conditions in the foreign exchange market are disorderly. On 10 August 2009, the Bank of Israel announced that it was ending the program of fixed daily purchases of US\$ 100 million.

From March 2008 through August 2009, the Bank of Israel's foreign currency balances had increased by some US\$ 29 billion, of which some US\$ 15 billion during 2009. The total balances as of the end of September 2009 amount to some US\$ 60 billion.

As of 17 February 2009, the Bank of Israel acts in the open market, carrying out transactions in government debentures in the secondary market. According to the Bank of Israel's announcement at the end of March 2009, the purchasers of shekel and CPI-linked government debentures would be made at a rate of some NIS 200 million per day, up to an aggregate amount of NIS 15-20 billion. On 7 July, the Bank of Israel announced that on 5 August it would discontinue the purchase of government debentures in the secondary market and that it did not intend to sell the securities that it had purchased.

Against the background of the large liquidity surpluses in the system, the Bank of Israel announced on 21 September 2009 that it would suspend the repo tenders until further notice. The Bank of Israel clarified in its announcement that after the repo market is re-organized it will be

possible to carry out repo transactions both through the Tel Aviv Stock Exchange central clearing house and on an "over-the-counter" basis.

### **The Bank -**

The structure of the Bank's assets and liabilities continues to indicate a high level of liquidity. This is the result of a deliberate policy of raising stable and diversified sources, while placing importance on the raising of deposits from a large number of customers, for varying periods of time, including long term. The high level of liquidity also reflects the expansive monetary policy implemented by the Bank of Israel. Some 42.9% of the Bank's assets are deposited in banks and/or are invested in securities, primarily in government debentures.

The Bank has cash and deposits in banks amounting to some NIS 70 billion.

The Bank also has a securities portfolio of some NIS 50 billion, which is mainly invested in Israeli government debentures, foreign government debentures, and foreign banks.

The Bank's net liquid assets – cash, deposits at banks and securities (excluding shares and funds) less deposits from banks – stood at 40.2% of the Bank's total assets as at 30 September 2009, compared with 33.3% as at 31 December 2008.

The ratio of credit to the public to deposits of the public at the 30 September 2009 was 58.2%, compared with 65.3% as at 31 December 2008 and the ratio to total assets was 47.5%, compared with 54.0% at the end of 2008.

Leumi monitors, on an ongoing basis, its liquidity status and the indices that are intended to warn of changes in the liquidity position, *inter alia*, by using an internal model that was developed at the Bank pursuant to a directive of the Bank of Israel. The various assumptions forming the basis of the model are examined and updated regularly according to developments in the major relevant parameters.

Shekel deposits of the public grew during the third quarter of 2009. This increase included the raising of some NIS 2.3 billion in subordinated capital notes. During this period, funds were diverted from short-term deposits to current accounts, in light of the low interest rates. The increase in deposits of the public contributed to an increase in shekel liquidity surpluses and these surpluses were used to enlarge the government debenture portfolio. In foreign currency, there was an increase in the debentures portfolio, in place of deposits in overseas banks.

For additional details regarding the liquidity status, see the Risk Management section on page 92.

### **Sources and Uses in the Bank -**

During the first nine months of 2008, against the background of the crisis in the capital markets a trend began of the diversion of monies held by the public from investments in the capital market to deposits. In contrast, the first nine months of 2009 was marked by a slow return to the capital market.

The balance of deposits of the public at the Bank rose during the first nine months of 2009 by NIS 8.0 billion, 3.6%. After neutralizing the impact of changes in the shekel's exchange rate against foreign currencies, deposits of the public grew by 3.4%.

During the months of April and May 2009, the Bank issued CPI-linked subordinated capital notes (unlisted) which are classified as upper Tier II capital in the amount of some NIS 1 billion, and through Leumi Finance Company, it issued to the public CPI-linked subordinated capital notes which are classified as lower Tier II capital in the amount of an additional NIS 1.5 billion.

In August 2009, Leumi Finance issued some NIS 2 billion of subordinated capital notes which are classified as upper Tier II capital. Of this, NIS 1 billion is CPI-linked with fixed interest of 5%, and NIS 1 billion is in unlinked shekels, with floating interest with a par of 2% above the annual yield on *Makam* bills. Leumi Finance also issued some NIS 0.3 billion of subordinated capital notes that were classified as lower Tier II Capital, bearing shekel interest at a rate of 7%.

During the first nine months of 2009, the Group issued a total of some NIS 4.8 billion subordinated capital notes.

The capital notes were issued for a period of 50 years, with the issuer having an option for early repayment each year after the end of 11 years, upon the fulfillment of certain conditions.

During the first nine months of 2009, the balance of credit to the public dropped by some NIS 11.1 billion, a decrease of 7.6%. The decrease was in all sectors. After neutralizing the impact of changes in the shekel's exchange rate against foreign currencies, credit decreased by 8.0%.

## **Preparations for Basel II**

In June 2006, the Basel Committee on Banking Supervision published the final version of a capital adequacy measurement accord (the "Basel II directives") which is intended to be implemented following instructions by the central banks.

The innovation in the Basel II directives is that for the first time, banking corporations are required to allocate capital for operating risks, as well as for credit risks and market risks, which are required at present under the provisions of Proper Banking Management Directive 311 ("Basel I"). In addition, Basel II allows the possibility of using, for internal rating, models relating to the borrowers' sensitivity to risk - unlike the provisions of Basel I which relate to risk weighting for groups of assets.

Over the course of 2007-2008, the Supervisor of Banks published a succession of documents, directives and requirements, mostly based on the documents produced by the Basel Committee, along with drafts of documents and directives for consultation with the banking system. The Supervisor of Banks also published a set of questions and answers on the Bank of Israel website, updated as of June 2009, presenting the Supervisor's position regarding various issues and clarifications that had been raised by the banking system.

The core part of the directives and documents is the interim directive relating to Basel II which was published in December 2008, and which relies in most part on the Basel Committee's accord, and also includes changes and adjustments made by the local regulator.

The Supervisor of Banks has announced that at the time of the first implementation of the Basel II provisions at the end of 2009, the banking corporations would be required to comply, at the least, with the capital calculation requirements of the standard method for market risk, credit risk and operational risk, as described in the Basel Committee's working framework.

The Banking Supervision Department announced that, as of 31 December 2008, the banks would be required to report to the Banking Supervision Department regarding the capital requirements according to the standard method set out in the first pillar of Basel II, and that such reporting would be required on a quarterly basis throughout 2009, although the actual allocation of capital during this period would still be in accordance with the existing directives. The actual allocation of capital in accordance with the requirements of Basel II's standard method would only be required as of 31 December 2009.

The Bank has reported capital adequacy data to the Bank of Israel as at 31 December 2008 and according to the initial calculations, the capital adequacy according to the first pillar of Basel II is 10.5%, compared with 11.6% according to Basel I. Additional reports as of 31 March 2009 and as of 30 June 2009 showed that the capital adequacy ratio was 10.6% and 12.08%, compared with 11.9% and 12.85% according to Basel I. A significant part of the difference between the calculations results from the negative capital fund as of the end of December 2008 and the end of March 2009.

### **The Leumi Group's Preparations**

Since 2006, the Leumi Group has been preparing for the implementation of the Basel II directives through a Group-wide project in Israel and abroad. The project's management coordinates the activity regarding this subject and it is responsible to the Senior Deputy Chief Executive Officer, who heads the project's steering committee, which acts through designated work teams throughout the Bank.

The following actions have been taken in the context of the preparations:

1. The requirements in the Basel and Bank of Israel documents have been studied and gap analyses prepared accordingly.
2. A detailed work program has been prepared for the Bank and Group units for closing the gaps.
3. The infrastructure systems have been adapted, and risk management and capital calculation systems have been purchased or upgraded, and these have been linked to the existing systems. These systems are intended to upgrade and significantly improve the Bank's capacities with regard to risk-focused management.
4. Data has been collected and databases have been established as required for the assessment of risk variables.
5. Organizational and process changes have been made in the area of credit risk management.
6. Model development processes, as required for the implementation of the advanced methods of risk management.
7. Surveying and mapping of operational risks as part of a three year program.
8. Commencement of the process of carrying out required adjustments in risk management policy and guidelines (credit, market and operational risk policy).

9. Measurement of the profitability of the lines of business also on the basis of the return adjusted to risk models – RORAC (Return on Risk Adjusted Capital).

The Bank is preparing for the implementation, beginning at the end of 2009, of the Bank of Israel's requirements to implement the standard method set out in the first pillar with respect to credit and market risks, and of the basic method with regard to operational risks during a three year transition period, after which the standard method will also be implemented for operational risks.

In the context of these preparations, many business adjustments and computer system adjustments are being carried out at the Bank and Group level, in order to meet the requirements of the standard method. The Bank is relying for this purpose on a centralized computer system that it has purchased for this purpose, for calculating the capital requirements and managing the credit risks. This system will serve the Bank, the auxiliary corporations and the Group units. The Bank is also continuing to prepare for the advanced Internal Ratings-Based Approach (IRB) with regard to credit risks, through the collection of data, construction of data bases, and the processes for the development of internal models for internal rating, calculation of the PD (Probability of Default) and of the severity of the LGD (Loss Given Default). This process also involves the replacement and upgrading of the systems used to rate retail and corporate borrowers.

During the second quarter of 2008, an Internal Capital Adequacy Assessment Process – ICAAP – was initiated in the Leumi Group. This process co-ordinates compliance with the requirements of the second pillar of the Basel recommendations regarding a "Supervisory Review Process," and is necessary for the completion of the preparations for Basel II by the end of 2009, in accordance with the Bank of Israel requirements.

The process is divided into two main components:

1. Assessment of the Group's capital adequacy and an examination of the ability to bear losses in accordance with the risk appetite and the risk profile. When assessing capital adequacy, it is necessary to take into account the Group's strategic plans and its future capital needs as reflected in the three-year plan, in the light of the economic forecasts. Additionally, it is necessary to examine the planning's resilience and the changes required, in light of stress scenarios of varying severity, such as a mild or a severe recession. After the process is fully prepared, the definitions of the various levels of severity that are used for defining the severity of the risk factors are likely to change, which would, of course, lead to an updating of the risk levels.
2. An annual survey of risk management within the Group, an examination of risk management's compliance with the standards established in the context of Basel II, the identification of strengths and weaknesses and the construction of work programs for the improvement and updating of risk management processes. The assessment of the risk management processes is closely linked to the capital adequacy assessment, since without strong and adequate risk management, a larger cushion of capital is required as protection against losses.

The results of the process are included in the ICAAP document. A first draft of the document was submitted to the Bank of Israel on 1 July 2009, and the annual document is expected to be submitted in 2010.

On 10 June 2009, the Supervisor of Banks published a draft consultation document on the subject of “The Chief Risk Management Officer and the Risk Management Function.” The document details the Banking Supervision Department’s requirement to appoint and establish the above-mentioned functions in the banking corporations, while determining their principles, rules and responsibility. The banking corporations were asked to respond to the draft during the course of the third quarter of 2009 and afterwards discussions on the subject are to be held with each banking corporation.

The Bank has sent its response and comments regarding this document to the Bank of Israel.

The Leumi Group’s preparations require the investment of significant management and financial resources that have already been invested and will be invested in the coming years in order to comply with the Bank of Israel's requirements, and for the improvement and upgrading of the Group’s risk management processes.

## **Legal Proceedings**

- a. The Directors' Report in the Annual Report for 2008 provides details of civil and other legal proceedings to which the Bank and consolidated companies are parties.

As of the date of the publication of this Report, no material changes have occurred in these proceedings, except as detailed in Note 6 to the Financial Statements.

None of the proceedings pending against the Bank involves a sum exceeding 1% of the shareholders’ equity of the Bank (some NIS 210 million as of 30 September 2009), other than the proceedings detailed in Note 6 to the Financial Statements.

For details regarding petitions for the approval of class actions that were filed during the first nine months of 2009, see Note 6 C. to the Financial Statements.

In the opinion of the Management of the Bank, based on legal opinions, appropriate provisions have been recorded in the Financial Statements to cover possible damages in respect of all the claims.

- b. On 26 April 2009, a ruling of the Antitrust General Director was received at the Bank pursuant to section 43(a)(1) of the Antitrust Law, 1988, according to which restrictive trade agreements, relating to the transfer of information regarding commissions, had existed between the Bank, Bank Hapoalim B.M., Israel Discount Bank Ltd., Mizrahi-Tefahot Bank Ltd. and the First International Bank of Israel Ltd., during the period from the beginning of the 1990s until the commencement of the Antitrust Authority's investigation of the matter, in November 2004. This is a civil ruling, which constitutes prima facie evidence of the matters therein determined in any legal proceedings. The Bank has decided to appeal the ruling. At this early stage, the effects of the ruling cannot be assessed.

## **D. Additional Matters**

### **Leumi for the Community - Social Involvement**

In May 2009, the Leumi Group published its complete corporate responsibility report for the years 2007-2008. The report included reporting on the Group's five most significant subsidiaries, and was rated A+ by the GRI. The report details Leumi's social and environmental investment, as well as the subjects of corporate governance and business ethics.

**Maala's Rating** - Maala's corporate responsibility rating for 2009 was published at the beginning of June 2009. Leumi was rated in the highest rating group, and was noted as excelling in the area of corporate governance.

Leumi's community-oriented activity continues in 2009, in the areas on which the Group has chosen to concentrate: education, youth, culture and art, and focused assistance to distressed sections of the population.

#### **“Leumi Tomorrow - The Centennial Fund for Endowing Israel's Future Generation”**

Some 15,000 young people started the year's activities in the programs supported by the "Leumi Tomorrow – The Centennial Fund for Endowing Israel's Future" non-profit association.

530 students received scholarships through the “Leumi Scholarship Fund for Exceptional Students,” in a total amount of some NIS 2.8 million.

#### **Leumi Center for Robotics at the Technion**

The Leumi Center for Robotics has been launched at the Technion's Department of Mechanical Engineering.

At the Center, the high school students and students studying there will acquire the skills that will qualify them and enable them to participate in national and international competitions in the field of robotics, thus obtaining important knowledge and skills in applied mathematics and science.

Leumi is sponsoring the Center for 7 years at a total cost of US\$ 1.5 million.

#### **The “Turning-Point” Program, in cooperation with the Buchmann-Mehta School of Music at Tel Aviv University, and the Israel Philharmonic Orchestra**

Together with the Arab-Israel Bank of the Leumi Group, the Group is collaborating with the renowned conductor, Maestro Zubin Mehta, for the purpose of promoting a future generation of young musicians, while bringing together gifted Arab and Jewish young people.

The program, led academically by the Buchmann-Mehta School of Music at Tel Aviv University and the Israel Philharmonic Orchestra, seeks to promote musical artistry within Arab society and to create a future generation of children with high levels of musical talent. The program will focus on promoting classical Arab and Western music through the study of different musical instruments and through master classes, workshops and music camps, as well as joint activities and exchanges of visits between the students in the program in the Galilee and the students at the campus of the



Buchmann-Mehta School of Music. The mutual relations with the students at Tel Aviv University will create opportunities for connecting the country's center and its geographical periphery, and for bringing Jews and Arabs together.

The sponsorship of the program is for a period of five years, and its financial scope is of some NIS 2 million.

### **Summary of Leumi's Donations and Sponsorships During the First Nine Months of 2009**

During the first nine months of 2009, the Leumi Group donated and provided sponsorships for the social welfare and community purposes described above, and others, in the amount of some NIS 20.0 million, of which the donations totaled some NIS 16.8 million.

### **Internal Auditor**

Details regarding the Group's Internal Audit, including the professional standards according to which it operates, the annual and multi-year work plans and the considerations used in establishing same, were included in the Annual Report for 2008.

The Chief Internal Auditor's annual report for 2008 was submitted on 30 April 2009 and was discussed by the Audit Committee on 3 May 2009.

The Chief Internal Auditor's annual report for 2008 regarding the subsidiaries was submitted on 2 June 2009 and was discussed by the Audit Committee on 7 June 2009.

The Chief Internal Auditor's report for the first half of 2009 was submitted on 19 October 2009 and was discussed by the Audit Committee on 22 October 2009.

### **Controls and Procedures Regarding Disclosure in the Financial Statements**

The Management of the Bank, together with the President and Chief Executive Officer and the Head of Finance, Accounting and Capital Markets, have, as at the end of the period covered by this Report, evaluated the effectiveness of the disclosure controls and procedures of the Bank. On the basis of this evaluation, the President and Chief Executive Officer of the Bank and the Head of Finance, Accounting and Capital Markets, have concluded that, as at the end of the said period, the disclosure controls and procedures of the Bank are effective for the recording, processing, summarizing and reporting of the information that the Bank is required to disclose in its quarterly financial statements, in accordance with the public reporting Directives of the Supervisor of Banks and at the time required in these Directives.

During the quarter ending on 30 September 2009, no material change occurred to the internal controls on financial reporting of the Bank that materially affected or is reasonably anticipated to materially affect the Bank's internal control of financial reporting.

## **Management's Responsibility for the Internal Control of Financial Reporting (Sox Act 404)**

The Supervisor of Banks has published a circular detailing provisions for the implementation of the requirements of section 404 of the Sox Act. In section 404, the SEC and the Public Company Accounting Oversight Board determined provisions as to management's responsibility for the internal control over financial reporting and as to the external auditors' opinion with regard to the audit of the internal control over financial reporting.

The Supervisor's directives in the said circular prescribe that:

- Banking corporations shall apply the requirements of section 404 and also the SEC's directives that were published thereunder.
- Proper internal control requires the existence of a control system in accordance with a defined and recognized framework, and the COSO (Committee of Sponsoring Organizations of the Treadway Commission) model meets with the requirements and can be used in order to assess the internal control.

The COSO model provides defined standards for the purpose of assessing the internal control system in the organization and the ways in which it can be improved, and defines internal control as a process which is influenced by the board of directors, the management and other persons within the company.

According to the COSO model, reference should be made to five components:

1. The Control Environment: this component involves the examination of the management's conduct with reference to various subjects such the existence of a code of ethics, management's aggressiveness in reports, etc.
2. Risk Assessment: this component involves the examination of the relevant risks regarding each process and sub-process that is checked, which have an impact on the financial statements.
3. Control Activities: this component involves the examination of the relevant controls regarding each of the risks that was identified at the risk assessment stage.
4. Information & Communication: this component involves checking that the information required for the Bank's activity is available, and that there is a mechanism that processes the information received and transfers it to the appropriate parties at the Bank.
5. Monitoring: this component involves the examination of the existence of a mechanism that checks the monitoring of the correction of deficiencies. Proper supervision may be expressed in a periodic examination of the internal control system, continuous implementation of opportunities for improvement, response by the management to the internal control recommendations made by external auditors as well as internal parties, rapid adaptation to new regulatory directives, etc.

The Bank has been working to implement the directive in the Leumi Group on an ongoing basis, together with consultants who have been engaged for the purpose of carrying out the project.

## **Board of Directors**

During the first nine months of 2009, and up to the date of publication of the Report, the following changes took place in the composition of the Board of Directors:

At the Annual General Meeting held on 16 July 2009, Mr. Reuven Adler was chosen to serve as an external director for a period of three years, from 24 July 2009, in place of Mr. Meir Dayan who concluded his second term of office in accordance with the Companies Law, 1999, on 23 July 2009. Mr. Dayan contributed much to the advancement of the business of the Bank and to its betterment. In addition, Messrs Zipora Gal Yam, Arie Gans, Doron Cohen and Efraim Sadka who retired by rotation and offered themselves for re-election, were all re-elected.

The Bank's Board of Directors approved the continued service of Mr. Eitan Raff as Chairman of the Board of Directors for an additional year, in accordance with the approval of the Bank's shares committee.

At the meeting of the Board of Directors held on 29 November 2009, it was resolved to approve and publish the Group's condensed unaudited consolidated Financial Statements as of 30 September 2009 and for the periods ending on that date.

During the period of January to September 2009, the Board of Directors held 24 plenary meetings and 127 committee meetings.

The Bank's Board of Directors expresses its appreciation and gratitude to employees and managers of the Bank and of its subsidiaries in Israel and overseas, for their dedicated work and their contribution to the promotion of the Group's business.

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Eitan Raff  
Chairman of the Board of Directors

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Galia Maor  
President and Chief Executive Officer

**29 November 2009**

**Rates of Financing Income and Expenses (on a Consolidated Basis) (a)****Reported amounts****Exhibit A**

|  | For the three months ended 30 September |                                  |  |  |                                       |                                  |  |  |
|--|---|----------------------------------|--|--|---------------------------------------|----------------------------------|--|--|
|  | 2009                                    |                                  |  |  | 2008                                  |                                  |  |  |
|  | Rate of income (expenses)               |                                  |  | Rate of income (expenses)                |                                       |                                  |  |  |
|  | Average balance (b)<br>(NIS millions)   | Financing income (expenses)<br>% | Excluding the effect of derivatives<br>% | Including the effect of derivatives<br>% | Average balance (b)<br>(NIS millions) | Financing income (expenses)<br>% | Excluding the effect of derivatives<br>% | Including the effect of derivatives<br>% |
| <b>Israeli currency - unlinked</b>                             |   |                                  |  |  |                                       |                                  |  |  |
| Assets (c) (d)   | 147,323                                 | 1,076                            | 2.95                                     |  | 112,511                               | 1,655                            | 6.01                                     |  |
| Effect of embedded and ALM derivatives (e)                     | 36,719                                  | 44                               |  |  | 38,418                                | 146                              |  |  |
| Total assets   | 184,042                                 | 1,120                            |  | 2.46                                     | 150,929                               | 1,801                            |  | 4.86                                     |
| Liabilities (d)  | 126,334                                 | (313)                            | (0.99)                                   |  | 109,689                               | (869)                            | (3.22)                                   |  |
| Effect of embedded and ALM derivatives (e)                     | 36,687                                  | (35)                             |  |  | 30,351                                | (36)                             |  |  |
| Total liabilities  | 163,021                                 | (348)                            |  | (0.86)                                   | 140,040                               | (905)                            |  | (2.62)                                   |
| Interest margin  |   |                                  | 1.96                                     | 1.60                                     |                                       |                                  | 2.79                                     | 2.24                                     |
| <b>Israeli currency – linked to the CPI</b>                    |   |                                  |  |  |                                       |                                  |  |  |
| Assets (c) (d)   | 58,997                                  | 2,045                            | 14.60                                    |  | 60,745                                | 1,975                            | 13.66                                    |  |
| Effect of embedded and ALM derivatives (e)                     | 3,126                                   | 28                               |  |  | 2,458                                 | 30                               |  |  |
| Total assets   | 62,123                                  | 2,073                            |  | 14.03                                    | 63,203                                | 2,005                            |  | 13.31                                    |
| Liabilities (d)  | 47,939                                  | (1,657)                          | (14.56)                                  |  | 44,521                                | (1,361)                          | (12.79)                                  |  |
| Effect of embedded and ALM derivatives (e)                     | 12,823                                  | (250)                            |  |  | 10,990                                | (33)                             |  |  |
| Total liabilities  | 60,762                                  | (1,907)                          |  | (13.16)                                  | 55,511                                | (1,394)                          |  | (10.42)                                  |
| Interest margin  |   |                                  | 0.04                                     | 0.87                                     |                                       |                                  | 0.87                                     | 2.89                                     |
| <b>Foreign currency –</b>                                      |   |                                  |  |  |                                       |                                  |  |  |
| <b>(including Israeli currency linked to foreign currency)</b> |   |                                  |  |  |                                       |                                  |  |  |
| Assets (c) (d) (h)   | 100,371                                 | (2,217)                          | (8.55)                                   |  | 101,420                               | 1,065                            | 4.25                                     |  |
| Effect of derivatives: (e)                                     |   |                                  |  |  |                                       |                                  |  |  |
| Hedging derivatives  | 1,612                                   | (1)                              |  |  | 2,739                                 | 4                                |  |  |
| Embedded derivatives and ALM                                   | 111,337                                 | (2,135)                          |  |  | 72,062                                | 283                              |  |  |
| Total assets   | 213,320                                 | (4,353)                          |  | (7.92)                                   | 176,221                               | 1,352                            |  | 3.09                                     |
| Liabilities (d)  | 112,683                                 | 3,356                            | 11.39                                    |  | 103,473                               | (605)                            | (2.33)                                   |  |
| Effect of derivatives: (e)                                     |   |                                  |  |  |                                       |                                  |  |  |
| Hedging derivatives  | 1,488                                   | 3                                |  |  | 2,600                                 | 2                                |  |  |
| Embedded derivatives and ALM (d)                               | 103,236                                 | 1,637                            |  |  | 72,429                                | (400)                            |  |  |
| Total liabilities  | 217,407                                 | 4,996                            |  | 8.88                                     | 178,502                               | (1,003)                          |  | (2.25)                                   |
| Interest margin  |   |                                  | 2.84                                     | 0.96                                     |                                       |                                  | 1.92                                     | 0.84                                     |

See footnotes on page 117.

**Rates of Financing Income and Expenses (on a Consolidated Basis) (Cont'd) (a)****Reported amounts****Exhibit A (Cont'd)**

|   | For the three months ended 30 September |               |               |                           |               |               |             |
|---|---|---------------|---------------|---------------------------|---------------|---------------|-------------|
|   | 2009                                    |               |               | 2008                      |               |               |             |
|   | Rate of income (expenses)               |               |               | Rate of income (expenses) |               |               |             |
|   | Financing                               | Excluding     | Including     | Financing                 | Excluding     | Including     |             |
|   | Average                                 | the effect of | the effect of | Average                   | the effect of | the effect of |             |
|   | balance (b)                             | derivatives   | derivatives   | balance (b)               | derivatives   | derivatives   |             |
|   | (NIS millions)                          | %             | %             | (NIS millions)            | %             | %             |             |
| Total monetary assets generating interest   |   |               |               |                           |               |               |             |
| Income (d) (f)  | 306,691                                 | 904           | 1.18          | 274,676                   | 4,695         | 7.01          |             |
| Effect of derivatives: (e)  |   |               |               |                           |               |               |             |
| Hedging derivatives   | 1,612                                   | (1)           |               | 2,739                     | 4             |               |             |
| Embedded derivatives and ALM  | 151,182                                 | (2,063)       |               | 112,938                   | 459           |               |             |
| Total assets  | 459,485                                 | (1,160)       | (1.01)        | 390,353                   | 5,158         | 5.39          |             |
| Total monetary liabilities generating interest expenses (d)   | 286,956                                 | 1,386         | 1.92          | 257,683                   | (2,835)       | (4.46)        |             |
| Effect of derivatives: (e)  |   |               |               |                           |               |               |             |
| Hedging derivatives   | 1,488                                   | 3             |               | 2,600                     | 2             |               |             |
| Embedded derivatives and ALM (d)  | 152,746                                 | 1,352         |               | 113,770                   | (469)         |               |             |
| Total liabilities   | 441,190                                 | 2,741         | 2.46          | 374,053                   | (3,302)       | (3.57)        |             |
| <b>Interest margin</b>  |   |               | <b>3.10</b>   |                           |               | <b>2.55</b>   | <b>1.82</b> |
| In respect of options   |   | (62)          |               |                           | 53            |               |             |
| In respect of other derivatives (excluding options,<br>hedging derivative instruments, ALM derivatives<br>and embedded derivatives which have been separated) |   | 20            |               |                           | (107)         |               |             |
| Financing commissions and other financing<br>income (g)   |   | 372           |               |                           | (250)         |               |             |
| Other financing expenses  |   | 12            |               |                           | (61)          |               |             |
| Net interest income before provision for doubtful<br>debts  |   | 1,923         |               |                           | 1,491         |               |             |
| Provision for doubtful debts (including general<br>and supplementary provision)   |   | (443)         |               |                           | (495)         |               |             |
| Net interest income after provision for doubtful<br>debts   |   | 1,480         |               |                           | 996           |               |             |
| Monetary assets generating interest income (d) (f)  | 306,691                                 |               |               | 274,676                   |               |               |             |
| Assets derived from derivative instruments (h)  | 6,025                                   |               |               | 5,576                     |               |               |             |
| Other monetary assets (d)   | 1,948                                   |               |               | 2,650                     |               |               |             |
| General provision and supplementary provision<br>for doubtful debts   | (918)                                   |               |               | (847)                     |               |               |             |
| Total monetary assets   | 313,746                                 |               |               | 282,055                   |               |               |             |
| Monetary liabilities generating interest expenses (d)   | 286,956                                 |               |               | 257,683                   |               |               |             |
| Liabilities derived from derivative instruments (h)   | 7,359                                   |               |               | 6,234                     |               |               |             |
| Other monetary liabilities (d)  | 7,751                                   |               |               | 8,019                     |               |               |             |
| Total monetary liabilities  | 302,066                                 |               |               | 271,936                   |               |               |             |
| Total monetary assets exceed monetary liabilities   | 11,680                                  |               |               | 10,119                    |               |               |             |
| Non-monetary assets   | 8,900                                   |               |               | 10,936                    |               |               |             |
| Non-monetary liabilities  | 314                                     |               |               | 417                       |               |               |             |
| Total capital resources   | 20,266                                  |               |               | 20,638                    |               |               |             |

See footnotes on page 117.

- (a) The data in this exhibit includes before and after the effect of derivative instruments (including the effect of off-balance sheet derivative instruments).
- (b) Based on monthly opening balances, and quarterly opening balances in foreign subsidiaries, except for the unlinked Israeli currency sector where the average balance is based on daily figures, and after deduction of the average balance sheet balance of the specific provision for doubtful debts.

- (c) The average balance of unrealized profits (losses) from adjustment to fair value of debentures held for trading and available for sale has been deducted from (added to ) the average balance of the assets as follows:  
The unlinked Israeli currency sector for the three month and nine month periods amounts to NIS 78 million and 183 million respectively (September 30 2008 - NIS 43 million and 55 million respectively).

The linked Israeli currency sector for the three month and nine month periods amounts to NIS 303 million and 225 million respectively (September 30 2008 - NIS 119 million and 132 million respectively).

The foreign currency sector (which includes Israeli currency linked to foreign currency) for the three month and nine month periods amounts to NIS (1,063) million and (1,873) million respectively (September 30 2008 - NIS (829) million and (712) million respectively).

- (d) Excluding derivative instruments.
- (e) Includes hedging derivative instruments (excluding options), embedded derivatives which have been separated, and ALM derivatives, which constitute part of the Bank's asset and liability management system.
- (f) The average balance of unrealized losses on adjustment to fair value of debentures held for trading and available for sale has been added to the average balance of the assets in the various sectors.  
The three month periods amounts and nine month periods amounts to NIS 682 million and 1,465 million respectively (September 30 2008 - NIS 667 million and 525 million respectively).
- (g) This includes profits and losses on sales of investments in debentures and adjustments to fair value of debentures held for trading.
- (h) Includes the average balance for derivative instruments (does not include average of off-balance sheet derivative instruments).

**Rates of Financing Income and Expenses (on a Consolidated Basis) (Cont'd) (a)****Nominal U.S. \$****Exhibit A (Cont'd)**

|   | For the three months ended 30 September |            |               |                           |            |               |
|---|---|------------|---------------|---------------------------|------------|---------------|
|   | 2009                                    |            |               | 2008                      |            |               |
|   | Rate of income (expenses)               |            |               | Rate of income (expenses) |            |               |
|   | Financing                               | Excluding  | Including     | Financing                 | Excluding  | Including     |
|   | Average                                 | income     | the effect of | Average                   | income     | the effect of |
|   | balance (b)                             | (expenses) | derivatives   | balance (b)               | (expenses) | derivatives   |
|   | (U.S.\$ millions)                       | %          | %             | (U.S.\$ millions)         | %          | %             |
| <b>Foreign currency:</b>  |   |            |               |                           |            |               |
| <b>Local operations (including Israeli currency linked to foreign currency)</b> |   |            |               |                           |            |               |
| Assets (c) (d)  | 16,391                                  | 86         | 2.12          | 19,093                    | 199        | 4.24          |
| Effect of derivatives: (e)  |   |            |               |                           |            |               |
| Hedging derivatives   | 415                                     | -          |               | 799                       | 1          |               |
| Embedded derivatives and ALM  | 28,606                                  | 19         |               | 20,948                    | (36)       |               |
| Total assets  | 45,412                                  | 105        | 0.93          | 40,840                    | 164        | 1.61          |
| Liabilities (d)   | 19,600                                  | (36)       | (0.73)        | 21,171                    | (128)      | (2.43)        |
| Effect of derivatives: (e)  |   |            |               |                           |            |               |
| Hedging derivatives   | 383                                     | (1)        |               | 759                       | 1          |               |
| Embedded derivatives and ALM  | 26,513                                  | -          |               | 21,022                    | (39)       |               |
| Total liabilities   | 46,496                                  | (37)       | (0.31)        | 42,952                    | (166)      | (1.56)        |
| <b>Interest margin</b>  |   | 1.39       | 0.62          |                           | 1.81       | 0.05          |
| <b>Foreign currency –</b>   |   |            |               |                           |            |               |
| <b>Foreign operations</b>   |   |            |               |                           |            |               |
| <b>(integrated operations)</b>  |   |            |               |                           |            |               |
| Assets (c) (d)  | 9,344                                   | 69         | 2.98          | 10,533                    | 137        | 5.31          |
| Effect of embedded and ALM derivatives (e)                                      | 45                                      | -          |               | 67                        | 12         |               |
| Total assets  | 9,389                                   | 69         | 2.96          | 10,600                    | 149        | 5.76          |
| Liabilities (d)   | 9,327                                   | (27)       | (1.14)        | 9,047                     | (81)       | (3.61)        |
| Effect of embedded and ALM derivatives (e)                                      | 49                                      | (22)       |               | 110                       | 2          |               |
| Total liabilities   | 9,376                                   | (49)       | (2.08)        | 9,157                     | (79)       | (3.47)        |
| <b>Interest margin</b>  |   | 1.84       | 0.88          |                           | 1.70       | 2.29          |
| <b>Total:</b>   |   |            |               |                           |            |               |
| Monetary assets in foreign currency generating financing income (c) (d)         | 25,735                                  | 155        | 2.43          | 29,626                    | 336        | 4.62          |
| Effect of derivatives: (e)  |   |            |               |                           |            |               |
| Hedging derivatives   | 415                                     | -          |               | 799                       | 1          |               |
| Embedded derivatives and ALM  | 28,651                                  | 19         |               | 21,015                    | (24)       |               |
| Total assets  | 54,801                                  | 174        | 1.28          | 51,440                    | 313        | 2.45          |
| Monetary liabilities in foreign currency generating financing expense (d)       | 28,927                                  | (63)       | (0.86)        | 30,218                    | (209)      | (2.79)        |
| Effect of derivatives: (e)  |   |            |               |                           |            |               |
| Hedging derivatives   | 383                                     | (1)        |               | 759                       | 1          |               |
| Embedded derivatives and ALM  | 26,562                                  | (22)       |               | 21,132                    | (37)       |               |
| Total liabilities   | 55,872                                  | (86)       | (0.61)        | 52,109                    | (245)      | (1.89)        |
| <b>Interest margin</b>  |   | 1.57       | 0.67          |                           | 1.83       | 0.56          |

See footnotes on page 119.

- (a) The data in this exhibit includes before and after the effect of derivative instruments (including the effect of off-balance sheet derivative instruments).
- (b) Based on monthly opening balances for the Bank and subsidiaries in Israel and on quarterly opening balances for foreign subsidiaries, and after deduction of the average balance sheet balance of the specific provision for doubtful debts.
- (c) The average balance of unrealized losses on adjustment to fair value of debentures held for trading and available for sale has been added to the average balance of the assets for local and foreign operations, in the amount of US\$ 268 million.
- (d) Excluding derivative instruments.
- (e) Includes hedging derivative instruments (excluding options), embedded derivatives which have been separated, and ALM derivatives, which constitute part of the Bank's asset and liability management system.



**Rates of Financing Income and Expenses (on a Consolidated Basis) (a)****Reported amounts****Exhibit A**

|  | For the nine months ended 30 September |   |  |  |                                       |   |  |  |
|--|--|---|--|--|---------------------------------------|---|--|--|
|  | 2009                                   |   |  |  | 2008                                  |   |  |  |
|  | Rate of income (expenses)              |   |  |  | Rate of income (expenses)             |   |  |  |
|  | Average balance (b)<br>(NIS millions)  | Financing income (expenses)<br>(NIS millions) | Excluding the effect of derivatives<br>% | Including the effect of derivatives<br>% | Average balance (b)<br>(NIS millions) | Financing income (expenses)<br>(NIS millions) | Excluding the effect of derivatives<br>% | Including the effect of derivatives<br>% |
| <b>Israeli currency - unlinked</b>                             |  |   |  |  |                                       |   |  |  |
| Assets (c) (e)   | 135,749                                | 3,181   | 3.14                                     |  | 108,632                               | 4,686   | 5.79                                     |  |
| Effect of embedded and ALM derivatives (d)                     | 39,067                                 | 298   |  |  | 41,889                                | 385   |  |  |
| Total assets   | 174,816                                | 3,479   |  | 2.66                                     | 150,521                               | 5,071   |  | 4.52                                     |
| Liabilities (e)  | 122,155                                | (825)   | (0.90)                                   |  | 107,880                               | (2,389)                                       | (2.96)                                   |  |
| Effect of embedded and ALM derivatives (d)                     | 34,197                                 | (160)   |  |  | 31,447                                | (73)  |  |  |
| Total liabilities  | 156,352                                | (985)   |  | (0.84)                                   | 139,327                               | (2,462)                                       |  | (2.36)                                   |
| Interest margin  |  |   | 2.24                                     | 1.82                                     |                                       |   | 2.83                                     | 2.16                                     |
| <b>Israeli currency – linked to the CPI</b>                    |  |   |  |  |                                       |   |  |  |
| Assets (c) (e)   | 58,804                                 | 4,045   | 9.28                                     |  | 60,831                                | 5,191   | 11.54                                    |  |
| Effect of embedded and ALM derivatives (d)                     | 3,286                                  | 148   |  |  | 2,028                                 | 104   |  |  |
| Total assets   | 62,090                                 | 4,193   |  | 9.10                                     | 62,859                                | 5,295   |  | 11.39                                    |
| Liabilities (e)  | 46,442                                 | (3,123)                                       | (9.07)                                   |  | 44,617                                | (3,569)                                       | (10.80)                                  |  |
| Effect of embedded and ALM derivatives (d)                     | 12,823                                 | (1,091)                                       |  |  | 11,492                                | (756)   |  |  |
| Total liabilities  | 59,265                                 | (4,214)                                       |  | (9.59)                                   | 56,109                                | (4,325)                                       |  | (10.41)                                  |
| Interest margin  |  |   | 0.21                                     | (0.49)                                   |                                       |   | 0.74                                     | 0.98                                     |
| <b>Foreign currency –</b>                                      |  |   |  |  |                                       |   |  |  |
| <b>(including Israeli currency linked to foreign currency)</b> |  |   |  |  |                                       |   |  |  |
| Assets (c) (e)   | 106,018                                | 3,789   | 4.79                                     |  | 108,451                               | (9,728)                                       | (11.78)                                  |  |
| Effect of derivatives: (e)                                     |  |   |  |  |                                       |   |  |  |
| Hedging derivatives  | 2,059                                  | (1)   |  |  | 3,207                                 | 18  |  |  |
| Embedded derivatives and ALM                                   | 112,291                                | 978   |  |  | 77,317                                | (7,676)                                       |  |  |
| Total assets   | 220,368                                | 4,766   |  | 2.89                                     | 188,975                               | (17,386)                                      |  | (12.08)                                  |
| Liabilities (e)  | 113,888                                | (1,812)                                       | (2.13)                                   |  | 108,842                               | 11,404  | 13.72                                    |  |
| Effect of derivatives: (e)                                     |  |   |  |  |                                       |   |  |  |
| Hedging derivatives  | 1,915                                  | 4   |  |  | 3,030                                 | (9)   |  |  |
| Embedded derivatives and ALM                                   | 108,537                                | (1,422)                                       |  |  | 78,848                                | 7,537   |  |  |
| Total liabilities  | 224,340                                | (3,230)                                       |  | (1.92)                                   | 190,720                               | 18,932  |  | 13.01                                    |
| Interest margin  |  |   | 2.66                                     | 0.97                                     |                                       |   | 1.94                                     | 0.93                                     |

See footnotes on page 117.

**Rates of Financing Income and Expenses (on a Consolidated Basis) (a)****Reported amounts****Exhibit A (Cont'd)**

|   | For the nine months ended 30 June  |                               |                                       |                                       |                                    |                               |                                       |
|---|------------------------------------|-------------------------------|---------------------------------------|---------------------------------------|------------------------------------|-------------------------------|---------------------------------------|
|   | 2009                               |                               |                                       | 2008                                  |                                    |                               |                                       |
|   | Rate of income (expenses)          |                               |                                       | Rate of income (expenses)             |                                    |                               |                                       |
|   | Average balance (b) (NIS millions) | Financing income (expenses) % | Excluding the effect of derivatives % | Including the effect of derivatives % | Average balance (b) (NIS millions) | Financing income (expenses) % | Excluding the effect of derivatives % |
|   |                                    |                               |                                       |                                       |                                    |                               | Including the effect of derivatives % |
| Total monetary assets generating interest   |                                    |                               |                                       |                                       |                                    |                               |                                       |
| Income (e) (f)  | 300,571                            | 11,015                        | 4.92                                  |                                       | 277,914                            | 149                           | 0.07                                  |
| Effect of derivatives:  |                                    |                               |                                       |                                       |                                    |                               |                                       |
| Hedging derivatives   | 2,059                              | (1)                           |                                       |                                       | 3,207                              | 18                            |                                       |
| Embedded derivatives and ALM (d)  | 154,644                            | 1,424                         |                                       |                                       | 121,234                            | (7,187)                       |                                       |
| Total assets  | 457,274                            | 12,438                        |                                       | 3.64                                  | 402,355                            | (7,020)                       | (2.32)                                |
| Total monetary liabilities generating interest  | 282,485                            | (5,760)                       | (2.73)                                |                                       | 261,339                            | 5,446                         | 2.77                                  |
| Effect of derivatives: (e)  |                                    |                               |                                       |                                       |                                    |                               |                                       |
| Hedging derivatives   | 1,915                              | 4                             |                                       |                                       | 3,030                              | (9)                           |                                       |
| Embedded derivatives and ALM  | 155,557                            | (2,673)                       |                                       |                                       | 121,787                            | 6,708                         |                                       |
| Total liabilities   | 439,957                            | (8,429)                       |                                       | (2.56)                                | 386,156                            | 12,145                        | 4.17                                  |
| <b>Interest margin</b>  |                                    |                               | <b>2.19</b>                           | <b>1.08</b>                           |                                    |                               | <b>2.84</b>                           |
| In respect of options   |                                    | 12                            |                                       |                                       |                                    | 136                           |                                       |
| In respect of other derivatives (excluding options, hedging derivative instruments, ALM derivatives and embedded derivatives which have been separated) (e) |                                    | 13                            |                                       |                                       |                                    | (129)                         |                                       |
| Financing commissions and other financing income (g)  |                                    | 1,144                         |                                       |                                       |                                    | 348                           |                                       |
| Other financing expenses  |                                    | 33                            |                                       |                                       |                                    | (76)                          |                                       |
| Net interest income before provision for doubtful debts   |                                    | 5,211                         |                                       |                                       |                                    | 5,404                         |                                       |
| Provision for doubtful debts (including general and supplementary provision)  |                                    | (1,136)                       |                                       |                                       |                                    | (1,055)                       |                                       |
| Net interest income after provision for doubtful debts  |                                    | 4,075                         |                                       |                                       |                                    | 4,349                         |                                       |
| Monetary assets generating interest income (d) (f)  | 300,571                            |                               |                                       |                                       | 277,914                            |                               |                                       |
| Assets derived from derivative instruments (h)  | 7,655                              |                               |                                       |                                       | 6,309                              |                               |                                       |
| Other monetary assets (d)   | 2,143                              |                               |                                       |                                       | 3,119                              |                               |                                       |
| General provision and supplementary provision for doubtful debts  | (945)                              |                               |                                       |                                       | (854)                              |                               |                                       |
| Total monetary assets   | 309,424                            |                               |                                       |                                       | 286,488                            |                               |                                       |
| Monetary liabilities generating interest expenses (d)   | 282,485                            |                               |                                       |                                       | 261,339                            |                               |                                       |
| Liabilities derived from derivative instruments (h)   | 8,408                              |                               |                                       |                                       | 6,871                              |                               |                                       |
| Other monetary liabilities (d)  | 7,808                              |                               |                                       |                                       | 8,618                              |                               |                                       |
| Total monetary liabilities  | 298,701                            |                               |                                       |                                       | 276,828                            |                               |                                       |
| Total monetary assets exceed monetary liabilities   | 10,723                             |                               |                                       |                                       | 9,660                              |                               |                                       |
| Non-monetary assets   | 8,884                              |                               |                                       |                                       | 10,983                             |                               |                                       |
| Non-monetary liabilities  | 359                                |                               |                                       |                                       | 489                                |                               |                                       |
| Total capital resources   | 19,248                             |                               |                                       |                                       | 20,154                             |                               |                                       |

See footnotes on page 117.

**Rates of Financing Income and Expenses (on a Consolidated Basis) (Cont'd) (a)****Nominal U.S. \$****Exhibit A (Cont'd)**

|   | For the nine months ended 30 September |            |               |               |                           |            |               |               |
|---|--|------------|---------------|---------------|---------------------------|------------|---------------|---------------|
|   | 2009                                   |            |               |               |                           |            | 2008          |               |
|   | Rate of income (expenses)              |            |               |               | Rate of income (expenses) |            |               |               |
|   | Average                                | Financing  | Excluding     | Including     | Average                   | Financing  | Excluding     | Including     |
|   | balance (b)                            | income     | the effect of | the effect of | balance (b)               | income     | the effect of | the effect of |
|   | (U.S.\$ millions)                      | (expenses) | derivatives   | derivatives   | (U.S.\$ millions)         | (expenses) | derivatives   | derivatives   |
|   |  |            | %             | %             |                           |            | %             | %             |
| Foreign currency:   |  |            |               |               |                           |            |               |               |
| Local operations (including Israeli currency linked to foreign currency)  |  |            |               |               |                           |            |               |               |
| Assets (c) (d)  | 16,419                                 | 323        | 2.63          |               | 19,412                    | 661        | 4.56          |               |
| Effect of derivatives: (e)  |  |            |               |               |                           |            |               |               |
| Hedging derivatives   | 514                                    | 7          |               |               | 900                       | 7          |               |               |
| Embedded derivatives and ALM  | 27,975                                 | 117        |               |               | 21,680                    | 133        |               |               |
| Total assets  | 44,908                                 | 447        |               | 1.33          | 41,992                    | 801        |               | 2.55          |
| Liabilities (d)   | 19,442                                 | (139)      | (0.96)        |               | 20,940                    | (427)      | (2.73)        |               |
| Effect of derivatives: (e)  |  |            |               |               |                           |            |               |               |
| Hedging derivatives   | 478                                    | (20)       |               |               | 850                       | (5)        |               |               |
| Embedded derivatives and ALM  | 27,013                                 | (54)       |               |               | 22,092                    | (150)      |               |               |
| Total liabilities   | 46,933                                 | (213)      |               | (0.61)        | 43,882                    | (582)      |               | (1.77)        |
| Interest margin   |  |            | 1.67          | 0.72          |                           |            | 1.83          | 0.78          |
| Foreign currency –  |  |            |               |               |                           |            |               |               |
| Foreign operations  |  |            |               |               |                           |            |               |               |
| (integrated operations)   |  |            |               |               |                           |            |               |               |
| Assets (c) (d)  | 10,156                                 | 259        | 3.42          |               | 11,002                    | 439        | 5.35          |               |
| Effect of embedded and ALM derivatives (e)                                | 104                                    | 16         |               |               | 76                        | 14         |               |               |
| Total assets  | 10,260                                 | 275        |               | 3.59          | 11,078                    | 453        |               | 5.49          |
| Liabilities (d)   | 9,102                                  | (103)      | (1.51)        |               | 9,569                     | (271)      | (3.79)        |               |
| Effect of embedded and ALM derivatives (e)                                | 115                                    | (22)       |               |               | 108                       | -          |               |               |
| Total liabilities   | 9,217                                  | (125)      |               | (1.81)        | 9,677                     | (271)      |               | (3.75)        |
| Interest margin   |  |            | 1.78          | 1.91          |                           |            | 1.56          | 1.74          |
| Total:  |  |            |               |               |                           |            |               |               |
| Monetary assets in foreign currency generating financing income (c) (d)   | 26,575                                 | 582        | 2.93          |               | 30,414                    | 1,100      | 4.85          |               |
| Effect of derivatives: (e)  |  |            |               |               |                           |            |               |               |
| Hedging derivatives   | 514                                    | 7          |               |               | 900                       | 7          |               |               |
| Embedded derivatives and ALM  | 28,079                                 | 133        |               |               | 21,756                    | 147        |               |               |
| Total assets  | 55,168                                 | 722        |               | 1.75          | 53,070                    | 1,254      |               | 3.16          |
| Monetary liabilities in foreign currency generating financing expense (d) | 28,544                                 | (242)      | (1.13)        |               | 30,509                    | (698)      | (3.06)        |               |
| Effect of derivatives: (e)  |  |            |               |               |                           |            |               |               |
| Hedging derivatives   | 478                                    | (20)       |               |               | 850                       | (5)        |               |               |
| Embedded derivatives and ALM  | 27,128                                 | (76)       |               |               | 22,200                    | (150)      |               |               |
| Total liabilities   | 56,150                                 | (338)      |               | (0.80)        | 53,559                    | (853)      |               | (2.13)        |
| Interest margin   |  |            | 1.80          | 0.95          |                           |            | 1.79          | 1.03          |

See footnotes on page 123.

- (a) The data in this exhibit includes before and after the effect of derivative instruments (including the effect of off-balance sheet derivative instruments).
- (b) Based on monthly opening balances for the Bank and subsidiaries in Israel and on quarterly opening balances for foreign subsidiaries, and after deduction of the average balance sheet balance of the specific provision for doubtful debts.
- (c) The average balance of unrealized losses on adjustment to fair value of debentures held for trading and available for sale has been added to the average balance of the assets for local and foreign operations, in the amount of US \$ 464 million.
- (d) Excluding derivative instruments.
- (e) Includes hedging derivative instruments (excluding options), embedded derivatives which have been separated, and ALM derivatives, which constitute part of the Bank's asset and liability management system.

## Credit to the Public - Risk by Economic Sector - on a Consolidated Basis

### Reported amounts

Exhibit B

| 30 September 2009 (Unaudited)                             |                               |                                   |                   |  |                                  |
|---|-------------------------------|-----------------------------------|-------------------|--|----------------------------------|
|   | Balance sheet credit risk (a) | Off-balance sheet credit risk (b) | Total credit risk | Addition for the year to the specific provision for doubtful debts | Balance of problematic debts (c) |
| NIS millions  |                               |                                   |                   |  |                                  |
| Activities of borrowers in Israel                         |                               |                                   |                   |  |                                  |
| Agriculture   | 1,790                         | 346                               | 2,136             | 20   | 180                              |
| Industry  | 20,774                        | 14,022                            | 34,796            | 154  | 2,472                            |
| Construction and real estate                              | 35,407                        | 18,099                            | 53,506            | 270  | 6,519                            |
| Electricity and water                                     | 1,242                         | 312                               | 1,554             | -  | 3                                |
| Commerce  | 14,042                        | 4,037                             | 18,079            | 33   | 1,412                            |
| Hotels and restaurants                                    | 3,727                         | 329                               | 4,056             | 17   | 1,533                            |
| Transport and storage                                     | 4,051                         | 1,326                             | 5,377             | 52   | 914                              |
| Communications and computer services                      | 3,905                         | 1,636                             | 5,541             | 41   | 373                              |
| Financial services  | 13,652                        | 7,634                             | 21,286            | 130  | 1,574                            |
| Business and other services                               | 4,404                         | 1,299                             | 5,703             | 24   | 294                              |
| Public and community services                             | 6,304                         | 1,016                             | 7,320             | 4  | 249                              |
| Private individuals - loans for housing                   | 43,411                        | 2,092                             | 45,503            | 1  | 843                              |
| Private individuals - other                               | 22,776                        | 25,153                            | 47,929            | 215  | 1,154                            |
|   | 175,485                       | 77,301                            | 252,786           | 961  | 17,520                           |
| Activities of borrowers abroad                            | 39,961                        | 14,654                            | 54,615            | 210  | 3,712                            |
| Total   | 215,446                       | 91,955                            | 307,401           | 1,171  | 21,232                           |
| Credit risk included within the various economic sectors: |                               |                                   |                   |  |                                  |
| Settlement movements (d)                                  | 2,864                         | 1,060                             | 3,924             | 3  | 851                              |
| Local authorities (e)                                     | 3,179                         | 144                               | 3,323             | -  | 90                               |

- (a) Including credit to the public in the amount of NIS 204,747 million, investments in debentures of the public in the amount of NIS 8,020 million and other assets in respect of derivative instruments which represent transactions of the public in the amount of NIS 2,679 million.
- (b) Credit risk on off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations.
- (c) Balances of problematic debt net of credit covered by collateral allowed as a deduction for purposes of individual and group borrower limits, including off-balance sheet risk components.
- (d) Kibbutzim and moshavim, regional and national organizations and corporations controlled by the settlement movement.
- (e) Including corporations under their control.

Note - Balances of credit risk and balances of problematic debts are stated net of specific provisions for doubtful debts.

# Credit to the Public - Risk by Economic Sector - on a Consolidated Basis (Cont'd)

## Reported amounts

Exhibit B (Cont'd)

| 30 September 2008 (Unaudited)                             |                               |                                   |                   |  |                                  |
|---|-------------------------------|-----------------------------------|-------------------|--|----------------------------------|
|   | Balance sheet credit risk (a) | Off-balance sheet credit risk (b) | Total credit risk | Addition for the year to the specific provision for doubtful debts | Balance of problematic debts (c) |
| NIS millions  |                               |                                   |                   |  |                                  |
| Activities of borrowers in Israel                         |                               |                                   |                   |  |                                  |
| Agriculture   | 1,910                         | 393                               | 2,303             | (35)   | 218                              |
| Industry  | 24,354                        | 13,018                            | 37,372            | 436  | 2,403                            |
| Construction and real estate                              | 32,691                        | 18,749                            | 51,440            | 65   | 6,257                            |
| Electricity and water                                     | 1,343                         | 145                               | 1,488             | -  | 5                                |
| Commerce  | 16,886                        | 3,873                             | 20,759            | (50)   | 1,201                            |
| Hotels and restaurants                                    | 3,706                         | 468                               | 4,174             | 7  | 1,376                            |
| Transport and storage                                     | 4,376                         | 1,019                             | 5,395             | 23   | 373                              |
| Communications and computer services                      | 4,813                         | 1,337                             | 6,150             | 23   | 360                              |
| Financial services  | 16,512                        | 7,068                             | 23,580            | 263  | 1,944                            |
| Business and other services                               | 5,298                         | 1,494                             | 6,792             | 8  | 160                              |
| Public and community services                             | 5,838                         | 1,209                             | 7,047             | -  | 328                              |
| Private individuals - loans for housing                   | 40,060                        | 2,408                             | 42,468            | 89   | 964                              |
| Private individuals - other                               | 22,777                        | 24,023                            | 46,800            | 139  | 1,340                            |
|   | 180,564                       | 75,204                            | 255,768           | 968  | 16,929                           |
| Activities of borrowers abroad                            | 39,652                        | 20,570                            | 60,222            | 112  | 1,839                            |
| Total   | 220,216                       | 95,774                            | 315,990           | 1,080  | 18,768                           |
| Credit risk included within the various economic sectors: |                               |                                   |                   |  |                                  |
| Settlement movements (d)                                  | 2,913                         | 580                               | 3,493             | (41)   | 431                              |
| Local authorities (e)                                     | 3,364                         | 158                               | 3,522             | (1)  | 135                              |

- (a) Including credit to the public in the amount of NIS 208,216 million, investments in debentures of the public in the amount of NIS 8,815 million and other assets in respect of derivative instruments which represent transactions of the public in the amount of NIS 3,185 million.
- (b) Credit risk on off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations.
- (c) Balances of problematic debt net of credit covered by collateral allowed as a deduction for purposes of individual and group borrower limits, including off-balance sheet risk components.
- (d) Kibbutzim and moshavim, regional and national organizations and corporations controlled by the settlement movement.
- (e) Including corporations under their control.

Note - Balances of credit risk and balances of problematic debts are stated net of specific provisions for doubtful debts.

# Credit to the Public - Risk by Economic Sector - on a Consolidated Basis (Cont'd)

## Reported amounts

Exhibit B (Cont'd)

| 31 December 2008 (Audited) *                              |                               |                                   |                   |  |                                  |
|---|-------------------------------|-----------------------------------|-------------------|--|----------------------------------|
|   | Balance sheet credit risk (a) | Off-balance sheet credit risk (b) | Total credit risk | Addition for the year to the specific provision for doubtful debts | Balance of problematic debts (c) |
| NIS millions  |                               |                                   |                   |  |                                  |
| Activities of borrowers in Israel                         |                               |                                   |                   |  |                                  |
| Agriculture   | 2,018                         | 385                               | 2,403             | (44)   | 256                              |
| Industry  | 23,940                        | 14,447                            | 38,387            | 596  | 3,031                            |
| Construction and real estate                              | 34,257                        | 18,579                            | 52,836            | 420  | 6,807                            |
| Electricity and water                                     | 1,203                         | 186                               | 1,389             | 1  | 5                                |
| Commerce  | 16,190                        | 3,447                             | 19,637            | 47   | 1,260                            |
| Hotels and restaurants                                    | 3,953                         | 339                               | 4,292             | 18   | 1,582                            |
| Transport and storage                                     | 4,336                         | 1,182                             | 5,518             | 21   | 391                              |
| Communications and computer services                      | 4,625                         | 1,332                             | 5,957             | 12   | 450                              |
| Financial services  | 17,888                        | 7,815                             | 25,703            | 339  | 2,539                            |
| Business and other services                               | 5,126                         | 1,386                             | 6,512             | 28   | 352                              |
| Public and community services                             | 5,539                         | 1,804                             | 7,343             | 7  | 330                              |
| Private individuals - loans for housing                   | 40,904                        | 1,742                             | 42,646            | 97   | 979                              |
| Private individuals - other                               | 22,374                        | 24,169                            | 46,543            | 227  | 1,345                            |
|   | 182,353                       | 76,813                            | 259,166           | 1,769  | 19,327                           |
| Activities of borrowers abroad                            | 44,491                        | 16,837                            | 61,328            | 303  | 3,355                            |
| Total   | 226,844                       | 93,650                            | 320,494           | 2,072  | 22,682                           |
| Credit risk included within the various economic sectors: |                               |                                   |                   |  |                                  |
| Settlement movements (d)                                  | 3,120                         | 596                               | 3,716             | (36)   | 928                              |
| Local authorities (e)                                     | 3,236                         | 145                               | 3,381             | (2)  | 154                              |

\* Reclassified.

- (a) Including credit to the public in the amount of NIS 214,044 million, investments in debentures of the public in the amount of NIS 8,204 million and other assets in respect of derivative instruments which represent transactions of the public in the amount of NIS 4,596 million.
- (b) Credit risk on off-balance sheet financial instruments as calculated for the purpose of per borrower credit limitations.
- (c) Balances of problematic debts net of credit covered by collateral allowed as a deduction for purposes of individual and group borrower limits, including off-balance sheet risk components.
- (d) Kibbutzim and moshavim, regional and national organizations and corporations controlled by the settlement movement.
- (e) Including corporations under their control.

Note - Balances of credit risk, off balance sheet credit risk and balances of problematic debts are stated net of specific provisions for doubtful debts

## Exposure to Interest Rate Fluctuations - on Consolidated Basis

## Exhibit C:

| 30 September 2009                                     |                           |                           |                          |                         |                           |                              |                                |                            |       | 31 December 2008          |                        |                           |                        |        |
|---|---------------------------|---------------------------|--------------------------|-------------------------|---------------------------|------------------------------|--------------------------------|----------------------------|-------|---------------------------|------------------------|---------------------------|------------------------|--------|
|   | On Demand up to one Month | One month to three months | Three months to one year | One year to three years | Three years to five years | Over five years to ten years | Over ten years to twenty years | Without fixed maturity (a) | Total | Internal rate of return % | Average maturity Years | Internal rate of return % | Average maturity Years |        |
|   |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| (NIS millions)  |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| <b>Israeli currency - unlinked</b>                    |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| Total assets  | 116,361                   | 6,219                     | 18,725                   | 6,210                   | 1,281                     | 1,513                        | 103                            | -                          | 1,460 | 151,872                   | 3.75                   | 0.36                      | 3.99                   | 0.45   |
| Total liabilities                                     | 106,648                   | 4,596                     | 7,033                    | 6,528                   | 3,006                     | 892                          | 180                            | 78                         | 310   | 129,271                   | 3.65                   | 0.36                      | 3.17                   | 0.37   |
| Difference  | 9,713                     | 1,623                     | 11,692                   | (318)                   | (1,725)                   | 621                          | (77)                           | (78)                       | 1,150 | 22,601                    | 0.10                   | 0.00                      | 1.53                   | 0.08   |
| Effect of future transactions and special commitments |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| Exposure to interest rate fluctuations in the sector  | (1,534)                   | (3,974)                   | (2,195)                  | 1,316                   | 378                       | 98                           | (52)                           | -                          | -     | (5,963)                   |                        |                           |                        |        |
| Accumulated exposure in the sector                    |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
|   | 8,179                     | (2,351)                   | 9,497                    | 998                     | (1,347)                   | 719                          | (129)                          | (78)                       | 1,150 | 16,638                    |                        |                           |                        |        |
| <b>Israeli currency – linked to the CPI</b>           |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| Total assets  | 1,816                     | 1,193                     | 10,378                   | 24,452                  | 9,870                     | 9,389                        | 2,641                          | 170                        | 95    | 60,004                    | 4.77                   | 3.42                      | 4.92                   | 3.33   |
| Total liabilities                                     | 1,048                     | 1,306                     | 6,847                    | 15,469                  | 9,769                     | 15,126                       | 2,396                          | 714                        | 280   | 52,955                    | 4.55                   | 4.37                      | 3.95                   | 4.18   |
| Difference  | 768                       | (113)                     | 3,531                    | 8,983                   | 101                       | (5,737)                      | 245                            | (544)                      | (185) | 7,049                     | 0.22                   | (0.95)                    | 0.97                   | (0.85) |
| Effect of future transactions and special commitments |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| Exposure to interest rate fluctuations in the sector  | (111)                     | (878)                     | (449)                    | (2,899)                 | (1,977)                   | (1,722)                      | (96)                           | -                          | -     | (8,132)                   |                        |                           |                        |        |
| Accumulated exposure in the sector                    |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
|   | 657                       | (991)                     | 3,082                    | 6,084                   | (1,876)                   | (7,459)                      | 149                            | (544)                      | (185) | (1,083)                   |                        |                           |                        |        |
| <b>Foreign currency (b)</b>                           |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| Total assets  | 49,607                    | 24,673                    | 7,154                    | 9,757                   | 2,430                     | 1,994                        | 463                            | 3                          | 395   | 96,476                    | 2.45                   | 0.65                      | 3.55                   | 0.55   |
| Total liabilities                                     | 63,254                    | 21,677                    | 23,031                   | 3,736                   | 1,415                     | 859                          | 181                            | -                          | 71    | 114,224                   | 1.47                   | 0.38                      | 1.88                   | 0.39   |
| Difference  | (13,647)                  | 2,996                     | (15,877)                 | 6,021                   | 1,015                     | 1,135                        | 282                            | 3                          | 324   | (17,748)                  | 0.98                   | 0.27                      | 1.67                   | 0.16   |
| Effect of future transactions and special commitments |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
| Exposure to interest rate fluctuations in the sector  | 8,539                     | 5,717                     | 3,338                    | (1,757)                 | (645)                     | (1,222)                      | 125                            | -                          | -     | 14,095                    |                        |                           |                        |        |
| Accumulated exposure in the sector                    |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |
|   | (5,108)                   | 8,713                     | (12,539)                 | 4,264                   | 370                       | (87)                         | 407                            | 3                          | 324   | (3,653)                   |                        |                           |                        |        |
| See footnotes on next page.                           |                           |                           |                          |                         |                           |                              |                                |                            |       |                           |                        |                           |                        |        |

See footnotes on next page.



## Exposure to Interest Rate Fluctuations - on Consolidated Basis

## Exhibit C (cont'd):

|   | 30 September 2009 |                 |                          |                           |                              | 31 December 2008               |                            |        |                           |                        |
|---|-------------------|-----------------|--------------------------|---------------------------|------------------------------|--------------------------------|----------------------------|--------|---------------------------|------------------------|
|   | On Demand         | One month       | Three months to one year | One year to three years   | Over five years to ten years | Over ten years to twenty years | Without fixed maturity (a) | Total  | Internal rate of return % | Average maturity Years |
|   | up to one month   | to three months | one year                 | three years to five years | years                        | years                          |                            |        | %                         | Years                  |
| (NIS millions)  |                   |                 |                          |                           |                              |                                |                            |        |                           |                        |
| <b>Total exposure to interest rate fluctuations</b>     |                   |                 |                          |                           |                              |                                |                            |        |                           |                        |
| Total assets (c)  | 167,784           | 32,085          | 36,257                   | 40,419                    | 13,581                       | 12,896                         | 3,207                      | 173    | 10,615                    | 317,017                |
| Receivables in respect of open credit card transactions |                   |                 |                          |                           |                              |                                |                            | 6,613  | 6,613                     |                        |
| Total liabilities (c)                                   | 170,950           | 27,579          | 36,911                   | 25,733                    | 14,190                       | 16,877                         | 2,757                      | 792    | 1,450                     | 297,239                |
| Payables in respect of open credit card transactions    |                   |                 |                          |                           |                              |                                |                            | 5,050  | 5,050                     |                        |
| Difference  | (3,166)           | 4,506           | (654)                    | 14,686                    | (609)                        | (3,981)                        | 450                        | (619)  | 10,728                    | 21,341                 |
| Effect of future transactions and special commitments   | 6,894             | 865             | 694                      | (3,340)                   | (2,244)                      | (2,846)                        | (23)                       | -      | -                         | -                      |
| Total exposure to interest rate fluctuations            | 3,728             | 5,371           | 40                       | 11,346                    | (2,853)                      | (6,827)                        | 427                        | (619)  | 10,728                    | 21,341                 |
| Total accumulated exposure                              | 3,728             | 9,099           | 9,139                    | 20,485                    | 17,632                       | 10,805                         | 11,232                     | 10,613 | 21,341                    | 21,341                 |

(a) The figures in the "Without fixed maturity" column are the non-discounted figures as stated in the balance sheet, including overdue balances in the amount of NIS 969 million.

(b) Local operations, including Israeli currency linked to foreign currency and integrated operations abroad.

(c) Including non-monetary assets in the "Without fixed maturity" column.

## General notes:

(1) Full details of the effect of changes in the interest rates in each sector, for the various balance sheet categories, are available on request.

(2) In this table, the data for each period represent the present value of the future cash flows discounted at the internal rate of return of the balance sheet category. The capitalized future cash flows, as stated, include interest to be accrued up to the earlier of repayment date or the date of change of the interest.

(3) The effect of hedging transactions is included in total assets or total liabilities, as relevant

## Country Exposure Reported Amounts

Exhibit D:

Part A – Information on total country exposure and on exposure to countries whose total individual exposure exceeds 1% of total assets or exceeds 20% of equity for purposes of calculating capital ratios, whichever is the lower

### 30 September 2009

| Balance Sheet Exposure              |                |  |        |          |           |   |        |                                 |  |                                  |
|-------------------------------------|----------------|--|--------|----------|-----------|---|--------|---------------------------------|--|----------------------------------|
| Cross-Border Balance Sheet Exposure |                | Net Foreign-office Claims on Local Residents |        |          |           | Total balance sheet exposure                              |        |                                 |  |                                  |
| Country                             | (NIS millions) | To governments (a)                           |        | To banks | To others | Balance sheet exposure before deducting local liabilities |        | Deduction for local liabilities | Balance sheet exposure after deducting local liabilities | Balance of problematic debts (b) |
|                                     |                |  |        |          |           |   |        |                                 |  |                                  |
| United States                       | 85             | 7,550  | 7,171  | 17,524   | 7,711     | 9,813   | 24,619 | 922                             |  |                                  |
| England                             | 19             | 6,441  | 1,233  | 4,794    | 1,858     | 2,936   | 10,629 | 514                             |  |                                  |
| France                              | 2,215          | 2,648  | 531    | 19       | 4         | 15  | 5,409  | 14                              |  |                                  |
| Holland                             | -              | 1,601  | 1,614  | -        | -         | -   | 3,215  | 13                              |  |                                  |
| Germany                             | 101            | 1,487  | 1,327  | -        | -         | -   | 2,915  | -                               |  |                                  |
| Others                              | 216            | 7,429  | 5,876  | 2,558    | 1,584     | 974   | 14,495 | 389                             |  |                                  |
| Total country exposure              | 2,636          | 27,156                                       | 17,752 | 24,895   | 11,157    | 13,738  | 61,282 | 1,852                           |  |                                  |
| Total exposure to LDC countries     | 175            | 289  | 1,263  | 2,092    | 1,213     | 879   | 2,606  | 34                              |  |                                  |

### 30 September 2009

| Off - Balance Sheet Exposure    |                | Cross-Border Balance Sheet Exposure |   |                          |                         |
|---------------------------------|----------------|-------------------------------------|---|--------------------------|-------------------------|
| Country                         | (NIS millions) | Total off-balance sheet exposure    | Of which:                                 |                          | Repayment over one year |
|                                 |                |                                     | Problematic off-balance sheet credit risk | Repayment up to one year |                         |
| United States                   | 9,391          | -                                   | -   | 5,946                    | 8,860                   |
| England                         | 10,557         | 30                                  | 30  | 5,183                    | 2,510                   |
| France                          | 2,062          | -                                   | -   | 2,143                    | 3,251                   |
| Holland                         | 339            | -                                   | -   | 1,042                    | 2,173                   |
| Germany                         | 807            | -                                   | -   | 1,606                    | 1,309                   |
| Others                          | 2,617          | -                                   | -   | 7,772                    | 5,749                   |
| Total country exposure          | 25,773         | 30                                  | 30  | 23,692                   | 23,852                  |
| Total exposure to LDC countries | 449            | -                                   | -   | 1,220                    | 507                     |

(a) Includes governments, official institutions and central banks.

(b) Problem Debt balances less debt covered by eligible collateral for purposes of per borrower or group borrowers' debt limitation. This does not include off balance credit risk.

## Country Exposure Reported Amounts

Exhibit D (con'd):

Part A – Information on total country exposure and on exposure to countries whose total individual exposure exceeds 1% of total assets or exceeds 20% of equity for purposes of calculating capital ratios, whichever is the lower

31 December 2008

### Balance Sheet Exposure

| Country                         | Cross-Border Balance Sheet Exposure |          | Net Foreign-office Claims on Local Residents |  |                                    |   | Total balance sheet exposure |       |
|---------------------------------|-------------------------------------|----------|--|--|------------------------------------|---|------------------------------|-------|
|                                 | To governments(a)<br>(NIS millions) | To banks | To others                                    | Balance sheet<br>exposure before<br>deducting local<br>liabilities | Deduction for<br>local liabilities | Balance sheet<br>exposure after<br>deducting local<br>liabilities |                              |       |
| United States                   | 3,516                               | 6,466    | 8,801  | 20,504   | 9,367                              | 11,137  | 29,920                       | 904   |
| England                         | 8                                   | 6,391    | 967  | 5,253  | 1,812                              | 3,441   | 10,807                       | 378   |
| France                          | 566                                 | 1,759    | 521  | 18   | 5                                  | 13  | 2,859                        | 33    |
| Holland                         | -                                   | 1,849    | 1,445  | -  | -                                  | -   | 3,294                        | 147   |
| Germany                         | -                                   | 2,195    | 1,177  | -  | -                                  | -   | 3,372                        | 36    |
| Others                          | 320                                 | 9,597    | 5,095  | 3,614  | 2,132                              | 1,482   | 16,494                       | 737   |
| Total country exposure          | 4,410                               | 28,257   | 18,006                                       | 29,389   | 13,316                             | 16,073  | 66,746                       | 2,235 |
| Total exposure to LDC countries | 264                                 | 596      | 1,029  | 1,752  | 1,000                              | 752   | 2,641                        | 16    |

31 December 2008

### Off - Balance Sheet Exposure

| Off-balance sheet exposure       |   |   |                                     |                            |
|----------------------------------|---|---|-------------------------------------|----------------------------|
| Country                          | Total off-balance<br>sheet exposure<br>(NIS millions) | Of which:<br>Problematic off-<br>balance sheet<br>credit risk | Cross-Border Balance Sheet Exposure |                            |
|                                  |   |   | Repayment up to<br>one year         | Repayment over<br>one year |
| United States                    | 12,599  | 40  | 7,785                               | 10,998                     |
| England                          | 10,758  | -   | 5,079                               | 2,287                      |
| France                           | 1,698   | -   | 1,630                               | 1,216                      |
| Holland                          | 846   | -   | 2,138                               | 1,156                      |
| Germany                          | 661   | -   | 2,123                               | 1,249                      |
| Others                           | 3,830   | -   | 9,176                               | 5,836                      |
| Total country exposure           | 30,392  | 40  | 27,931                              | 22,742                     |
| Total exposure to LDC countries* | 623   | -   | 1,542                               | 347                        |

(a) Includes governments, official institutions and central banks.

(b) Problem Debt balances less debt covered by eligible collateral for purposes of per borrower or group borrowers' debt limitation. This does not include off balance credit risk.

## Country Exposure

Exhibit D (cont'd):

### Footnotes:

In accordance with the Directive of the Supervisor of Banks, country exposure is shown on an end-risk basis, as follows:

- The accounting balance of a debt is to be dealt with as the amount of exposure to the legal country of residence of the debtor who bears the end risk after the effect of guarantees, liquid collateral and credit derivatives.
- The accounting balance of an investment in shares is to be dealt with as the amount of exposure to the country of residence of the issuer of the security.
- Off-balance sheet credit risk is shown as an off-balance sheet exposure to the country of residence of the counterparty to the transaction as it was calculated for the purposes of per borrower debt limitation.

From the aspect of determining end-risk, collateral is to be considered as follows:

- Third party guarantees according to the country of residence of the guarantor.
- Securities - The country of residence is that of the issuer of the security.
- The Directive makes it clear that real estate and debtors' balances do not represent collateral for purposes of determining end-risk.
- For purposes of determining end-risk only specific collaterals were taken into account.

Part B – The aggregate amount of balance sheet exposure to countries whose total individual exposure is between 0.75% and 1% of total consolidated assets or 15%-20% of the equity, whichever is the lower: No country is relevant for this criteria as of September 2009 (31 December 2008 – NIS 2,455 as it relates to Belgium only)

Part C – The exposure to the foreign countries with liquidity difficulties as defined by Bank of Israel (a country who receives financial assistance from IMF or its liabilities a rating of CCC or lower) amounts to NIS 445 million and relates to 13 countries.

## **Certification**

I, Galia Maor, certify that:

1. I have reviewed the Quarterly Report of Bank Leumi le-Israel B.M. (the "Bank") for the quarter ended on 30 September 2009 (the "Report").
2. Based on my knowledge, the Report does not contain any untrue statement of a material fact or omit to state a material fact that is necessary so that the statements included therein, in light of the circumstances under which such statements were included, are not misleading with reference to the period covered by the Report.
3. Based on my knowledge, the financial statements, and other financial information included in the Report, fairly present in all material respects the financial condition, results of operations and changes in shareholders' equity and cash flows of the Bank for the dates and periods covered by the Report.
4. I and the Bank's other certifying officers are responsible for establishing and maintaining controls and procedures with regard to the Bank's disclosure and internal control of financial reporting (as defined in the Public Reporting Directives concerning "The Directors' Report"), and also:
  - (a) We have established such controls and procedures, or caused such controls and procedures to be determined under our supervision, so as to ensure that material information relating to the Bank, including its consolidated corporations, is made known to us by others within the Bank and in those corporations, particularly during the period of preparation of the Report;
  - (b) We have established such internal control over financial reporting, or caused such internal control to be established under our supervision, so as to provide a reasonable level of confidence regarding the reliability of financial reporting and that the financial statements for external purposes are prepared in accordance with accepted accounting principles and the directives of the Supervisor of Banks and his instructions; and
  - (c) We have evaluated the effectiveness of the Bank's disclosure controls and procedures and presented in this Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by the Report, based on our evaluation; and
  - (d) We have disclosed in the Report any change in the Bank's internal control over financial reporting that occurred during this quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting; and
5. I and the Bank's other certifying officers have disclosed to the Joint Auditors, the Board of Directors, the Audit Committee and the Financial Statements Review Committee of the Board of Directors of the Bank, based on our most recent evaluation of internal control over financial reporting:
  - (a) All significant deficiencies and material weaknesses in the establishment or operation of internal control over financial reporting which are reasonably likely to adversely affect the Bank's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether material or immaterial, in which Management was involved or in which other employees were involved who have a significant role in the Bank's internal control over financial reporting.

The above does not derogate from my responsibility or the responsibility of any other person, pursuant to any law.

**29 November 2009**

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**Galia Maor**  
**President and Chief Executive Officer**

## Certification

I, Zeev Nahari, certify that:

1. I have reviewed the Quarterly Report of Bank Leumi le-Israel B.M. (the "Bank") for the quarter ended on 30 September 2009 (the "Report").
2. Based on my knowledge, the Report does not contain any untrue statement of a material fact or omit to state a material fact that is necessary so that the statements included therein, in light of the circumstances under which such statements were included, are not misleading with reference to the period covered by the Report.
3. Based on my knowledge, the financial statements, and other financial information included in the Report, fairly present in all material respects the financial condition, results of operations and changes in shareholders' equity and cash flows of the Bank for the dates and periods covered by the Report.
4. I and the Bank's other certifying officers are responsible for establishing and maintaining controls and procedures with regard to the Bank's disclosure and internal control of financial reporting (as defined in the Public Reporting Directives concerning "The Directors' Report"), and also:
  - (a) We have established such controls and procedures, or caused such controls and procedures to be determined under our supervision, so as to ensure that material information relating to the Bank, including its consolidated corporations, is made known to us by others within the Bank and in those corporations, particularly during the period of preparation of the Report;
  - (b) We have established such internal control over financial reporting, or caused such internal control to be established under our supervision, so as to provide a reasonable level of confidence regarding the reliability of financial reporting and that the financial statements for external purposes are prepared in accordance with accepted accounting principles and the directives of the Supervisor of Banks and his instructions; and
  - (c) We have evaluated the effectiveness of the Bank's disclosure controls and procedures and presented in the Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by the Report, based on our evaluation; and
  - (d) We have disclosed in the Report any change in the Bank's internal control over financial reporting that occurred during this quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting; and
5. I and the Bank's other certifying officers have disclosed to the Joint Auditors, the Board of Directors, the Audit Committee and the Financial Statements Review Committee of the Board of Directors of the Bank, based on our most recent evaluation of internal control over financial reporting:
  - (a) All significant deficiencies and material weaknesses in the establishment or operation of internal control over financial reporting which are reasonably likely to adversely affect the Bank's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether material or immaterial, in which Management was involved or in which other employees were involved who have a significant role in the Bank's internal control over financial reporting.

The above does not derogate from my responsibility or the responsibility of any other person, pursuant to any law.

**29 November 2009**

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**Zeev Nahari**  
**Senior Deputy Chief Executive Officer**  
**Chief Financial Officer,**  
**Head of Finance, Accounting and Capital Markets**

## **Joint Auditors' review report to the shareholders of Bank Leumi le-Israel B.M.**

### **Introduction**

We have reviewed the accompanying financial information of Bank Leumi le-Israel B.M. (The Bank) and its subsidiaries, which comprises the condensed interim consolidated balance sheet as of September 30, 2009 and the related interim condensed consolidated statements of profit and loss, changes in shareholders equity and cash flows for the three and nine month periods then ended. The board of directors and management are responsible for the preparation and presentation of interim financial information for these interim periods in accordance with Accounting Standard No. 14 of the Israel Accounting Standards Board, "Interim Financial Reporting" and with directives and guidelines of the Supervisor of Banks. Our responsibility is to express a conclusion on this interim financial information based on our review.

We did not review the condensed interim financial information of foreign subsidiaries, whose assets constitute approximately 2% of total consolidated assets as of September 30, 2009, and whose interest income before provision for doubtful debts constitute some 6% and some 3% of the total net interest income before provision for doubtful debts for the three and nine month periods then ended, respectively. The condensed interim financial information of those companies was reviewed by other auditors, whose review reports have been furnished to us, and our conclusion, insofar as it relates to the financial information in respect of those companies, is based on the review reports of the other auditors.

### **Scope of review**

We conducted our review in accordance with Review Standard 1 of the Institute of Certified Public Accountants in Israel, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" and a review standard implementation of which in review of banking institutions was required in guidelines of the Supervisor of Banks. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards in Israel and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

### **Conclusion**

Based on our review and the review reports of other auditors, nothing has come to our attention that causes us to believe that the accompanying interim financial information was not prepared, in all material respects, in accordance with Accounting Standard No. 14 of the Israel Accounting Standards Board and with directives and guidelines of the Supervisor of Banks.

Without qualifying our Conclusion, we draw attention:

1. to the contents of Note 6C. clauses 2, 4 and 5 of the condensed interim balance sheet concerning claims against the Bank and against consolidated subsidiaries, including applications for their approval as class actions.
2. to the contents of Note 6F. concerning the ruling of the Antitrust General Director.
3. to the contents of Note 6 clauses D1 and E concerning claims relating to companies included on equity basis and a debt arrangement related to a subsidiary of a company included on equity basis.

The Bank is unable to estimate the effect of the said matters on the Bank, if any, on its financial position and on its operating results, and whether or not they will be of a material nature.

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**Kost Forer Gabbay & Kasierer**  
**Certified Public Accountants (Isr.)**

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**Somekh Chaikin**  
**Certified Public Accountants (Isr.)**

29 November 2009

**Condensed Consolidated Balance Sheet as at 30 September 2009**  
**For the Periods Ended 30 September 2009**  
**Reported amounts**

|  | <b>30 September 2009</b> | <b>30 September 2008</b> | <b>31 December 2008</b> |
|--|--------------------------|--------------------------|-------------------------|
|  | (Unaudited)              | (Unaudited)              | (Audited)               |
|  | (NIS millions)           |                          |                         |
| <b>Assets</b>  |                          |                          |                         |
| Cash and deposits with banks                               | <b>43,934</b>            | 29,027                   | 33,130                  |
| Securities   | <b>58,381</b>            | 41,566                   | 44,910                  |
| Securities borrowed or purchased under agreement to resell | <b>1,823</b>             | 483                      | 201                     |
| Credit to the public                                       | <b>203,971</b>           | 207,489                  | 213,215                 |
| Credit to governments                                      | <b>430</b>               | 512                      | 520                     |
| Investments in companies included on the equity basis      | <b>1,908</b>             | 2,031                    | 1,842                   |
| Buildings and equipment                                    | <b>3,544</b>             | 3,368                    | 3,445                   |
| Other assets   | <b>9,639</b>             | 9,335                    | 13,529                  |
| <b>Total assets</b>  | <b>323,630</b>           | 293,811                  | 310,792                 |
| <b>Liabilities and equity capital</b>                      |                          |                          |                         |
| Deposits of the public                                     | <b>249,433</b>           | 225,952                  | 244,783                 |
| Deposits from banks  | <b>5,395</b>             | 6,457                    | 3,742                   |
| Deposits from governments                                  | <b>719</b>               | 827                      | 831                     |
| Securities loaned or sold under agreement to repurchase    | <b>1,316</b>             | 549                      | 549                     |
| Debentures, bonds and subordinated notes                   | <b>25,471</b>            | 22,257                   | 20,636                  |
| Other liabilities  | <b>19,955</b>            | 17,978                   | 21,334                  |
| <b>Total liabilities</b>                                   | <b>302,289</b>           | 274,020                  | 291,875                 |
| Minority interest  | <b>274</b>               | 229                      | 245                     |
| Shareholders' equity                                       | <b>21,067</b>            | 19,562                   | 18,672                  |
| <b>Total liabilities and equity capital</b>                | <b>323,630</b>           | 293,811                  | 310,792                 |

The accompanying notes are an integral part of these Financial Statements.

**Eitan Raff**  
Chairman of the  
Board of Directors

**Galia Maor**  
President and Chief  
Executive Officer

**Zeev Nahari**  
Senior Deputy Chief Executive Officer  
Chief Financial Officer,  
Head of Finance, Accounting and Capital  
Markets

**Date of approval of the Financial Statements: 29 November 2009**



**Condensed Consolidated Statement of Profit and Loss**  
**For the Period Ended 30 September 2009**  
**Reported Amounts**

|  | For the Three Months<br>Ended 30 September |               | For the Nine Months<br>Ended 30 September |             | For the Year Ended<br>31 December |
|--|--|---------------|---|-------------|-----------------------------------|
|  | 2009                                       | 2008          | 2009                                      | 2008        | 2008                              |
|  | (Unaudited)                                |               | (Unaudited)                               |             | (Audited)                         |
|  | (NIS millions)                             |               |   |             |                                   |
| Net interest income before provision for doubtful debts                                  | 1,923                                      | 1,491         | 5,211                                     | 5,404       | 6,380                             |
| Provision for doubtful debts   | 443  | 495           | 1,136                                     | 1,055       | 2,145                             |
| Net interest income after provision for doubtful debts                                   | 1,480                                      | 996           | 4,075                                     | 4,349       | 4,235                             |
| <b>Operating and other income</b>  |  |               |   |             |                                   |
| Operating commissions  | 915  | 887 (a)       | 2,586                                     | 2,671 (a)   | 3,538 (a)                         |
| Profits (losses) from investments in shares, net   | 286  | (363)         | 471                                       | (478)       | (912)                             |
| Other income   | 91   | 16 (a)        | 251                                       | 62 (a)      | 174 (a)                           |
| Total operating and other income   | 1,292                                      | 540           | 3,308                                     | 2,255       | 2,800                             |
| <b>Operating and other expenses</b>  |  |               |   |             |                                   |
| Salaries and related expenses  | 1,052                                      | 1,043         | 2,864                                     | 3,149       | 4,118                             |
| Building and equipment maintenance and depreciation                                      | 366  | 353           | 1,110                                     | 1,020       | 1,397                             |
| Other expenses   | 340  | 350           | 988                                       | 1,033       | 1,488                             |
| Total operating and other expenses   | 1,758                                      | 1,746         | 4,962                                     | 5,202       | 7,003                             |
| Operating profits before taxes   | 1,014                                      | (210)         | 2,421                                     | 1,402       | 32                                |
| Provision for taxes on operating profit  | 499  | 61            | 950                                       | 844         | 421                               |
| Operating profit (loss) after taxes  | 515  | (271)         | 1,471                                     | 558         | (389)                             |
| Equity in after-tax operating profits (losses) of companies included on the equity basis | 30   | 191           | -   | 471         | 249                               |
| Minority interest in after-tax operating (profits) of subsidiaries                       | (11)                                       | (5)           | (29)                                      | (3)         | (18)                              |
| Net operating profit (loss)  | 534  | (85)          | 1,442                                     | 1,026       | (158)                             |
| After-tax profit from extraordinary items  | -  | 1             | 28  | 249         | 250                               |
| Net profit for the period  | 534  | (84)          | 1,470                                     | 1,275       | 92                                |
|  | (NIS)                                      |               |   |             |                                   |
| <b>Basic and diluted earnings per share</b>  |  |               |   |             |                                   |
| Net operating profit (loss)  | 0.36                                       | (0.06)        | 0.98                                      | 0.70        | (0.11)                            |
| After-tax profit from extraordinary items  | -  | -             | 0.02                                      | 0.17        | 0.17                              |
| <b>Total</b>   | <b>0.36</b>                                | <b>(0.06)</b> | <b>1.00</b>                               | <b>0.87</b> | <b>0.06</b>                       |

(a) Reclassified.

The accompanying notes are an integral part of these Financial Statements.

**Condensed Consolidated Statement of Changes in Shareholders' Equity**  
**For the Periods Ended 30 September 2009**  
**Reported Amounts**

| <b>For the Three Months Ended 30 September 2009 (Unaudited)</b>   |               |         |                |          |   |                         |                   |  |  |                            |
|---|---------------|---------|----------------|----------|---|-------------------------|-------------------|--|--|----------------------------|
|   | Share capital | Premium | and others (a) | reserves | Total share capital and securities available for sale at fair value (b) | Translation adjustments | Retained earnings | Dividend declared after balance sheet date | Loans to employees for purchase of the Bank's shares | Total shareholders' equity |
|   | NIS millions  |         |                |          |   |                         |                   |  |  |                            |
| Balance at the beginning of the period  | 7,059         | 972     | 167            | 8,198    | (70)  | (558)                   | 13,025            | -  | (373)  | 20,222                     |
| Net profit for the period   | -             | -       | -              | -        | -   | -                       | 534               | -  | -  | 534                        |
| Other comprehensive income in companies included on the equity basis which was directly recorded in retained earnings | -             | -       | -              | -        | -   | -                       | (63)              | -  | -  | (63)                       |
| Adjustments in respect of presentation of securities available for sale at fair value                                 | -             | -       | -              | -        | 878   | -                       | -                 | -  | -  | 878                        |
| Profits in respect of securities available for sale that were realized and classified to profit and loss              | -             | -       | -              | -        | (399)   | -                       | -                 | -  | -  | (399)                      |
| Related tax effect  | -             | -       | -              | -        | (181)   | -                       | -                 | -  | -  | (181)                      |
| Translation adjustments for companies included on the equity basis  | -             | -       | -              | -        | -   | 82                      | -                 | -  | -  | 82                         |
| Loans to employees for purchase of Bank's shares  | -             | -       | -              | -        | -   | -                       | -                 | -  | (6)  | (6)                        |
| Balance at the end of the period  | 7,059         | 972     | 167            | 8,198    | 228   | (476)                   | 13,496            | -  | (379)  | 21,067                     |

The accompanying notes are an integral part of these Financial Statements.

See footnotes on page 141.

## Condensed Consolidated Statement of Changes in Shareholders' Equity (cont'd)

## Reported Amounts

| For the Three Months Ended 30 September 2008 (Unaudited)  |  |         |   |          |  |            |  |                   |  |                            |
|---|--|---------|---|----------|--|------------|--|-------------------|--|----------------------------|
|   | Capital reserves in respect of share-based payment transactions and others (a) |         | Total share capital and securities available for sale at fair value |          | Accumulated other comprehensive income |            | Dividend declared after balance sheet date |                   | Loans to employees for purchase of the Bank's shares |                            |
|   | Share capital  | Premium | and others (a)  | reserves | capital                                | securities | Translation adjustments (b)                | Retained earnings | date   | Total shareholders' equity |
|   | NIS millions   |         |   |          |  |            |  |                   |  |                            |
| Balance at the beginning of the period  | 7,345  | 520     | 323   | 8,188    | (85)                                   | (630)      | 13,328                                     | -                 | (373)  | 20,428                     |
| Net profit for the period   | -  | -       | -   | -        | -                                      | -          | (84)                                       | -                 | -  | (84)                       |
| Issue of shares   | 3  | 32      | -   | 35       | -                                      | -          | -  | -                 | -  | 35                         |
| Other comprehensive income in companies included on the equity basis which was directly recorded in retained earnings | -  | -       | -   | -        | -                                      | -          | (34)                                       | -                 | -  | (34)                       |
| Benefit in respect of shares based payment transactions   | -  | -       | (30)  | (30)     | -                                      | -          | -  | -                 | -  | (30)                       |
| Adjustments in respect of presentation of securities available for sale at fair value                                 | -  | -       | -   | -        | (1,640)                                | -          | -  | -                 | -  | (1,640)                    |
| Losses in respect of securities available for sale that were realized and classified to profit and loss               | -  | -       | -   | -        | 481                                    | -          | -  | -                 | -  | 481                        |
| Related tax effect  | -  | -       | -   | -        | 418                                    | -          | -  | -                 | -  | 418                        |
| Translation adjustments for companies included on the equity basis  | -  | -       | -   | -        | -                                      | (7)        | -  | -                 | -  | (7)                        |
| Loans to employees for purchase of Bank's shares  | -  | -       | -   | -        | -                                      | -          | -  | -                 | (5)  | (5)                        |
| Balance at the end of the period  | 7,348  | 552     | 293   | 8,193    | (826)                                  | (637)      | 13,210                                     | -                 | (378)  | 19,562                     |

The accompanying notes are an integral part of these Financial Statements.

See footnotes on page 141.

## Condensed Consolidated Statement of Changes in Shareholders' Equity (cont'd)

## Reported Amounts

## For the Nine Months Ended 30 September 2009 (Unaudited)

|   | Share capital | Premium | and others | (a) | reserves | Total share capital and securities available for sale at fair value | Accumulated other comprehensive income    |                         |                   | Dividend declared after balance sheet date | Loans to employees for purchase of the Bank's shares | Total shareholders' equity |
|---|---------------|---------|------------|-----|----------|---|---|-------------------------|-------------------|--|--|----------------------------|
|   |               |         |            |     |          |   | Adjustments in respect of presentation of | Translation adjustments | Retained earnings |  |  |                            |
| Share capital   |               |         |            |     |          |   |   |                         |                   |  |  |                            |
| NIS millions  |               |         |            |     |          |   |   |                         |                   |  |  |                            |
| Balance as at 1 January 2009  | 7,059         | 855     | 284        |     | 8,198    | (648)   |   | (502)                   | 11,998            | -  | (374)  | 18,672                     |
| Net profit for the period   | -             | -       | -          | -   | -        | -   | -   | -                       | 1,470             | -  | -  | 1,470                      |
| Expiry of options   | -             | 117     | (117)      | -   | -        | -   | -   | -                       | -                 | -  | -  | -                          |
| Other comprehensive income in companies included on the equity basis which was directly recorded in retained earnings | -             | -       | -          | -   | -        | -   | -   | -                       | 28                | -  | -  | 28                         |
| Adjustments in respect of presentation of securities available for sale at fair value                                 | -             | -       | -          | -   | -        | 2,050   |   | -                       | -                 | -  | -  | 2,050                      |
| Profits in respect of securities available for sale that were realized and classified to profit and loss              | -             | -       | -          | -   | -        | (685)   |   | -                       | -                 | -  | -  | (685)                      |
| Related tax effect  | -             | -       | -          | -   | -        | (489)   |   | -                       | -                 | -  | -  | (489)                      |
| Translation adjustments for companies included on the equity basis  | -             | -       | -          | -   | -        | -   |   | 26                      | -                 | -  | -  | 26                         |
| Loans to employees for purchase of Bank's shares  | -             | -       | -          | -   | -        | -   |   | -                       | -                 | -  | (5)  | (5)                        |
| Balance at the end of the period  | 7,059         | 972     | 167        |     | 8,198    | 228   |   | (476)                   | 13,496            | -  | (379)  | 21,067                     |

See footnotes on page 141.

See footnotes on page 141.

**Condensed Consolidated Statement of Changes in Shareholders' Equity**  
**Reported Amounts**

| For the Year Ended 31 December 2008 (Audited)   |               |            |            |          |   |   |   |                             |  |  |
|---|---------------|------------|------------|----------|---|---|---|-----------------------------|--|--|
|   | Share capital | Premium    | and others | (a)      | reserves  | Total share capital and securities available for sale at fair value | Accumulated other comprehensive income    |                             | Dividend declared after balance sheet date | Loans to employees for purchase of the Bank's shares |
|   |               |            |            |          |   |   | Adjustments in respect of presentation of | Translation adjustments (b) |  |  |
| Share capital   | Premium       | and others | (a)        | reserves | Total share capital and securities available for sale at fair value | Translation adjustments (b)   | Adjustments in respect of presentation of | Translation adjustments (b) | Dividend declared after balance sheet date | Loans to employees for purchase of the Bank's shares |
| NIS millions  |               |            |            |          |   |   |   |                             |  |  |
| Balance as at 1 January 2008  | 7,000         | -          | -          | 610      | 7,610   | 502   | (445)                                     | 12,016                      | 270  | (404)  |
| Net profit for the year   | -             | -          | -          | -        | -   | -   | -   | 92                          | -  | -  |
| Issue of shares   | 59            | 855        | (300)      | 614      | 614   | -   | -   | -                           | -  | -  |
| Dividend paid   | -             | -          | -          | -        | -   | -   | -   | -                           | (270)                                      | -  |
| Benefit in respect of shares based payment transactions   | -             | -          | (26)       | (26)     | (26)  | -   | -   | -                           | -  | -  |
| Other comprehensive loss in companies included on the equity basis which was directly recorded in retained earnings | -             | -          | -          | -        | -   | -   | -   | (110)                       | -  | -  |
| Adjustments in respect of presentation of securities available for sale at fair value                               | -             | -          | -          | -        | -   | (3,636)   | -   | -                           | -  | -  |
| Losses in respect of securities available for sale that were realized and classified to profit and loss             | -             | -          | -          | -        | -   | 1,852   | -   | -                           | -  | -  |
| Related tax effect  | -             | -          | -          | -        | -   | 634   | -   | -                           | -  | -  |
| Translation adjustments for companies included on the equity basis  | -             | -          | -          | -        | -   | -   | (57)                                      | -                           | -  | -  |
| Loans to employees for purchase of Bank's shares  | -             | -          | -          | -        | -   | -   | -   | -                           | -  | 30   |
| Balance as at 31 December 2008  | 7,059         | 855        | 284        | 8,198    | 8,198   | (648)   | (502)                                     | 11,998                      | -  | (374)  |
|   |               |            |            |          |   |   |   |                             |  | 18,672   |

(a) Including 10 million of other capital reserves.

(b) Adjustments arising from translation of the financial statements of foreign subsidiaries, which operating currency is different from reporting currency.

**Consolidated Statements of Cash Flows**  
**For the Periods Ended 30 September 2009**  
**Reported amounts**

|   | <b>For the three<br/>months ended<br/>30 September<br/>2009</b> | <b>For the nine<br/>months ended<br/>30 September<br/>2009</b> | <b>For the year<br/>ended<br/>31 December<br/>2008</b> |
|---|---|--|--|
|   | Unaudited   | Unaudited  | Audited  |
|   | (NIS millions)  |  |  |
| <b>Cash flows generated by operating activities:</b>  |   |  |  |
| Net profit for the year   | 534   | 1,470  | 92   |
| <b>Adjustments required to cash flows generated by operating activities:</b>                          |   |  |  |
| Equity in undistributed profits of companies included on equity basis (a)                             | (30)  | -  | (128)  |
| Minority interest in profits of subsidiaries  | 11  | 29   | 18   |
| Benefit in respect of share-based payment transactions  | -   | -  | 24   |
| Depreciation of buildings and equipment   | 152   | 455  | 520  |
| Amortization  | 4   | 12   | 17   |
| Provision for doubtful debts  | 443   | 1,136  | 2,145  |
| Change in provision for decrease in value of assets transferred to the Group's ownership              | 1   | (2)  | 10   |
| Net gain on sale of securities available for sale   | (410)   | (846)  | (52)   |
| Realized and unrealized loss (gain) from adjustment of held for trading securities to fair value      | (59)  | (227)  | 446  |
| Gain on receipt of shares without payment   | -   | -  | (27)   |
| After-tax profit on realization of investments in subsidiaries and companies included on equity basis | -   | -  | (17)   |
| Net (gains) losses, after tax, on sale of buildings and equipment                                     | -   | (28)   | 2  |
| Provision for impairment of debentures available for sale   | 11  | 151  | 1,328  |
| Provision for impairment of shares available for sale   | -   | 10   | 576  |
| Cancellation of special provisions in connection with fixed assets                                    | -   | -  | (2)  |
| Deferred taxes in respect of operating profit, net  | 58  | 204  | 33   |
| Increase (decrease) in excess of provisions for severance pay and pensions over amounts funded        | (15)  | (263)  | 672  |
| Gain on issue of shares to third party in subsidiary  | -   | -  | (234)  |
| Other, net  | (6)   | (6)  | (1)  |
| <b>Net cash generated by operating activities</b>   | <b>694</b>  | <b>2,095</b>   | <b>5,422</b>   |

(a) Net of dividend received.

The accompanying notes are an integral part of these Financial Statements.

**Consolidated Statements of Cash Flows (cont'd)**  
**For the Periods Ended 30 September 2009**  
**Reported amounts**

|  | For the three<br>months ended<br>30 September<br>2009 | For the nine<br>months ended<br>30 September<br>2009 | For the year<br>ended<br>31 December<br>2008 |
|--|---|--|--|
|  | Unaudited   | Unaudited  | Audited                                      |
|  | (NIS millions)  |  |  |
| <b>Cash flows generated by activities in assets:</b>                                   |   |  |  |
| Net decrease in deposits with banks for an initial period exceeding three months       | 212   | 177  | 5,380  |
| Acquisition of debentures held to maturity   | (28)  | (46)   | (32)   |
| Proceeds from redemption of debentures held to maturity                                | 29  | 665  | 104  |
| Acquisition of securities available for sale   | (9,818)   | (29,680)   | (46,165)                                     |
| Proceeds from sale of securities available for sale                                    | 4,955   | 10,035   | 5,810  |
| Proceeds from redemption of securities available for sale                              | 1,721   | 7,688  | 41,530                                       |
| Net increase in securities held for trading  | 2,577   | (12)   | (3,241)                                      |
| Net decrease (increase) in credit to the public  | 2,799   | 8,108  | (16,615)                                     |
| Net decrease in credit to governments  | 22  | 90   | 122  |
| Net decrease (increase) in securities borrowed or purchased under agreements to resell | (742)   | (1,622)  | 454  |
| Issue of shares to third party in subsidiary   | -   | -  | 360  |
| Proceeds from sale of investment in companies included on equity basis                 | -   | -  | 29   |
| Acquisition of shares in companies included on equity basis                            | (4)   | (45)   | (13)   |
| Acquisition of buildings and equipment   | (167)   | (578)  | (715)  |
| Proceeds from sale of buildings, net of related taxes                                  | 2   | 40   | 45   |
| Proceeds from realization of assets transferred to Group ownership                     | -   | 41   | 9  |
| Net decrease (increase) in other assets  | (941)   | 3,392  | (5,781)                                      |
| <b>Net cash used for activities in assets</b>  | <b>617</b>  | <b>(1,747)</b>                                       | <b>(18,719)</b>                              |
| <b>Cash flows generated by activities in liabilities and capital</b>                   |   |  |  |
| Net increase (decrease) in:  |   |  |  |
| Deposits of the public   | (3,821)   | 4,650  | 6,738  |
| Deposits from banks  | 2,491   | 1,653  | (2,397)                                      |
| Deposits from governments  | (22)  | (112)  | (367)  |
| Issue of debentures, bonds and subordinated notes                                      | 1,937   | 4,806  | 5,089  |
| Redemption of debentures, bonds and subordinated notes                                 | (40)  | (628)  | (3,701)                                      |
| Increase (decrease) in other liabilities   | 2,763   | (495)  | 4,838  |
| Net increase in securities loaned or sold under agreements to repurchase               | 142   | 767  | 318  |
| Issue of shares to employees   | -   | -  | 614  |
| Dividend paid to shareholders  | -   | -  | (1,684)                                      |
| Repayment of loans to employees for purchase of the Bank's shares                      | -   | 1  | 30   |
| <b>Net cash generated by activities in liabilities and capital</b>                     | <b>3,450</b>  | <b>10,642</b>  | <b>9,478</b>                                 |
| <b>Increase (decrease) in cash</b>   | <b>4,761</b>  | <b>10,990</b>  | <b>(3,819)</b>                               |
| <b>Balance of cash at beginning of period</b>  | <b>37,234</b>   | <b>31,005</b>  | <b>34,824</b>                                |
| <b>Balance of cash at end of period</b>  | <b>41,995</b>   | <b>41,995</b>  | <b>31,005</b>                                |

(a) Reclassified. See also footnote in note 2.



**Consolidated Statements of Cash Flows (cont'd)****For the Periods Ended 30 September 2009****Reported amounts**

Appendix A - Transactions not involving cash flows:

In the period of three months ended 30 September 2009:

- (1) During the period, shares were transferred from credit to the public to the available for sale portfolio, in the amount of NIS 65 million, due to the end of borrowing securities/loaning of securities.
- (2) Transfer during the period of real estate from credit to the public to other assets in the amount of NIS 18 million in respect of loans that were repaid.

In the period of Nine months ended 30 September 2009:

- (1) During the period, shares were transferred from available for sale portfolio to credit to the public, in the amount of NIS 152 million, due to the end of borrowing securities.
- (2) Transfer during the period of real estate from credit to the public to other assets in the amount of NIS 61 million in respect of loans that were repaid.
- (3) During the period fixed assets in the amount of NIS 12 million were bought versus obligation to vendors.

In 2008:

- (1) During the year, shares were transferred from the available for sale portfolio the credit to the public, In the amount of NIS 73 million, due to loaning of securities.
- (2) During the year, a capital note was received in the available for sale portfolio from a customer against credit that was repaid in the amount of NIS 73 million.
- (3) During the year, fixed assets were acquired against liabilities to suppliers, in the amount of NIS 19 million.

The accompanying notes are an integral part of these financial statements.

## Note 1 – Significant Accounting Policies

**A.** The Condensed Consolidated Interim Financial Statements as at 30 September 2009 have been prepared in accordance with accounting principles used in the preparation of interim reports. The accounting principles used in preparing the interim reports are consistent with those used in preparing the audited Financial Statements as at 31 December 2008, and according to a new format for quarterly reports determined in the circular of the Supervisor of Banks of 18 March 2008. These Statements should be read in conjunction with the Annual Financial Statements as at 31 December 2008 and for the year ended on that date, and their accompanying Notes.

### **B. Future Application of Accounting Standards and the Supervisor of Banks' Directives**

#### **1. Accounting Standard No. 29 - "Adoption of International Financial Reporting Standards (IFRS)"**

In July 2006, the Israel Accounting Standards Board published Accounting Standard No. 29 - "Adoption of International Financial Reporting Standards (IFRS)" (the "Standard"). The Standard prescribes that entities that are subject to the Securities Law, 1968, and are obliged to report in accordance with the regulations issued under the said Law, shall prepare their financial statements in accordance with IFRS for the periods commencing from 1 January 2008. This does not apply to banking corporations and credit card companies, the financial statements of which are prepared in accordance with the directives and guidelines of the Supervisor of Banks.

In June 2009, the Supervisor of Banks published a circular on the topic "Reporting of Banking Corporations and Credit Card Companies in Israel in accordance with International Financial Reporting Standards (IFRS)", which determines the expected manner of adoption of IFRS by banking corporations and credit card companies.

Pursuant to the circular, the target date for reporting of banking corporations and credit card companies according to IFRS is:

1. Topics that are not a core part of the banking business – beginning 1 January 2011. From this date onwards, banking corporations and credit card companies will be required to update the accounting treatment of these topics on an ongoing basis, pursuant to the transitional provisions contained in the new International Standards published in this regard, and in accordance with clarifications to be provided by the Supervisor of Banks.
2. Topics that are a core part of the banking business – beginning 1 January 2013, while the Banking Supervision Department intends to make a final decision in this regard during 2011. The final decision will be made while taking into account the timetable laid down in the USA, and the progress made in the convergence process between IFRS and the American standards.

The circular clarifies that following completion of the process of adaptation of the directives to IFRS, the Banking Supervision Department will continue to have the authority to lay down binding clarifications regarding the manner of implementation of the requirements of IFRS, and to determine additional directives where such is required in light of the requirements of regulatory authorities in developed countries, and on topics not dealt with by IFRS. In addition, the Banking Supervision Department retains its authority to determine disclosure and reporting requirements.

Therefore, until the target dates for the adoption of IFRS as detailed above, the financial statements of a banking corporation or credit card company will continue to be prepared in accordance with the directives and guidelines of the Supervisor of Banks. At this stage, no directives have been laid down regarding the transitional provisions to be applied upon adoption of IFRS for the first time.

Two companies included on the equity basis have been implementing the Standard as from January 2008.

## 2. **Accounting Standard No. 23 – “The Accounting Treatment of Transactions between an Entity and its Controlling Shareholder”**

In December 2006, the Israel Accounting Standards Board published Accounting Standard No. 23, “The Accounting Treatment of Transactions between an Entity and its Controlling Shareholder” (“Standard 23”). Standard 23 effectively replaces the main provisions of the Securities (Presentation of Transactions between a Company and its Controlling Shareholder in the Financial Statements) Regulations, 1996, as adopted in the directives dealing with reporting to the public of the Supervisor of Banks. Standard 23 provides that assets (other than an intangible asset with no active market) and liabilities included in a transaction between the entity and its controlling shareholder shall be measured on the date of the transaction at fair value and that the difference between the fair value and the consideration recorded from the transaction shall be included in shareholders’ equity. A debit difference effectively constitutes a dividend and accordingly reduces the retained earnings. A credit difference effectively constitutes an investment by the shareholder and shall therefore be presented under a separate item of shareholders’ equity called “capital reserve from transaction between an entity and its controlling shareholder.”

Standard 23 discusses three issues relating to transactions between an entity and its controlling shareholder, as follows: the transfer of an asset to the entity by the controlling shareholder, or alternatively, the transfer of an asset from the entity to the controlling shareholder; the assumption by the controlling shareholder of all or part of a liability of the entity to a third party, indemnification of the entity by the controlling shareholder in respect of an expense, and the waiving by the controlling shareholder of all or part of the entity’s debt to it; and loans that were granted to the controlling shareholder or loans that were received from the controlling shareholder. Standard 23 also determines the disclosure that is to be made in the financial statements regarding transactions between the entity and its controlling shareholder during the period.

In a letter of the Supervisor of Banks it is indicated that he is re-examining the rules to be applied to banking corporations and to credit card companies with respect to the treatment of transactions between an entity and its controlling shareholder. As at the date of publication of this Report, the Supervisor of Banks has not yet published a final directive regarding the adoption of specific rules on this subject and on the manner of their initial implementation.

## 3. **Measurement and Disclosure of Impaired Debts, Credit Risk and Provisions for Credit Losses**

On 31 December 2007, the Banking Supervision Department published a circular to the banking corporations amending the directives regarding reporting to the public, on the subject of “Measurement and Disclosure of Impaired Debts, Credit Risk and Provision for Credit Losses” and a draft amendment of the said directive was received on 20 August 2009. The directive is based on US accounting standards (FAS 114 and 118), US banking regulatory provisions, and the directives of the SEC dealing with banks. It is also adapted to suit the reports made by banks in the US. The provisions included in the circular constitute a significant change as compared with the existing provisions regarding classification of problem loans and the measurement of provisions for credit losses in respect of such debts.

The main changes included in the directive are:

- a. New categories of problem loans are set out, which are defined as impaired debts, including:
  - credit in respect of which the banking corporation cannot collect the entire amount due, according to the contractual terms of the loan agreement,
  - a problem loan whose terms have been modified within the framework of a restructuring,
  - a loan whose principal or interest has been in arrears for 90 days or more, unless such is well secured and also in the process of collection proceedings,

- a loan in a debitory or current account where the customer's account has been charged with additional excess interest and a special handling commission for a debitory or current account which has deviated from a credit line (as described in section 4(c) of Proper Banking Management Directive No. 325).
  - further, credit which is insufficiently protected by the present established value and the debtor's ability to pay or by the pledged collateral, and which is characterized by a clear possibility that the banking corporation will suffer some loss if the deficiencies are not remedied, is defined as an inferior credit risk.
- b. Banking corporations are required to maintain a provision for credit losses at a level which is sufficient to cover the expected credit losses relating to the banking corporation's credit portfolio, including for off-balance sheet credit risk.

The provisions for credit losses will include:

- A specific provision for credit losses for each debt whose contractual balance is above NIS 1.0 million or more, and any other debt identified for specific consideration by the banking corporation.

The provision will be based on the measurement of the debt's reduced value, based on the present value of the expected cash flows, discounted at the debt's effective interest rate; or where a debt is dependent on collateral or where the seizure of a property is anticipated, based on the fair value of the collateral pledged to secure such credit.

- Group provisions for credit losses – for large groups of relatively small and homogeneous debts, the decrease in value of which is examined on a group basis, and for debts that have been separately examined and found not to be impaired.

Measurement of credit losses will be carried out based on past credit loss rates for each homogeneous group. The determination of the estimates of credit losses is to be documented.

- c. No interest income is to be recorded for impaired debts (not including CPI linkage differentials and exchange rate differentials on the principal.)
- d. A change regarding the requirements for writing off debts:
- Any part of a debt whose collection is dependent on collateral, which exceeds the collateral's fair value and is identified as uncollectible, is to be immediately written off in the accounts.
  - Generally, specific provisions are to be written off after two years.
  - Group provisions for credit losses - debts that are in arrears for over 150 days are to be written off.
- e. The qualitative and quantitative disclosure requirements for financial statements with respect to problem loans have been expanded.
- f. Detailed requirements have been laid down for preparing guidelines to ensure a methodical process for establishing the provisions for credit losses, which are to be consistently applied, for documentation required to support the credit process and for internal controls for the methods and processes that are established.
- g. The directive will be implemented, in accordance with the draft, in the financial statements as from 1 July 2010 (1 January 2010 in the original). The directive will not be implemented retroactively in the

financial statements for previous periods. Transitional adjustments arising from the adoption of the directive as of 1 July 2010 will be included directly in the retained earnings item in shareholders' equity. At the time of the first implementation, the following, *inter alia*, will be required:

- To write off in the accounts, any debt which at that date meets the conditions for being written off in the accounts.
  - To classify as requiring special supervision, inferior or impaired, any debt that meets the conditions for such classification.
  - To cancel all interest income which has accumulated but not been paid for any debt which at that date meets the relevant conditions.
  - To examine the need for adjusting the balance for current taxes and deferred taxes to be received or paid.
- h. Adjustments to the requirements of the directive of the balance of the provision for credit losses to the public in respect of off-balance-sheet credit instruments as of the date of the directive's first application, will be included directly in the "retained earnings" shareholders' equity.

A steering committee has been appointed as part of the Bank's preparations for the implementation of the above directive. The committee's members include representatives of the business divisions, and the accounting and computerization functions. Sub-committees have been set up to deal with the establishment of work methods and with the directive's requirements.

The preparations for the modification of the computer systems have begun, since material changes in the information systems are required in order to carry out the required processes.

As of the date of the publication of this Report, the design of the main component of the computerization process for managing and documenting credit losses has been completed. Preparations have begun for writing work procedures for classification of impaired debts in accordance with the new rules. The training of the employees in the business divisions began during the fourth quarter.

Also, additional draft directives have been published by the Supervisor of Banks regarding the manner of implementation of the requirements for the determination of a group provision for credit losses, the adaptation of the classification requirements for debts in excess in current accounts to the acceptable treatment in the USA, and the adaptation of certain Proper Banking Management Directives to the new directives, as well as the commencement date for the new directive and the related transitional provisions.

The Bank is examining the new draft directives published by the Bank of Israel, and their effect on the Bank's preparations for implementing the above directive.

It is not possible at this stage to estimate the implications of the implementation of the directive and the draft, when they are adopted, on the Bank's future financial results.

4. Pursuant to the Supervisor of Banks' Circular dated 6 September 2009, banking corporations and credit card companies ("Banking Corporations") are required to implement the rules laid down in FAS 166 - Accounting for Transfers of Financial Assets and in FAS 167 – Consolidation of Variable Interest Entities, including the disclosure requirements established therein, from 1 January 2010 and onwards, in accordance with the transitional provisions established in those standards. Generally, these transitional provisions require the following:
  - The implementation of the standard's recognition and measurement requirements regarding transfers of financial assets that are carried out from 1 January 2010 and onwards.

## FINANCIAL STATEMENTS

- The examination, as of 1 January 2010 and onwards, of the question of whether, in accordance with the FAS 167, it is necessary to consolidate entities that were defined pursuant to the old rules as qualified special purpose entities.

In addition, a banking corporation is not required to disclose comparative figures for 2009 with regard to the disclosure requirements that were added for the first time because of the Banking Supervision Department's circular.

The impact of the implementation for the said standards is not expected to be material.

## Note 2 - Securities

### Reported Amounts

| <b>30 September 2009 (Unaudited)</b>     |                               |                   |  |   |                   |
|--|-------------------------------|-------------------|--|---|-------------------|
|  | Amount<br>in balance<br>Sheet | Amortized<br>cost | Unrealized<br>profits from<br>adjustments<br>to fair value | Unrealized<br>losses from<br>adjustments<br>to fair value | Fair<br>Value (a) |
| (NIS millions)                           |                               |                   |  |   |                   |
| <b>1. Debentures held to maturity:</b>   |                               |                   |  |   |                   |
| <b>Debentures and bonds</b>              |                               |                   |  |   |                   |
| Government of Israel                     | 269                           | 269               | 9  | -   | 278               |
| Foreign Governments                      | 550                           | 550               | -  | -   | 550               |
| Other companies                          | 71                            | 71                | -  | (3)   | 68                |
| <b>Total debentures held to maturity</b> | <b>890</b>                    | <b>890</b>        | <b>9</b>   | <b>(3)</b>  | <b>896</b>        |

  

| <b>30 September 2009 (Unaudited)</b>                  |                               |   |  |                  |                   |
|---|-------------------------------|---|--|------------------|-------------------|
|   | Amount<br>in balance<br>Sheet | Amortized<br>cost (in<br>Shares - cost) | Accumulated<br>other comprehensive income<br>Profits | Losses           | Fair<br>Value (a) |
| (NIS millions)  |                               |   |  |                  |                   |
| <b>2. Securities available for sale:</b>              |                               |   |  |                  |                   |
| <b>Debentures and bonds -</b>                         |                               |   |  |                  |                   |
| Government of Israel                                  | 23,508                        | 23,325                                  | 190  | (7)              | 23,508            |
| Foreign Governments                                   | 295                           | 290                                     | 6  | (1)              | 295               |
| Other companies                                       | 20,221                        | 20,726                                  | 329  | (834)            | 20,221            |
|   | 44,024                        | 44,341                                  | 525  | (842)            | 44,024            |
| <b>Shares of other companies and mutual funds (b)</b> | <b>2,373</b>                  | <b>1,687</b>                            | <b>687</b>   | <b>(1)</b>       | <b>2,373</b>      |
| <b>Total securities available for sale</b>            | <b>46,397</b>                 | <b>46,028</b>                           | <b>1,212 (c)</b>                                     | <b>(843) (c)</b> | <b>46,397</b>     |

  

| <b>30 September 2009 (Unaudited)</b>       |                               |  |  |   |                   |
|--|-------------------------------|--|--|---|-------------------|
|  | Amount<br>in balance<br>Sheet | Amortized<br>cost<br>(in shares -<br>cost) | Unrealized<br>profits from<br>adjustments<br>to fair value | Unrealized<br>losses from<br>adjustments<br>to fair value | Fair<br>Value (a) |
| (NIS millions)                             |                               |  |  |   |                   |
| <b>3. Securities held for trading:</b>     |                               |  |  |   |                   |
| <b>Debentures and bonds</b>                |                               |  |  |   |                   |
| Government of Israel                       | 6,304                         | 6,187                                      | 119  | (2)   | 6,304             |
| Foreign Governments                        | 2,327                         | 2,313                                      | 14   | -   | 2,327             |
| Other companies                            | 2,371                         | 2,383                                      | 36   | (48)  | 2,371             |
|  | 11,002                        | 10,883                                     | 169  | (50)  | 11,002            |
| <b>Shares and mutual funds:</b>            |                               |  |  |   |                   |
| Other companies                            | 92                            | 442  | -  | (350)   | 92                |
| <b>Total securities available for sale</b> | <b>11,094</b>                 | <b>11,325</b>                              | <b>169 (d)</b>   | <b>(400) (d)</b>  | <b>11,094</b>     |
| <b>Total securities</b>                    | <b>58,381</b>                 | <b>58,243</b>                              | <b>1,390</b>   | <b>(1,246)</b>  | <b>58,387</b>     |

See footnotes on page 153.

**Note 2 - Securities (Cont'd)**  
**Reported Amounts**

|  | 30 September 2008 (Unaudited)                   |  |  |   |                   |
|--|---|--|--|---|-------------------|
|  | Amount<br>in balance<br>Sheet<br>(NIS millions) | Amortized<br>cost                          | Unrealized<br>profits from<br>adjustments<br>to fair value | Unrealized<br>losses from<br>adjustments<br>to fair value | Fair<br>Value (a) |
| <b>1. Securities available for sale:</b>       |   |  |  |   |                   |
| <b>Debentures and bonds -</b>                  |   |  |  |   |                   |
| Government of Israel                           | 867   | 867  | 13   | -   | 880               |
| Foreign Governments                            | 478   | 478  | -  | (9)   | 469               |
| Other companies (e)                            | 96  | 96   | -  | -   | 96                |
| <b>Total debentures held to maturity</b>       | <b>1,441</b>                                    | <b>1,441</b>                               | <b>13</b>  | <b>(9)</b>  | <b>1,445</b>      |
|  |   |  |  |   |                   |
|  | 30 September 2008 (Unaudited)                   |  |  |   |                   |
|  | Amount<br>in balance<br>Sheet<br>(NIS millions) | Amortized<br>cost (in<br>Shares - cost)    | Accumulated<br>other comprehensive income                  |   | Fair<br>value (a) |
|  |   |  | Profits  | Losses  |                   |
| <b>2. Securities available for sale:</b>       |   |  |  |   |                   |
| <b>Debentures and bonds-</b>                   |   |  |  |   |                   |
| Government of Israel                           | 8,743   | 8,729                                      | 106  | (92)  | 8,743             |
| Foreign Governments                            | 304   | 301  | 3  | -   | 304               |
| Other companies (e)                            | 19,540  | 21,062                                     | 17   | (1,539)   | 19,540            |
|  | 28,587  | 30,092                                     | 126  | (1,631)   | 28,587            |
| <b>Shares and mutual funds</b>                 |   |  |  |   |                   |
| Shares of other companies and mutual funds (b) | 3,635   | 3,392                                      | 406  | (163)   | 3,635             |
| Total securities available for sale            | 32,222  | 33,484                                     | 532 (c)  | (1,794) (c)   | 32,222            |
|  |   |  |  |   |                   |
|  | 30 September 2008 (Unaudited)                   |  |  |   |                   |
|  | Amount<br>in balance<br>Sheet<br>(NIS millions) | Amortized<br>cost<br>(in Shares -<br>cost) | Unrealized<br>profits from<br>adjustments<br>to fair value | Unrealized<br>losses from<br>adjustments<br>to fair value | Fair<br>Value (a) |
| <b>3. Securities held for trading:</b>         |   |  |  |   |                   |
| <b>Debentures and bonds -</b>                  |   |  |  |   |                   |
| Government of Israel                           | 5,472   | 5,475                                      | 13   | (16)  | 5,472             |
| Foreign Governments                            | 141   | 141  | -  | -   | 141               |
| Other companies                                | 1,428   | 1,517                                      | 3  | (92)  | 1,428             |
|  | 7,041   | 7,133                                      | 16   | (108)   | 7,041             |
| <b>Shares and mutual funds:</b>                |   |  |  |   |                   |
| Other companies                                | 862   | 1,326                                      | -  | (464)   | 862               |
| <b>Total securities held for trading</b>       | <b>7,903</b>                                    | <b>8,459</b>                               | <b>16 (d)</b>  | <b>(572) (d)</b>  | <b>7,903</b>      |
| <b>Total securities</b>                        | <b>41,566</b>                                   | <b>43,384</b>                              | <b>561</b>   | <b>(2,375)</b>  | <b>41,570</b>     |

See footnotes on page 153.



## Note 2 – Securities Reported Amounts

|   | 31 December 2008 (Audited)                      |   |  |   |                   |
|---|---|---|--|---|-------------------|
|   | Amount<br>in balance<br>Sheet<br>(NIS millions) | Amortized<br>cost                       | Unrealized<br>profits from<br>adjustments<br>to fair value | Unrealized<br>losses from<br>adjustments<br>to fair value | Fair<br>Value (a) |
| <b>1. Debentures held to maturity:</b>            |   |   |  |   |                   |
| <b>Debentures and bonds -</b>                     |   |   |  |   |                   |
| Government of Israel                              | 880   | 880                                     | 18   | -   | 898               |
| Foreign Governments                               | 558   | 558                                     | 12   | (1)   | 569               |
| Other companies (e)                               | 71  | 71                                      | -  | -   | 71                |
| <b>Total debentures held to maturity</b>          | <b>1,509</b>                                    | <b>1,509</b>                            | <b>30</b>  | <b>(1)</b>  | <b>1,538</b>      |
|   |   |   |  |   |                   |
|   | 31 December 2008 (Audited)                      |   |  |   |                   |
|   | Amount<br>in balance<br>Sheet<br>(NIS millions) | Amortized<br>cost (in<br>Shares - cost) | Accumulated<br>other comprehensive income<br>Profits       | Losses  | Fair<br>value (a) |
| <b>2. Securities available for sale:</b>          |   |   |  |   |                   |
| <b>Debentures and bonds -</b>                     |   |   |  |   |                   |
| Government of Israel                              | 10,063  | 9,629                                   | 457  | (23)  | 10,063            |
| Foreign Governments                               | 336   | 327                                     | 9  | -   | 336               |
| Other companies (e)                               | 18,928  | 20,792                                  | 36   | (1,900)   | 18,928            |
|   | 29,327  | 30,748                                  | 502  | (1,923)   | 29,327            |
| <b>Shares and mutual funds</b>                    |   |   |  |   |                   |
| Shares of other companies and mutual<br>funds (b) | 3,219   | 2,790                                   | 430  | (1)   | 3,219             |
| <b>Total securities available for sale</b>        | <b>32,546</b>                                   | <b>33,538</b>                           | <b>932 (c)</b>   | <b>(1,924) (c)</b>  | <b>32,546</b>     |

See footnotes on page 153.

**Note 2 - Securities (Cont'd)**

|  | 31 December 2008 (Audited)                      |  |  |   |                   |
|--|---|--|--|---|-------------------|
|  | Amount<br>in balance<br>Sheet<br>(NIS millions) | Amortized<br>cost<br>(in Shares -<br>cost) | Unrealized<br>profits from<br>adjustments<br>to fair value | Unrealized<br>losses from<br>adjustments<br>to fair value | Fair<br>Value (a) |
| <b>3. Securities held for trading:</b>   |   |  |  |   |                   |
| <b>Debentures and bonds-</b>             |   |  |  |   |                   |
| Government of Israel                     | 5,554   | 5,465                                      | 117  | (28)  | 5,554             |
| Foreign Governments                      | 3,707   | 3,674                                      | 44   | (11)  | 3,707             |
| Other companies                          | 1,489   | 1,639                                      | 7  | (157)   | 1,489             |
|  | 10,750  | 10,778                                     | 168  | (196)   | 10,750            |
| <b>Shares and mutual funds:</b>          |   |  |  |   |                   |
| Other companies                          | 105   | 457  | -  | (352)   | 105               |
| <b>Total securities held for trading</b> | <b>10,855</b>                                   | <b>11,235</b>                              | <b>168 (d)</b>   | <b>(548) (d)</b>  | <b>10,855</b>     |
| <b>Total securities</b>                  | <b>44,910</b>                                   | <b>46,282</b>                              | <b>1,130</b>   | <b>(2,473)</b>  | <b>44,939</b>     |

- (a) Such quotations do not necessarily reflect the price which will be obtained upon sale of securities in large volumes.
- (b) Including NIS 1,007 million with respect to shares which have no readily available fair value, which are presented at cost (31 December 2008 - NIS 1,263 million and 30 September 2008 - NIS 1,417 million). In accordance with Directives of the Supervisor of Banks from July 2003, credit to a certain customer in the communications sector was classified in the balance sheet as an investment in shares in the available for sale portfolio instead of in loans to the public, and shown with a fair value not exceeding the value of the loan. Also includes holding in Migdal holdings insurance and finance Ltd.
- (c) Regarding securities available for sale, total other income is included in shareholders' equity in the item "adjustments in respect of presentation of securities available for sale according to fair value", except securities intended for hedging for purposes of determining fair value.
- (d) Reported in the profit and loss statement, but not yet realized.
- (e) Reclassified balances of debentures available for sale to debentures held to maturity for a subsidiary abroad. This reclassification reverses an opposite change made by the subsidiary in the past. The effect on the adjustments of fair value is not material.

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

|   | 30 September 2009 (Unaudited)                   |                   |   |                |       |
|---|---|-------------------|---|----------------|-------|
|   | Amount<br>in balance<br>sheet<br>(NIS millions) | Amortized<br>Cost | Accumulated other<br>comprehensive income (loss) *<br>profits | Fair<br>losses | value |
| 1. Additional details of asset-backed securities available for sale |   |                   |   |                |       |
| Mortgage-backed securities (MBS):                                   |   |                   |   |                |       |
| Pass-through securities:  |   |                   |   |                |       |
| Securities guaranteed by GNMA                                       | 1,336   | 1,324             | 14  | (2)            | 1,336 |
| Securities issued by FNMA and FHLMC                                 | 879   | 865               | 19  | (5)            | 879   |
| Total   | 2,215   | 2,189             | 33  | (7)            | 2,215 |
| Other Mortgage-backed securities (including CMO and STRIPPED MBS)   |   |                   |   |                |       |
| Securities issued by FNMA, FHLMC, or GNMA, or                       |   |                   |   |                |       |
| guaranteed by these entities  | 2,346   | 2,348             | 20  | (22)           | 2,346 |
| Other Mortgage-backed securities                                    | 30  | 62                | -   | (32)           | 30    |
| Total   | 2,376   | 2,410             | 20  | (54)           | 2,376 |
| Asset-backed securities (ABS):                                      |   |                   |   |                |       |
| Lines of credit for any purpose secured by dwelling                 | 3   | 6                 | -   | (3)            | 3     |
| Credit for purchase of vehicle                                      | 15  | 15                | -   | -              | 15    |
| Other credit to private persons                                     | 7   | 7                 | -   | -              | 7     |
| CLO   | 857   | 761               | 153   | (57)           | 857   |
| CDO   | 32  | 25                | 7   | -              | 32    |
| SCDO  | 121   | 99                | 26  | (4)            | 121   |
| Others  | 30  | 31                | -   | (1)            | 30    |
| Total   | 1,065   | 944               | 186   | (65)           | 1,065 |
| Total Asset-backed securities available for sale                    | 5,656   | 5,543             | 239   | (126)          | 5,656 |

\* Amounts that raised up to the capital fund as part of adjustments of securities available for sale at fair value.

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

| <b>30 September 2009 (Unaudited)</b>   |                               |                   |   |  |               |
|--|-------------------------------|-------------------|---|--|---------------|
|  | Amount<br>In balance<br>sheet | Amortized<br>Cost | Unrealized<br>profits from<br>adjustments<br>to fair value* | Unrealized<br>losses from<br>adjustments<br>to fair value* | Fair<br>value |
| (NIS millions)   |                               |                   |   |  |               |
| <b>2. Additional details of Asset-backed securities held for trading Mortgage-backed securities (MBS):</b> |                               |                   |   |  |               |
| <b>Pass-through securities:</b>  |                               |                   |   |  |               |
| Securities issued by FNMA and FHLMC  | 1                             | 1                 | -   | -  | 1             |
| <b>Total</b>   | <b>1</b>                      | <b>1</b>          | <b>-</b>  | <b>-</b>   | <b>1</b>      |
| <b>Other Mortgage-backed securities (including CMO and STRIPPED MBS)</b>                                   |                               |                   |   |  |               |
| Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities                                 |                               |                   |   |  |               |
|  | 40                            | 39                | 1   | -  | 40            |
| Other Mortgage-backed securities   | 64                            | 83                | -   | (19)   | 64            |
| <b>Total</b>   | <b>104</b>                    | <b>122</b>        | <b>1</b>  | <b>(19)</b>  | <b>104</b>    |
| <b>Asset-backed securities (ABS):</b>  |                               |                   |   |  |               |
| Lines of credit for any purpose secured by dwelling  | 9                             | 13                | -   | (4)  | 9             |
| Credit for purchase of vehicle   | 1                             | 1                 | -   | -  | 1             |
| Credit not to private persons  | 2                             | 5                 | -   | (3)  | 2             |
| CDO  | 2                             | 4                 | -   | (2)  | 2             |
| Others   | 2                             | 5                 | -   | (3)  | 2             |
| <b>Total</b>   | <b>16</b>                     | <b>28</b>         | <b>-</b>  | <b>(12)</b>  | <b>16</b>     |
| <b>Total Asset-backed securities held for trading</b>  | <b>121</b>                    | <b>151</b>        | <b>1</b>  | <b>(31)</b>  | <b>121</b>    |

\* These amounts reported in the profit and loss statement.

3. The redemption portfolio includes a security issued by the FHLMC in the amount of about NIS 8 million.

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

|   | 30 September 2008 (Unaudited) |           |                               |        |       |
|---|-------------------------------|-----------|-------------------------------|--------|-------|
|   | Amount                        |           | Accumulated other             |        |       |
|   | in balance                    | Amortized | comprehensive income (loss) * |        | Fair  |
|   | sheet                         | Cost      | profits                       | losses | value |
|   | (NIS millions)                |           |                               |        |       |
| <b>1. Additional details of Asset-backed securities</b> |                               |           |                               |        |       |
| <b>available for sale Mortgage-backed securities</b>    |                               |           |                               |        |       |
| <b>Pass-through securities:</b>                         |                               |           |                               |        |       |
| Securities guaranteed by GNMA                           | 82                            | 82        | -                             | -      | 82    |
| Securities issued by FNMA and FHLMC                     | 1,133                         | 1,148     | 3                             | (18)   | 1,133 |
| Securities issued by others                             | 10                            | 10        | -                             | -      | 10    |
| <b>Total</b>  | 1,225                         | 1,240     | 3                             | (18)   | 1,225 |
| <b>Other Mortgage-backed securities</b>                 |                               |           |                               |        |       |
| <b>(including CMO and STRIPPED MBS)</b>                 |                               |           |                               |        |       |
| Securities issued by FNMA, FHLMC, or GNMA, or           |                               |           |                               |        |       |
| guaranteed by these entities                            | 1,753                         | 1,776     | 5                             | (28)   | 1,753 |
| Other Mortgage-backed securities                        | 63                            | 86        | -                             | (23)   | 63    |
| <b>Total</b>  | 1,816                         | 1,862     | 5                             | (51)   | 1,816 |
| <b>Asset-backed securities (ABS):</b>                   |                               |           |                               |        |       |
| Lines of credit for any purpose secured by dwelling     | 5                             | 7         | -                             | (2)    | 5     |
| Credit for purchase of vehicle                          | 30                            | 32        | -                             | (2)    | 30    |
| Other credit to private persons                         | 34                            | 34        | -                             | -      | 34    |
| CLO   | 905                           | 1,135     | -                             | (230)  | 905   |
| CDO   | 26                            | 28        | -                             | (2)    | 26    |
| SCDO  | 159                           | 160       | -                             | (1)    | 159   |
| Others  | 1                             | 2         | -                             | (1)    | 1     |
| <b>Total</b>  | 1,160                         | 1,398     | -                             | (238)  | 1,160 |
| <b>Total Asset-backed securities available for sale</b> | 4,201                         | 4,500     | 8                             | (307)  | 4,201 |

\* Amounts that raised up to the capital fund as part of adjustments of securities available for sale at fair value.

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

|  | 30 September 2008 (Unaudited) |           |                |                |       |
|--|-------------------------------|-----------|----------------|----------------|-------|
|  | Amount                        |           | Unrealized     | Unrealized     |       |
|  | In balance                    | Amortized | profits from   | losses from    | Fair  |
|  | sheet                         | Cost      | adjustments    | adjustments    | value |
|  |                               |           | to fair value* | to fair value* | value |
|  | (NIS millions)                |           |                |                |       |
| <b>2. Additional details of Asset-backed securities held for trading Mortgage-backed securities (MBS):</b> |                               |           |                |                |       |
| <b>Pass-through securities:</b>  |                               |           |                |                |       |
| Securities issued by FNMA and FHLMC  | 5                             | 5         | -              | -              | 5     |
| <b>Total</b>   | 5                             | 5         | -              | -              | 5     |
| <b>Other Mortgage-backed securities (including CMO and STRIPPED MBS)</b>                                   |                               |           |                |                |       |
| Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities                                 | 35                            | 35        | -              | -              | 35    |
| Other Mortgage-backed securities   | 124                           | 145       | -              | (21)           | 124   |
| <b>Total</b>   | 159                           | 180       | -              | (21)           | 159   |
| <b>Asset-backed securities (ABS):</b>  |                               |           |                |                |       |
| Credit card debtors  | 3                             | 3         | -              | -              | 3     |
| Lines of credit for any purpose secured by dwelling  | 19                            | 21        | -              | (2)            | 19    |
| Credit for purchase of vehicle   | 8                             | 8         | -              | -              | 8     |
| Credit not to private persons  | 10                            | 10        | -              | -              | 10    |
| CDO  | 4                             | 7         | -              | (3)            | 4     |
| Others   | 2                             | 2         | -              | -              | 2     |
| <b>Total</b>   | 46                            | 51        | -              | (5)            | 46    |
| <b>Total Asset-backed securities held for trading</b>  | 210                           | 236       | -              | (26)           | 210   |

\* Amounts that reported in the profit and loss statement.

3. The redemption portfolio includes a security issued by the FHLMC in the amount of about NIS 7 million.

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

|   | 31 December 2008 (Audited) |              |                                      |              |              |
|---|----------------------------|--------------|--------------------------------------|--------------|--------------|
|   | Amount                     |              | Accumulated other                    |              |              |
|   | in balance                 | Amortized    | <u>comprehensive income (loss) *</u> |              | Fair         |
|   | sheet                      | Cost         | profits                              | losses       | value        |
|   | (NIS millions)             |              |                                      |              |              |
| <b>1. Additional details of Asset-backed securities</b>     |                            |              |                                      |              |              |
| <b>available for sale Mortgage-backed securities (MBS):</b> |                            |              |                                      |              |              |
| <b>Pass-through securities:</b>                             |                            |              |                                      |              |              |
| Securities guaranteed by GNMA                               | 84                         | 87           | -                                    | (3)          | 84           |
| Securities issued by FNMA and FHLMC                         | 1,211                      | 1,226        | 10                                   | (25)         | 1,211        |
| Securities issued by others                                 | 10                         | 10           | -                                    | -            | 10           |
| <b>Total</b>  | <b>1,305</b>               | <b>1,323</b> | <b>10</b>                            | <b>(28)</b>  | <b>1,305</b> |
| <b>Other Mortgage-backed securities</b>                     |                            |              |                                      |              |              |
| <b>(including CMO and STRIPPED MBS)</b>                     |                            |              |                                      |              |              |
| Securities issued by FNMA, FHLMC, or GNMA, or               |                            |              |                                      |              |              |
| guaranteed by these entities                                | 1,939                      | 1,987        | 5                                    | (53)         | 1,939        |
| Other Mortgage-backed securities                            | 64                         | 67           | -                                    | (3)          | 64           |
| <b>Total</b>  | <b>2,003</b>               | <b>2,054</b> | <b>5</b>                             | <b>(56)</b>  | <b>2,003</b> |
| <b>Asset-backed securities (ABS):</b>                       |                            |              |                                      |              |              |
| Lines of credit for any purpose secured by dwelling         | 6                          | 8            | -                                    | (2)          | 6            |
| Credit for purchase of vehicle                              | 24                         | 27           | -                                    | (3)          | 24           |
| Other credit to private persons                             | 10                         | 10           | -                                    | -            | 10           |
| CLO debentures  | 690                        | 790          | -                                    | (100)        | 690          |
| CDO debentures  | 26                         | 27           | -                                    | (1)          | 26           |
| SCDO debentures   | 112                        | 122          | -                                    | (10)         | 112          |
| others  | 35                         | 36           | -                                    | (1)          | 35           |
| <b>Total</b>  | <b>903</b>                 | <b>1,020</b> | <b>-</b>                             | <b>(117)</b> | <b>903</b>   |
| <b>Total Asset-backed securities available for sale</b>     | <b>4,211</b>               | <b>4,397</b> | <b>15</b>                            | <b>(201)</b> | <b>4,211</b> |

\* Amounts that raised up to the capital fund as part of adjustments of securities available for sale at fair value.

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

| 31 December 2008 (Audited)   |            |            |               |                |            |
|--|------------|------------|---------------|----------------|------------|
|  | Amount     | Amortized  | Unrealized    | Unrealized     |            |
|  | In balance | Cost       | profits from  | losses from    | Fair       |
|  | sheet      |            | adjustments   | adjustments    | value      |
|  |            |            | to fair value | to fair value* | value      |
| (NIS millions)   |            |            |               |                |            |
| <b>2. Additional details of Asset-backed securities held for trading Mortgage-backed securities (MBS):</b> |            |            |               |                |            |
| <b>Pass-through securities:</b>  |            |            |               |                |            |
| Securities issued by FNMA and FHLMC  | 3          | 3          | -             | -              | 3          |
| <b>Total</b>   | <b>3</b>   | <b>3</b>   | <b>-</b>      | <b>-</b>       | <b>3</b>   |
| <b>Other Mortgage-backed securities (including CMO and STRIPPED MBS)</b>                                   |            |            |               |                |            |
| Securities issued by FNMA, FHLMC, or GNMA, or guaranteed by these entities                                 | 55         | 54         | 1             | -              | 55         |
| Other Mortgage-backed securities   | 111        | 150        | -             | (39)           | 111        |
| <b>Total</b>   | <b>166</b> | <b>204</b> | <b>1</b>      | <b>(39)</b>    | <b>166</b> |
| <b>Asset-backed securities (ABS):</b>  |            |            |               |                |            |
| Credit card debtors  | 16         | 22         | -             | (6)            | 16         |
| Lines of credit for any purpose secured by dwelling  | 6          | 6          | -             | -              | 6          |
| Credit not to private persons  | 10         | 12         | -             | (2)            | 10         |
| CDO debentures   | 3          | 7          | -             | (4)            | 3          |
| Others   | 3          | 3          | -             | -              | 3          |
| <b>Total</b>   | <b>38</b>  | <b>50</b>  | <b>-</b>      | <b>(12)</b>    | <b>38</b>  |
| <b>Total Asset-backed securities held for trading</b>  | <b>207</b> | <b>257</b> | <b>1</b>      | <b>(51)</b>    | <b>207</b> |

\* Amounts that reported in the profit and loss statement.

3. The redemption portfolio includes a security issued by the FHLMC at fair value in the amount of about NIS 8 million.



**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

| <b>30 September 2009 (Unaudited)</b>   |                     |       |                    |       |               |       |
|--|---------------------|-------|--------------------|-------|---------------|-------|
|  | Less than 12 months |       | More than 12 month |       | Total         |       |
|  | Unrealized          |       | Unrealized         |       | Unrealized    |       |
|  | losses from         |       | losses from        |       | losses from   |       |
| Fair   | adjustment          | Fair  | adjustment         | Fair  | adjustments   |       |
| Value  | to fair             | Value | to fair            | Value | to fair value |       |
| (NIS millions)   |                     |       |                    |       |               |       |
| <b>Additional details of asset-backed securities available for sale which include unrealized losses from adjustments to fair value</b> |                     |       |                    |       |               |       |
| Pass-through (MBS)   | 173                 | (2)   | 192                | (5)   | 365           | (7)   |
| Other Mortgage-Backed Securities<br>(including REMIC, CMO and STRIPPED MBS)  | 142                 | (28)  | 869                | (26)  | 1,011         | (54)  |
| Asset-backed securities (ABS)  | 32                  | -     | 513                | (65)  | 545           | (65)  |
| Total  | 347                 | (30)  | 1,574              | (96)  | 1,921         | (126) |

  

| <b>30 September 2008 (Unaudited)</b>   |                     |       |                    |       |               |       |
|--|---------------------|-------|--------------------|-------|---------------|-------|
|  | Less than 12 months |       | More than 12 month |       | Total         |       |
|  | Unrealized          |       | Unrealized         |       | Unrealized    |       |
|  | losses from         |       | losses from        |       | losses from   |       |
| Fair   | adjustment          | Fair  | adjustment         | Fair  | adjustments   |       |
| Value  | to fair             | Value | to fair            | Value | to fair value |       |
| (NIS millions)   |                     |       |                    |       |               |       |
| <b>Additional details of asset-backed securities available for sale which include unrealized losses from adjustments to fair value</b> |                     |       |                    |       |               |       |
| Pass-through (MBS)   | 394                 | (5)   | 477                | (13)  | 871           | (18)  |
| Other Mortgage-Backed Securities<br>(including REMIC, CMO and STRIPPED MBS)  | 635                 | (28)  | 754                | (23)  | 1,389         | (51)  |
| Asset-backed securities (ABS)  | 518                 | (115) | 535                | (123) | 1,053         | (238) |
| Total  | 1,547               | (148) | 1,766              | (159) | 3,313         | (307) |

**Note 2 - Securities (Cont'd)**  
**Of which: Asset-backed securities**  
**Reported amounts**

| 31 December 2008 (Audited)   |                     |   |                    |   |              |  |
|--|---------------------|---|--------------------|---|--------------|--|
|  | Less than 12 months |   | More than 12 month |   | Total        |  |
|  | Fair Value          | Unrealized losses from adjustment to fair | Fair Value         | Unrealized losses from adjustment to fair | Fair Value   | Unrealized losses from adjustments to fair value |
| (NIS millions)   |                     |   |                    |   |              |  |
| <b>Additional details of asset-backed securities available for sale which include unrealized losses from adjustments to fair value</b> |                     |   |                    |   |              |  |
| Pass-through (MBS)   | 321                 | (8)                                       | 425                | (20)                                      | 746          | (28)   |
| Other Mortgage-Backed Securities<br>(including REMIC, CMO and STRIPPED MBS)  | 246                 | (4)                                       | 1,171              | (52)                                      | 1,417        | (56)   |
| Asset-backed securities (ABS)  | 119                 | (14)                                      | 398                | (103)                                     | 517          | (117)  |
| <b>Total</b>   | <b>686</b>          | <b>(26)</b>                               | <b>1,994</b>       | <b>(175)</b>                              | <b>2,680</b> | <b>(201)</b>                                     |

**Note 3 - Provision for Doubtful Debts**  
**Reported amounts (Unaudited)**

|   | <b>For the three months ended 30 September 2009 (unaudited)</b>    |                                     |                                |               |
|---|--|-------------------------------------|--------------------------------|---------------|
|   | Specific<br>Provision<br>According to<br>Specific<br>Provision (a) | Specific<br>depth of<br>arrears (a) | Supplementary<br>Provision (b) | Total         |
|   | (NIS millions)   |                                     |                                |               |
| Balance of the provision at the beginning of the period               | <b>8,661</b>   | <b>638</b>                          | <b>922</b>                     | <b>10,221</b> |
| Provisions during the period  | <b>667</b>   | <b>43</b>                           | <b>(3)</b>                     | <b>707</b>    |
| Decrease in provisions  | <b>(204)</b>   | <b>(42)</b>                         | <b>(15)</b>                    | <b>(261)</b>  |
| Collection of past years' write-offs                                  | <b>(3)</b>   | <b>-</b>                            | <b>-</b>                       | <b>(3)</b>    |
| Net amount charged to statement of profit and loss                    | <b>460</b>   | <b>1</b>                            | <b>(18)</b>                    | <b>443</b>    |
| Net Write-offs (c)  | <b>(129)</b>   | <b>(24)</b>                         | <b>-</b>                       | <b>(153)</b>  |
| Balance of provision at end of the period                             | <b>8,992</b>   | <b>615</b>                          | <b>904</b>                     | <b>10,511</b> |
| Including balance of provision not deducted from credit to the public | <b>133</b>   | <b>-</b>                            | <b>126</b>                     | <b>259</b>    |

|   | <b>For the three months ended 30 September 2008 (unaudited)</b>    |                                     |                                |       |
|---|--|-------------------------------------|--------------------------------|-------|
|   | Specific<br>Provision<br>According to<br>Specific<br>Provision (a) | Specific<br>depth of<br>arrears (a) | Supplementary<br>Provision (b) | Total |
|   | (NIS millions)   |                                     |                                |       |
| Balance of the provision at the beginning of the period               | 7,479  | 721                                 | 855                            | 9,055 |
| Provisions during the period  | 628  | 84                                  | 20                             | 732   |
| Decrease in provisions  | (144)  | (60)                                | (25)                           | (229) |
| Collection of past years' write-offs                                  | (8)  | -                                   | -                              | (8)   |
| Net amount charged to statement of profit and loss (c)                | 476  | 24                                  | (5)                            | 495   |
| Net Write-offs  | (340)  | (31)                                | -                              | (371) |
| Balance of provision at end of the period                             | 7,615  | 714                                 | 850                            | 9,179 |
| Including balance of provision not deducted from credit to the public | 269  | -                                   | 120                            | 389   |

- (a) Not including provision for interest in respect of the period after the loans were determined to be doubtful. With respect to loans in arrears for which a provision was established to the extent of the arrears, no accrual for interest was recorded thereon.
- (b) Including the general and special provision for doubtful debts.
- (c) After deducting collection of debts written off in previous years.

**Note 3 - Provision for Doubtful Debts (cont'd)****Reported amounts (Unaudited)**

|   | For Nine months ended 30 September 2009                            |  |                                |        |
|---|--|--|--------------------------------|--------|
|   | Specific<br>Provision<br>According to<br>Specific<br>Provision (a) | Specific<br>Provision<br>According to<br>depth of<br>arrears (a) | Supplementary<br>Provision (b) | Total  |
|   | (NIS millions)   |  |                                |        |
| Balance of the provision at the beginning of the period               | 8,246  | 675  | 948                            | 9,869  |
| Provisions during the period  | 1,728  | 148  | 39                             | 1,915  |
| Decrease in provisions  | (537)  | (149)  | (83)                           | (769)  |
| Collection of past years' write-offs                                  | (10)   | -  | -                              | (10)   |
| Net amount charged to statement of profit and loss (c)                | 1,181  | (1)  | (44)                           | 1,136  |
| Net Write-offs  | (435)  | (59)   | -                              | (494)  |
| Balance of provision at end of the period                             | 8,992  | 615  | 904                            | 10,511 |
| Including balance of provision not deducted from credit to the public | 133  | -  | 126                            | 259    |

  

|   | For the three months ended 30 September 2008                       |  |                                |       |
|---|--|--|--------------------------------|-------|
|   | Specific<br>Provision<br>According to<br>Specific<br>Provision (a) | Specific<br>Provision<br>According to<br>depth of<br>arrears (a) | Supplementary<br>Provision (b) | Total |
|   | (NIS millions)   |  |                                |       |
| Balance of the provision at the beginning of the period               | 7,250  | 688  | 875                            | 8,813 |
| Provisions during the period  | 1,442  | 247  | 11                             | 1,700 |
| Decrease in provisions  | (427)  | (157)  | (36)                           | (620) |
| Collection of past years' write-offs                                  | (25)   | -  | -                              | (25)  |
| Net amount charged to statement of profit and loss (c)                | 990  | 90   | (25)                           | 1,055 |
| Net Write-offs  | (625)  | (64)   | -                              | (689) |
| Balance of provision at end of the period                             | 7,615  | 714  | 850                            | 9,179 |
| Including balance of provision not deducted from credit to the public | 269  | -  | 120                            | 389   |

- (a) Not including provision for interest in respect of the period after the loans were determined to be doubtful. With respect to loans in arrears for which a provision was established to the extent of the arrears, no accrual for interest was recorded thereon.
- (b) Including the general and special provision for doubtful debts.
- (c) After deducting collection of debts written off in previous years.

**Note 3 - Provision for Doubtful Debts (cont'd)****Details on housing loans and the method of calculating the specific provision -  
Reported amounts (Unaudited)**

| <b>30 September 2009 (unaudited)</b>   |                          |                                  |                                       |   |       |       |
|--|--------------------------|----------------------------------|---------------------------------------|---|-------|-------|
|  | Credit<br>(NIS millions) | Problematic debts                |                                       |   |       |       |
|  |                          | Balance<br>sheet debt<br>balance | Including<br>amount in<br>arrears (c) | Specific provision                      |       |       |
|  |                          |                                  |                                       | According<br>to depth of<br>arrears (d) | Other | Total |
|  |                          |                                  |                                       |   |       |       |
| Housing loans that require<br>calculating the provision<br>according to depth of arrears | 29,088                   | 558                              | 194                                   | 436                                     | -     | 436   |
| "Large" loans (a)  | 8,314                    | 120                              | 145                                   | 138                                     | -     | 138   |
| Other loans (b)  | 7,364                    | 191                              | 24                                    | 41                                      | 6     | 47    |
| Balance of provision at end of the period  | 44,766                   | 869                              | 363                                   | 615                                     | 6     | 621   |

| <b>30 September 2008 (unaudited)</b>   |                          |                                  |                                       |   |       |       |
|--|--------------------------|----------------------------------|---------------------------------------|---|-------|-------|
|  | Credit<br>(NIS millions) | Problematic debts                |                                       |   |       |       |
|  |                          | Balance<br>sheet debt<br>balance | Including<br>amount in<br>arrears (c) | Specific provision                      |       |       |
|  |                          |                                  |                                       | According<br>to depth of<br>arrears (d) | Other | Total |
|  |                          |                                  |                                       |   |       |       |
| Housing loans that require<br>calculating the provision<br>according to depth of arrears | 28,241                   | 638                              | 234                                   | 494                                     | -     | 494   |
| "Large" loans (a)  | 6,128                    | 123                              | 209                                   | 171                                     | -     | 171   |
| Other loans (b)  | 6,920                    | 230                              | 27                                    | 49                                      | 7     | 56    |
| Balance of provision at end of the period  | 41,289                   | 991                              | 470                                   | 714                                     | 7     | 721   |

- (a) Housing loans the balance of each is higher than NIS 871 thousand (30 September 2008 - NIS 845 thousand), including loans for purchase and loans for any purpose that are secured by a mortgage.
- (b) Loans for any purpose secured by mortgage, the balance of each is lower than NIS 871 thousand (30 September 2008 - NIS 845 thousand).
- (c) Including interest on the amount in arrears.
- (d) Including balance of specific provision in excess of amount according to depth of arrears in the amount of NIS 106 million (30 September 2008 - NIS 143 million).

**Note 4 - Shareholders' Equity and Capital Adequacy**

Calculated pursuant to Directives Nos. 311 and 341 issued by the Supervisor of Banks regarding "minimum capital ratio" and "allocation of capital in respect of exposure to market risks"

**Reported amounts**

|  | <b>30 September 2009</b> | 30 September 2008 | 31 December 2008 |
|--|--------------------------|-------------------|------------------|
|  | (Unaudited)              |                   | (Audited)        |
|  | (NIS millions)           |                   |                  |
| <b>1. Bank's capital for purposes of calculating the capital ratio</b> |                          |                   |                  |
| Tier I capital   | <b>20,868</b>            | 20,250            | 19,307           |
| Total capital  | <b>35,168</b>            | 31,182 (b)        | 29,765 (b)       |

|                                      | 30 September 2009 |  | 30 September 2008 |  | 31 December 2008 |  |
|--------------------------------------|-------------------|--|-------------------|--|------------------|--|
|                                      | (Unaudited)       |  | (Unaudited)       |  | (Audited)        |  |
|                                      | Balances*         | Weighted average balances of credit risk | Balances*         | Weighted average balances of credit risk | Balances*        | Weighted average balances of credit risk |
|                                      | (NIS millions)    |  |                   |  |                  |  |
| 2. Weighted average balances of risk |                   |  |                   |  |                  |  |
| Credit risk:                         |                   |  |                   |  |                  |  |
| Assets                               | 323,963           | 204,301                                  | 294,144           | 213,524                                  | 311,125          | 217,747                                  |
| Off-balance sheet instruments        | 53,699            | 35,070                                   | 51,635            | 35,204                                   | 50,883 (a)       | 33,743 (a)                               |
| Total credit risk assets             | 377,662           | 239,371                                  | 345,779           | 248,728                                  | 362,008          | 251,490                                  |
| Market risk                          | -                 | 9,391                                    | -                 | 6,913                                    | -                | 5,476                                    |
| Total risk assets                    | 377,662           | 248,762                                  | 345,779           | 255,641                                  | 362,008          | 256,966                                  |

\* Assets - balance sheet balances, off-balance sheet instruments - stated value weighted on the basis of credit conversion factors.

**Note 4 - Shareholders' Equity and Capital Adequacy (cont'd)**

Calculated pursuant to Directives Nos. 311 and 341 issued by the Supervisor of Banks regarding "minimum capital ratio" and "allocation of capital in respect of exposure to market risks"

**Reported amounts**

|   | <b>30 September 2009</b> | 30 September 2008 | 31 December 2008 |
|---|--------------------------|-------------------|------------------|
|   |                          | (Unaudited)       | (Audited)        |
|   | (%)                      |                   |                  |
| <b>3. Ratio of capital to risk assets</b>   |                          |                   |                  |
| The ratio of tier I capital to risk assets  | <b>8.39</b>              | 7.92              | 7.51             |
| The ratio of total capital to risk assets   | <b>14.14</b>             | 12.20 (b)         | 11.58 (b)        |
| Ratio of total minimum capital to risk assets required by the Supervisor of Banks | <b>9.00</b>              | 9.00              | 9.00             |

**Capital adequacy in principal subsidiaries****Bank Leumi Mortgage Bank Ltd.**

|   |             |      |      |
|---|-------------|------|------|
| The ratio of tier I capital to risk assets  | <b>6.55</b> | 6.31 | 6.15 |
| The ratio of total capital to risk assets   | <b>9.84</b> | 9.48 | 9.24 |
| Ratio of total minimum capital to risk assets required by the Supervisor of Banks | <b>9.00</b> | 9.00 | 9.00 |

**Arab-Israel Bank Ltd.**

|   |              |       |       |
|---|--------------|-------|-------|
| The ratio of tier I capital to risk assets  | <b>15.70</b> | 16.49 | 13.41 |
| The ratio of total capital to risk assets   | <b>20.02</b> | 16.83 | 17.84 |
| Ratio of total minimum capital to risk assets required by the Supervisor of Banks | <b>9.00</b>  | 9.00  | 9.00  |

**Bank Leumi USA**

|   |              |       |       |
|---|--------------|-------|-------|
| The ratio of tier I capital to risk assets                                      | <b>10.51</b> | 8.69  | 9.31  |
| The ratio of total capital to risk assets                                       | <b>13.72</b> | 11.71 | 12.40 |
| Ratio of total minimum capital to risk assets required by the local Authorities | <b>10.00</b> | 10.00 | 10.00 |

(a) Restated.

(b) Reclassified as a result of a change in allocation of Tier 1 and Tier 2 capital against market risk exposure like the allocation of capital against credit risk and this is as a result of a clarification from the Bank of Israel.

**Note 5 - Assets and Liabilities Classified According to Linkage Basis  
as at 30 September 2009 (Unaudited)  
Reported amounts**

|   | Israeli currency           |                      | Foreign currency (a) |         |                        |                       |         |
|---|----------------------------|----------------------|----------------------|---------|------------------------|-----------------------|---------|
|   | Unlinked<br>(NIS millions) | Linked to the<br>CPI | In U.S.<br>dollars   | In Euro | Non-                   |                       |         |
|   |                            |                      |                      |         | In other<br>currencies | monetary<br>items (c) | Total   |
|   |                            |                      |                      |         |                        |                       |         |
| <b>Assets</b>   |                            |                      |                      |         |                        |                       |         |
| Cash and deposits with banks securities                                       | 28,455                     | 454                  | 7,969                | 2,940   | 4,110                  | 6                     | 43,934  |
| Securities  | 19,821                     | 9,294                | 15,184               | 10,522  | 1,095                  | 2,465                 | 58,381  |
| Securities borrowed or purchased<br>under agreement to resell                 | 1,823                      | -                    | -                    | -       | -                      | -                     | 1,823   |
| Credit to the public (b)  | 104,494                    | 49,849               | 32,294               | 7,231   | 10,090                 | 13                    | 203,971 |
| Credit to governments   | -                          | 257                  | 173                  | -       | -                      | -                     | 430     |
| Investments in affiliated companies   | 8                          | -                    | -                    | -       | -                      | 1,900                 | 1,908   |
| Buildings and equipment   | -                          | -                    | -                    | -       | -                      | 3,544                 | 3,544   |
| Other assets  | 3,866                      | 150                  | 2,434                | 587     | 1,865                  | 737                   | 9,639   |
| Total assets  | 158,467                    | 60,004               | 58,054               | 21,280  | 17,160                 | 8,665                 | 323,630 |
| <b>Liabilities</b>  |                            |                      |                      |         |                        |                       |         |
| Deposits of the public  | 116,166                    | 27,557               | 71,671               | 24,152  | 9,836                  | 51                    | 249,433 |
| Deposits from banks   | 3,633                      | 441                  | 563                  | 395     | 363                    | -                     | 5,395   |
| Deposits from governments   | 42                         | 496                  | 169                  | 12      | -                      | -                     | 719     |
| Securities loaned or sold under<br>agreement to repurchase                    | 1,260                      | -                    | 56                   | -       | -                      | -                     | 1,316   |
| Debentures, bonds and subordinated notes                                      | 3,186                      | 20,458               | 1,827                | -       | -                      | -                     | 25,471  |
| Other liabilities   | 10,016                     | 4,003                | 2,052                | 860     | 2,286                  | 738                   | 19,955  |
| Total liabilities   | 134,303                    | 52,955               | 76,338               | 25,419  | 12,485                 | 789                   | 302,289 |
| Difference  | 24,164                     | 7,049                | (18,284)             | (4,139) | 4,675                  | 7,876                 | 21,341  |
| <b>Effect of derivative instruments<br/>that are not hedging derivatives:</b> |                            |                      |                      |         |                        |                       |         |
| Derivative instruments (excluding options)                                    | (4,256)                    | (8,113)              | 14,037               | 4,416   | (6,084)                | -                     | -       |
| Options in the money, net<br>(in terms of underlying asset)                   | (795)                      | (19)                 | 1,119                | (305)   | -                      | -                     | -       |
| Options out of the money, net<br>(in terms of underlying asset)               | (912)                      | -                    | 561                  | 21      | 330                    | -                     | -       |
| Total   | 18,201                     | (1,083)              | (2,567)              | (7)     | (1,079)                | 7,876                 | 21,341  |
| <b>Effect of derivative instruments<br/>that are not hedging derivatives:</b> |                            |                      |                      |         |                        |                       |         |
| Options in the money, net<br>(discounted par value)                           | (1,183)                    | (32)                 | 1,573                | (345)   | (13)                   | -                     | -       |
| Options out of the money, net<br>(discounted par value)                       | (3,061)                    | (7)                  | 2,401                | 136     | 531                    | -                     | -       |

(a) Including linked to foreign currency.

(b) The general and supplementary provisions for doubtful debts have been deducted proportionately from the different linkage bases.

(c) Including derivative instruments that their basis is applicable for a non-monetary item.



**Note 5 - Assets and Liabilities Classified According to Linkage Basis (cont'd)**  
**as at 30 September 2008 (Unaudited)**  
**Reported amounts**

|   | Israeli currency           |                      | Foreign currency (a) |         |                        |                       |         |
|---|----------------------------|----------------------|----------------------|---------|------------------------|-----------------------|---------|
|   | Unlinked<br>(NIS millions) | Linked to the<br>CPI | In U.S.<br>dollars   | In Euro | In other<br>currencies | Non-                  | Total   |
|   |                            |                      |                      |         |                        | monetary<br>items (c) |         |
|   |                            |                      |                      |         |                        |                       |         |
| <b>Assets</b>   |                            |                      |                      |         |                        |                       |         |
| Cash and deposits with banks  | 4,534                      | 523                  | 17,217               | 4,228   | 2,525                  | -                     | 29,027  |
| Securities  | 9,142                      | 5,527                | 13,225               | 8,316   | 859                    | 4,497                 | 41,566  |
| Securities borrowed or purchased<br>under agreement to resell                 | 397                        | -                    | 86                   | -       | -                      | -                     | 483     |
| Credit to the public (b)  | 99,535                     | 55,569               | 34,730               | 7,067   | 10,583                 | 5                     | 207,489 |
| Credit to governments   | -                          | 256                  | 256                  | -       | -                      | -                     | 512     |
| Investments in affiliated companies   | 8                          | -                    | -                    | -       | -                      | 2,023                 | 2,031   |
| Buildings and equipment   | -                          | -                    | -                    | -       | -                      | 3,368                 | 3,368   |
| Other assets  | 4,076                      | 114                  | 2,563                | 679     | 1,083                  | 820                   | 9,335   |
| Total assets  | 117,692                    | 61,989               | 68,077               | 20,290  | 15,050                 | 10,713                | 293,811 |
| <b>Liabilities</b>  |                            |                      |                      |         |                        |                       |         |
| Deposits of the public  | 101,652                    | 26,167               | 68,940               | 20,075  | 8,991                  | 127                   | 225,952 |
| Deposits from banks   | 3,636                      | 852                  | 1,129                | 349     | 491                    | -                     | 6,457   |
| Deposits from governments   | 59                         | 627                  | 129                  | 12      | -                      | -                     | 827     |
| Securities loaned or sold under<br>agreement to repurchase                    | 392                        | -                    | 157                  | -       | -                      | -                     | 549     |
| Debentures, bonds and subordinated notes                                      | 2,824                      | 17,426               | 2,007                | -       | -                      | -                     | 22,257  |
| Other liabilities   | 9,584                      | 3,864                | 2,247                | 572     | 1,104                  | 607                   | 17,978  |
| Total liabilities   | 118,147                    | 48,936               | 74,609               | 21,008  | 10,586                 | 734                   | 274,020 |
| Difference  | (455)                      | 13,053               | (6,532)              | (718)   | 4,464                  | 9,979                 | 19,791  |
| <b>Effect of hedging derivative<br/>instruments:</b>                          |                            |                      |                      |         |                        |                       |         |
| Derivative instruments (excluding options)                                    | -                          | -                    | 8                    | (8)     | -                      | -                     | -       |
| <b>Effect of derivative instruments<br/>that are not hedging derivatives:</b> |                            |                      |                      |         |                        |                       |         |
| Derivative instruments (excluding options)                                    | 8,335                      | (8,278)              | 5,557                | (894)   | (4,720)                | -                     | -       |
| Options in the money, net<br>(in terms of underlying asset)                   | 796                        | (31)                 | (1,155)              | 28      | 362                    | -                     | -       |
| Options out of the money, net<br>(in terms of underlying asset)               | 115                        | 3                    | (288)                | 239     | (69)                   | -                     | -       |
| Total   | 8,791                      | 4,747                | (2,410)              | (1,353) | 37                     | 9,979                 | 19,791  |
| <b>Effect of derivative instruments<br/>that are not hedging derivatives:</b> |                            |                      |                      |         |                        |                       |         |
| Options in the money, net<br>(discounted par value)                           | 286                        | (41)                 | (678)                | 79      | 354                    | -                     | -       |
| Options out of the money, net<br>(discounted par value)                       | 2,377                      | 12                   | (3,721)              | 931     | 401                    | -                     | -       |

(a) Including linked to foreign currency.

(b) The general and supplementary provisions for doubtful debts have been deducted proportionately from the different linkage bases.

(c) Including derivative instruments that their basis is applicable for a non-monetary item.

**Note 5 - Assets and Liabilities Classified According to Linkage Basis (cont'd)**  
**as at 31 December 2008 (Audited)**  
**Reported amounts**

|   | Israeli currency           |                      | Foreign currency (a) |                |                        |              |                                     |
|---|----------------------------|----------------------|----------------------|----------------|------------------------|--------------|-------------------------------------|
|   | Unlinked<br>(NIS millions) | Linked to the<br>CPI | In U.S.<br>dollars   |                | In other<br>currencies |              | Non-<br>monetary<br>items (c) Total |
|   |                            |                      | In Euro              |                |                        |              |                                     |
| <b>Assets</b>   |                            |                      |                      |                |                        |              |                                     |
| Cash and deposits with banks  | 15,116                     | 529                  | 11,990               | 2,938          | 2,557                  | -            | 33,130                              |
| Securities  | 9,464                      | 5,994                | 16,414               | 8,813          | 901                    | 3,324        | 44,910                              |
| Securities borrowed or purchased<br>under agreement to resell                 | 125                        | -                    | 76                   | -              | -                      | -            | 201                                 |
| Credit to the public (b)  | 101,569                    | 53,457               | 39,959               | 7,498          | 10,732                 | -            | 213,215                             |
| Credit to governments   | -                          | 256                  | 264                  | -              | -                      | -            | 520                                 |
| Investments in affiliated companies   | 8                          | -                    | -                    | -              | -                      | 1,834        | 1,842                               |
| Buildings and equipment   | -                          | -                    | -                    | -              | -                      | 3,445        | 3,445                               |
| Other assets  | 4,559                      | 141                  | 5,109                | 1,011          | 2,090                  | 619          | 13,529                              |
| <b>Total assets</b>   | <b>130,841</b>             | <b>60,377</b>        | <b>73,812</b>        | <b>20,260</b>  | <b>16,280</b>          | <b>9,222</b> | <b>310,792</b>                      |
| <b>Liabilities</b>  |                            |                      |                      |                |                        |              |                                     |
| Deposits of the public  | 111,976                    | 27,522               | 74,595               | 22,161         | 8,469                  | 60           | 244,783                             |
| Deposits from banks   | 1,581                      | 800                  | 668                  | 288            | 405                    | -            | 3,742                               |
| Deposits from governments   | 53                         | 592                  | 175                  | 11             | -                      | -            | 831                                 |
| Securities loaned or sold under<br>agreement to repurchase                    | 374                        | -                    | 175                  | -              | -                      | -            | 549                                 |
| Debentures, bonds and subordinated notes                                      | 1,894                      | 16,684               | 2,058                | -              | -                      | -            | 20,636                              |
| Other liabilities   | 9,090                      | 3,687                | 4,224                | 1,151          | 2,582                  | 600          | 21,334                              |
| <b>Total liabilities</b>  | <b>124,968</b>             | <b>49,285</b>        | <b>81,895</b>        | <b>23,611</b>  | <b>11,456</b>          | <b>660</b>   | <b>291,875</b>                      |
| <b>Difference</b>   | <b>5,873</b>               | <b>11,092</b>        | <b>(8,083)</b>       | <b>(3,351)</b> | <b>4,824</b>           | <b>8,562</b> | <b>18,917</b>                       |
| <b>Effect of hedging derivative<br/>instruments:</b>                          |                            |                      |                      |                |                        |              |                                     |
| Derivative instruments (excluding options)                                    | -                          | -                    | 8                    | (8)            | -                      | -            | -                                   |
| <b>Effect of derivative instruments<br/>that are not hedging derivatives:</b> |                            |                      |                      |                |                        |              |                                     |
| Derivative instruments (excluding options)                                    | 8,733                      | (8,619)              | 4,751 (d)            | 986 (d)        | (5,851)                | -            | -                                   |
| Options in the money, net<br>(in terms of underlying asset)                   | (445)                      | (5)                  | (265)                | 687            | 28                     | -            | -                                   |
| Options out of the money, net<br>(in terms of underlying asset)               | (150)                      | (11)                 | (180)                | 201            | 140                    | -            | -                                   |
| <b>Total</b>  | <b>14,011</b>              | <b>2,457</b>         | <b>(3,769)</b>       | <b>(1,485)</b> | <b>(859)</b>           | <b>8,562</b> | <b>18,917</b>                       |
| <b>Effect of derivative instruments<br/>that are not hedging derivatives:</b> |                            |                      |                      |                |                        |              |                                     |
| Options in the money, net<br>(discounted par value)                           | (1,142)                    | (9)                  | (54)                 | 1,139          | 66                     | -            | -                                   |
| Options out of the money, net<br>(discounted par value)                       | 442                        | (23)                 | (1,374)              | 208            | 747                    | -            | -                                   |

(a) Including linked to foreign currency.

(b) The general and supplementary provisions for doubtful debts have been deducted proportionately from the different linkage bases.

(c) Including derivative instruments that their basis is applicable for a non-monetary item.

(d) Reclassified.

**Note 6 - Contingent Liabilities and Special Commitments**

## Reported Amounts

|  | 30 September 2009<br>(Unaudited)<br>(NIS millions) | 30 September 2008<br>(Unaudited) | 31 December 2008<br>(Audited) |
|--|--|----------------------------------|-------------------------------|
| <b>A. Off-balance sheet financial instruments</b>  |  |                                  |                               |
| <b>Balances of contracts or their stated amounts as at the end of the year</b>   |  |                                  |                               |
| <b>Transactions in which the balance reflects a credit risk</b>  |  |                                  |                               |
| Documentary credits  | 1,916  | 2,705                            | 1,631                         |
| Credit guarantees  | 6,549  | 7,306                            | 6,821                         |
| Guarantees to apartment purchasers   | 8,935  | 8,359                            | 8,117                         |
| Other guarantees and liabilities   | 14,331   | 13,270                           | 14,454                        |
| Commitments regarding uncompleted credit card transactions<br>unutilized credit card facilities  | 18,156   | 16,143                           | 16,651                        |
| Other unutilized revolving credit facilities to the public and credit<br>facilities on demand  | 14,009   | 16,609                           | 16,967                        |
| Irrevocable commitments to provide credit which has been<br>approved and not yet granted (a)   | 18,653   | 22,601                           | 19,627                        |
| Commitments to issue guarantees  | 6,864  | 6,088                            | 7,361                         |
| (a) Of which: credit exposures in respect of liabilities to supply liquidity to securitization structures under the<br>auspices of other parties not utilized in the amount of NIS 376 million (30 September 2008 - NIS 342 million,<br>31 December 2008 - NIS 380 million). |  |                                  |                               |
| <b>B. Other contingent liabilities and special commitments:</b>  |  |                                  |                               |
| <b>(1) Long-term rental contracts -</b>  |  |                                  |                               |
| <b>Commitments in respect of rental of buildings, equipment<br/>and motor vehicles payable in the following years:</b>   |  |                                  |                               |
| First year   | 156  | 187                              | 170                           |
| Second year  | 135  | 124                              | 132                           |
| Third year   | 106  | 104                              | 105                           |
| Fourth year  | 84   | 77                               | 89                            |
| Fifth year   | 50   | 49                               | 54                            |
| After five years   | 123  | 88                               | 117                           |
| Total  | 654  | 629                              | 667                           |
| <b>(2) Commitments to purchase securities</b>  | 319  | 391                              | 371                           |
| <b>(3) Commitments to invest in buildings, equipment and in other assets</b>   | 179  | 168                              | 214                           |
| <b>(4) Future deposits</b>   |  |                                  |                               |
| Transactions with depositors for purposes of receipt of large deposits at various future dates and at<br>determined in advance as of the date of the investment fixed interest rates   |  |                                  |                               |
| Details of future deposits and deposits dates as was determined by the terms of<br>the transactions:   |  |                                  |                               |
| First year   | 17   | 17                               | 17                            |
| Second year  | 17   | 17                               | 17                            |
| Third year   | 17   | 17                               | 17                            |
| Fourth year  | 17   | 17                               | 17                            |
| Fifth year   | 17   | 17                               | 17                            |
| After five years   | 18   | 35                               | 32                            |
| Total future deposits  | 103  | 120                              | 117                           |

## Note 6 – Contingent Liabilities and Special Commitments

- C. In the regular course of business, legal claims have been filed against the Bank and certain consolidated companies, including petitions for approval of class actions.

In the opinion of the Management of the Bank and the managements of the consolidated companies, based on legal opinions regarding the chances of the claims succeeding, including the petitions for approval of class actions, appropriate provisions have been recorded in the Financial Statements, insofar as required, to cover damages resulting from the said claims.

In the opinion of the Management of the Bank and the managements of the consolidated companies, the total additional exposure arising from legal claims filed against the Bank and against the consolidated companies on various subjects, the amount of each of which exceeds NIS 2 million, and regarding which the chances of the claims succeeding are not remote, amounts to some NIS 93 million.

1. The following are details of claims in material amounts.

- A. On 15 June 2000, a claim was filed against the Bank in the Tel Aviv-Jaffa District Court, together with a petition to approve the claim as a class action, in the amount of NIS 1 billion.

The plaintiff alleges that the Bank, in various publications, promised depositors of shekel deposits made by self service through direct banking channels, that they would receive a preferred annual interest rate of 1% over the accepted rate, and that the various publications and the information provided to the depositors at the time of the original deposit could have misled the depositors into thinking that the 1% additional interest would be paid also in respect of the periods in which the deposit was automatically renewed and not only in respect of the original deposit period, as was the actual case.

Accordingly, the plaintiff is requesting that the Bank pay to him and all the relevant depositors he represents, the preferred interest also in respect of the periods in which the deposits were automatically renewed. In December 2003 the Court approved the claim as a class action. The Bank submitted an appeal on the decision to the Supreme Court, which has not yet rendered a ruling on the matter. The District Court granted the plaintiff's petition to cancel the stay of proceedings in the case and set a hearing for the case, although the Supreme Court has not yet rendered a decision. The Bank has petitioned the Supreme Court for a stay of the proceedings until the Supreme Court renders a decision in the appeal. On 13 January 2009, the parties signed a settlement agreement. On 15 January 2009, the Court ordered that the proceedings prescribed by law for the approval of the signed settlement agreement be held. The Attorney General filed a response to the petition to approve the settlement agreement, in which he made various objections to the arrangement that had been agreed upon and asked that an inspector be appointed as provided by law. On 3 May 2009, the Court ordered the appointment of an inspector, who was asked to give the court an opinion regarding the questions relating to the settlement arrangement.

- B. On 14 October 2004 a petition to approve a claim as a class action in the amount of some NIS 2 billion was filed against the Bank with the Tel Aviv-Jaffa District Court on the basis of the Banking (Service to Customer) Law, 1981 and Regulation 29 of the Civil Procedure Regulations, 1984.

The subject of the claim was originally the allegations of the petitioner that he and all other customers of the Bank were charged fixed management fees, credit provision fees and securities deposit management fees unlawfully and contrary to the exemptions indicated beside the fees on the Bank's price list. The petitioner maintains that the Bank misled its customers and breached the disclosure duties owed to them, and breached contractual obligations to them by charging them the fees, despite the fact that according to the Bank's price list they were entitled to exemptions from the payment of such fees. The petitioner is also claiming that in this way the Bank was unlawfully enriched.

After the Bank submitted to the Court its response to the petition to approve the claim as a class action, and the petitioner submitted a reply to the Bank's response to the petition for approval of a class action, a petition was filed with the Court to amend the statement of claim, pursuant to which the petitioner requested to strike out all that part of the claim relating to the securities deposit management fee commission. The Court approved the request for such amendment and the amount of the claim was reduced to some NIS 1.12 billion.

On 25 December 2007, the Tel Aviv District Court denied the petition for approval of the claim as a class action. The plaintiff filed an appeal to the Supreme Court regarding this ruling on 10 February 2008.

- C. In February 2006 a petition for the approval of filing a class action was filed against the Bank by a customer of the Bank in the Tel Aviv-Jaffa District Court, in an amount estimated by the petitioner at some NIS 300 million.

According to the petitioner, in the framework of the sale of structured products to Bank customers, the Bank does not disclose the full pricing and therefore charges a hidden "commission" that is expressed in a financial margin which inures to the benefit of the Bank in the transaction, which in the petitioner's view contradicts the duty for disclosure imposed upon the Bank in accordance with the law.

The group to which the requested class action relates, according to the claim, is made up of all Bank customers who invested in various structured products marketed by the Bank, from January 1999 until January 2006, and to whom the Bank did not disclose what allegedly should have been disclosed. The Bank filed its response to the petition for the approval of the claim as a class action. On 11 September 2008, the Tel Aviv District Court issued its decision denying the petition for approval of the class action. On 10 November 2008, the petitioner filed an appeal against the decision to the Supreme Court. On 19 July 2009, the Supreme Court issued a decision denying the appeal, in accordance with the parties' agreement.

- D. On 12 September 2006, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, Bank Hapoalim B.M. and Israel Discount Bank Ltd. The amount claimed in the class action for which approval has been requested is NIS 7 billion, while in the body of the claim, it is contended that the damage to the claimed group amounts to NIS 10 billion. No specific sum of the amount of the claim has been clearly attributed to each respondent. According to the petitioner, the respondent banks charged their customers with interest for unlinked shekel credit, a commission for credit allotment and fixed management fees with regard to debitory current accounts at identical rates and amounts, as a result of price coordination and a restrictive arrangement, which are prohibited under the Restrictive Trade Practices Law. The remedy requested by the petitioner is refund of the alleged over-charging to

the respondents' customers, who took unlinked shekel credit or a "retroactive reduction" of the said interest and commission rates that the respondent banks collected during the past decade. The Bank has filed its response to the petition for the approval of the claim as a class action.

On 21 January 2008, the Tel Aviv District Court granted the petition, and approved the pursuance of the claim as a class action. The Bank submitted a petition for leave to appeal the ruling to the Supreme Court. The Supreme Court's ruling of 29 May 2008 provided that the Attorney General must submit his position in writing regarding the petition. The Attorney General has notified the Supreme Court that he will take part in the proceeding regarding the petitions for leave to appeal submitted by the banks and will submit his position in writing.

- E. On 23 November 2006, a claim and a petition to approve the claim as a class action were filed in the Jerusalem District Court against the Bank and against Bank Hapoalim B.M. and Israel Discount Bank Ltd. The petitioners allege that in respect to credit to the households sector, the banks collect interest at a rate that is much higher than that collected from the commercial sector and from the corporate sector, this in spite of the fact that the risk in extending credit to the households sector is significantly lower than the risk for those sectors, and that this excessive interest rate derives from the exploitation of the low level of bargaining power of the households sector and from the monopolistic power of the respondents. The petitioners allege that this is an infringement of the Restrictive Trade Practices Law, 1988, which prohibits a monopolist from abusing its position in the market, and that there is a real fear that the lack of competition among the respondents, regarding all matters concerning the households sector, is the result of a restrictive arrangement among the parties.

The petitioners also allege that the interest rate was determined while misleading the consumers regarding the normal price for credit service to the households sector, contrary to the provisions of the Consumer Protection Law, 1981 and the Banking (Service to Customer) Law, 1981.

The petitioners allege that the damage caused to them and the members of the group is the result of the multiple of (1) the gap between the interest rate actually collected and the fair interest rate that would have been established for loans to the households sector in a competitive market, (2) the amounts of credit that each of the petitioners and members of the group took during the seven years preceding the filing of the claim.

The damage alleged by them is NIS 5.6 billion according to one method, and NIS 5.2 billion according to a second method. The estimated damage attributed to the Bank's customers is at least NIS 1.6 billion. The Bank filed its response to the petition for the approval of the claim as a class action. The court granted a petition filed by the Bank for a stay of these proceedings and ordered they be stayed until the Supreme Court renders a decision regarding the petition for leave to appeal filed by the Bank with respect to the decision to approve as a class action the claim described in paragraph D above. The Supreme Court denied the petition for leave to appeal filed by the petitioners with respect to the District Court's above-mentioned decision to stay the proceedings in the claim.

- F. On 31 January 2008, 260 identical claims were filed in the Tel Aviv-Jaffa Magistrate's Court against the Bank and receivers who had been appointed by the court. The amounts of the claims vary between some NIS 787,000 and some NIS 1,350,000. Pursuant to the Court's ruling, the proceedings for all the above-mentioned claims were combined, and they will be heard as one claim.

The total amount of the claims is some NIS 270 million. The plaintiffs are the purchasers of vacation apartments in the Nofit Hotel in Eilat. According to the plaintiffs, the Bank and the receivers were negligent in supervising the project and refrained from paying for guarding it, and as a result, the plaintiffs suffered significant damages, including a decline in the value of the apartments. These claims are in addition to five other claims that have been filed against the Bank on the same ground, and which are being heard separately. The total amount of all the claims in connection with this project is some NIS 288.6 million. On 10 August 2009, the Tel Aviv-Jaffa District Court rejected one of the additional claims submitted against the Bank, which had been submitted separately by 3 purchasers and was identical to the above-mentioned 260 claims. The plaintiffs appealed the ruling.

- G. On 1 April 2007, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, additional banks, and entities that purchased the control of the mutual fund managers from the banks. The amount claimed against the Bank is estimated by the petitioners at some NIS 131 million.

The petitioners claim that they held and hold units in mutual funds that were managed by fund managers controlled by the Bank. According to the petitioners, the Bank, beginning in 2004, charged the fund managers it controlled brokerage commissions with respect to the execution of securities and foreign currency transactions, at a rate higher than the rate it charged other entities, and in doing so, it acted unlawfully.

According to them, although during 2006 the Bank sold its holdings in the fund managers to third parties, it continues to provide the same services to the mutual funds in exchange for even higher commissions than those charged prior to the sale of the control. The continued provision of the said services suggests that the Bank and the purchasers of the control of the fund managers had agreed that in exchange for a reduction in the price paid for the mutual fund managers, the Bank would continue to provide the trading services that it had provided prior to the sale, in exchange for the high commissions that had been charged up until the sale – a matter which removes all substance, they allege, from the sale of the control of the fund managers.

The petitioners argue that they and the other holders of mutual fund units that were or are under the Bank's control have suffered damages that reflect the reduction in the value of the mutual fund units due to the alleged over-charging. The Bank has not yet filed its response to the petition for the approval of the claim as a class action.

- H. On 26 June 2007, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, for a claim in the amount of NIS 200 million. The plaintiff claims that the Bank charges its customers securities deposit management fee commissions which are higher than agreed. He claims that each time he carried out a low volume partial sale of a particular share for which the commission was less than the minimum, the Bank charged him with the minimum commission as well as the management fee commission collected at the end of the quarter, with the aggregate amount of the two commissions being higher than the agreed maximum management fees that the Bank was entitled to collect. The plaintiff claims that the Bank was required to deduct the minimum commission collected at the time of the partial sale from the total amount of the management fees. The plaintiff also argues that the Bank's documents and announcements do not reflect the amounts of the management

fee commissions that are actually charged during a single quarter. The Bank has filed its response to the petition for the approval of the claim as a class action.

- I. On 25 September 2007, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, in the amount of some NIS 435 million, which includes 8 different causes of action. Following the Court's ruling pursuant to which the plaintiff was required to choose a single cause of action and have the others stricken from the petition, the plaintiffs informed the court that they had chosen the cause of action which was based on a claim that the Bank charges its customers for securities management fees at the time a security is sold during a particular quarter and does not deduct this amount from the minimum management fee that the bank charges for that quarter. In the petition, the plaintiffs attributed some NIS 30 million to this cause of action.
- J. On 3 April 2008, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, Bank Hapoalim and Israel Discount Bank ("Banks") in an amount between NIS 35 million and NIS 84 million. The plaintiffs claim that the Banks are unjustly enriching themselves, at their customers' expense, by receiving profits from interest on the amounts of the tax they withhold at source in accordance with the provisions of Section 164 of the Income Tax Ordinance; those amounts remain with the Banks until the date fixed in the Ordinance and its regulations and are not therefore transferred to the Tax Authority on the date of actual deduction. Therefore, it is claimed in the petition, the Banks have breached their duties under the Trust Law and the Custodians Law and their obligation to carry out their agreements with their customers in good faith. The Bank filed its response to the petition for the approval of the claim as a class action. On 9 June 2009, the Court granted the plaintiffs' petition to withdraw from the claim; the Court struck the claim and the petition to approve it as a class action.
- K. On 6 May 2008, a claim and a petition to approve it as a class action were filed in the Tel Aviv-Jaffa District Court. According to the plaintiff, the Bank charges its customers' accounts with the legal expenses incurred in handling such customers' debts, without obtaining the approval of any legal tribunal, and in violation of the directives of the Supervisor of Banks – "Proper Banking Management Directives – Charging Customers for Attorneys' Fees." Additionally, when the Bank charges its customers' accounts with legal expenses (both those approved by a legal tribunal and those that have not been so approved), the Bank collects interest on such expenses at the interest rate applicable to the account (which in many cases is excess interest on arrears) and not at the interest and linkage rates which the Bank is permitted to collect in accordance with the Adjudication of Interest and Linkage Law, 1961. The requested remedy is the reimbursement of all excess amounts charged by the Bank, without an indication of the amount, although it is alleged that "this is a vast amount" and that the lawsuit is filed in the name of all the Bank's customers whose accounts were charged with legal expenses during the seven years preceding the filing of the petition to approve the class action. The Bank has submitted its response to the petition for approval of the claim as a class action. On 18 October 2009, the District Court approved the claim as a class action.
- L. On 14 May 2008, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank and against Bank Hapoalim (the "Banks"). The petitioner alleges that he maintains current accounts at these Banks and that no interest has been paid to him in respect of the periods during which there was a credit balance in the accounts. The petitioner further claims that it was not explained to him that there is an investment channel which can produce daily



interest in respect of amounts held in credit in his accounts. The Banks' alleged behavior constitutes, according to the petitioner, a violation of several legal provisions, including the Restrictive Trade Practices Law, the Trusts Law, the Custodians Law, the Unjust Enrichment Law, the Banking Ordinance and the Banking (Service to Customer) Law. The group in whose name the claim has been filed and which the court is being asked to approve consists of anyone who has been a customer of the Banks and who, at any time during the 7 years preceding the filing of the claim, had a credit balance in a current account with respect to which no interest was paid. The amount of the alleged class action is estimated by the petitioner at NIS 3.4 billion, while the claim does not specify the amount of damage attributed to each of the Banks. However, the opinion attached to the petition for approval, which presents the manner in which the alleged damage was calculated, indicates that the part of the damage attributed to the Bank is NIS 1.69 billion. The Bank has submitted its response to the petition for approval of the claim as a class action.

- M. On 28 September 2008, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, Bank Hapoalim, Israel Discount Bank and the Bank Otzar Hachayal the amount of some NIS 672 million. According to the allegations, the Bank secretly collects an illegal commission from customers engaged in continuous trading of options on the Tel Aviv 25 stock index (such options consisting of a right to buy or sell the basket of shares comprising the Tel Aviv 25 Index at a given time and at a given price); the banks take advantage of the fact that the amounts pass from the stock exchange to those holding the options through the banks, and an exercise commission of 0.5% is collected from the amounts received by customers who are the holders of expiring options which entitle their holders to a payment; the calculation of the amount due to the option holder is not simple because the expiration index is not an exact amount and is not published in any official publication and therefore the customer does not know exactly what amount is due to him and cannot know that a commission has been deducted from the amount that he receives. The ground for the action is based on the fact that the banks did not announce that they collect an exercise commission, did not include this commission in their agreements with the customers and they made a false representation to the customers according to which the only commission that they collect is sale and purchase commission. The banks do specify the commission that is collected in a separate notice that they send at later stages, after the transactions are carried out, but according to the plaintiffs, customers like them do not take note of them and are not capable of analyzing them. The defined group consists of customers who contracted with portfolio managers in connection with the trading of Tel Aviv 25 Index options. According to the plaintiffs they used a narrow definition of this group of customers in order to argue that it is easier to hide the charging of commissions from this group (relative to the group of customers who do not trade through portfolio managers). The relief requested is the damage which is common to all the customers of the banks in respect of the amount of the exercise commissions collected during the past seven years. The Bank has submitted its response to the petition for approval of the claim as a class action.
- N. On 4 August 2008, a claim and a petition to approve it as a class action were filed in the Jerusalem District Court against the Bank, Israel Discount Bank, "Kahal" Supplementary Training Funds Management (1996) Ltd. ("Kahal") and the Supervisor of the Capital Market, Insurance and Savings (as a formal defendant). According to the petitioner, Kahal had transferred, in accordance with the Intensification of Competition and Reduction of Concentration and Conflicts of Interest in the Israeli Capital Market (Legislative Amendments)

Law, 2005, and at the banks' instruction, the control of the assets of the provident funds controlled by Kahal to a "different management company" and that the banks allegedly illegally assumed and appropriated to themselves the consideration amounts that they received from the other management company, for "the transfer of the control of the assets of the provident funds as well as their management and the trusteeship of them," since a management company and a management company's controlling shareholder may not receive any benefit whatsoever, directly or indirectly, in connection with the management of a provident fund, other than expenses and management fees. It is claimed that the consideration amounts received for the said transfer of control of the provident funds are proceeds produced by the assets of the provident funds, and their source is the members' rights stemming from such assets, and that this is a profit which therefore belongs to the members of the provident funds and not to any of the defendants. It is claimed that the consideration received by the banks amounts to some NIS 260 million, with the Bank's share in this amount being NIS 149.5 million.

The petitioner bases the claim on, *inter alia*, violation of the Control of Financial Services (Provident Funds) Law, 2005, the Joint Investments Trusts Law, 1994, the Unjust Enrichment Law, the Contracts Law, the Banking (Licensing) Law, the Agency Law and the Trusts Law. The group in whose name the approval of the class action is sought is composed of: all members of all the provident funds whose assets were controlled and managed by each of the trust managers (apparently referring to Kahal) that were owned and/or controlled by the respondent bank, and transferred to their replacements. The petitioner added the Supervisor of the Capital Market, Insurance and Savings to the claim and to the petition for approval since, according to the petitioner, the Supervisor is charged with licensing, control and implementation of the provisions of the Provident Funds Law, and it is therefore appropriate that he present his position, both from the substantive and public viewpoints, since this would assist in clarifying and deciding the questions raised in the class action. On 30 June 2009 the court ruled that Kahal was wrongfully added as a respondent and dismissed the petition against it. The Bank has submitted its response to the petition for approval of the claim as a class action.

- O. On 4 August 2008, a claim and a petition to approve it as a class action were filed in the Jerusalem District Court against the Bank, Leumi Gemel Ltd. and the Supervisor of the Capital Market, Insurance and Savings (as a formal defendant). According to the petitioner, Leumi Gemel transferred, in accordance with the Intensification of Competition and Reduction of Concentration and Conflicts of Interest in the Israeli Capital Market (Legislative Amendments) Law, 2005, and at the Bank's instruction, the control of the assets of the provident funds controlled by Leumi Gemel to "different management companies." According to the petitioner, the Bank allegedly illegally assumed and appropriated to itself the consideration amounts that it received from the other management companies, for "the transfer of the control and management of the assets of the provident funds and the trusteeship thereof," since according to the petitioner, a management company, and a management company's controlling shareholder may not receive any benefit whatsoever, directly or indirectly, in connection with the management of a provident fund, other than expenses and management fees. It is claimed that the consideration amounts received for the said transfer of control of the provident funds are proceeds arising from the assets of the provident funds, and their source is the provident funds' members' rights stemming from such assets, and that this is therefore a profit which belongs to the members of the provident funds and not to any of the respondents. The amount being claimed amounts to some NIS 1.0016 billion, which constitutes,

according to the petitioner, the consideration received by the Bank from the sale. The petitioner bases the claim on, *inter alia*, violation of the Control of Financial Services (Provident Funds) Law, 2005, the Joint Investments Trusts Law, 1994, the Unjust Enrichment Law, the Contracts Law, the Banking (Licensing) Law, the Agency Law and the Trusts Law. The group in whose name the approval of the class action is sought is composed of: all members of all the provident funds whose assets were controlled and managed by each of the trust managers (apparently referring to Leumi Gemel) that were owned and/or controlled by the respondent bank, and transferred to their replacements. The petitioner added the Supervisor of the Capital Market, Insurance and Savings to the claim and to the petition for approval since, according to the petitioner, the Supervisor is charged with licensing, control and implementation of the provisions of the Provident Funds Law, and it is therefore appropriate that he, both from the substantive and public viewpoints, present his position, since this would assist in clarifying and deciding the questions raised in the class action. The Bank has submitted its response to the petition for approval of the claim as a class action.

- P. On 4 August 2008, a claim and a petition to approve it as a class action were filed in the Jerusalem District Court against the Bank, Leumi Pia Trust Management Company Ltd., Psagot Managers of Mutual Funds - Leumi Ltd., Kesselman & Kesselman Trust Company (1971) Ltd., and the Israel Securities Authority (as a formal defendant). According to the petitioner, each manager transferred the control and management of the mutual funds it owned to “different management companies,” in accordance with the Intensification of Competition and Reduction of Concentration and Conflicts of Interest in the Israeli Capital Market (Legislative Amendments) Law, 2005, and the Bank allegedly illegally obtained the consideration amounts that it received from the other management companies, for “the transfer of the control and management of the assets of the mutual funds.” According to the petitioner, a management company, trustee and a management company’s controlling shareholder may not receive any benefit whatsoever, in connection with the management of mutual funds, other than expenses and management fees, and it is therefore claimed that the consideration amounts received for the said transfer of control of the mutual funds are proceeds arising from the assets of the mutual funds, and their source is the rights stemming from such assets, and that this is a profit which belongs to the funds and to the owners of the units thereof, and not to any of the respondents. According to the petitioner, the consideration received by the Bank amounts to some NIS 1.885 billion, and this is the amount claimed by the petitioner for the members of the group. The petitioner bases the claim on, *inter alia*, violation of the Joint Investments Trusts Law, 1994, the Unjust Enrichment Law, the Contracts Law, the Banking (Licensing) Law, the Agency Law and the Trusts Law. The group in whose name the approval of the class action is sought is composed of: all owners of units in all the mutual funds whose assets were controlled and managed by each of the managers who were controlled by the Bank, and were transferred to their replacements. The petitioner added the Israel Securities Authority to the complaint and to the petition for approval since, according to the petitioner, the Authority is charged with licensing, control and implementation of the provisions of the Joint Investments Trusts Law and it is therefore appropriate that it, in terms of the public interest, present its position, and since this would assist in clarifying and deciding the questions raised in the class action. The Bank has submitted its response to the petition for approval of the claim as a class action.
- Q. On 2 August 2009, a financial claim was filed against the Bank in the Haifa District Court for NIS 100 million. The plaintiff claims that the Bank had breached its commitment to finance a construction project that had been initiated

by a company in which the plaintiff held shares at that time, that the Bank transferred funds from the company's account to the account of one of the plaintiff's partners in violation of the agreements and the instructions given to the Bank and that the Bank had unreasonably refused to make credit available to the company. The damages claimed by the plaintiff include various lost profits, loss of investment, loss of the plaintiff's share in the company and damage to reputation.

- R. On 29 October 2009 a claim was filed in the Central District Court for declaratory judgments to the effect that the seven respondent banks (the Bank, Bank Hapoalim, Israel Discount Bank, the First International Bank of Israel, Mizrahi Bank, Mercantile Discount Bank and Union Bank) are not entitled to charge the petitioners with "default" interest differentials, as defined in the claim, and that the amount of the default interest differentials must be reduced from an amount of NIS 841 million to an amount of NIS 37 million. Alternatively, they request a ruling that the banks are entitled to charge the petitioners with interest differentials in accordance with the Adjudication of Interest and Linkage Law, 1961 only, this being with regard to the petitioners' debt that had accrued from 12 May 2009 and onward. The petitioners claim is, *inter alia*, that the "default interest" is nothing other than "agreed compensation" as defined in Section 15(A) of the Contracts Law (Remedies), 1970, which a court may reduce "if it finds that the compensation was established without any reasonable relation to the damage that had been foreseeable as being the reasonable result of a breach at the time the contract was made"; that the reduction of the default interest amounts is also required in accordance with the interpretation of the loan agreement and according to the intention of the parties; that the charging of the petitioners with default interest will constitute unjustified enforcement of the loan agreement; that the banks' insistence on charging the petitioners with default interest constitutes a lack of good faith, and that the banks' charging of default interest will constitute unjust enrichment on their part. The claim does not make a monetary attribution of a specific claimed share of each of the banks in the amount of the default interest differentials, but details are provided of each bank's participation in the financing, with the Bank's share being claimed to be 24%.
2. In addition, there are legal claims pending against the Bank, including petitions for approval of class actions, as detailed below. In the opinion of the Management of the Bank, based on legal opinions with regard to the chances of these legal proceedings, it is not possible at this stage to estimate the chances of the claims and therefore no provision has been recorded in respect thereof. The following are the details of the legal claims:
    - A. On 30 June 2008, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, Israel Discount Bank Ltd. and Bank Hapoalim B.M., ("Banks"). The claim relates to the commissions charged by the Banks for various banking services provided by them to their private customers ("operating" commissions, as distinguished from commissions for the allocation, granting and handling of credit, which are not part of the claim). It is claimed that the Banks had agreed among themselves regarding the increase or reduction of the rates of the commissions, and that it is suspected that agreements were also reached regarding the creation of new commissions. It is claimed that in so doing, the Banks maintained an illegal restrictive arrangement regarding the rates of the commissions they collect from their customers, that they abused their monopolistic power (the Banks constituting, it is argued, an oligopoly), and that they unjustly enriched themselves at the expense of their customers. The petition claims that because of these said restrictive

arrangements, the Banks' customers paid an unfair rate for the commissions, higher than would have been paid were it not for the existence of the cartel that prevented free competition. The calculation of the amount claimed is presented as being derived from the Banks' income from commissions paid by households and those resulting from private banking. It is claimed, as an estimation, that half of this income was collected following the coordination of rates as a result of the restrictive practices, and had the rates not been coordinated between the Banks, the commissions would have been significantly lower, by at least 25%. Therefore, in accordance with the various assumptions indicated in the petition, the total aggregated amount of the damage is estimated in the amount of NIS 3.5 billion, while the petition's caption indicates that the amount of the claim is NIS 3 billion. No specific attribution has been made of the damage claimed to each of the Banks, but the petition mentions that the Bank's relative share of banking activity in Israel is estimated at some 30%. The Bank submitted its response to the petition for approval of the claim as a class action. On 1 June 2009, the petitioners filed a petition to attach as evidence, within the framework of the petition for approval as a class action, the Antitrust General Director's determination dated 26 April 2009, pursuant to which the Banks (Leumi, Hapoalim, Discount., Mizrahi and the International) had maintained restrictive trade agreements regarding the transfer of information concerning commissions. The respondent Banks opposed this and the Court has not yet ruled on the matter.

In the opinion of the Bank's Management, which is based on the opinion of the Bank's legal advisors, it is not possible at this early stage to estimate the chances of the petition.

- B. On 26 November 2008, a claim and a petition to approve it as a class action were filed in the Tel Aviv District Court against the Bank, the First International Bank of Israel Ltd., Union Bank of Israel Ltd. and Mizrahi Bank Ltd. The claim is based on damages claimed in the amount of about NIS 68,125,000 (according to the petitioner's calculations), caused to all the customers of the banks from whose profits from interest in respect of debentures and/or dividends in respect on shares - tax was deducted at source, this from 1 January 2003 until the day the claim was filed. According to the claim, the banks over-deducted tax, by deducting tax at source in respect of commissions collected from the income received. According to the petitioner's calculation, the banks should have deducted the commissions from the income subject to deduction at source, and only then carried out the deduction at source.

The petitioner bases his claim on Section 17 of the Income Tax Ordinance, which classifies commissions as an expense incurred in the production of income during the tax year, which is to be taken into account in the calculation of taxable income. According to the petitioner's claim, by acting as stated the banks violated their duty of care, fiduciary duty and duty to make proper disclosure towards the group, which apply to them under the Banking Law, the Consumer Protection Law and the Torts Ordinance, as well as the duty of good faith applying to them. It was also claimed that the banks caused the group damage and monetary loss and that their behavior is tantamount to negligence, violation of statutory duties and unjust enrichment.

In the opinion of the Bank's Management, which is based on the opinion of the Bank's legal advisors, it is not possible at this early stage to estimate the chances of the petition.

- C. On 27 April 2009, a petition to approve a class action was filed in the Tel Aviv-Jaffa District Court against the Bank, Bank Hapoalim, Israel Discount Bank, Mizrahi Bank and the First International Bank. The petition is based on the Antitrust General Director's determination of 26 April 2009. The petitioners allege that in accordance with the determination, the banks made restrictive arrangements regarding the exchange of information concerning commissions, which harmed the competition between them and caused damage to the members of the group whose representation is sought in the petition, and that such was reflected in over-payments of commissions. The petitioners estimate the amount of the claim sought in the class action against all the respondents at NIS 1 billion, while noting that this is merely an estimate and while reserving their right to amend the amount at a later time. The petition does not make any clear attribution of a specific claimed amount to each of the respondents and the matter of requesting provisions for linkage and interest is not sufficiently addressed. The petitioners claim that they have a cause of action because of the existence of the said restrictive arrangements between the banks, which could harm and have harmed competition. These arrangements, they argue, fall both within section 2(a) of the Restrictive Trade Practices Law and within section 2(b)(1) of the Restrictive Trade Practices Law.

In the opinion of the Bank's Management, which is based on the opinion of the Bank's legal advisors, it is not possible at this early stage to estimate the chances of the petition.

- D. Note 18(M) on pages 397-398 of the 2008 Annual Report details were provided regarding demands concerning the assets of Holocaust victims, which were addressed to the Bank prior to the filing of the originating motion described below, and regarding the Bank's appointment of an external examiner for the purpose of investigating this matter. On 24 June 2009, an originating motion was filed against the Bank in the Jerusalem District Court, under which the Court was asked to make various declarations regarding the "assets of Holocaust victims" as defined in the Assets of Holocaust Victims (Restitution to Heirs and Endowment for the purpose of Assistance and Commemoration) Law, 2006, and *inter alia*, to declare as follows: (a) that the Bank has financial obligations regarding the assets of Holocaust victims in an aggregate amount of NIS 246,845,410, as at 31 May 2009; and that (b) the Bank's financial obligations also apply to assets of Holocaust victims that the Bank held in the past but which the Bank had transferred to third parties prior to the Law's enactment; and (c) that in the cases in which there is evidentiary doubt, including doubt as to whether a particular asset is an "asset of a Holocaust victim" or as whether a particular asset is currently held by the Bank, the burden of proof should be borne by the Bank.

In the opinion of the Bank's Management, which is based on the opinion of the Bank's legal advisors, it is not possible at this early stage to estimate the chances of the originating motion or whether it is necessary to add to the provision that has been made with respect to the above-mentioned demands or with respect to the contents of the examiner's report.

3. The following are details of petitions for approval of class actions in material amounts that were filed against Leumi Mortgage Bank Ltd. ("Leumi Mortgage Bank"). In the opinion of the Management of the Bank, and in reliance on the opinion of the management of Leumi Mortgage Bank, which is based on the opinion of Leumi Mortgage Bank's legal advisors as to the chances of these proceedings,

appropriate provisions have been included in the Financial Statements, insofar as required, to cover damages resulting from such claims:

- A. On 21 June 2000, a petition for approval of a class action was filed against Leumi Mortgage Bank in the Tel Aviv-Jaffa District Court based on the Banking (Service to Customer) Law, 1981, Regulation 29 of the Civil Procedure Regulations, 1984, and the Supervision of Insurance Practices Law, 1981. The amount of the claim for which approval as a class action has been requested is estimated by the petitioners at some NIS 100 million.

The petitioners, who took out loans from Leumi Mortgage Bank, are making claims regarding the value of buildings for purposes of property insurance in the framework of loans taken from Leumi Mortgage Bank. According to the petitioners, Leumi Mortgage Bank or its representatives prepared excessive valuations of the buildings, resulting in overpayment of premiums by Leumi Mortgage Bank customers. The petitioners contend that this was also done in their case. In accordance with the decision of the District Court, the hearing of the claim has been stayed until the appeals regarding the matter mentioned in Note 4A. below are decided. The petition filed by the petitioners for the cancellation of the stay in proceedings was rejected by the court, which decided that the stay in proceedings in the claim still stands.

- B. On 2 December 2006, a petition to approve a class action was filed in the Tel Aviv - Jaffa District Court against Leumi Mortgage Bank and against Migdal Insurance Company Ltd. ("Migdal") regarding the partial payment of life insurance compensation. The estimated amount of the class action, as claimed by the petitioner, is NIS 150 million.

The petitioner and her deceased spouse took a loan from Leumi Mortgage Bank. According to what is alleged in the request: borrowers who took out loans from Leumi Mortgage Bank were able to join a life insurance arrangement for borrowers, in which the insurer was Migdal; numbered among the borrowers who joined the said life insurance are borrowers who, when an insurance event occurred, received partial insurance compensation at a rate lower than the amount of the insurance and of the balance of the loan; contrary to the amount actually paid, Leumi Mortgage Bank and Migdal had promised to pay such insured-borrower parties, "insurance compensation at the level of the loan balance due or at the level of the amount of insurance (the lower of them)" - so alleges the petitioner. On 18 January 2009, the court handed down a ruling instructing that the proceedings determined in the law be undertaken for the approval of the compromise agreement signed by the parties, including carrying-out a number of actions for examining of the approval of the agreement and the appointment of an examiner.

- 4. In addition, the petitions for approval of class actions set out below are pending against Leumi Mortgage Bank. In the opinion of the Management of the Bank, in reliance on the opinion of the management of Leumi Mortgage Bank, which is based on the opinion of the legal advisors of Leumi Mortgage Bank with regard to the chances of these legal proceedings, it is not possible at this stage to estimate their chances and therefore no provision has been recorded in their respect. The following are details of the legal proceedings:

- A. On 17 July 1997 a petition for approval of a class action in an amount exceeding NIS 1 billion was filed with the Tel Aviv-Jaffa District Court against Leumi Mortgage Bank and against other mortgage banks in connection with collection of borrowers' life insurance and property insurance commissions. Each of the

petitioners took out a loan from one of the respondent mortgage banks. According to the petitioners, in the context of taking out the loan, they were included in life insurance or property insurance policies taken out through the respondent banks and, according to their assertions, part of the insurance premiums illegally reached the respondent banks.

On 17 November 1997 the Court ruled that the claim could not be heard as a class action according to the Banking (Service to Customer) Law, 1981, and the Restrictive Trade Practices Law, 1988. Accordingly, the Court struck off the monetary claim.

Nevertheless, the Court decided that the claim could be heard in the framework of Regulation 29 of the Civil Procedure Regulations, 1984, but only with regard to the claim for declaratory relief relating to causes of action that had arisen before 10 May 1996. The Court ruled that the causes of action that could be heard in this framework related to the "restrictive arrangement and various insurance issues."

Appeals to the Supreme Court submitted against this decision by Leumi Mortgage Bank, all the other respondent mortgage banks and the petitioners, are pending. Pursuant to the decision of the Supreme Court, implementation of the District Court's decision was stayed. Accordingly, the claim will not be determined until the Supreme Court rules with regard to all the appeals.

On 1 September 2005 the Supreme Court handed down a judgment in which it was determined, in short, that although it was possible to utilize interpretive means to convert Regulation 29 into an instrument for submission of class actions, such utilization was not appropriate at that time, mainly because of the legislative procedures underway in the field of class actions; and on 12 March 2006 the Class Actions Law was published. On 25 September 2008, the court approved the withdrawal of one of the petitioners from the claim. A hearing on the petition to add another petitioner to the claim, in place of the one who withdrew, has not yet taken place.

In the opinion of the Management of the Bank, based on the opinion of management of Leumi Mortgage Bank, which is based on the opinion of its legal advisors, it is not possible at this stage to estimate the chances of the appeals.

- B. On 19 August 2007, a petition to approve a class action was filed in the Jerusalem District Court against Leumi Mortgage Bank, together with a statement of class action claim regarding the joining of an "additional borrower" to some of the loans granted by Leumi Mortgage Bank. The amount of the class action is estimated, according to the petitioners, at over NIS 5 million.

The petitioners are claiming that Leumi Mortgage Bank demanded the joining of an "additional borrower" within the framework of a loan taken out. According to the petitioners, the additional borrower is not a borrower at all but a fiction and in fact he is a guarantor of the loan. The petitioners claim that, if the person joined as an "additional borrower" was actually joined as a guarantor of the loan, he would not have been required to take out life insurance for the purposes of the loan, as he was required to do in practice.

The petitioners are requesting the approval of a class action on behalf of all people who were classified as "additional borrowers" by Leumi Mortgage Bank, who have no rights to the pledged property and who, in connection with the



loan, were required to take out life insurance and pay insurance premiums in respect thereof, either directly or through the principal borrowers, during the seven years prior to the filing of the petition.

The petitioners are requesting the reimbursement of insurance premiums that were paid as mentioned, and an order instructing Leumi Mortgage Bank to cancel the requirement to take out life insurance, and the pledging thereof with regard to the additional borrowers who are members of the group.

With the consent of the class action plaintiff, it was agreed that the date for Leumi Mortgage Bank's submission of its response to the petition would be deferred until a decision is rendered in another case which deals with a similar issue. The decision has not been rendered yet.

In the opinion of the Management of the Bank, based on the opinion of management of Leumi Mortgage Bank, which is based on the opinion of its legal advisors, it is not possible at this early stage to estimate the chances of the claim.

5. The following is a description of petitions for approval of class actions that have been submitted against the Bank Leumi le-Israel Trust Company (the "Trust Company"), as will be described below. In the opinion of the Bank's Management, which is based on the opinion of the Trust Company's legal advisors, it is not possible at this early stage to estimate the chances of these petitions, and for this reason, no provision was made for them.
  - A. On 5 April 2009, a petition for approval of a class action was filed with the Tel Aviv-Jaffa District Court against Standard & Poor's Ma'alot Ltd., World Currencies Ltd., the Bank Leumi le-Israel Trust Company, Eran Fuchs, Rony Biram, Yaakov Harpaz and Excellence Investments Ltd. The amount claimed against all the respondents in the class action stands at NIS 84 million. The complaint makes no clear attribution of a specific claimed amount against any of the respondents. According to the petitioner, Ma'alot failed in its rating of debentures issued by World Currencies Ltd., in that it reduced the rating of the debentures from AAA to D only after the Lehman Group's insolvency, despite information regarding the Lehman Group's difficulties that had been publicized previously, and that Ma'alot created a false and misleading representation to the debenture-holders, to the effect that there was no change in the level of the debentures' risk and/or that the deterioration of the Lehman Group's condition was not relevant to the level of the debentures' risk. The petition alleged that World Currencies was required to report to the debenture-holders regarding the financial entity backers and the mechanism according to which the Notes' risks were divided amongst them. It further alleged that World Currencies should have reported to the debenture-holders regarding the implications of the Lehman Group's deterioration with respect to the chances that the debentures would be repaid, and regarding the fact that the Lehman Bank was in significant business difficulty. It was further claimed that World Currencies unlawfully refrained from publishing immediate reports regarding these matters, and that as a result the debenture-holders suffered massive damage. Excellence is a shareholder and a controlling shareholder of World Currencies. Regarding the Trust Company, which served as the trustee for the holders of the debentures issued by World Currencies, the petitioner alleges that it did not do all that it could in order to ensure the fulfilment of World Currencies' obligations to the debenture-holders as established in the prospectus, because it should have requested that World Currencies inform the debenture-holder public regarding the identity of the financial entities with which World Currencies had contracted regarding the

purchase of the Notes and the mechanism according to which the risks were divided amongst them, and that it should have demanded that World Currencies provide information regarding consequences of the Lehman Group's condition for the rating of the debentures and/or regarding the ability of World Currencies to repay the debentures. The petitioner further alleges that once the Trust Company became aware of the difficulties that the Lehman Bank was encountering, it should have demanded of World Currencies that it replace the Notes with Notes of other financial entities, in order to reduce the scope of the damage caused to the debenture-holders.

In the opinion of the Bank's Management, on the basis of the opinion of the management of the Trust Company, which is based on the opinion of the Trust Company's legal advisors, it is not possible at this early stage to estimate the chances of the petition.

- B. On 23 June 2009, a petition for approval of a class action was filed with the Tel Aviv-Jaffa District Court against Standard & Poors Ma'alot Ltd., Keshet Debentures Ltd. ("Keshet"), Bank Leumi le-Israel Trust Company, Aaron Biram, Eran Fuchs, Moti Ma'aravi, Rami Ordan, Excellence Nashua Underwriting (1993) Ltd. and Express Finances Ltd. The amount claimed against all the respondents in the class action stands at NIS 220 million. The complaint makes no clear attribution of a specific claimed amount against any of the respondents. According to the petitioner, Ma'alot failed in its rating of the debentures issued by Keshet, in that it reduced the rating of the debentures from AA+ to D only after the Lehman Group's insolvency despite information regarding the Lehman Group's difficulties that had been publicized previously, and that Ma'alot created a false and misleading representation to the debenture-holders, to the effect that there was no change in the level of the debentures' risk and/or that the deterioration of the Lehman Group's condition was not relevant to the level of the debentures' risk. The petition alleged that Keshet was required to report to the debenture-holders regarding the implications of the Lehman Group's business deterioration with respect to the chances that the debentures would be repaid, and regarding the fact that the Lehman Bank was in significant business difficulty. It was further alleged that Keshet should have published an immediate report regarding the absolute dependence on the income from the Notes backing the debentures and regarding the significant danger concerning its ability to make payments with respect to the debentures. It was further claimed that Keshet was negligent to the point of being in breach of trust in failing to take measures to prevent a failure to pay the debenture holders, including in failing to do the following: take measures to replace the Notes that backed the debentures; requesting that Ma'alot update and/or adjust and/or change the debentures' rating. It was further alleged that Keshet failed in not insuring the deposits and in issuing debentures that were backed in full by the assets of only one bank. In addition, it was alleged that Keshet significantly reduced the scope of its assets through a significant change in the service agreement between it and Excellence Investments (which controls Excellence Nessuah). Excellence Nessuah Underwriting (1993) Ltd. and Express Financing Ltd. are the owners, in equal parts, of Keshet. Regarding the Trust Company, which served as the trustee for the holders of the debentures issued by Keshet, the petitioner alleges that it did not do all that it could in order to ensure the fulfilment of Keshet's obligations to the debenture-holders as established in the prospectus, because it should have asked Keshet to inform the debenture-holder public regarding the implications of the Lehman Bank's deterioration for the debentures' rating and/or for the company's ability to repay the debentures at the time set for their repayment. The petitioner further alleges that once the Trust Company became aware of the difficulties that the Lehman Bank was encountering, it should have demanded that Keshet replace the

Notes with Notes of other financial entities, in order to reduce the scope of the damage caused to the debenture-holders. It is further alleged that the Trust Company should have requested that Keshet insure the deposits, for the purpose of insuring the funds that the public had effectively invested in the Lehman Bank.

In the opinion of the Bank's Management, on the basis of the opinion of the management of the Trust Company, which is based on the opinion of the Trust Company's legal advisors, it is not possible at this early stage to estimate the chances of the petition.

#### **D. Paz Oil Company Ltd**

1. Legal claims have been made against Paz Oil Company Ltd. ("Paz") and its consolidated companies, including class actions, and there are legal proceedings concerning supervision by governmental authorities and other pending matters relating to the fuel and gas markets and infrastructure installations. With regard to these claims, in the estimation of Paz, based on opinions of its legal, professional and other advisors, it is not possible to estimate at this stage the effect, if any, of such on the financial statements, and therefore no provision has been made in respect thereof.

For further details of these proceedings, see the Paz financial statements as at 30 September 2009.

2. In a letter dated 3 July 2007, the Bank of Israel notified the Bank that Paz is considered to be a conglomerate, as detailed in Note 11 A below.

#### **E. The Israel Corporation Ltd.**

1. Legal claims been made against certain consolidated companies of the Israel Corporation Ltd. contending that personal and property damage caused to the plaintiffs resulted from the pollution of the Kishon River. The plaintiffs contend that the above-mentioned consolidated companies had a part in this process. Claims have also been made regarding the demand of the Ministry of Environmental Protection that they bear the costs of removing polluting sediments from the Kishon River.

The managements of the above companies, based on the opinions of their legal advisers, cannot estimate the amount of the exposure from the said claims and demand, if any, and therefore no provision has been made in this regard in the financial statements of the Israel Corporation Ltd. and of its consolidated companies.

2. A consolidated subsidiary of the Israel Corporation is dependant on receiving services from infrastructure companies in order to carry on its activities.
3. A consolidated subsidiary of the Israel Corporation Ltd., Zim Integrated Shipping Services Ltd. ("Zim") has a deficit in its working capital as at 30 September 2009, which mainly resulted from a classification of short term liabilities due to the failure to comply with financial standards set in the loan agreements. The Israel Corporation Ltd.'s financial statements include details of the understandings and agreements reached with creditors, suppliers and service providers, as well as with the shareholders, before and after the balance sheet date (and to some extent, even signed in a binding manner before the publication of these financial statements). These agreements and

understandings mainly lay down the deferment, waiver and/or payment plan for the debts, as well as the transfer of capital by the shareholders, and which, in the opinion of the management and board of directors of Zim, will allow Zim to finance its activities and to comply with its commitments during the twelve months from the balance sheet date.

For further details of these matters, see the Israel Corporation Ltd.'s financial statements as at 30 September 2009.

- F.** On 26 April 2009, a ruling of the Antitrust General Director was received at the Bank pursuant to section 43(a)(1) of the Antitrust Law, 1988, according to which restrictive trade agreements, relating to the transfer of information regarding commissions, had existed between the Bank, Bank Hapoalim B.M., Israel Discount Bank Ltd., Mizrahi Tefahot Bank Ltd. and the First International Bank of Israel Ltd., during the period from the beginning of the 1990s until the commencement of the Antitrust Authority's investigation of the matter, in November 2004. This is a civil ruling, which constitutes *prima facie* evidence of the matters therein determined in any legal proceedings. The Bank has decided to appeal the ruling in the Antitrust Tribunal. At this early stage, the effects of the ruling cannot be assessed.

## Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates

### Reported Amounts (Unaudited)

#### A. Scope of Activity

|   | 30 September 2009  |         |                            |                                |                                       |
|---|--------------------|---------|----------------------------|--------------------------------|---------------------------------------|
|   | Interest contracts |         | Foreign currency contracts | Contracts in respect of shares | Contracts respect of goods and Others |
|   | Shekel – index     | Other   |                            |                                |                                       |
|   | (NIS millions)     |         |                            |                                |                                       |
| <b>(1) Amount of derivative instruments</b>                             |                    |         |                            |                                |                                       |
| a) Hedged instruments (1)   |                    |         |                            |                                |                                       |
| Forward contracts   | -                  | -       | -                          | -                              | -                                     |
| Swaps   | -                  | 1,289   | -                          | -                              | -                                     |
| Total   | -                  | 1,289   | -                          | -                              | -                                     |
| Of which: Swap contracts in which the banking institution agreed to pay |                    |         |                            |                                |                                       |
| a fixed rate of interest  | -                  | 745     | -                          | -                              | -                                     |
| b) ALM derivatives (1)(2)   |                    |         |                            |                                |                                       |
| Futures contracts   | -                  | 6,815   | -                          | 309                            | 127                                   |
| Forward contracts   | 10,063             | 15,729  | 90,183                     | -                              | 701                                   |
| Traded options  |                    |         |                            |                                |                                       |
| Put options   | -                  | 162     | 4,432                      | 7,138                          | 32                                    |
| Call options  | -                  | 163     | 4,875                      | 7,138                          | 39                                    |
| Put options   | 41                 | 20,542  | 22,823                     | 653                            | 41                                    |
| Call options  | -                  | 17,632  | 23,144                     | 800                            | 41                                    |
| Swaps   | 1,369              | 104,696 | 11,901                     | -                              | -                                     |
| Total   | 11,473             | 165,739 | 157,358                    | 16,038                         | 981                                   |
| Of which: Swap contracts in which the banking institution agreed to     |                    |         |                            |                                |                                       |
| pay a fixed rate of interest  | -                  | 53,797  | -                          | -                              | -                                     |
| c) Other derivatives (1)  |                    |         |                            |                                |                                       |
| Swaps   | -                  | -       | -                          | -                              | -                                     |
| Total   | -                  | -       | -                          | -                              | -                                     |
| d) Credit derivatives and Spot contracts                                |                    |         |                            |                                |                                       |
| Credit derivatives in which the banking institution is a guarantor      |                    |         |                            |                                |                                       |
|   | -                  | -       | -                          | -                              | 827                                   |
| Credit derivatives in which the banking institution is a beneficiary    |                    |         |                            |                                |                                       |
|   | -                  | -       | -                          | -                              | -                                     |
| Spot contracts  | -                  | -       | 11,926                     | -                              | -                                     |
| Total   | -                  | -       | 11,926                     | -                              | 827                                   |
| Overall total   | 11,473             | 167,028 | 169,284                    | 16,038                         | 1,808                                 |

(1) Except credit derivatives and Spot contracts.

(2) Derivatives constituting part of the Bank's system of management of assets and liabilities, not intended for hedging.

**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)**  
**Reported Amounts (Unaudited)**

|   | 30 September 2009                |       |                                  |                                      |  |
|---|----------------------------------|-------|----------------------------------|--------------------------------------|--|
|   | Interest contracts               |       | Foreign<br>currency<br>contracts | Contracts<br>in respect of<br>shares | Contracts<br>respect of<br>goods and<br>Others |
|   | Shekel – index<br>(NIS millions) | Other |                                  |                                      |  |
| <b>(2) Gross fair value of derivative instruments</b>                 |                                  |       |                                  |                                      |  |
| a) Hedged derivatives (1)   |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | 36    | -                                | -                                    | -  |
| Gross negative fair value   | -                                | 27    | -                                | -                                    | -  |
| b) ALM derivatives (1)(2)   |                                  |       |                                  |                                      |  |
| Gross positive fair value   | 54                               | 3,372 | 3,043                            | 315                                  | 25   |
| Gross negative fair value   | 470                              | 3,190 | 4,398                            | 308                                  | 24   |
| c) Other derivatives (1)  |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | -     | -                                | -                                    | -  |
| Gross negative fair value   | -                                | -     | -                                | -                                    | -  |
| d) Credit derivatives   |                                  |       |                                  |                                      |  |
| Credit derivatives in which the<br>banking institution is a guarantor |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | -     | -                                | -                                    | -  |
| Gross negative fair value   | -                                | -     | -                                | -                                    | 1  |

(1) Except credit derivatives.

(2) Derivatives constituting part of the Bank's system of management of assets and liabilities, not intended for hedging.

**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)**  
**Reported Amounts (Unaudited)**

|   | 30 September 2008  |            |                            |                                |                                       |
|---|--------------------|------------|----------------------------|--------------------------------|---------------------------------------|
|   | Interest contracts |            | Foreign currency contracts | Contracts in respect of shares | Contracts respect of goods and Others |
|   | Shekel – index     | Other      |                            |                                |                                       |
|   | (NIS millions)     |            |                            |                                |                                       |
| <b>(1) Amount of derivative instruments</b>                             |                    |            |                            |                                |                                       |
| a) Hedged instruments (1)   | -                  | -          | -                          | -                              | 16                                    |
| Swaps   | -                  | 1,547      | 21                         | -                              | -                                     |
| Total   | -                  | 1,547      | 21                         | -                              | 16                                    |
| Of which: Swap contracts in which the banking institution agreed to pay |                    |            |                            |                                |                                       |
| a fixed rate of interest  | -                  | 682 (a)    | -                          | -                              | -                                     |
| b) ALM derivatives (1)(2)   |                    |            |                            |                                |                                       |
| Futures contracts   | 18                 | 5,439      | -                          | 37                             | 56                                    |
| Forward contracts   | 9,384              | 20,314     | 84,694                     | -                              | 1,256                                 |
| Traded options  |                    |            |                            |                                |                                       |
| Put options   | -                  | 3,096      | 4,748                      | 7,250                          | 123                                   |
| Call options  | -                  | 3,096      | 5,604                      | 7,250                          | 123                                   |
| Other options   |                    |            |                            |                                |                                       |
| Put options   | 52                 | 21,151     | 46,636                     | 1,330                          | -                                     |
| Call options  | 20                 | 18,328     | 42,888                     | 1,601                          | -                                     |
| Swaps   | 1,295              | 62,075     | 11,392                     | -                              | -                                     |
| Total   | 10,769             | 133,499    | 195,962                    | 17,468                         | 1,558                                 |
| Of which: Swap contracts in which the banking institution agreed to     |                    |            |                            |                                |                                       |
| pay a fixed rate of interest  | -                  | 30,371 (a) | -                          | -                              | -                                     |
| c) Other derivatives (1)  |                    |            |                            |                                |                                       |
| Swaps   | -                  | -          | -                          | -                              | -                                     |
| Total   | -                  | -          | -                          | -                              | -                                     |
| d) Credit derivatives and Spot contracts                                |                    |            |                            |                                |                                       |
| Credit derivatives in which the banking institution is a guarantor      | -                  | -          | -                          | -                              | 434                                   |
| Spot contracts  | -                  | -          | 7,811                      | -                              | -                                     |
| Total   | -                  | -          | 7,811                      | -                              | 434                                   |
| Overall total   | 10,769             | 135,046    | 203,794                    | 17,468                         | 2,008                                 |

(a) Reclassified

(1) Except credit derivatives and Spot contracts.

(2) Derivatives constituting part of the Bank's system of management of assets and liabilities, not intended for hedging.

**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)**  
**Reported Amounts (Unaudited)**

|   | 30 September 2008                |       |                                  |                                      |  |
|---|----------------------------------|-------|----------------------------------|--------------------------------------|--|
|   | Interest contracts               |       | Foreign<br>currency<br>contracts | Contracts<br>in respect of<br>shares | Contracts<br>respect of<br>goods and<br>Others |
|   | Shekel – index<br>(NIS millions) | Other |                                  |                                      |  |
| (2) Gross fair value of derivative instruments                        |                                  |       |                                  |                                      |  |
| a) Hedged derivatives (1)   |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | 55    | -                                | -                                    | 16   |
| Gross negative fair value   | -                                | 22    | 14                               | -                                    | 16   |
| b) ALM derivatives (1)(2)   |                                  |       |                                  |                                      |  |
| Gross positive fair value   | 66                               | 1,832 | 3,680                            | 384                                  | 63   |
| Gross negative fair value   | 286                              | 1,798 | 4,182                            | 393                                  | 62   |
| c) Other derivatives (1)  |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | -     | -                                | -                                    | -  |
| Gross negative fair value   | -                                | -     | -                                | -                                    | -  |
| d) Credit derivatives   |                                  |       |                                  |                                      |  |
| Credit derivatives in which the<br>banking institution is a guarantor |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | -     | -                                | -                                    | -  |
| Gross negative fair value   | -                                | -     | -                                | -                                    | 111  |

(1) Except credit derivatives.

(2) Derivatives constituting part of the Bank's system of management of assets and liabilities, not intended for hedging.



**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)**  
**Reported Amounts (Audited)**

|  | 31 December 2008                 |            |                                  |                                      |  |
|--|----------------------------------|------------|----------------------------------|--------------------------------------|--|
|  | Interest contracts               |            | Foreign<br>currency<br>contracts | Contracts<br>in respect of<br>shares | Contracts<br>respect of<br>goods and<br>Others |
|  | Shekel – index<br>(NIS millions) | Other      |                                  |                                      |  |
| (1) Amount of derivative instruments   |                                  |            |                                  |                                      |  |
| a) Hedged instruments (1)  |                                  |            |                                  |                                      |  |
| Swaps  | -                                | 1,490      | 24                               | -                                    | -  |
| Total  | -                                | 1,490      | 24                               | -                                    | -  |
| Of which: Swap contracts in which the<br>banking institution agreed to pay<br>a fixed rate of interest |                                  |            |                                  |                                      |  |
|  | -                                | 792        | -                                | -                                    | -  |
| b) ALM derivatives (1)(2)  |                                  |            |                                  |                                      |  |
| Futures contracts  | 6                                | 21,637     | -                                | 41                                   | 66   |
| Forward contracts  | 11,223                           | 15,678     | 85,754 (a)                       | -                                    | 949  |
| Traded options   |                                  |            |                                  |                                      |  |
| Put options  | -                                | 2          | 8,847                            | 4,891                                | 265  |
| Call options   | -                                | 1          | 10,296                           | 4,891                                | 265  |
| Other options  |                                  |            |                                  |                                      |  |
| Put options  | 57                               | 16,176     | 32,384                           | 1,179                                | -  |
| Call options   | 20                               | 13,421     | 31,533                           | 1,403                                | -  |
| Swaps  | 1,395                            | 80,052     | 8,810                            | -                                    | -  |
| Total  | 12,701                           | 146,967    | 177,624                          | 12,405                               | 1,545  |
| Of which: Swap contracts in which the<br>banking institution agreed to<br>pay a fixed rate of interest |                                  |            |                                  |                                      |  |
|  | -                                | 38,505 (a) | -                                | -                                    | -  |
| c) Other derivatives (1)   |                                  |            |                                  |                                      |  |
| Swaps  | -                                | -          | -                                | -                                    | -  |
| Total  | -                                | -          | -                                | -                                    | -  |
| d) Credit derivatives and Spot contracts   |                                  |            |                                  |                                      |  |
| Credit derivatives in which the<br>banking institution is a guarantor                                  |                                  |            |                                  |                                      |  |
|  | -                                | -          | -                                | -                                    | 247  |
| Spot contracts   | -                                | -          | 7,511                            | -                                    | -  |
| Total  | -                                | -          | 7,511                            | -                                    | 247  |
| Overall total  | 12,701                           | 148,457    | 185,159                          | 12,405                               | 1,792  |

(a) Reclassified

(1) Except credit derivatives and Spot contracts.

(2) Derivatives constituting part of the Bank's system of management of assets and liabilities, not intended for hedging.

**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)**  
**Reported Amounts (Audited)**

|   | 31 December 2008                 |       |                                  |                                      |  |
|---|----------------------------------|-------|----------------------------------|--------------------------------------|--|
|   | Interest contracts               |       | Foreign<br>currency<br>contracts | Contracts<br>in respect of<br>shares | Contracts<br>respect of<br>goods and<br>Others |
|   | Shekel – index<br>(NIS millions) | Other |                                  |                                      |  |
| (2) Gross fair value of derivative instruments                        |                                  |       |                                  |                                      |  |
|   |                                  |       |                                  |                                      |  |
| a) Hedged derivatives (1)   |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | 75    | -                                | -                                    | -  |
| Gross negative fair value   | -                                | 44    | 16                               | -                                    | -  |
| b) ALM derivatives (1)(2)   |                                  |       |                                  |                                      |  |
| Gross positive fair value   | 180                              | 3,396 | 6,050                            | 280                                  | 66   |
| Gross negative fair value   | 214                              | 3,438 | 6,535                            | 277                                  | 66   |
| c) Other derivatives (1)  |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | -     | -                                | -                                    | -  |
| Gross negative fair value   | -                                | -     | -                                | -                                    | -  |
| d) Credit derivatives   |                                  |       |                                  |                                      |  |
| Credit derivatives in which the<br>banking institution is a guarantor |                                  |       |                                  |                                      |  |
| Gross positive fair value   | -                                | -     | -                                | -                                    | -  |
| Gross negative fair value   | -                                | -     | -                                | -                                    | 10   |

(1) Except credit derivatives.

(2) Derivatives constituting part of the Bank's system of management of assets and liabilities, not intended for hedging.

**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)**  
**Reported Amounts**

**B. Credit Risk in Respect of Derivative Instruments According to Other Party of the Contract**

|  | 30 September 2009 (Unaudited) |            |                  |                               |        |        |
|--|-------------------------------|------------|------------------|-------------------------------|--------|--------|
|  | Stock Exchanges               | Banks      | Dealers/ brokers | Governments and central banks | Others | Total  |
|  | (NIS millions)                |            |                  |                               |        |        |
| Balance sheet balances of assets derived from derivative instruments (1) (2) | 232                           | 3,843      | -                | -                             | 2,770  | 6,845  |
| Off-balance sheet credit risk in respect of derivative Instruments (3)       | 865                           | 17,826     | 4                | -                             | 9,525  | 28,220 |
| Total credit risk in respect of derivative instruments                       | 1,097                         | 21,669     | 4                | -                             | 12,295 | 35,065 |
|  | 30 September 2008 (Unaudited) |            |                  |                               |        |        |
|  | Stock Exchanges               | Banks      | Dealers/ brokers | Governments and central banks | Others | Total  |
|  | (NIS millions)                |            |                  |                               |        |        |
| Balance sheet balances of assets derived from derivative instruments (1) (2) | 385                           | 2,711      | 26               | -                             | 2,974  | 6,096  |
| Off-balance sheet credit risk in respect of derivative Instruments (3)       | 1,395                         | 14,961     | 506              | 3                             | 8,239  | 25,104 |
| Total credit risk in respect of derivative instruments                       | 1,780                         | 17,672     | 532              | 3                             | 11,213 | 31,200 |
|  | 31 December 2008 (Audited)    |            |                  |                               |        |        |
|  | Stock Exchanges               | Banks      | Dealers/ brokers | Governments and central banks | Others | Total  |
|  | (NIS millions)                |            |                  |                               |        |        |
| Balance sheet balances of assets derived from derivative instruments (1) (2) | 653                           | 5,058      | 18               | 1                             | 4,317  | 10,047 |
| Off-balance sheet credit risk in respect of derivative Instruments (3)       | 2,463                         | 15,955 (a) | 207              | 2                             | 6,813  | 25,440 |
| Total credit risk in respect of derivative instruments                       | 3,116                         | 21,013     | 225              | 3                             | 11,130 | 35,487 |

1) Net accounting arrangements do not exist.

(2) Of which, balance sheet balance from derivative instruments which are stand alone – NIS 6,845 million (30 September 2008 – NIS 6,096 million, 31 December 2008 – NIS 10,047 million), that is included in other assets

(3) Off-balance credit risk of derivative instruments (including derivative instruments with negative fair value) as was calculated for purposes of per borrower debt limitations.

**Note 7 – Activity in Derivatives – Scope, Credit Risks and Repayment Dates (cont'd)****Reported Amounts****c. Repayment Dates – Nominal Amounts**

|   | <b>30 September 2009 (Unaudited)</b> |                                |                      |                         |                |
|---|--------------------------------------|--------------------------------|----------------------|-------------------------|----------------|
|   | Up to three<br>Months                | three<br>months to<br>one year | one<br>five<br>years | More than<br>five years | Total          |
|   | (NIS millions)                       |                                |                      |                         |                |
| <b>Interest (Swap) contracts:</b>                 |                                      |                                |                      |                         |                |
| Shekel – index                                    | <b>3,201</b>                         | <b>3,714</b>                   | <b>2,786</b>         | <b>1,772</b>            | <b>11,473</b>  |
| Other   | <b>26,646</b>                        | <b>48,661</b>                  | <b>55,826</b>        | <b>35,895</b>           | <b>167,028</b> |
| Foreign currency contracts                        | <b>104,049</b>                       | <b>51,416</b>                  | <b>6,062</b>         | <b>7,757</b>            | <b>169,284</b> |
| Contracts in respect of shares                    | <b>13,969</b>                        | <b>1,516</b>                   | <b>553</b>           | <b>-</b>                | <b>16,038</b>  |
| Contracts in respect of<br>commodities and others | <b>603</b>                           | <b>1,086</b>                   | <b>31</b>            | <b>88</b>               | <b>1,808</b>   |
| <b>Total</b>                                      | <b>148,468</b>                       | <b>106,393</b>                 | <b>65,258</b>        | <b>45,512</b>           | <b>365,631</b> |
|   | <b>-</b>                             | <b>-</b>                       | <b>-</b>             | <b>-</b>                | <b>-</b>       |
| 31 September 2008 (Unaudited)                     | 169,465                              | 112,272                        | 48,630               | 38,718                  | 369,085        |
| 31 December 2008 (Audited)                        | 186,690 (a)                          | 81,748                         | 48,776               | 43,300                  | 360,514        |

(a) Reclassified

**Note 8 – Net Interest Income Before Provision for Doubtful Debts**  
**Reported amounts (Unaudited)**

|  | For the three months ended<br>30 September |         | For the nine months ended<br>30 September |         |
|--|--|---------|---|---------|
|  | 2009                                       | 2008    | 2009                                      | 2008    |
|  | (NIS millions)                             |         |   |         |
| <b>A. Income on assets (a)</b>   |  |         |   |         |
| Credit to the public   | 1,392                                      | 3,879   | 8,756                                     | 4,382   |
| Credit to governments  | 2  | 19      | 26  | (9)     |
| Deposits with Bank of Israel and cash  | (107)                                      | 35      | 86  | (101)   |
| Deposits with banks  | (116)                                      | 502     | 811                                       | (2,492) |
| Securities borrowed or purchased under agreement to resell   | (1)  | 11      | 4   | 18      |
| Debentures   | (268)                                      | 249     | 1,333                                     | (1,651) |
| Total income on assets   | 902  | 4,695   | 11,016                                    | 147     |
| <b>B. Expenses on liabilities (a)</b>  |  |         |   |         |
| Deposits of the public   | 2,284                                      | (1,969) | (4,049)                                   | 6,983   |
| Deposits from governments  | (14)                                       | (25)    | (38)                                      | (23)    |
| Deposits from Bank of Israel   | -  | (15)    | 1   | (53)    |
| Deposits from banks  | (213)                                      | (153)   | (231)                                     | (161)   |
| Securities loaned or sold under agreement to repurchase  | 4  | (12)    | (7)                                       | (5)     |
| Debentures, bonds and subordinated notes   | (671)                                      | (653)   | (1,434)                                   | (1,287) |
| Total expense on liabilities   | 1,390                                      | (2,827) | (5,758)                                   | 5,454   |
| <b>C. From derivative instruments and hedging activities</b>   |  |         |   |         |
| Ineffective portion of hedge relationships (b)   | -  | (2)     | -   | 3       |
| Net income (expenses) from ALM derivative instruments (c)  | (773)                                      | 43      | (1,237)                                   | (343)   |
| Net income (expenses) from other derivative instruments  | 20   | (107)   | 13  | (129)   |
| Total income from derivative instruments and hedging activities                                      | (753)                                      | (66)    | (1,224)                                   | (469)   |
| <b>D. Other income and expenses</b>  |  |         |   |         |
| Financing commissions  | 89   | 97      | 256                                       | 252     |
| Profits (losses) from sale of debentures available for sale, net (e)                                 | 120  | (456)   | 295                                       | (508)   |
| Losses realized and not yet realized in respect of fair value adjustments of trading debentures, net | 60   | (135)   | 221                                       | (65)    |
| Other financing income (expenses)  | 103  | 244     | 372                                       | 669     |
| Other financing income (expenses)  | 12   | (61)    | 33  | (76)    |
| Total other income and expenses  | 384  | (311)   | 1,177                                     | 272     |
| Total net interest income before provision for doubtful debts  | 1,923                                      | 1,491   | 5,211                                     | 5,404   |
| Of which: net, exchange difference   | (1)  | 33      | (71)                                      | 60      |
| <b>E. Detail of net effect of hedging derivative instruments on net interest income</b>              |  |         |   |         |
| Financing income (expenses) on assets  | (2)  | -       | 1   | (2)     |
| Financing income (expenses) on liabilities   | 4  | 8       | 2   | 8       |

(a) Including effective portion of hedge relationships.

(b) Excluding effective portion of hedge relationships.

(c) Derivative instruments that are included in the Bank's asset and liability management system which are not designated for hedging relationships.

(d) Including negative interest and exchange difference in respect of mortgage-backed bonds (MBS) in the amount of about NIS 5 million (30 September 2008 – NIS 350 million).

(e) Including provision for decline in value that was not temporary in nature.

**Note 9 – Profits (losses) from Investments in Shares (a), Net  
Reported amounts (Unaudited)**

|   | For the three months ended<br>30 September |       | For the Nine months ended<br>30 September |       |
|---|--|-------|---|-------|
|   | 2009                                       | 2008  | 2009                                      | 2008  |
|   | (NIS millions)                             |       | (NIS millions)                            |       |
| Gains on sale of shares available for sale                | 281  | 97    | 402                                       | 106   |
| Profits (losses) on sale of shares available for sale (b) | (2)  | (122) | (12)                                      | (225) |
| Realized and unrealized losses from adjustments           |  |       |   |       |
| to fair value of held for trading shares, net             | (1)  | (350) | 6   | (444) |
| Dividend on shares available for sale                     |  |       |   |       |
| and on held for trading shares                            | 8  | 12    | 75  | 85    |
| Total from investments on shares                          | 286  | (363) | 471                                       | (478) |

(a) Including mutual funds.

(b) Including provision for decline in value that was not temporary in nature.

**Note 10 - Information on activity by banking sectors (cont'd)**  
Reported amounts

| Statement of profit and loss for the Three Months Ended 30 September 2009 (Unaudited) |                      |                     |                      |                       |                    |                                  |                       |
|---|----------------------|---------------------|----------------------|-----------------------|--------------------|----------------------------------|-----------------------|
|   | Small                |                     |                      |                       |                    |                                  |                       |
|   | Household<br>banking | business<br>banking | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Financial<br>management<br>Other | Total<br>consolidated |
| (NIS millions)  |                      |                     |                      |                       |                    |                                  |                       |
| Net interest income (loss) before<br>provision for doubtful debts                     |                      |                     |                      |                       |                    |                                  |                       |
| From outside entities -   | 227                  | 280                 | 1,111                | 495                   | (50)               | (142)                            | 2 1,923               |
| Intercompany operations -   | 290                  | (76)                | (624)                | (154)                 | 183                | 384                              | (3) -                 |
| Total   | 517                  | 204                 | 487                  | 341                   | 133                | 242                              | (1) 1,923             |
| Operating and other income:   |                      |                     |                      |                       |                    |                                  |                       |
| From outside entities -   | 437                  | 131                 | 361                  | 112                   | 109                | 121                              | 21 1,292              |
| Intercompany operations -   | 62                   | (27)                | (16)                 | (14)                  | 6                  | -                                | (11) -                |
| Total   | 499                  | 104                 | 345                  | 98                    | 115                | 121                              | 10 1,292              |
| Total income  | 1,016                | 308                 | 832                  | 439                   | 248                | 363                              | 9 3,215               |
| Provision for doubtful debts  | 75                   | 63                  | 198                  | 117                   | 1                  | (11)                             | - 443                 |
| Net profit (loss)   | 97                   | 37                  | 314                  | 54                    | 54                 | 75                               | (97) 534              |

**Note 10 - Information on activity by banking sectors (cont'd)**  
Reported amounts

| Statement of profit and loss for the Three Months Ended 30 September 2008 (Unaudited) (a) |                   |                  |                   |                    |                 |                      |                    |
|---|-------------------|------------------|-------------------|--------------------|-----------------|----------------------|--------------------|
|   | Small             |                  |                   |                    |                 |                      |                    |
|   | Household banking | business banking | Corporate banking | Commercial banking | Private banking | Financial management | Total consolidated |
| (NIS millions)  |                   |                  |                   |                    |                 |                      |                    |
| <b>Net interest income (loss) before provision for doubtful debt:</b>                     |                   |                  |                   |                    |                 |                      |                    |
| From outside entities -   | 100               | 324              | 1,104             | 420                | (192)           | (265)                | - 1,491            |
| Intercompany operations -   | 593               | (96)             | (663)             | (64)               | 222             | 5                    | 3 -                |
| Total   | 693               | 228              | 441               | 356                | 30              | (260)                | 3 1,491            |
| <b>Operating and other income:</b>  |                   |                  |                   |                    |                 |                      |                    |
| From outside entities -   | 423               | 103              | 101               | 96                 | 94              | (349)                | 72 540             |
| Intercompany operations -   | 77                | (5)              | (44)              | (8)                | 3               | 1                    | (24) -             |
| Total   | 500               | 98               | 57                | 88                 | 97              | (348)                | 48 540             |
| Total income  | 1,193             | 326              | 498               | 444                | 127             | (608)                | 51 2,031           |
| Provision for doubtful debts  | 97                | 43               | 258               | 49                 | -               | 31                   | 17 495             |
| After-tax profit(loss) from extraordinary items   | -                 | -                | -                 | -                  | -               | -                    | 1                  |
| Net profit (loss)   | 181               | 74               | 60                | 102                | (21)            | (484)                | 4 (84)             |

(a) Reclassified.



**Note 10 - Information on activity by banking sectors (cont'd)**  
Reported amounts

| Statement of profit and loss for the Nine Months Ended 30 September 2009 (audited) |                      |                      |                       |                    |                         |       |                       |
|--|----------------------|----------------------|-----------------------|--------------------|-------------------------|-------|-----------------------|
|  | Small                |                      |                       |                    |                         |       |                       |
|  | Household<br>banking | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Financial<br>management | Other | Total<br>consolidated |
|  | (NIS millions)       |                      |                       |                    |                         |       |                       |
| Net interest income (loss) before provision for doubtful debt:                     |                      |                      |                       |                    |                         |       |                       |
| From outside entities -  | 723                  | 780                  | 2,461                 | 1,355              | (169)                   | 59    | 2 5,211               |
| Intercompany operations -  | 846                  | (152)                | (1,031)               | (333)              | 609                     | 69    | (8) -                 |
| Total  | 1,569                | 628                  | 1,430                 | 1,022              | 440                     | 128   | (6) 5,211             |
| Operating and other income:  |                      |                      |                       |                    |                         |       |                       |
| From outside entities -  | 1,265                | 339                  | 609                   | 309                | 310                     | 396   | 80 3,308              |
| Intercompany operations -  | 173                  | (44)                 | (89)                  | (30)               | 13                      | 1     | (24) -                |
| Total  | 1,438                | 295                  | 520                   | 279                | 323                     | 397   | 56 3,308              |
| Total income   | 3,007                | 923                  | 1,950                 | 1,301              | 763                     | 525   | 50 8,519              |
| Provision for doubtful debts   | 207                  | 150                  | 511                   | 256                | 1                       | 11    | - 1,136               |
| After-tax profit from extraordinary items  | -                    | -                    | -                     | -                  | -                       | -     | 28                    |
| Net profit   | 205                  | 155                  | 667                   | 246                | 161                     | 123   | (87) 1,470            |

**Note 10 - Information on activity by banking sectors (cont'd)**  
**Reported amounts**

| Statement of profit and loss for the Nine Months Ended 30 September 2008 (audited) (a) |                      |                     |                      |                       |                    |                         |                       |
|--|----------------------|---------------------|----------------------|-----------------------|--------------------|-------------------------|-----------------------|
|  | Small                |                     |                      |                       |                    |                         |                       |
|  | Household<br>banking | business<br>banking | Corporate<br>banking | Commercial<br>banking | Private<br>banking | Financial<br>management | Total<br>consolidated |
| (NIS millions)   |                      |                     |                      |                       |                    |                         |                       |
| <b>Net interest income (expenses) before<br/>provision for doubtful debt:</b>          |                      |                     |                      |                       |                    |                         |                       |
| From outside entities -  | 138                  | 942                 | 2,987                | 1,611                 | (501)              | 227                     | - 5,404               |
| Intercompany operations -  | 1,840                | (264)               | (1,511)              | (484)                 | 744                | (290)                   | (35) -                |
| Total  | 1,978                | 678                 | 1,476                | 1,127                 | 243                | (63)                    | (35) 5,404            |
| <b>Operating and other income:</b>   |                      |                     |                      |                       |                    |                         |                       |
| From outside entities -  | 1,272                | 333                 | 249                  | 312                   | 291                | (342)                   | 140 2,255             |
| Intercompany operations -  | 200                  | (23)                | (121)                | (24)                  | 11                 | 2                       | (45) -                |
| Total  | 1,472                | 310                 | 128                  | 288                   | 302                | (340)                   | 95 2,255              |
| <b>Total income</b>  | 3,450                | 988                 | 1,604                | 1,415                 | 545                | (403)                   | 60 7,659              |
| Provision for doubtful debts   | 227                  | 76                  | 532                  | 207                   | (1)                | (3)                     | 17 1,055              |
| After-tax profit(loss) from<br>extraordinary items                                     | 202                  | 18                  | 2                    | 26                    | 3                  | (2)                     | - 249                 |
| Net profit (loss)  | 692                  | 276                 | 445                  | 374                   | 53                 | (541)                   | (24) 1,275            |

(a) Reclassified

**Note 10 - Information on activity by banking sectors (cont'd)**  
Reported amounts

| Statement of profit and loss for the Nine Months Ended 30 September 2008 (Unaudited) |                   |                  |                   |                    |                 |                      |                    |
|--|-------------------|------------------|-------------------|--------------------|-----------------|----------------------|--------------------|
|  | small             |                  |                   |                    |                 |                      |                    |
|  | Household banking | business banking | Corporate banking | Commercial banking | Private banking | Financial management | Other consolidated |
| (NIS millions)   |                   |                  |                   |                    |                 |                      |                    |
| <b>Net interest income (expenses) before provision for doubtful debt:</b>            |                   |                  |                   |                    |                 |                      |                    |
| From outside entities -  | 300               | 1,208            | 3,905             | 2,295              | (597)           | (732)                | 1 6,380            |
| Intercompany operations -  | 2,337             | (302)            | (2,022)           | (906)              | 959             | (51)                 | (15) -             |
| Total  | 2,637             | 906              | 1,883             | 1,389              | 362             | (783)                | (14) 6,380         |
| <b>Operating and other income:</b>   |                   |                  |                   |                    |                 |                      |                    |
| From outside entities -  | 1,689             | 434              | 335               | 402                | 397             | (624)                | 167 2,800          |
| Intercompany operations -  | 237               | (26)             | (164)             | (32)               | 15              | 2                    | (32) -             |
| Total  | 1,926             | 408              | 171               | 370                | 412             | (622)                | 135 2,800          |
| <b>Total income</b>  | 4,563             | 1,314            | 2,054             | 1,759              | 774             | (1,405)              | 121 9,180          |
| Provision for doubtful debts   | 340               | 182              | 1,070             | 485                | 10              | 58                   | - 2,145            |
| After-tax profit(loss) from extraordinary items                                      | 202               | 18               | 2                 | 26                 | 3               | -                    | (1) 250            |
| Net profit (loss)  | 818               | 253              | 296               | 272                | 113             | (1,469)              | (191) 92           |

## Note 11 – Miscellaneous Matters and Post Balance Sheet Events

### A. Holdings in Non-banking Holding Corporations (Conglomerates)

The Bank's holdings in non-banking corporations are subject to restrictions determined in the Banking (Licensing) Law, 1981 (the "Banking Law"). The Banking Law determines, *inter alia*, in section 24A that a banking corporation is entitled to hold means of control in only one conglomerate (a "non-banking holding corporation") (a corporation whose capital exceeds some NIS 1,901 million and operates in more than three branches of the economy). The Bank has holdings in one conglomerate - the Israel Corporation Ltd.

The financial statements of Paz for the first quarter of 2007, in which new accounting standards were implemented, indicate that the shareholders' equity of Paz exceeds the minimal amount of capital in the definition of a conglomerate (a non-banking holding corporation).

Prior to the publication of the said financial statements, discussions had already been held between the Bank and the Bank of Israel with regard to the interpretation of the Banking Law relating to the definition of Paz as a conglomerate. Further to these discussions, the Bank of Israel notified the Bank, in its letter of 3 July 2007, that it does not accept the Bank's interpretation that the energy sector constitutes one branch of the economy. Therefore, according to the Bank of Israel's position, Paz is a conglomerate under the Banking Law.

At the Bank's request, the Bank of Israel agreed that the sale of the Bank's holdings in Paz take place by 30 December 2010, subject to the Bank's holdings in Paz being transferred to a trustee. To this end, the Bank transferred its holdings to a trustee at the end of June 2009.

### B. Migdal Insurance and Financial Holdings Ltd.

The Bank holds 9.85% of the issued and fully paid share capital of Migdal Insurance and Financial Holdings Ltd. ("Migdal Holdings") (9.74%, fully diluted), the controlling shareholder of Migdal Insurance Company Ltd.

According to the Bank of Israel's interpretation of the Banking (Licensing) Law, with which the Bank disagrees, the Bank is also required to sell the holdings in Migdal Holdings, which, pursuant to the said law, is considered to be a conglomerate.

It should be noted that pursuant to legislation enacted following the capital market reform, a bank may hold 5% of the share capital of an insurance company, and 10% of the share capital of a corporation that controls an insurance company.

On 27 July 2009, the Knesset approved, in its first reading, a proposed law for the amendment of Section 24A of the Banking (Licensing) Law, pursuant to which, *inter alia*, a corporation which is an insurer operates in the insurance industry only, and is therefore not considered to be a conglomerate.

At the Bank's request, the Bank of Israel extended the permit issued to the Bank for the holding of the shares in Migdal, provided that the shares be transferred to a trustee. The shares were transferred to a trustee on 4 January 2009. Pursuant to the Bank of Israel directives, if the shares held by the trustee are not sold by 31 August 2010, the trustee will sell the shares to a third party by no later than 31 December 2010. The trustee was vested with all the rights that the shares confer (excluding the right to receive dividends and the rights vested with the Bank – the right to sell the shares to a third party or the right to distribute them as a dividend *in specie* up until 31 August 2010).

- C. On 12 February 2009, the employee options plan ended, at which time the 24,062,240 options that remained in circulation and which had not been exercised, expired.

**D. Union Bank**

On 17 November 2003, an agreement was signed between the Bank, Sherodar Assets Ltd. (“Sherodar”) and Yeshayu Landau Holdings (1993) Ltd. (“Landau”) for the extension of the put option and of the call option that were granted in an agreement dated 18 November 1999, in respect of the balance of the shares in Union Bank held by the Bank, for a period ending on 17 November 2010.

On 11 May 2009, the Bank gave Sherodar and Landau notice regarding the exercise of the put option.

The transaction was completed on 28 June 2009 and the Bank sold the said shares, constituting all of the Bank’s holdings in Union Bank, to Landau and Sherodar, in consideration of a total amount of some NIS 108 million. The Bank’s profit from the sale of the said shares is some NIS 17 million, net.

**E. Hot Cable Communications Systems Ltd.**

On 3 August 2009, the Bank sold 11,376,902 ordinary shares of Hot-Cable Communications Systems Ltd., which had been held by the Bank to Cool Holding Ltd. for a total consideration of NIS 381,126,210. The Bank’s after-tax profit from the sale is some NIS 115 million.

- F.** In accordance with the Supervisor of Banks’ July 2003 instructions, the classification of credit granted to a certain customer for the financing of the purchase of shares in Bezeq was changed from the credit to the public item to the securities item. On 10 August 2009, the customer’s receiver announced that he had completed a transaction for the sale of 155,000,000 ordinary shares of NIS 1 par value each in the company, constituting 5.849% of Bezeq’s share capital, and that the consideration, some NIS 1,137 million after deducting commissions and expenses, would be used to reduce the customer’s debts to the banks, in accordance with each bank’s share in the financing of the purchase of the Bezeq shares in 1999. The Bank’s share in this consideration, after deducting commissions and expenses, amounted to some NIS 272 million and the net profit amounted to some NIS 55 million.

After the balance sheet date, on 19 October 2009, the customer’s receiver announced that he had completed a transaction for the sale of 120,000,000 ordinary shares in the company of NIS 1 par value each, constituting 4.52% of Bezeq’s share capital, and that the consideration, some NIS 977 million after deducting commissions and expenses, would be used to reduce the customer’s debts to the banks, in accordance with each bank’s share in the financing of the purchase of the Bezeq shares in 1999. The Bank’s share in this consideration, after deducting commissions and expenses, amounted to some NIS 233 million and the net profit totaled some NIS 60 million.

On 9 November 2009, the customer’s receiver announced that he had completed a transaction for the sale of all the Bezeq shares owned by the customer. The total number of shares sold amounted to some 184,331,617 ordinary shares of NIS 1 par value each, constituting 6.94% of Bezeq’s share capital, and the consideration would amount to some NIS 1.5 billion. The Bank’s share in this consideration will amount to some NIS 242 million and the net profit to some NIS 27 million.

**G. Publication of a shelf prospectus**

On 27 August 2009, in accordance with a permit received from the Israel Securities Authority, the Bank published a shelf prospectus allowing it to issue up to 6 series of debentures (series 400 to 405), up to 11 series of subordinated capital notes (series 250 to 256 and series 300 to 303) and up to 6 series of subordinated capital notes (series 200 to 205). The maximum amount of debentures and capital notes which the Bank may issue under this shelf prospectus is NIS 4 billion par value of each of the above series. The prospectus will remain valid for two years from the date of its publication.

- H.** On 21 August 2009, the Bank signed an agreement with the Scailex Corporation Ltd. (“Scailex”) for the acquisition of 7,677,037 ordinary shares constituting 4.99% of the issued and paid-up share capital of Partner Communications Ltd. (on an undiluted basis and after neutralizing dormant shares), for a consideration of some NIS 515 million. The agreement includes standard minority protection rights and an option to purchase debentures convertible into Scailex shares in the amount of some NIS 103 million.

Leumi Partners Ltd. (a wholly owned subsidiary of the Bank) acted as an investment house in all aspects related to this transaction, including vis-à-vis additional potential investors and therefore Scailex agreed to pay Leumi Partners a finders fee in the amount of US\$ 3 million to be paid upon the completion of the transaction.

After the balance sheet date, on 18 October 2009, in exercise of the option, Leumi Partners was allocated NIS 102,705,270 par value convertible debentures (Series 1) of Scailex at a price of NIS 1.002 for every NIS 1 par value, for a total consideration of some NIS 103 million (the "Debentures"). The Debentures were allocated through the expansion of the debenture series (Series 1), all in accordance with the provisions of the law, and the shelf prospectus published by Scailex on 21 August 2009. The banks and Scailex agreed that notwithstanding the provisions of the agreement, the exercise of the option and the allocation of the Debentures would not be conditional on the completion and execution of the transaction which is the subject of the agreement, and should the transaction not be completed, the provisions detailed in the Debentures' trust deed regarding such an event would apply.

The transaction between the Bank and Scailex was completed on 28 October 2009, and thereunder Leumi Partners Ltd. acquired 7,667,037 ordinary shares from Scailex, constituting 4.99% of the issued and paid-up capital of Partner Communications Ltd. (on an undiluted basis and after neutralizing dormant shares), for a consideration of NIS some 515 million.

- I. On 13 September 2009, Leumi Partners Ltd. (a wholly owned subsidiary of the Bank) signed an agreement with GN Communication Industries Ltd. (a company wholly owned by Ms. Gal Naor) (the "Purchaser") for the sale of 4,124 ordinary shares of Keshet Broadcasting Ltd. ("Keshet") and 20 deferred shares of Keshet, constituting 20% of Keshet's issued and paid-up capital, and for the sale of rights deriving from the owner's loans of NIS 6.5 million that it had extended to Keshet (the "Sold Shares and Rights" and the "Purchase Agreement".) The Purchaser will pay US\$ 6 million for the Sold Shares and Rights. The Purchase Agreement is subject to conditions precedent, which include receipt of approvals from the Council of the Second Authority for Television and Radio, Bank Hapoalim Ltd. and the Board of Directors of Keshet.

## **Note 12 – Changes in Tax Legislation**

### **A. Changes in Value Added Tax Rates**

On 1 July 2009, the Value Added Tax Order (Tax Rate for Non-profit Organizations and Financial Institutions) (Temporary Provision), 2009 was published in the Israel Government Gazette. The Order raised the rates for salary tax and profit tax that are applicable to financial institutions, as from 1 July 2009 and continuing through 31 December 2010, from 15.5% to 16.5%.

As the Bank is a "financial institution" for the purpose of the Value Added Tax Law, the increase in the profit tax will increase the overall tax rate to which the Bank is subject, such that in 2009 it will be subject to an overall tax rate of 36.21% instead of 35.93% (an increase of 0.28 percentage points) and in 2010, it will be subject to an overall tax rate 35.62% instead of 35.06% (an increase of 0.56 percentage points).

Deferred taxes as at 30 September 2009 were calculated according to the amended tax rates, in light of the fact that the amendment was approved during the reporting period.

In the first nine months of the year, the total impact of the change in the rate of value added tax on the provision for taxes was not material.

### **B. Changes in Companies Tax Rates**

In July 2009, the Knesset approved the Improved Economic Efficiency Law (Statutory Amendments for Implementation of the Economic Plan for 2009-2010), 2009, which gradually reduces the companies tax

rates from 25% in 2010 to 18% for the year 2016 and thereafter. The tax rate to which the banks will be subject, including the profit tax, will drop from 35.62% in 2010 to 29.0% for the year 2016 and thereafter.

The change in the tax rates increased the tax expense for the third quarter of 2009 in the amount of NIS 146 million, taking into account the balance of deferred taxes as at 30 June 2009.